

DERBYSHIRE COUNTY COUNCIL

CABINET

28 January 2014

**Joint Report of the Chief Executive, the Director of Finance and
the Director of Property**

**PRUDENTIAL CODE FOR CAPITAL FINANCE, CAPITAL PROGRAMME
APPROVALS & TREASURY MANAGEMENT STRATEGY
(COUNCIL SERVICES)**

1 Purpose of the Report

To obtain approval for proposals for submission to Council relating to:

- The Prudential Code for Capital Finance.
- The capital starts programme for 2014-15.
- The Minimum Revenue Provision (MRP) policy for 2014-15.
- A Treasury Management Strategy for 2014-15.
- Compliance with, and set limits under CIPFA's Prudential Code and the Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes

2 Information and Analysis

A CAPITAL PROGRAMME & FINANCING

- 2.1 The Prudential Code for Capital Finance in Local Authorities (the Code) is a professional Code that sets out a framework for self-regulation of capital spending; in effect allowing councils to invest in capital projects which best meet their service delivery objectives as long as they are affordable, prudent and sustainable, subject to Government reserve powers to restrict borrowing for national economic reasons.
- 2.2 To facilitate the decision making process and support capital investment decisions, the Code requires the Council to agree and monitor a number of prudential indicators. The indicators cover affordability, prudence, capital

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expenditure, debt levels and treasury management. These indicators will also form the basis of in-year monitoring and reporting.

- 2.3 The main limiting factor on the Council's ability to undertake capital expenditure is whether the revenue resource is available to support in full the implications of capital expenditure, both borrowing costs and running costs, after allowing for any support provided by central government, now mainly through capital grants.
- 2.4 The capital programme is affected by the downward pressure on public expenditure, with lower levels of new schemes, government support and related borrowing going forward.

Although the strategic aim is to reduce long term debt and therefore the ongoing revenue cost, investment into key priorities continues.

The Council will receive government grant of over £42m to address key issues in highways maintenance, develop integrated transport schemes and address the most immediate condition problems in schools. A number of smaller schemes to address urgent issues across the remainder of the Council's property portfolio are also proposed; they will require finance from borrowing.

A number of major invest to save schemes, designed to assist in meeting future years savings targets, have also been identified. These are not included in the proposed new starts at this stage but will be subject to the production of comprehensive business cases and adopted into the programme if and when approved.

The proposed new starts programme for 2014-15, as shown in Appendix 1, has been evaluated and is recommended to proceed. More details on each scheme are provided in Appendix 2. The proposals for capital expenditure related borrowing and the estimated impact on the Council's revenue accounts in the next three years are shown at 2.5 to 2.10 below.

- 2.5 Details of the actual and estimated figures are shown below. This table incorporates schemes already approved, completed or still in progress plus the proposed new starts for 2014-15, and estimates for 2015-16 and 2016-17. These figures include existing capital programme proposals with updated forecasts for phasing of expenditure. In relation to the larger schemes in the programme the key changes relate to MEGZ where previously expenditure was programmed fairly evenly over 2013-2017 but is now expected to be largely committed 2014-2016 and the waste project, with expenditure now forecast to occur in 2016-17 (previously 2014-15). The costs and financing are spread accordingly over future years.

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	2012-13 Actual £m	2013-14 Estimate £m	2014-15 Estimate £m	2015-16 Estimate £m	2016-17 Estimate £m
*Capital Expenditure	96.76	98.34	152.74	89.13	80.36
Funding sources:					
Borrowing	5.51	18.34	72.90	41.16	42.76
Capital receipts	9.51	1.22	12.12	1.79	9.75
Capital grants	63.82	61.27	58.92	40.82	26.25
Revenue	17.92	17.51	8.80	5.36	1.60
*Capital Financing Requirement (CFR) (underlying need to borrow for capital purposes)					
Total CFR at year end	496.91	494.24	546.13	563.84	582.40
Net movement in CFR	-19.49	-2.67	51.89	17.71	18.56
Minimum Revenue Provision	21.98	21.01	21.01	23.46	24.20
PFI & Leases in CFR	91.45	89.23	86.85	84.31	81.60
PFI & Leases in MRP	2.22	2.38	2.54	2.71	2.90

*(*These are prudential indicators.)*

The above table indicates proposals for capital expenditure and related borrowing. Within the framework of prudential indicators Members are required to assess the affordability of the capital investment plans. Members are asked to note the following indicators, which are designed to assist the consideration of affordability:

- 2.6 **Actual and Estimates of the ratio of financing costs to net revenue stream** - This indicator identifies the trend in the cost of capital against the net revenue stream, based on the Capital Programme set out above.

	2012-13 Actual £m	2013-14 Estimate £m	2014-15 Estimate £m	2015-16 Estimate £m	2016-17 Estimate £m
Financing costs of CFR	48.47	46.49	47.52	52.10	53.86
Net Revenue Stream* Including DSG	1,033.31	1,014.36	983.60	972.60	975.19
Percentage	4.69	4.50	4.68	5.30	5.54
Net Revenue Stream* Excluding DSG	533.31	514.36	483.60	472.60	475.19
Percentage	9.09	9.04	9.83	11.02	11.33

* Estimates of Government grants, Council Tax/Business Rates, including and excluding Dedicated Schools Grant (DSG). DSG is currently forecast to remain stable over the next 3 years but should schools become academies the net revenue stream excluding DSG will reduce although financing costs will remain with the Council.

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2.7 The estimates of financing costs include current commitments and the proposed starts programme for 2014-15, together with an estimate through to 2016-17.

2.8 **Estimates of the incremental impact of capital investment decisions on Council Tax** - This indicator illustrates the estimated effect of the Capital Programme set out above, including the provisional programme through to 2015-16. In practice, only part of the costs are met from Council Tax.

	2014-15 £	Forward Projection 2015-16 £	Forward Projection 2016-17 £
Council Tax - Band D			
Existing Commitments only	3.96	16.95	0.75
Implication of new starts 2014-17	0.47	2.63	6.70
Total Commitments	4.43	19.58	7.45

2.9 Provision is made in the proposed 2014-15 revenue budget and in the Forward Financial Plan for debt charges and other costs arising from the programme. The Plan indicates that the proposals in this report are affordable over future years, based on current assumptions on the overall level of resources likely to be available to the Council. The programme will be reviewed in the event of any future change in those assumptions.

