Governance and Audit Committee
Tuesday 21 January 2025

Subject: Draft Treasury Management Strategy 2025/26

Report by:	Director of Corporate Services (Section 151 Officer)
Contact Officer:	Peter Davy Financial Services Manager peter.davy@west-lindsey.gov.uk
Purpose / Summary:	To seek approval for the Treasury Management Strategy, Prudential Indicators, Minimum Revenue Provision Policy and Capital Investment Strategy to facilitate effective financial management and planning

RECOMMENDATION(S):

1. **That the Committee review, comment on and scrutinise the Treasury Management Strategy, Prudential Indicators and Minimum Revenue Provision (MRP) Policy 2025/26 and recommend to Council for approval.**

2. **To review, comment on and scrutinise the Capital Investment Strategy in conjunction with the Treasury Management Strategy.**

3. **Approval of any changes to the Capital Strategy and Minimum Revenue Provision (MRP) Policy and Prudential Indicators be delegated to the Section 151 Officer in consultation with the Chair of the Governance and Audit Committee, prior to the final strategy being presented to Council in March.**

IMPLICATIONS

Legal:

The Local Government and Finance Act 2003, the Prudential Code and the Treasury Management Code of Practice and Sectorial Guidance include a key principal that an organisations appetite for risk is included in their annual Treasury Management Strategy and this should include any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and liquidity when investing.

Financial: FIN/126/25/PD

There are no direct financial implications arising from this report.

Staffing:

None from this report.

Equality and Diversity including Human Rights:

None from this report.

Data Protection Implications:

None from this report.

Climate Related Risks and Opportunities:

The strategy includes for investment in Environmental, Social and Governance (ESG) financial instruments where such factors are taken into account when choosing investment products.

Section 17 Crime and Disorder Considerations:

None from this report.

Health Implications:

None from this report.

Title and Location of any Background Papers used in the preparation of this report:
Prudential Code for Capital Finance in Local Authorities 2021 Treasury Management Code of Practice and Cross-Sectorial Guidance Notes 2021 Treasury Management in Public Services: Guidance Notes 2021 All papers are located in the Financial Services section, Guildhall

Risk Assessment:
Interest Rate Risk: A rise in interest rates may lead to capital investment loss due to the inverse price and yield relationship and vice versa. Inflation Risk: Real returns can be eroded if inflation is expected to or rises during the term of the investment, therefore capital value may be reduced Re-Investment Risk: the effect of changing interest rates on re-investment before maturity. Credit Risk: The value of an investment can be affected by the credit quality/rating of the issuer. Default Risk: Possibility that total principal may not be returned before maturity, or partially returned. Net Cost of Services Risk: Under the IFRS9 amendments in 2018/19 there is a risk that adverse fair value valuations for some investments (such as the Property Fund) would have a direct negative impact on the Comprehensive Income and Expenditure Statement for Net Cost of Services. A statutory over-ride is currently in place which is due to end on 31st March 2025. The government is currently looking at options after this date. Risks associated with investing for longer periods, and in instruments/assets where the values can go down as well as up, will require mitigation as there will be increased risk to the security and liquidity of investments. Mitigation of these risks will be undertaken by defining the restrictions of time and maximum value of investment made and with appropriate financial appraisals being undertaken for each investment. Close monitoring of the investment performance will also be undertaken. Risk to the Net cost of services due to IFRS9 will be mitigated through the maintenance of a reserve for Investments Volatility Reserve, this will prevent any adverse change in valuation have a direct impact on the Comprehensive Income and Expenditure Statement. Ongoing review and maintenance of this reserve will be required each year.

Call in and Urgency:

Is the decision one which Rule 14.7 of the Scrutiny Procedure Rules apply?

i.e., is the report exempt from being called in due to urgency (in consultation with C&I chairman)	**Yes**		**No**	**x**

Key Decision:

A matter which affects two or more wards, or has significant financial implications	Yes	x	No	

Executive Summary

1.1 The Council is required to approve a Treasury Management Strategy Statement for 2025/26 before 1 April 2025. In accordance with the constitution the Governance and Audit Committee are responsible for the scrutiny of the Council's Treasury Management Strategy and Policies. The Treasury Management Strategy is attached for this purpose. In addition the Capital Investment Strategy, which has direct links to the Treasury Management Strategy is also provided for scrutiny.

