Decision No: 2017/50

REPORT TO:	**POLICE AND CRIME COMMISSIONER FOR LANCASHIRE**
REPORT BY:	Steve Freeman
DATE:	**19 March 2018**
TITLE:	**TREASURY MANAGEMENT POLICY AND STRATEGY 2018/19**

Appendix A refers

EXECUTIVE SUMMARY

This report outlines the proposed Treasury Management Policy Framework for 2018/19 as required by the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management Code of Practice. It includes the Police and Crime Commissioner's borrowing and investment strategies, together with the treasury management prudential indicators which seek to ensure that the Commissioner's borrowing to fund capital expenditure remain both sustainable and affordable.

RECOMMENDATION

The Commissioner is asked to approve the treasury management strategy for 2018/19, including

a) Treasury management prudential indicators

b) The borrowing strategy

c) The investment strategy

d) The MRP strategy

e) To formally adopt the updated policy statement at Appendix A

Decision taken by the Police and Crime Commissioner for Lancashire:

Original decision, as set out in the attached report, approved without amendment (please delete as appropriate)	**YES**	**NO**

Original decision required to be amended and decision as detailed below:
The reasons for the amended decision are as detailed below:

Police and Crime Commissioner: Comments

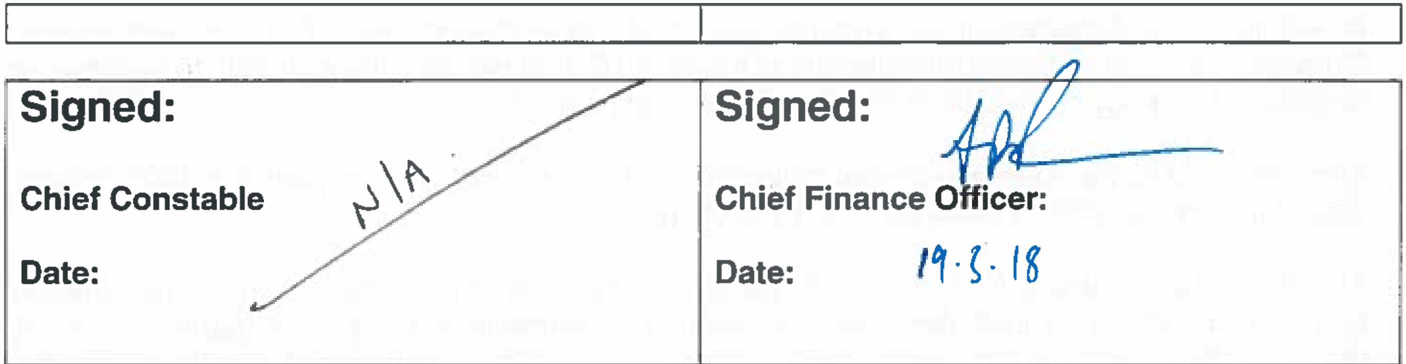
DECLARATIONS OF INTEREST

The PCC is asked to consider any personal / prejudicial interests he may have to disclose in relation to the matter under consideration in accordance with the law, the Nolan Principles and the Code of Conduct.

STATEMENT OF COMPLIANCE

The recommendations are made further to legal advice from the Monitoring Officer and the Section 151 Officer has confirmed that they do not incur unlawful expenditure. They are also compliant with equality legislation.

Signed:	**Signed:**
Police and Crime Commissioner	**Chief Officer:**
Date: 19th march 2018	**Date:** 20.3.2018



Signed:	Signed:
Chief Constable	Chief Finance Officer:
Date:	Date:

Background

Treasury management is defined as "The management of the authority'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."

In February 2012 The Police and Crime Commissioner adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the approval of a treasury management strategy before the start of each financial year. As a local authority the Police and Crime Commissioner for Lancashire ("the Commissioner") is also bound by the treasury management framework expressed within the code and therefore the requirements of the code must be met by Police and Crime Commissioners.

In addition, the Department for Communities and Local Government (CLG) issued revised guidance on local authority investments in March 2010 that requires Authorities, including police and crime Commissioners, to approve an investment strategy before the start of each financial year. The strategy also has regard to other CIPFA treasury management publications such as risk management in 'Treasury Risk Toolkit for Local Authorities' (2012) and the use of derivatives in 'Using Financial Instruments to Manage Risk' (2013.)