2.10 Minimum Revenue Provision

The Local Authorities (Capital Finance and Accounting) (England) Amendment Regulations 2008 require local authorities to agree a policy on the calculation of the Minimum Revenue Provision (MRP) for each financial year. The MRP is the amount the authority has to provide for the repayment of debt.

It is not proposed to change the policy, which is set out below.

- To provide 4% of debt outstanding on all debt as at 31 March 2008.
- On any new debt since this date to provide 4% of the balance on all borrowing unless any unsupported borrowing relates to any significant assets with a life of less than 20 years. In this case an annual amount based on the expected useful life of the individual assets is used and where those assets are vehicles then an average of 5 year lives are used.

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The Authority continues to have the option to make voluntary additional provision for debt repayment if it wishes.

The policy meets the requirement to make a prudent calculation of MRP.

B EXTERNAL DEBT

- 2.11 The Prudential Code (revised in 2011) specifies a number of prudential indicators in respect of external debt. These are described below.

Limits to Borrowing Activity

- 2.12 **The authorised limit** - This represents the limit beyond which borrowing is prohibited, and needs to be set and revised if necessary by members.

The figures for the proposed authorised limit for 2014-15 take into account:

- (a) The estimated amount of the Capital Financing Requirement at 31 March 2014 (£494.2m). This figure takes into account debt which the Council services on behalf of Derby City Council (approx £32.5m), which arose before Local Government Reorganisation. Derby City is recharged the relevant loan charges.
- (b) New borrowing for capital schemes of £72.9m during 2014-15 less Minimum Revenue Provision (£21.0m).
- (c) Short term borrowing from the other organisations. Deposits are taken from the Derbyshire Fire Authority and the Peak District National Park Authority pending their use. The deposits are treated as loans to the Council and therefore need to be included in its borrowing limits. It is suggested that a figure of £30m should be used to cover these items.
- (d) PFI liabilities are included in the CFR at a value of £ 86.9m and MRP at £2.5m

Based on the above, it is proposed that the authorised limit (including transferred debt & PFI) should be set at £573m for 2014-15. Proposed limits for future years have been calculated in a similar manner.

- 2.13 **The operational boundary** - This indicator is based on the probable external debt during the course of the year; it is not a limit and actual borrowing could vary around this boundary for short times during the year.

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In practice it is unlikely that all of the potential borrowing requirements included in the authorised limit will materialise at once, therefore the operational boundary requirements (including transferred debt & PFI) will be somewhat lower and £523m is suggested as a realistic figure for 2014-15.

- 2.14 The Cabinet is asked to approve the following authorised and operational limits:

Authorised limit for external debt	2014-15 Estimate £m	2015-16 Estimate £m	2016-17 Estimate £m
Borrowing	486	508	530
PFI liabilities	87	84	82
Total	573	592	612
Operational boundary for external debt	2014-15 Estimate £m	2015-16 Estimate £m	2016-17 Estimate £m
Borrowing	436	458	480
PFI & other long term liabilities	87	84	82
Total	523	542	562

These borrowing limits will be subject to monitoring and will be revised annually.

- 2.15 The Council has remained within all of the Prudential Indicators set for previous years, including in 2013-14.

C TREASURY MANAGEMENT

Prudential Indicators

- 2.16 The Prudential Code (revised in 2011) specifies only one prudential indicator in respect of Treasury Management which is that the Council has adopted the CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes as revised in November 2009, details of which are included in Appendix 3.
- 2.17 In addition, the Council is required to take account of guidance received from Communities and Local Government (CLG) in respect of Investment Strategy.
- 2.18 The proposed Treasury Management Strategy for 2014-15, which incorporates these requirements, is attached as Appendix 3. The key change to the previous strategy is the additional categories to the approved borrower list. In practice it is expected that existing borrowers

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will be used primarily but the inclusion of additional categories provides flexibility and resilience.

Clauses to be formally adopted

2.19 CIPFA recommends in the revised Treasury Management Code of Practice that councils should amend their financial regulations to adopt four important clauses in respect of treasury management activity. These clauses relate to:

- The creation and maintenance of a treasury management policy statement and treasury management practices.
- Minimum reporting requirements to council on treasury management matters.
- Delegation of responsibility for the implementation, regular monitoring and execution of its treasury management policies and practices
- Delegation of responsibility for the effective scrutiny of those policies and practices.

These clauses are reproduced in Appendix 3 together with the policy statement recommended by CIPFA.

3 Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal, prevention of crime and disorder, equality and diversity; human resources, environmental, health, property and transport considerations.

4 Key Decision

No.

5 Call-in

Not applicable.

6 Background Papers

Local Government Act 2003, Prudential Code, Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes, Guidance issued by CLG, Capital Accounting Working Papers.

7 OFFICERS' RECOMMENDATIONS

Cabinet recommends to Council:

1. The adoption of the Prudential Code including the Prudential Indicators as described in paragraphs 2.5, 2.6, 2.8 and 2.12-2.16.
2. The 2014-15 Capital Starts Programme as detailed in Appendix 1, and that further reports on the detailed schemes be brought to Cabinet.
3. The MRP policy for 2014-15 as detailed in paragraph 2.10.
4. The Treasury Management Strategy for 2014-15 as described in Appendix 3, and taking into account the guidance issued by the CLG as described in paragraph 9(b).
5. The adoption of CIPFA's Code of Practice on Treasury Management and Cross Sectoral Guidance Notes (revised 2011), as shown in Appendix 3, and the Treasury Management Policy Statement as specified in the Treasury Management Code of Practice and set out in Appendix 3.