1.2 The Council is required by statutory provision and regulation to 'have regard to' the Prudential Code when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003

1.3 By using the Prudential Code Framework, the Council ensures that the following objectives are met: -

- capital expenditure plans and investment plans are affordable and proportionate
- all external borrowing and other long-term liabilities are within prudent and sustainable levels
- the risks associated with investments for commercial purposes are proportionate to their financial capacity, and
- treasury management decisions are taken in accordance with good professional practice.

The Borrowing Strategy

1.4 HM Treasury announced reforms on Public Works Loan Board (PWLB) borrowing in November 2020, in that it would no longer support borrowing for the acquisitions of new investment assets purchased primarily for yield (Non-Treasury Activity i.e., Commercial property investment). In addition, the Prudential Code 2021 now precludes the use of any type of borrowing for primarily for a financial return (including internal borrowing) for this purpose. The Borrowing Strategy therefore no longer includes borrowing for this purpose.

However, borrowing is allowable to enable the effective management of the Property Portfolio.

The key objectives of the Council's Borrowing Strategy are.

- To ensure that future external debt is affordable and sustainable within the long term within the revenue budget constraints.
- To support schemes with a socio-economic value i.e., for the regeneration and growth of the district.

- To support significant service investment where the cost of borrowing will be offset by efficiencies and/or cost savings and/or income.
- All external debt undertaken will be repaid at loan maturity

1.6 To date Members have approved capital expenditure of £36.072m to be funded from external borrowing. The actual external borrowing value the Council holds is £24m, this is because just over £12m of cash is internally borrowed (funded from the cash we hold in reserves). The reason Councils do this is to reduce external borrowing costs especially when rates are high. The cost of borrowing almost always outweighs the interest received on investments so it is more efficient to fund capital expenditure from reserves than externally borrow. It is unlikely that a Council would need to access all of the cash held in reserves at short notice and therefore there will be a surplus of cash held on the balance sheet.

1.7 If Members decided to utilise significant levels of reserves as funding for projects, capital programme or service delivery, the Council would need to externally borrow up to the £36.072m level. There are no governance issues to prevent this as our Capital Financing Requirement has been approved to allow it but it will attract higher borrowing costs. These additional costs will need to be factored into future revenue budgets. As a guide a £5m PWLB loan over 50 years would cost around £293,000 in interest payments per year.

The Investment Strategy

1.5 The main objective of the strategy is the security, liquidity and finally yield of the investment, in the context of the Councils risk appetite and through the mitigation of risks.

1.6 The Council has a Climate Change strategy. As the Council will be interested in undertaking actions to reduce climate change, the Council as an ethical investor will consider the environmental, social and governance issues (ESG) when making treasury investment decisions.

1.7 The Treasury function is controlled by statute and professional guidance and its main priorities must remain as security, liquidity and yield.

1.8 Consideration of ESG will be undertaken when considering new investment opportunities and will be in accordance with our counterparty limits and rating criteria.

The Minimum Revenue Provision Policy (MRP)

1.9 The Council will repay an element of prudential borrowing annually. This policy has been revised in relation to where borrowing has previously been undertaken for Commercial Investment.

The MRP Policy will be as detailed below.

- Asset Life Method – debt repaid over the life of the asset
- Loan Principal repayment will be used to reduce the capital financing requirement instead of MRP. Where no repayment is made MRP will be charged.
- Where the Council has previously borrowed for the acquisition of Investment Properties the Asset Life Method will be used to calculate the MRP charge applicable on an annual basis. The maximum life that is used for this class of asset is fifty years.

Commercial Investments (Property Portfolio)

1.10 Whilst it is appreciated that these properties will be subject to wear and tear, all leases are fully insuring and repairing leases, with the liability for maintaining the asset at its current state being the responsibility of the Lessee.

1.11 The transactional costs of acquisition of these properties have been capitalised. Investment Properties will be revalued annually as at the Balance Sheet date.

1.12 Full MRP will be provided on investment properties in line with the latest government guidance. These amounts are factored into the Medium Term Financial Plan.

1.13 MRP Overpayments – The current DLUHC MRP Guidance allows that any charges made over the statutory minimum revenue provision (MRP) i.e., voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year.

1.14 Up until the 31 March 2024 the total Voluntary Revenue Provision (VRP) overpayments have been £1,081k however this relates to payments to reduce prudential borrowing against the Commercial Investments Property Portfolio and is therefore not deemed an overpayment.