Statutory requirements

The Local Government Act 2003 (the Act) and supporting Regulations requires the Commissioner to "have regard to" the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Commissioner's capital investment plans are affordable, prudent and sustainable. The PCC has adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year. CIPFA consulted on changes to the Code in 2017 and recently published a new version which requires the production of a Capital Strategy. Although effective from 2018/19 CIPFA Treasury Management Panel recognise "that the requirement included in the Prudential Code to produce a Capital Strategy may require a longer lead-in period. Therefore the Treasury and Capital Management Panel recognises that this requirement may not be able to be fully implemented until 2019/20 financial year".

In addition, the Department for Communities and Local Government (CLG) issued revised Guidance on Local Authority Investments in March 2010 that requires the Authority to approve an investment strategy before the start of each financial year.

This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance.

The DCLG has issued a Consultation Paper on Investments which it proposes will be effective from 1 April 2018. This includes a new definition of investments namely investments "covers all the financial assets of the organisation, as well as other non-financial assets which the organisation holds primarily for financial returns, such as investment property portfolios. This may therefore include investments which are not managed as part of normal treasury management or under treasury management delegations. All investments require an appropriate investment management and risk management framework under this Code."

In practice, this means that any loans given or investment in assets wholly for income generation purposes are covered by the Code. Under the proposed Code loans for economic development purposes can be made even if they do not meet the strict criteria for security and liquidity. However, the Code will expect the loans to be proportionate to the overall portfolio and limits to be set on the maximum to be given.

Similarly, authorities can hold non-financial investment, which will normally have a physical asset that can be realised to recoup the capital invested. The Code requires details on the assessment of risk and the action to be taken if the value of the asset no longer covers the investment.
Currently, the PCC does not make direct investment in property for income generation purposes.

CIPFA requirements

The primary requirements of the CIPFA Code are as follows-

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Commissioner's treasury management activities, the current version is shown at Appendix 1.

2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Commissioner will seek to achieve those policies and objectives.

3. The production of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.

4. Delegation by the Commissioner of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

This Strategy Statement has been prepared in accordance with the Code of Practice (2011). In accordance with the code, the Treasury Management Strategy will be approved by the Commissioner before the start of the financial year. In addition to this the Commissioner will also receive a mid-year report and a final year-end outturn report. In addition there will be monitoring and review reports provided in the event of any changes to Treasury Management policies or practices. The aim of these reporting arrangements is to ensure that those with ultimate responsibility for the treasury management function appreciate fully the implications of treasury management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

The following reporting arrangements will be adopted in accordance with the requirements of the revised Code: -

Area of Responsibility	Committee/ Officer	Frequency
Treasury Management Policy Statement	Police and Crime Commissioner	Annually before the start of the financial year.
Treasury Management Strategy / Annual Investment Strategy / MRP policy – scrutiny and approval	Police and Crime Commissioner	Annually before the start of the financial year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – mid year report, scrutiny of performance	Police and Crime Commissioner	Mid year – 6 months
Treasury Management Strategy / Annual Investment Strategy / MRP policy – updates or revisions at other times	Police and Crime Commissioner	As required
Annual Treasury Management Outturn Report	Police and Crime Commissioner	Annually by 30 September
Treasury Management Monitoring Reports	Chief Finance Officer	Quarterly
Treasury Management Practices	Chief Finance Officer	Annually

In setting the Treasury Management Strategy, the following factors have been taken into account; economic forecasts, the level of the approved Capital Programme and the current structure of the Commissioner's debt portfolio. It covers the following aspects of the Treasury Management function:-

- Prudential Indicators which will provide a controlling framework for treasury management activities.
- Long-term debt outstanding;
- Prospects for interest rates;
- The Borrowing Strategy;
- The Investment Strategy;
- Policy on borrowing in advance of need.