IAN STEPHENSON
Chief Executive

PETER HANDFORD
Director of Finance

JEREMY GOACHER
Director of Property

15 January 2014

Capital Programme 2014-15 Starts

		Gross Cost	Grant	Net Cost	Capital receipts	Borrowing
Proposed Approvals		£000s	£000s	£000s	£000s	£000s
Adult Care						
	Adaptations	3,000	-	3,000	-	3,000
	Maintaining minimum standards	1,800		1,800		1,800
	Sub total	4,800	-	4,800	-	4,800
CAYA						
	Schools Basic Need 13-14 Reserves	4,500	4,500	-	-	-
	Schools Modernisation/Capital Maintenance	12,000	12,000	-	-	-
	Schools Access Initiative (SAI)	800	-	800	-	800
	Devolved Formula Capital	2,500	2,500	-	-	-
	Sub total	19,800	19,000	800		800
Corporate						
	Chesterfield Register Office	500		500		500
	Buxton Crescent	8,000		8,000	8,000	
	Sub total	8,500	-	8,500	8,000	500
Corporate Resources						
	Health and Safety/Environmental Health/ Vacant Buildings/Radon/Demolitions	150	-	150	-	150
	Risk Management	250	100	150	-	150
	Kitchen Ventilation Schemes	1,000		1,000		1,000
	Fire Certificate work	750	-	750	-	750
	Sub total	2,150	100	2,050	-	2,050

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		Gross Cost	Grant	Net Cost	Capital receipts	Borrowing
		£000s	£000s	£000s	£000s	£000s
Environmental Services						
	Local Transport Plan	20,000	20,000	-	-	-
	Additional Local Highways Maintenance	1,405	1,405	-	-	-
	Green Lane Action Plan Improvements	140	-	140	-	140
	Land Reclamation	1,940	1,615	325	-	325
	Sub total	23,485	23,020	465	-	465
Contingency		500	-	500	-	500
	Total	<u>59,235</u>	<u>42,120</u>	<u>17,115</u>	<u>8,000</u>	<u>9,115</u>

New Start Proposals

Adult Care

Adaptations

Disabled people requiring major adaptation to their accommodation are able to apply for a Disabled Facilities Grant (DFG) administered by district councils. The DFG is mandatory if the applicant is unable to access essential facilities within their home. The County Council has a duty to identify suitable works based upon an assessment of individual needs; however, the decision to approve the grant lies with the relevant District Council.

The DFG process is prescribed by legislation and regulations and requires that applicants are subject to a Test of Resources (means test). The Test of Resources only looks at an applicant's income and does not take account of their outgoings or personal circumstances. There are three possible outcomes for applicants:

- a grant to cover the cost of all the work (up to a maximum of £30,000)
- a grant to cover part of the work with the requirement that the applicant meets the remaining costs (subsequently referred to as their assessed contribution)
- the grant application is deemed ineligible as the applicant is assessed to be able to meet all the costs of the work.

The decision on DFG funding is the responsibility of the relevant District Council. However, the County Council, as part of its legal duties under the Chronically Sick and Disabled Peoples Act (1970) s2(1)(e), is required to consider providing financial assistance where 1) the applicant requests assistance towards his/her assessed contribution due to financial hardship and/or 2) that the costs of the work assessed as being necessary are above the current £30,000 DFG limit and the applicant appears to be unable to meet the additional costs.

Maintaining Minimum Standards

The bid is for top priority work to existing Older Persons Homes and Supported Living schemes. The work has been delayed awaiting the outcome of the consultation for revised accommodation and support project; however, some of this work is now urgent. Works to Old Persons Homes comprises mechanical/engineering work and replacement of windows and doors to 18 homes. The cost of this element of the bid is likely to cost in the region of £1.5m.

In addition urgent works are also required at two supported living establishments for learning disability at 9 Victoria Street, Brimington and Hadfield Road, Glossop. This work would be general refurbishment including replacing the

bathrooms, refurbishing the bedrooms etc and landscaping to bring the building up to minimum standards. This work is expected to cost around £300,000 which would then enable inspection and registration of premises by the Care Quality Commission.

Children and Younger Adults

Schools Basic Need

The DfE grant allocation for Basic Need schemes is to provide additional school places in areas of population growth. There are a number of primary sector schools which are 'candidates' for this funding for which feasibility studies have been undertaken. A priority list of potential projects is being finalised.

Modernisation/Capital Maintenance (level of funding subject to confirmation)

This grant allocation is to address urgent condition and suitability issues in educational properties, including projects relating to essential re-roofing, re-heating, re-wiring, replacement windows, and replacement of 'buildings at risk'. A priority list of potential projects is being finalised.

Schools Access Initiative (SAI)

This allocation is used to address disabled access needs in mainstream schools. This helps to enable disabled pupils to attend their local mainstream school where appropriate.

Devolved Formula Capital

This grant funding is devolved directly to schools by the DfE to spend on their Asset Management Plan priorities, or to contribute to capital projects funded by the Authority in accordance with approved policies.

Corporate

Chesterfield Register Office

Chesterfield Register Office has been based in its current accommodation since the early 1970s and includes office accommodation for the Parent Partnership and the Bus Survey Team. The accommodation was not built for purpose and is seriously deficient in terms of disabled access. Many of these users are parents with pushchairs registering births and elderly residents registering deaths of relatives.

The office is the busiest of the County Council's Register offices and is officially designated as the County Register Office; it is also the central repository for the storage of registers from across the County. Additional and secure storage in line with General Register Office requirements will be provided as part of the project.

The access issues at these offices limit its use as a Registration facility. The refurbishment proposals include the installation of a disabled lift covering all floors which would open up the building to greater and more practical use. The first floor would be redesigned to provide separate birth and death registration areas - including waiting areas - considered good practice by the General Register Office in inspection visits.

Owing to the extent of the works proposed and to update the facility, the building will be refurbished throughout.

The proposals also include the installation of photovoltaic panels at an estimated cost of £12,000 with a payback period of approximately 12 years.

Buxton Crescent

The Buxton Crescent and Thermal Spa project is a vitally important heritage and regenerative project started by Derbyshire County Council and High Peak Borough Council to find a viable use for The Crescent and secure the future of this Grade I listed building and the Grade II Natural Baths in the heart of the historic town of Buxton. The Council has previously agreed a £1m contribution towards the total capital cost of £36m. The Capital Programme bid is to enable a loan to be made to the developers of the Buxton Crescent Project in the event they are unable to secure private sector debt financing in order to allow the project to progress.

Corporate Resources

Health and Safety/Environmental Health/Vacant Buildings/Radon/ Demolitions

Works in this category are generated from a variety of sources including fire officer reports, environmental health officer reports and health and safety assessments. Failure to comply with such reports or assessments could result in building closures or prosecutions. The category also covers security /risk issues which may occur when buildings are vacant for sale, temporarily not in use, or where vandalism/misuse - such as squatters - is regarded as possible. In some cases, demolition of buildings may be the most prudent solution.

Risk Management

This funding supports departments in implementing risk management initiatives usually on a shared funding basis. Traditionally this has targeted security priorities on a risk ranking basis. It is also intended to promote wider strategic risk management initiatives, as appropriate, in line with the risk management strategy.

