



## AGENDA NO: 9

### INDEPENDENT AUDIT COMMITTEE – 17 December 2019

### TREASURY MANAGEMENT COVERING REPORT

### REPORT BY JULIE STRANGE, CHIEF FINANCE OFFICER, DORSET OPCC

### PURPOSE OF THE REPORT

*The draft Treasury Management and Investment Strategy for 2020/21 including the Prudential Indicators and the Minimum Revenue Provision Policy Statement is appended to this report, for consideration and comment by the Independent Audit Committee before being finalised. Changes relative to last year's strategy are highlighted in this covering report.*

#### 1.0 INTRODUCTION

- 1.1 The Police and Crime Commissioner has adopted CIPFA's Treasury Management in the Public Services: Code of Practice (the Code), which requires, as a minimum, a Treasury Management and Investment Strategy to be approved before the start of each financial year, a mid-year stewardship report, and an annual report after the year end.
- 1.2 The Independent Audit Committee is responsible for scrutinising the Treasury Management and Investment Strategy and making recommendations to the Police and Crime Commissioner, before it is approved.
- 1.3 Any comments made will be considered by the Dorset Joint Executive Board, prior to approval by the Police and Crime Commissioner who is ultimately responsible for approving the Annual Treasury Management and Investment Strategy.
- 1.4 The Treasury Management and Investment Strategy is intrinsic to the annual Budget and Medium Term Financial Strategy which is considered by the Police and Crime Panel each year as part of the Police and Crime Commissioner's annual precept setting process. This is further supported by the Capital Strategy, and the Reserves Strategy (both being considered on the agenda).

## **2.0 DRAFT STRATEGY**

2.1 The timetable for the production of the draft Treasury Management and Investment Strategy has been brought forward for 2020/21, in order to allow for scrutiny in advance of the finalisation of the budget in February. In support of this members of the Committee have received treasury management training in November from our treasury management advisers, Arlingclose.

2.2 Consequently it has been necessary to produce this draft document at an earlier stage in the budget timetable, before all of the figures have been finalised. This means that some of the figures will be subject to change and some are not yet available such as those relating to the new accounting standard IFRS16.

### **2.3 Counterparties**

2.3.1 The primary focus of the Strategy has been the management of credit risk, or the risk of funds being lost through the failure of a counterparty. This has been mitigated through the use of counterparty limits and the quality of counterparties that we can use. These limits do need to be practical, enabling effective and efficient management of the portfolio.

2.3.2 When the 2019/20 Strategy was set in February 2019, the maximum amounts to be invested in individual investments was set based on an estimated year end cashflow of £10m, enabling unsecured bank deposits of up to £500,000 and secured deposits of up to £1m.

2.3.3 However, for a significant period of the year, cashflow has been in excess of £20m following receipt of the pensions grant in July. This presents real practical difficulties for the Technical Team in trying to identify up to 40 different counterparties to invest with, who will accept deposits as low as £500,000. This simply isn't possible therefore large quantities of cashflow are invested with the Governments Debt Management Office which earns interest at less than the Bank of England Base Rate.

2.3.4 In order to address this issue in 2019/20, a paper was presented to the Resources Control Board proposing that the cash limits are increased when cashflow is in excess of £10m. This proposal was approved.

2.3.5 Building on the changes that have been introduced to the 2019/20 strategy, it is proposed to have a single set of counterparty limits, based on the higher limits recently added into the Strategy. This will streamline the process and improve clarity, however it does introduce the risk of having a less diverse portfolio when cashflow drops to lower levels. As this is for a relative short period of the year,

perhaps 2 to 3 months, it is felt this can be managed through the Treasury Management practices, rather than being covered in the Strategy.

2.3.6 In previous Strategies named counterparties have been shown. Against each a maximum amount to invest and a duration period was allocated. However, this information is only correct at a point in time and therefore does not reflect changes as the year progresses. This information has therefore been removed from the 2020/21 Strategy. Instead, the Technical Team will follow the guidance and advice from Arlingclose regarding each counterparty as and when it is required.

## 2.4 Inflation Risk

2.4.1 Inflation risk is the risk that investments are eroded if interest does not keep pace with inflation. For example, if you have £1m and inflation is 2%, you would need £1,020,000 the following year to remain static. If you achieve interest rates of 0.5% then your cash is worth £15,000 less than it was the year before. This is an area where some changes could see an improvement in our mitigation of this risk.

2.4.2 The main change would be in including the ability to make some longer term investments, in particular the use of some pooled funds, in order to achieve improved interest rates and provide some mitigation against inflation risk. The Arlingclose benchmarking as at 30 September showed that the average days to maturity of the Dorset portfolio was 3 days, compared to an average of 60 days for their 14 Police and Fire clients and 28 days for their 139 Local Authority clients. This would support the approach of building in a bit more duration to the Strategy.

2.4.3 It is therefore proposed to increase the limit of long term investments to £4m, in line with the minimum level of general reserves. This approach may result in having to undertake temporary borrowing for cashflow purposes slightly more frequently, however, the additional interest earned on the longer term investments will more than cover the costs of temporary borrowing.

## 2.5 Liquidity Indicator

2.5.1 An area that has caused some confusion in the past has been the application of the liquidity indicator and whether this voluntary measure has been breached. In order to avoid this situation in the future we will simplify the indicator by having a single measure of funds required to be available within a period of time, i.e. £5m available within 90 days, but also clarify that this would also include credit such as the overdraft limit and availability of temporary borrowing, not just the actual 'cash at bank' funding.

## 2.6 Borrowing

2.6.1 The approach to borrowing is becoming more relevant to Dorset, given the position of the capital programme over the Medium Term Financial Plan. This is an area

which has changed in the last few weeks with the unexpected increase in Public Works Loan Board (PWLB) interest rates. As a result we will follow the Arlingclose advice of looking to fund our borrowing internally when we have positive cashflow from the top up grant and undertake shorter term temporary borrowing from other Local Authorities as required. This will involve slightly more hands on management but will still be more cost effective. This will be kept under review should PWLB rates reduce.

2.6.2 In light of the borrowing requirements, Arlingclose recommend relatively wide limits are set for the maturity structure, since this indicator is only to cover the risk of replacement of loans being unavailable, not interest rate risk.

### **3.0 RISK/THREAT ASSESSMENT**

#### **3.1 Financial/Resource/Value for Money Implications**

Effective treasury management supports the prudent management of the financial affairs of the PCC.

#### **3.2 Legal Implications**

The draft Treasury Management Strategy follows the latest MHCLG and CIPFA guidance.

#### **3.3 Implications for Policing Outcomes**

Effective treasury management supports all aspects for effective policing outcomes.

#### **3.4 Equality**

No direct implications.

### **4.0 RECOMMENDATION**

4.1. It is recommended that the Independent Audit Committee considers the draft Treasury Management and Investment Strategy Appended and provides any comments prior to approval by the PCC.

**Julie Strange**

**Chief Finance Officer for Dorset OPCC**

Members' Enquiries to: Julie Strange, CFO, Dorset OPCC (01202 229096)