Economic Context

Economic Forecast

The forecast economic conditions include an expectation that growth in the next few years will be low. Negotiations on the UK exit from the European Union and future trade relations is causing uncertainty. The progress and final outcome of these negotiations may impact on economic growth not only in 2018/19 but also in future years. In his budget in November 2017, the Chancellor of the Exchequer announced forecasts of growth which were significantly less than those given in the budget of spring 2017. The forecast was as follows:

	November 2017 Budget	Spring Budget
2017/18	1.5%	1.8%
2018/19	1.4%	1.6%
2019/20	1.3%	1.8%
2020/21	1.5%	1.9%
2021/22	1.5%	2.0%

Inflation increased during 2017 with the Consumer Price Index (CPI) rising to 3.0% in September. This was largely as a result of the impact of the fall in the value of sterling following the Brexit decision but it is anticipated that inflation will fall from this position. The forecast CPI in the Chancellor's budget was as follows:

2017/18	3.0%
2018/19	2.2%
2019/20	1.8%
2020/21	2.0%
2021/22	2.0%

With inflation increasing and unemployment remaining low during 2017/18 the Bank of England believed that the extent of spare capacity in the economy seemed limited and the pace at which the economy could grow without generating inflationary pressure had fallen over recent years.

Therefore the Monetary Policy Committee of the Bank of England concluded that a rise in interest rates was appropriate. In November 2017 they raised the base rate for the first time in a decade with the base rate increasing from 0.25% to 0.50%.

Looking forward the Monetary Policy Committee has heightened expectations of more increases in Bank Rate and at a quicker pace .This is based on the Bank's perceptions of impaired supply capacity and a desire to bring inflation back to target more quickly than initially anticipated.

Interest Rate Forecast and Prospects for Market Liquidity

The prevailing and forecast interest rate situation will be monitored to inform borrowing decisions and to ensure that opportunities for debt restructuring are maximised. Regular forecasts of interest rates are provided by Arlingclose Ltd, treasury management advisers to Lancashire County Council. Their central case is for the Bank Rate to rise twice in 2018 and once more in the first half of 2019.The risks to this forecast are weighted to the downside.

The latest forecast provided by Arlingclose Ltd is shown in the table below:

	Bank Rate %	3 month LIBID %	12 month LIBID %	5 year gilt yield %	10 year gilt yield %	20 year gilt yield %	50 year gilt yield %
March 18	0.50	0.50	0.7	1.15	1.65	2.00	1.80
June 18	0.75	0.75	0.95	1.35	1.80	2.10	1.95
September 18	0.75	0.85	1.1	1.40	1.85	2.15	2.00
December 18	1.00	1.00	1.3	1.50	1.90	2.15	2.00
March 19	1.00	1.10	1.4	1.55	2.00	2.20	2.05
June 19	1.25	1.35	1.65	1.60	2.05	2.25	2.10
September 19	1.25	1.35	1.65	1.65	2.10	2.25	2.10
December 19	1.25	1.35	1.6	1.70	2.15	2.20	2.05
March 20	1.25	1.35	1.55	1.70	2.15	2.15	2.00
June 20	1.25	1.30	1.5	1.70	2.15	2.20	2.05
September 20	1.25	1.30	1.5	1.65	2.05	2.20	2.05
December 20	1.25	1.30	1.5	1.65	2.05	2.20	2.05
March 21	1.25	1.30	1.5	1.65	2.05	2.20	2.05

In the above table 'bank rate' refers to the policy rate of the Bank of England. 'LIBID' is the London Interbank bid rate and can be used as a proxy for short term market interest rates. PWLB borrowing rates are based on 'Gilt Yield' and so this is a forecast of long term interest rates. The Commissioner can borrow at 80 basis points above the gilt yield, so for example a fixed interest rate to borrow PWLB money for 10 years would be 2.45%, 1.65% plus 0.80%.

Current Position

Current Treasury Portfolio Position

The current value of the Commissioner's Treasury Portfolio at 31.12.2017 is:	**Principal £m**	**%**
DEBT		
Fixed rate loans from PWLB	17.054	100
Variable rate loans	0	0
Total debt	**17.054**	
INVESTMENTS		
Variable rate investments in the County Council's General County Fund	20.297	
Total investments	**20.297**	

The level of investments represents the Commissioner's cumulative surplus on the General Fund, the balances on other cash-backed earmarked reserves and a cash-flow balance generated by a surplus of creditors over debtors and by grant receipts in advance of payments. There is net surplus position of £3.243m as at 31 December 2017 which is expected to fall by the end of the 2017/18 financial year.