The bulk of this funding tends to be spent on school security schemes to help protect pupils, staff and visitors. It is also used to assist in the protection of the council's assets against arson, theft and vandalism which can cause significant disruption to services.

Kitchen Ventilation Schemes

Following an oven back-blast, the 2010-11 Capital programme approved £3m to fund the first tranche of safety works to kitchens and a further £1m was approved as part of the 2011-12 programme. Current budgets are now almost fully committed and additional funding is required to continue with this work. The aim of this budget is to upgrade kitchens to be compliant with current legislation. Engineers have already replaced most Flame Failure Devices (FFD) and installed over 40 canopies with a further 20 currently in design ready for approval in the near future. The 2010-11 report noted that, overall, the costs of completing this work programme would be in the region of £8m-£9m. The current bid of £1m is to allow for this important work to continue, however, members need to be mindful that there may be future bids to continue this process.

Fire Certificate Work

Under The Regulatory Reform (Fire Safety) Order 2005 the Authority is required to undertake Fire Risk Assessments on its building stock. These consist of Operational assessments by establishment managers and Technical Assessment by survey teams.

Technical Assessments consider the building components, the means of escape, the suitability of compartmentation, warning systems and equipment etc. Assessments are carried out on an on-going basis, agreed with the Fire service, to identify and improve the building form/fabric to a suitable standard.

The Council's ongoing survey programme has identified the need for further funding to address these works.

Environmental Services

Local Transport Plan (level of funding subject to confirmation)

Direct grant allocation for highway maintenance and integrated transport.

The Highway Maintenance grant funds a programme of work that is key to effectively managing and maintaining the local highways network, the Council's largest and most visible asset. The Integrated Transport grant provides funding which is vital in providing local people with access to jobs, education, healthcare, shopping, leisure and other services, while reducing the impact of social and rural exclusion and improving safety.

Additional Local Highways Maintenance

Allocated by the Government to develop a programme of works to maximise the resilience of the network to extreme weather, both winter and flooding. There are likely to be a number of additional schemes to compliment rather than displace existing planned maintenance plus an additional programme of surface dressing.

Countryside NCH Programme - Green Lane Action Plan

The non-classified highway programme includes work to improve access to and safety of green lanes, to encourage more people to use the facilities. The work, which is carried out in partnership with local communities and other agencies, includes improvements and the tackling of erosion on routes in challenging environments due to topography, weather conditions and high levels of use. It assists the Council in avoiding claims and Section 56 notices, which requires the Council to undertake work if it hasn't complied with the action plan.

Land Reclamation

Funding for land reclamation programme is predominantly provided through capital grants secured from a variety of external funding organisations, with the Council providing some pump-prime investment. It is anticipated that the Council contribution of £325,000 will lever in an additional £1.615m to fund projects. The funding is also required to enable the Council to meet statutory obligations on land in its ownership, particularly around physical and environmental work on mines, tips and quarries to deal with hazards and contamination.

Contingency

The contingency sum is for unforeseen, essential works which may arise during the year.

DERBYSHIRE COUNTY COUNCIL

TREASURY MANAGEMENT
STRATEGY 2014-15

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A. Treasury Management Strategy 2014-15

1. Cabinet approved the CIPFA Code of Practice on Treasury Management, which included a Treasury Management Policy Statement, on 16 April 2002, and acceptance of the Code is reaffirmed on an annual basis as a prudential indicator.
2. The policy requires an annual strategy to be reported to Cabinet outlining the expected treasury activity for the forthcoming year. Further reports are produced at the half-year stage to monitor progress, and after the year-end to report on actual activity for the year.
3. In accordance with the provisions of CIPFA's Code of Practice, the Director of Finance has assessed the arrangements for the management and control of treasury management risk and is satisfied with their adequacy and suitability. A key requirement of this report is to explain both the risks, and the management of the risks, associated with treasury management. The report will incorporate guidance received from CLG in respect of the investment of temporary surpluses.
4. This strategy report covers:
 - Interest rate expectations
 - Current net borrowing and capital financing requirement
 - The Council's borrowing and debt strategy
 - The Council's investment strategy
 - Treasury Management performance indicators
5. Treasury Management activities will be subject to regular review to reflect changing circumstances, and further application and development of existing and emerging guidance.
6. **Interest rate expectations**

The Bank of England base rate has been 0.5% since March 2009. Under forward guidance, the MPC does not intend to raise Bank Rate from its current level of 0.5% at least until the unemployment rate has fallen to a threshold of 7%. The Chancellor's Autumn Statement predicted this would occur in mid 2015.

The Council's Treasury Management Policy places security and liquidity ahead of yield in order to minimise the risk of loss.

Short term interest rates determine the amount of interest received on the Council's temporary investments. Short term investments for up to 364 days average 0.50% in current market conditions.

The Bank of England's policy of purchasing £375 billion of gilts (quantitative easing) together with the UK's perceived status as a 'safe haven' had resulted in gilt yields being artificially low. However, improved financial stability and positive economic growth have resulted in gilt yields increasing towards more 'normal' levels during the last 12 months.

Long term fixed interest rates are more relevant for borrowing to fund the Capital Programme. The Public Works Loan Board ("PWLB") offers longer term borrowing at rates which change in line with the gilt market. At 5.12.13 these ranged from 3.92 % for 10 years to 4.62% for 25 years.

Gilt yields for durations between 5 and 20 years are expected to increase by approximately 1% by March 2017.

In November 2012 the PWLB introduced a 'Certainty Rate' offering a 0.20% discount on new borrowing for all Councils who met their eligibility criteria. The Council were successful in meeting this requirement.

7. (i) **Current Net Borrowing and Capital Financing Requirement**

At 31/12/13, the Authority had £408m of borrowing and £310m of investments.

Table 1 - Current Net Borrowing

	31.3.13 Actual £m	31.3.14 Estimate £m
Fixed Rate Debt - PWLB	342.3	337.4
Market	-	-
Short term	15.3	5.0
Variable Rate Debt - PWLB	-	-
Market	28.0	28.0
Short term	21.6	22.2
Total Debt	407.2	392.6
Fixed Investments	0	0
Variable Investments	(311.6)	(308.0)
Total Investments	(311.6)	(308.0)
Net Borrowing	95.6	84.6

NB: Assumes £15m PWLB loans to be repaid 31.3.14 and no new external borrowing in 2013-14.