1.15 To mitigate the risk of loss of the capital receipt not meeting outstanding debt, a Valuation Volatility Reserve had been created and a minimum balance of 4% of acquisition price set. It is intended that this reserve will be reduced over the medium term to reflect the implementation of an annual MRP.

1.16 To provide transparency the Treasury Management Strategy includes at 4.7 the (Non-Treasury) Investment Strategy in the context of the investing in commercial activity to ensure services can be maintained as government funding reduces and as previously approved by Corporate Policy and Resources Committee. Expert and legal advice will always be sought to ensure that any additional purchases, or replacement purchases are within our powers.

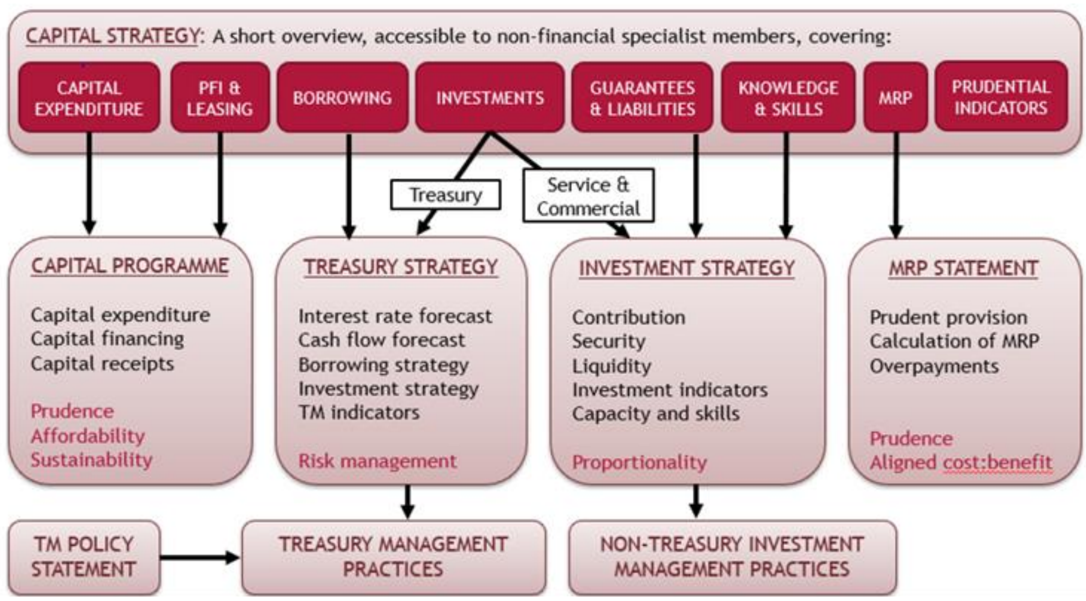
1.17 The Treasury Management Strategy including the Borrowing Strategy, Investment Strategy and Minimum Revenue Provision Policy are detailed below.

1.18 The Capital Investment Strategy is an appendix at the end of the Treasury Management Strategy. The Capital Investment Strategy forms a key part of the Council's overall Corporate Planning Framework. It provides a mechanism by which the Council's capital investment and financing decisions can be aligned with the Council's over-arching corporate priorities and objectives over a medium term (five year) planning horizon.

1.19 The Capital Investment Strategy provides a framework to enable both revenue and capital investment decisions which contribute to the achievement of the Council's priorities and objectives as set out in the Corporate Plan.

1.20 The strategy defines how the capital programme is to be formulated, and it identifies issues and options that influence revenue and capital spending and sets out how the resources will be managed.

The framework below illustrates the Prudential Framework.



1.21 Prudential indicators are designed to provide support and record local decision making and not as comparative performance indicators. These are contained within the Treasury Management Strategy. As we await the final finance settlement, indicators will be finalised prior to submission to Council for approval.

1.22 The draft strategy is attached at Appendix A and Members are asked to review, comment on and scrutinise the Strategy, Prudential Indicators and Minimum Revenue Provision (MRP) Policy 2025/26 and recommend to the Council for approval. To also review, comment on and scrutinise the Capital Investment Strategy in conjunction with the Treasury Management Strategy. Finally that any changes to the Capital Strategy and Minimum Revenue Provision (MRP) Policy and Prudential

Indicators be delegated to the Section 151 Officer in consultation with the Chair of the Governance and Audit Committee, prior to the final strategy being presented to Council in March.