Borrowing Requirement

In the medium term PCC borrows for capital purposes only. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The table below compares the estimated CFR to the debt which currently exists, adjusted for transferred debt. This gives an indication of the borrowing required. It also shows the estimated resources available for investment. An option is to use these balances to finance the expenditure rather than investing, often referred to as internal borrowing, so the table gives an indication of the minimum borrowing requirement through these method.

The CFR forecast includes the impact of the latest forecast of the funding of the Capital Programme.

	31/3/2017	31/3/2018	31/3/2019	31/3/2020	31/3/2021
	£m	£m	£m	£m	£m
Capital Financing Requirement	40.222	60.017	65.129	72.254	70.561
Less external borrowing	18.154	17.054	15.954	14.854	14.554
Borrowing requirement	22.068	42.963	49.175	57.400	56.007
Reserves and working capital	-49.743	-34.796	-24.493	-16.977	-16.642

Borrowing/(investment) need	-27.675	8.167	24.682	40.423	39.365

The Commissioner has not borrowed for capital purposes since 2007, preferring instead to fund capital expenditure and maturing borrowing from internal resources; hence the borrowing requirement identified in the table above. However, it is anticipated that with the proposed borrowing requirement in the Capital Programme and the falling level of reserves this may not be sustainable in the medium term. The position will continue to be reviewed by the Chief Finance Officer and borrowing either long term or short term will be taken as necessary.

Capital Funding Strategy

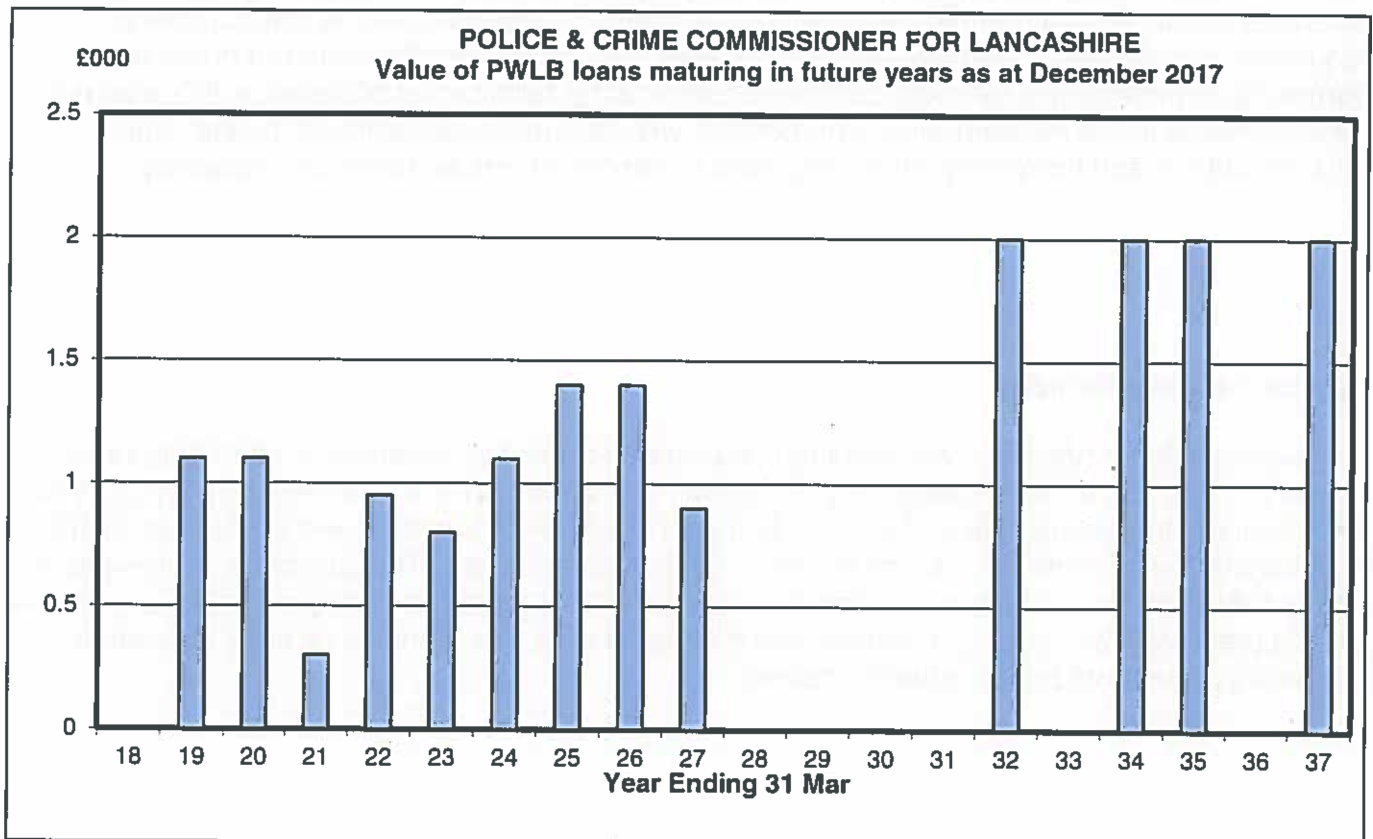
The Commissioner has set aside funding in ear-marked revenue reserves to contribute to the delivery of the investment included in the Capital Programme. This resource will be used, in the first instance, to provide finance for short life assets such as IT systems and equipment in order to avoid the use of borrowing where possible for this type of asset. This approach represents a prudent strategy for the funding of short life assets as the cost of borrowing over shorter terms is more expensive than for longer periods and the use of reserves to minimise such shorter life borrowing represents better value for money.