Investments comprise the Authority's cash held as usable reserves together with income received in advance of expenditure (working capital).

The Capital Financing Requirement (CFR) is the Council's underlying need to borrow for capital purposes.

Table 2 - Net Borrowing and Capital Financing Requirements

	2014-15 Estimate (year end) £m	2015-16 Estimate (year end) £m	2016-17 Estimate (year end) £m
Gross Borrowing*	389	374	381
Investments	248	217	204
Net Borrowing	141	157	177
CFR (Capital Financing Requirement)	546.1	563.8	582.4

* Debt managed on behalf of others is excluded from the Net Borrowing indicator.

The Council also manages debt on behalf of Derby City comprising of an additional £31m in 2014-15, £30m in 2015-16 and £29m in 2016-17.

Gross borrowing reduces by PWLB repayments of £5m in 2014-15, £15m in 2015-16 and £12.5m in 2016-17. It is assumed new borrowing will be internal (assuming short term interest rates remain low) until 2016-17. Net borrowing increases in line with CFR as new capital spend will have to be funded by additional borrowing or reduction in investments.

The above figures show that the Council's net borrowing is less than its forecast CFR in accordance with the requirements of the Prudential Code.

8. The Council's borrowing and debt strategy

The authority has previously raised the majority of its long term borrowing from PWLB but will consider other sources of funding if appropriate.

(a) Approved sources of borrowing/raising capital finance

(i) Public Works Loans Board (PWLB)

The principal source of the Council's borrowing requirement. Historically the PWLB has offered the lowest fixed rates together with flexibility to reschedule or repay early.

(ii) Market Loans

The banking sector offers loans, usually LOBO's (lender option borrower option). These loans are at competitive rates, however, the loss of control and flexibility must be considered.

(iii) Internal Borrowing

The use of internal resources (reserves and working capital) which are temporarily available to allow the Council to repay or defer borrowing to when market conditions are more favourable. In a low interest environment, the savings in interest paid more than offset the loss of interest earned invested in short term deposits. The limit on the use of internal resources will remain at 25% of the net Capital Finance Requirement (CFR) after deducting PFI debt. This limit is to avoid an over-reliance on this particular source of funding.

(iv) Bonds

Some larger public organisations such as the Greater London Authority (GLA) and Transport for London (TFL) have issued their own bonds to finance their long-term borrowing requirements. However, an issuance of at least £200m is deemed to be required to be cost effective, as the Council would need an individual credit rating and incur significant legal and advisory costs.

The Local Government Association has been working on a UK municipal bond agency as an alternative to the PWLB for some time. The founder councils would invest in the project with returns from a share of any borrowing and equity in the agency. In theory, other Local Authorities could borrow from the agency at rates lower than the PWLB rate of Gilts + 1.

(v) Other Local Authorities

The use by other Local Authorities of short-term borrowing of up to 364 days to cover cash-flow shortages is prevalent. The Council will consider use of such short-term borrowing and longer term deals could be considered on their individual merit after comparison to the PWLB.

- (vi) Derbyshire Fire & Rescue Service (DFA)/Peak District National Park Authority (PDNPA)

The Council has accepted callable deposits from DFA & PDNPA under individual Service Level Agreements (SLA's). Deposits are currently paid at the DMO deposit rate of 0.25%, but higher rates could be agreed for fixed term deposits of up to 364 days.

- (vii) Bank Overdraft

The Council does not have a formal overdraft facility with the Co-op Bank, as the costs deemed it superfluous. This option will be reconsidered with the new bank following the current procurement exercise.

- (viii) Leasing

This Council will consider leasing if more advantageous than borrowing.

It is recommended that the above-mentioned sources of borrowing be approved for 2014-15.

(b) Debt Repayment/Rescheduling

Debt repayment/rescheduling opportunities are sought as part of the day to day management of the Council's borrowing and lending activities.

Debt repayment is the early redemption of borrowing before its scheduled maturity date without replacement. If the rate payable is higher than the rate on an equivalent new loan then a premium will be paid, if lower then a discount will be received.

Debt rescheduling is amending the term of a loan and consequently the interest rate applicable, however, the amount borrowed remains unchanged. Premiums and discounts may also apply.

In November 2010, the PWLB increased the margin between its new borrowing rate and premature repayment rate, which effectively limits any benefits from early repayment or rescheduling.

It is proposed that early repayment/rescheduling should be subject to the following limits:

- No more than £80m will be repaid or rescheduled without the prior approval of Cabinet.
- Any early repayment or rescheduling exercise will leave the average maturity of the total debt between 10 and 35 years. Average maturity is currently 20.17 years.
- Any early repayment or rescheduling exercise will produce an overall benefit to the Council by either reducing total interest charges or providing an early redemption discount.

(c) Variable v Fixed Rate Loans

Long term borrowing can be taken at either fixed or variable rates of interest. The Council is required to approve limits for its fixed rate and variable rate debt which form indicators within the Treasury Management Code. The control of variable rate debt is important due to the risk of downside costs or upside benefits when interest rates change. All PWLB loans are currently held at fixed rates, to provide certainty. For example, a rate increase of 0.5% on £25m of short term borrowing from PDNPA & DFA would result in an additional £125k interest per annum.

Although no new long term borrowing is envisaged in the next financial year, the usual strategy is to borrow on a fixed rate basis provided the long term interest rates remain relatively low. If rates are high the option to borrow at a variable rate would be considered with a view to converting to fixed rates in the future.

Investments consist of the Council reserves together with temporarily surplus funds from peaks in cash-flow. These funds are variable, therefore subject to changes in short-term interest rates.

The recommended upper limits on the percentage of borrowing and investments held at fixed and variable rates, as required by the Code, are set out below:

Table 3 - Fixed and Variable Borrowing & Investment Limits

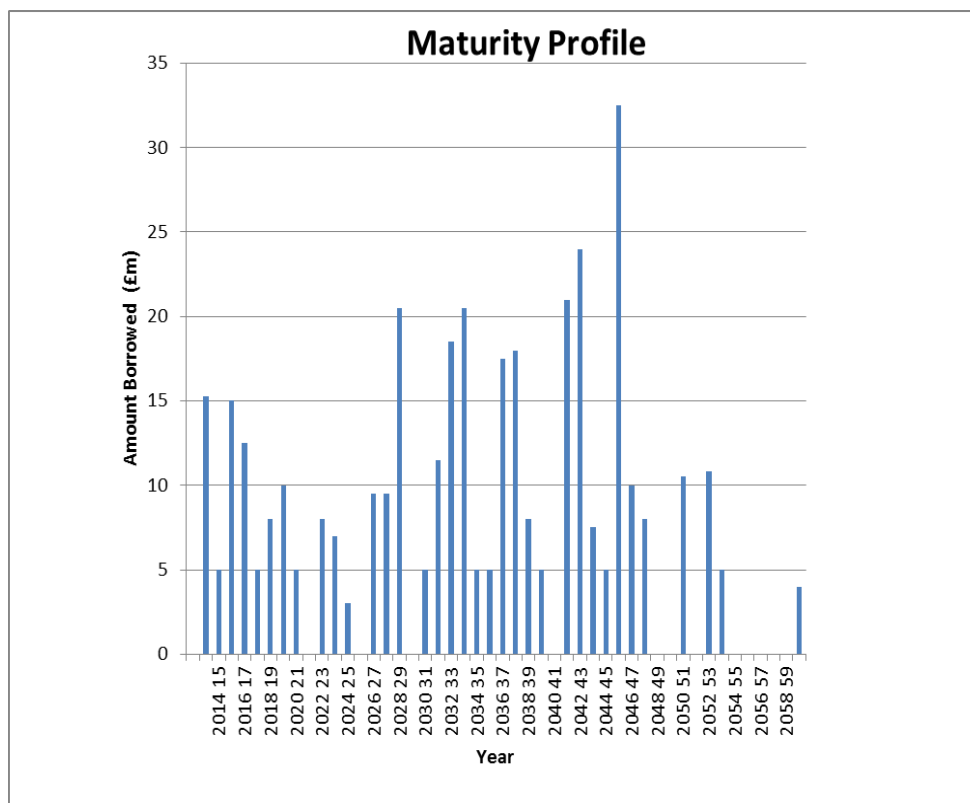
	2014-15 Upper	2015-16 Upper	2016-17 Upper
	%	%	%
Borrowing			
Limits on fixed interest rates	100	100	100
Limits on variable interest rates	40	40	40
Investments			
Limits on fixed interest rates	25	25	25
Limits on variable interest rates	100	100	100

For investments, fixed interest rates are deemed to apply to loans for more than one year.

Limits set at these levels will provide for efficient debt management, within an acceptable degree of risk. For the purposes of the Code, investments are to be deducted from borrowing to produce adjusted limits, but within the above parameters.

(d) Maturity Profile

The maturity profile is the rate at which long-term loans have to be repaid to the PWLB (or other lenders). It would be imprudent to have a large proportion of repayments due in any one year, thus a spread of redemptions is desirable. The Council's debt profile at 31 March 2014 is shown in the graph below:



The average redemption per year is £8.2m (2.2%) of the total debt, with a maximum redemption of £32.5m (8.8%) in 2045-46. The average duration for all loans is approximately 21 years. The maturity structure is a treasury indicator under the Code, with lower and upper limits recommended as shown in the table below. These are set quite widely to ensure that full advantage can be taken of interest rate movements and debt rescheduling opportunities, within an acceptable degree of risk.

Table 4 - Maturity Structure Limits - Fixed Borrowing

		2013-14
Under 12 months	Lower – Upper	0% - 15%
12 months to 2 years	Lower – Upper	0% - 15%
2 years to 5 years	Lower – Upper	0% - 40%
5 years to 10 years	Lower – Upper	0% - 40%
10 years to 20 years	Lower – Upper	10% - 40%
20 years to 30 years	Lower – Upper	10% - 40%
30 years and above	Lower – Upper	10% - 40%

9. The Council's Investment Strategy

The Council holds significant investment funds, representing income received in advance of expenditure plus balances and reserves held. In 2013, the Council's investment balances have ranged between £295m and £444m, however these balances are expected to fall by approximately £50m if the 2014-15 capital expenditure is funded from internal resources.

Under CIPFA's Treasury Management Code of Practice, the Council is required to formulate a strategy each year regarding the investment of its revenue funds/capital receipts pending their use. The Council is required to take the Code (supplemented by DCL Guidance on Local Authority Investments: revised in 2010) into account under Section 12 of the Local Government Act 2003.

Both the CIPFA Code and the CLG Guidance require the Council to invest its funds prudently and to have regard to the security and liquidity of its investments before seeking the highest rate of return or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

In 2013, the Council opened a contingency bank account with Lloyds due to concerns about the financial stability of its principal bankers the Co-

operative Bank. The Co-operative Bank subsequently announced their withdrawal from Local Authority banking. The Council are currently tendering to appoint new bankers with effect from 1.4.14.

The proposed investment strategy, the counterparty list (those organisations the Council has approved as borrowers) and limits are designed to accommodate Pension Fund cash as well as that of the County Council. Under the terms of the Local Authorities (Functions & Responsibilities) (England) Regulations 2000, the Cabinet is not permitted to take decisions relating to the Pension Fund. Pension Fund investments has been delegated to the Pensions and Investment Committee and relevant extracts from this report, insofar as they apply to the Pension Fund, will be submitted to the Pensions and Investment Committee for approval.

The investment strategy is subject to regular review and monitoring to reflect changing circumstances and external guidance.

(a) Strategy under CIPFA's Treasury Management Code of Practice

At 31.12.13 the Council held £310m of invested funds representing income received in advance of expenditure plus balances and reserves held. In the current financial year, the Council's investment balance has ranged from £310m to £444m.

At 31.12.13, the Pension Fund held £179m of cash balances with balances ranging from £157m to £200m during the financial year.

Interest receipts are highly sensitive to both interest rate changes and cash flows. For example, an additional 0.5% on investments of £200 million will result in an additional income of £1m per annum. Similarly an average £20m increase in balances invested at 0.5% will generate an additional £100k per annum.

Approval is requested for the Council to invest its surplus funds with the following counterparties subject to cash duration limits and credit ratings. Credit ratings are defined in Section C on page 18:

UK High Street Banks (minimum long term credit rating of A3/A-/A- from Fitch, Moody's & Standard & Poor).
The Council's current account bank
The Pension Fund's custodian bank
Part Nationalised Banks

Non UK Banks (minimum long term credit rating of A3/A-/A- from Fitch, Moody's & Standard & Poor together with relevant minimum long term sovereign rating of AA/AA/AA).