Borrowing Strategy

In view of the above interest rate forecast the Commissioner's borrowing strategy will be based upon the following information:-

- Official UK interest rates are not anticipated to rise in 2018/19. Gilt yields are projected to be fairly flat in the short term with some increase towards the end of the year. This will continued to be reviewed with the result that:
- If it were felt that there was a significant risk of a sharp fall in long and short term rates, e.g. due to a marked increase of risks around relapse into recession, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- If it were felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

The chart below shows the current maturity profile of the Commissioner's long term debt.



The interest rate on the loans ranges from 4.1% to 4.875%.

The cheapest borrowing at present is internal borrowing facilitated by running down cash balances and foregoing interest earned on investments at historically low rates - this is the policy the Commissioner has been pursuing for a number of years, funding capital expenditure and paying down debt maturities from existing balances. Although this policy has been beneficial the significant capital expenditure funded from borrowing and the anticipated reduction in the level of reserves may result in a need for new borrowing.

The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Continuing the policy of using internal balances is likely to increase the need for the Commissioner to incur short term loans to cover cash flow shortages.

The approved sources of long-term and short-term borrowing currently are:

- Public Works Loan Board
- UK local authorities
- any institution approved for investments
- any other bank or building society authorised by the Prudential Regulation Authority to operate in the UK

- UK public and private sector pension funds

In the past the Commissioner has raised all long-term borrowing from the Public Works Loan Board, but it continues to investigate other sources of finance, such as local authority loans and bank loans, that may be available at more favourable rates.

GLA Municipal Bond Agency

The Municipal Bond Agency was established by the Local Government Association in June 2014 with the primary objective of setting up an alternative capital funding source for the local government sector and reducing UK local authority financing costs by becoming the most efficient and cost effective provider of finance. The company is owned by the LGA who are the founder shareholder and 56 other local authority shareholders one of which is Lancashire County Council.

As yet the MBA has not made any borrowing available to local authorities. In order to borrow from the MBA the each local authority is required to sign a joint and several guarantee contained within a framework agreement.

If following due diligence it is decided the Municipal Bond Agency is a suitable counterparty for borrowing, a separate report including information on the joint and several guarantee will be presented for consideration.

Debt Restructuring

The Chief Finance Officer, together with the County Council's treasury management team reviews options for debt restructuring on a regular basis. A recent review found that given the relatively favourable interest rates at which these have been taken out (below 5%) and the penalties associated with any early repayment, restructure is not considered financially viable at the present time. A better option for the immediate future is to continue to utilise reserves to reduce the future borrowing requirement rather than repay debt.

Frequent discussions will continue to take place between the Chief Finance Officer and the Treasury Management Team to monitor this situation and any future decisions on debt financing will be put through the same rigorous cost and prudence analysis that external borrowing has traditionally gone through and will be reported to the Commissioner in due course.