Building Societies (minimum long term credit rating of A3/A-/A- from Fitch, Moody's & Standard & Poor).

UK Central Government (DMO/Treasury Bills/Gilts)

UK Local Authorities (including Police/Fire, TFL)

Supranational and Multilateral Development Banks

UK Registered Providers of Social Housing (minimum A- long term credit rating).

Money Market Funds

The new investment categories of Non UK Banks, Supranational/Multilateral Development Banks & UK Registered Social Providers (Housing Associations) have been recommended by Arlingclose, the Council's Treasury Management advisors. Although these categories are unlikely to be the Council's main investment options, they will provide the Council with greater flexibility.

(b) CLG Guidance

The guidance also requires councils to categorise their investments as either "specified" or "non-specified" investments.

(i) Specified Investments

Specified investments are deemed as "safer" investments and must meet certain conditions, ie they must

- be denominated in sterling
- have less than 12 months' duration
- not constitute the acquisition of share or loan capital
- either be invested in the government, a local authority, or in a body or investment scheme with a "high" credit quality

The Council is required to specify what constitutes a high credit quality for each type of investment and how frequently these should be monitored. It must also specify the minimum level of such investments.

The Council's investments with the UK Government, Supra-nationals and Other Local Authorities automatically qualify as specified investments provided that they are of less than 12 months' duration and are denominated in sterling.

The classification of the other investments is dependent on the counterparty being of a high credit quality. It is suggested that minimum definition of high credit quality should be:-

Moody's:	long term A3; short term P1
Fitch:	long term A-; short term F1
Standard & Poor's:	long term A-; short term A1

It is recommended that, in order to be classified as specified investments, approved counterparties should have credit ratings no lower than those shown above, with the lending limit for UK banks and Nationwide Building Society maintained at £30m plus accrued interest.

It is recommended that the total lending limit for durations in excess of 100 days be increased to £150m (£100m) for UK banks and the Nationwide Building Society. This will allow the Council to utilise the front end loading of Revenue Support Grant (payments made by the government), of which 75% will be received in April 2014.

The minimum level for short-term specified investments for 2014-15 is to remain at £150m as this sum is a sufficient liquidity buffer.

It is recommended that an additional £10m limit for operational and transactional purposes (overnight) is added to the limit of the successful tenderer for the banking contract.

A limit of £10m is recommended for individual non UK banks which meet the individual criteria for specified investments together with minimum AA sovereign rating. Some foreign banks such as National Australia Bank & Svenska Handelsbanken take direct deposits, however the majority of non-UK banks will only fund through Certificates of Deposit, therefore it is recommended that the overall limit is increased to £50m (£20m) and the duration limit increased to 364 days (3 months).

It is recommended that the credit limit for the UK Government (DMO/Treasury Bills) be unlimited for investments up to 100 days. The existing limits of £50m County Fund and additional £20m Pension Fund for durations between of 100 days and 6 months should be widened to include Supranational & Multilateral Development Banks.

It is recommended that the limit for Other Local Authorities (as defined by the Local Government Act 2003) be increased from £17m to £20m per Upper Tier Authorities (Counties, Unitary, London Boroughs, Scottish/ Welsh). A lower limit of £10m per authority should apply to Lower Tier (Borough & District) authorities.

The Council receives a fully updated list of counterparty credit ratings every month from Arlingclose, the Council's treasury management advisers. However, credit ratings should not be relied upon in isolation and supplementary information including ratings watches, financial press and other market information will also be considered. The status of all approved counterparties will be kept under regular review.

It is recommended that in the event of a counterparty losing its P1/F1/A1 short term credit rating, the investment is re-classified as a non-specified investment.

(ii) Non Specified Investments

The Council is required to look at non-specified investments in more detail. It must set out:

- procedures for determining which categories of non-specified investments should be used
- the categories deemed to be prudent
- the maximum amount to be held in each category

The Strategy must also set out procedures for determining the maximum period for committing funds.

It is recommended that the following procedure be adopted for determining which categories of non-specified investments should be used:

- the Cabinet should approve categories on an annual basis
- advice should be provided by the Director of Finance
- priority should be given to security and liquidity ahead of yield

On this basis, the following categories of non-specified investments, and relevant limits are currently considered as prudent and are recommended for use:

(a) Investments of good credit quality

Banks and building societies must have a minimum short term P2/F2/A2 rating. It is recommended that the limit for this category be fixed at £10m (plus accrued interest) per individual counterparty, subject to a total exposure of £50m. Loans will be subject to a maximum duration of 100 days.

(b) Part Nationalised Banks

A higher limit of £30m plus accrued interest is to be maintained for Part Nationalised Banks (Lloyds/TSB & RBS/National Westminster Bank), provided the Government's stake remains over 25% & they maintain a minimum P2/F2/A2 short term credit rating.

(c) Pension Fund Custodian Bank

A £20m Sterling equivalent limit is requested for the Pension Fund's custodian bank (currently BNY Mellon) for the daily (overnight) cash management of the Pension Fund's US \$ and € funds by their external fund managers.

(d) Co-operative Bank

A £1m limit with the Co-operative Bank for receipts would be useful during the transitional arrangements of the transfer of banking to the Council's new provider.

(e) Money Market Funds

Under a European Commission proposal for Money Market Funds, Constant Net Asset Value (CNAV) funds are to be replaced by Variable Net Asset Value (VNAV) funds. Money Market Funds will no longer attract a credit rating for the fund as a whole, therefore it is recommended that the average weighted credit rating for the fund's individual holdings be a minimum of A-.

(f) Investments in excess of 364 days

Whilst most of the Council's surpluses are temporary, others, for example the insurance fund reserve, could reasonably be invested for periods in excess of one year.

It is recommended that a total limit of £100m be agreed for investments greater than 364 days. It is recommended that the maximum duration for UK Gilts and loans to other Local Authorities be 5 years. The maximum duration for loans to UK Banks and Building Societies, Supranational and Multilateral Development Banks and UK Registered Providers of Social Housing should be limited to 5 years.

10. Treasury Management Performance Indicators

The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the Prudential Indicators which are predominantly forward looking.

The results of these indicators will be reported in the Treasury Management Annual Review following the end of the financial year.

It is recommended that the performance indicators used should be as described below:

Long Term Borrowing:

Comparison of the Council's cost of borrowing for the latest financial year with:

- the average interest rate for 25 year PWLB maturity loans for the latest financial year
- the average rate of interest for county councils for the latest financial year (taken from the CIPFA publication - Capital Expenditure and Borrowing Statistics)

Investments:

The average 3 month London Inter Bank Deposit (LIBID) rate. This variable rate produced by the British Bankers Association reflects the supply and demand in the cash markets.

The final decision on treasury matters remains with the Council.

B. Approved Borrowers**1. UK Banks**

Counterparty	Short term			Long term			Limit £m
	Fitch	Moody's	S&P	Fitch	Moody's	S&P	
Santander UK	F1	P1	A1	A	A2	A	30
Barclays Bank Group	F1	P1	A1	A	A2	A	30
Co-operative Bank	B	NP	n/a	B	Caa1	n/a	1
HSBC Group	F1+	P1	A1+	AA-	Aa3	AA-	30
Lloyds TSB Group							30
Bank of Scotland Plc	F1	P1	A1	A	A2	A	
Lloyds TSB Bank	F1	P1	A1	A	A2	A	
Royal Bank of Scotland							30
Royal Bank of Scotland	F1	P2	A2	A	A3	A	
Nat West	F1	P2	A2	A	A3	A	
National Australia Bank							
Clydesdale Bank Yorkshire Bank	F1	P2	A2	Baa2	A2	BBB+	10
Standard Chartered Bank	F1+	P1	A1+	AA-	A1	AA-	30

2. Building Societies

Building Society	Short term			Long term			Limit £m
	Fitch	Moody's	S&P	Fitch	Moody's	S&P	
Coventry	F1	P2	n/a	A	A3	n/a	10
Leeds	F2	P2	n/a	A-	A3	n/a	10
Nationwide	F1	P1	A1	A	A2	A	30
Yorkshire	F2	P2	n/a	BBB+	Baa2	n/a	10

3 Council's Main Bank (to be confirmed)

4 Pension Fund Custodians Bank (BNY Mellon)

5 Non UK Banks (A- Individual Long Term rating plus Sovereign AA rating)

6 UK Government

- 7 Other Local Authorities
- 8 Supranational & Multilateral Development Banks
- 9 UK Registered Providers of Social Housing
- 10 Money Market & Other Pooled Fund

C. Credit Ratings**Moody's Credit Ratings****Long-Term Obligation Ratings****Aaa**

Obligations rated Aaa are judged to be of the highest quality, with minimal credit risk.

Aa

Obligations rated Aa are judged to be of high quality and are subject to very low credit risk.

A

Obligations rated A are considered upper-medium grade and are subject to low credit risk.

B

Obligations rated B are considered speculative and are subject to high credit risk.

Caa

Obligations rated Caa are judged to be of poor standing and subject to very high credit risk.

Short-Term Obligation Ratings**P-1**

Issuers (or supporting institutions) rated Prime-1 have a superior ability to repay short-term debt obligations.

P-2

Issuers (or supporting institutions) rated Prime-2 have a strong ability to repay short-term debt obligations.

P3

Issuers (or supporting institutions) rated Prime - 3 have an acceptable ability to repay short-term obligations.

NP

Issuers (or supporting institutions) rated Non-Prime do not fall within any of the Prime rating categories.

Fitch Credit Ratings**Long-Term Ratings****AAA - Highest credit quality.**

AAA ratings denote the lowest expectation of default risk. They are assigned only in cases of exceptionally strong capacity for payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.

AA - Very high credit quality

AA ratings denote expectations of very low default risk. They indicate very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.

A - High credit quality

A ratings denote expectations of low default risk. The capacity for payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to adverse business or economic conditions than is the case for higher ratings.

Short-Term Ratings**F1 - Highest short-term credit quality**

Indicates the strongest intrinsic capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.

F2 - Good short-term credit quality

Good intrinsic capacity for timely payment of financial commitments.

Standard & Poor's Credit Ratings**Long-Term Ratings****AAA**

An obligation rated AAA has the highest rating assigned by Standard & Poor's. The obligor's capacity to meet its financial commitment on the obligation is extremely strong.

AA

An obligation rated AA differs from the highest rated obligations only to a small degree. The obligor's capacity to meet its financial commitment on the obligation is very strong.

A

An obligation rated A is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher rated categories. However, the obligor's capacity to meet its financial commitment on the obligation is still strong.

Short-Term Ratings**A1**

A short term obligation rated 'A-1' is rated in the highest category by Standard & Poor's. The obligor's capacity to meet its financial commitment on the obligation is strong. Within this category certain obligations are designated with a (+) sign. This indicates that the obligor's capacity to meet its financial commitment is extremely strong.

A2

A short term obligation rated 'A-2' is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher rating categories. However, the obligor's capacity to meet its financial commitment on the obligation is satisfactory.

D. Clauses to be formally adopted

CIPFA recommends that all public service organisations adopt, as part of their standing orders, financial regulations, or other formal policy documents appropriate to their circumstances, the following four clauses:

1. This Council will create and maintain, as the cornerstones for effective treasury management:
 - a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities
 - suitable treasury management practices (TMPs) setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Treasury Management Code of Practice, subject only to amendment where necessary to reflect the particular circumstances of this Council. Such amendments will not result in the organisation materially deviating from the Code's key principles.

2. This Council will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.
3. This Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Cabinet, and for the execution and administration of treasury management decisions to the Director of Finance, who will act in accordance with the organisation's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.
4. This Council nominates the Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

E. Treasury Management Practices (TMPs)

CIPFA recommends that an organisation's treasury management practices (TMPs) include those of the following that are relevant to its treasury management powers and the scope of its treasury management activities.

TMP1	Risk management
TMP2	Performance measurement
TMP3	Decision-making and analysis
TMP4	Approved instruments, methods and techniques
TMP5	Organisation, clarity and segregation of responsibilities, and dealing arrangements
TMP6	Reporting requirements and management information arrangements
TMP7	Budgeting, accounting and audit arrangements
TMP8	Cash and cash flow management
TMP9	Money laundering
TMP10	Training and qualifications
TMP11	Use of external service providers
TMP12	Corporate governance

Note

TMPs are the detailed procedures which are held by the Director of Finance and are subject to regular review.

F. The Treasury Management Policy Statement

CIPFA recommends that the Council's treasury management policy statement adopts the following forms of words to define the policies and objectives of its treasury management activities:

1. This organisation defines its treasury management activities as:

The management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.

2. This organisation regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.
3. This organisation acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.