Policy on Borrowing in Advance of Need

The Commissioner will not borrow more than or in advance of need purely in order to profit from the investment of the extra sums borrowed. However advance borrowing may be taken if it is considered that current rates are more favourable than future rates and that this advantage outweighs the cost of carrying advance borrowing. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the Commissioner can ensure the security of such funds and relationships.

In determining whether borrowing will be undertaken in advance of need the Commissioner will:-

- Ensure that there is a clear link between the capital programme and the maturity profile of the existing debt portfolio which supports the need to take funding in advance of need.

- Ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered.
- Evaluate the economic and market factors that might influence the manner and timing of any decision to borrow.
- Consider the merits and demerits of alternative forms of funding.
- Consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.

Investment Strategy

The Commissioner will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") issued in March 2004, any revisions to that guidance, the Audit Commission's report on Icelandic investments and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Guidance Notes ("the CIPFA TM Code"). The Commissioner's investment priorities are: -

(a) The security of capital and
(b) The liquidity of its investments.

The Commissioner will also aim to achieve the optimum return on his investments commensurate with proper levels of security and liquidity. The risk appetite of the Commissioner is low in order to give priority to security of its investments and in accordance with this the 2018/19 policy needs to take into account the recent developments in banking reform legislation.

Current Investments

At 31st December 2017 the Commissioner held £20.297m invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2017/18 the Commissioner's investment balance has averaged at £39.015m, with the highest balance being £76.712m. Levels for 2018/19 will be dependent upon the use of reserves and the level of internal borrowing used to fund capital expenditure In line with the treasury management strategy, the Commissioner will only use very high quality counterparties for investments. All of the Commissioner's investments are currently with LCC although there was a long term investment with another local authority which matured in October 2017.

The Commissioner currently has access to a call (instant access) account with LCC. This currently pays bank rate, (currently 0.50%). Each working day the balance on the Commissioner's Current Account is invested in this to ensure that the interest received on surplus balances is maximised.

The overall combined amount of interest earned on Fixed/Call balances as at 31st December 2017 is £0.122m.at an annualised rate of 0.42%. The current interest rate is 0.50%.This compares favourably with the benchmark 7 day LIBID which averages 0.17% over the same period.

The economy is currently in a low yield environment but both the CIPFA Code and the CLG Guidance require the Commissioner 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 Commissioner'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.

The Commissioner can invest with other local authorities. Following the downgrade of the UK credit rating by the rating agencies, several local authorities saw a reduction in their ratings. Therefore, consideration has been given to reducing the risk associated with the Commissioners investment with other local authorities. Arlingclose, the County Council's Treasury Management advisor, state they are "comfortable with clients making loans to UK local authorities for periods up to four years, subject to this meeting their approved strategy. For periods longer than four years we recommend that additional due diligence is undertaken prior to a loan being made." On this basis it is proposed that the investments to local authorities are limited as follows:

	Maximum individual investment (£m)	Maximum total investment (£m)	Maximum period
Up to 4 years	10	250	4 years
Over 4 years	10	50	10 years

The investment in LCC as part of the call account arrangement is excluded from the above limits. The balance on this account is dependent upon short term cash flows and therefore does not have a limit.

The Commissioner may invest surplus funds with any of the counterparties in the table below, subject to the cash and time limits shown.

Counterparty		**Cash limit**	**Time limit †**
Secured Bank Deposits, Reverse repurchase Agreements	AAA	£5m each	5 years*
	AA+		3 years*
	AA		2 years*
	AA-		2 years*
Call Accounts with banks and other organisations with minimum AA- credit rating		£10m	next day
UK Central Government (irrespective of credit rating)		unlimited	50 years**
UK Local Authorities (irrespective of credit rating)		£10m	10 years
Secured Bond Funds AA rating and WAL not more than 3 years		£5m each	n/a

Secured Bond Funds AAA rated and WAL not more than 5 years	£5m each	n/a

* but no longer than 2 years in fixed-term deposits and other illiquid instruments
** but no longer than 5 years in fixed-term deposits and other illiquid instruments

Legislative Context

Bail-in legislation, which aims to ensure that failing banks are no longer rescued from taxpayers is now in place. There is a hierarchy of loss with equity being the first to suffer loss. Deposits by local authorities would be deemed to be senior unsecured deposits and have some of the least protection. Therefore if a bank should be failing there is a higher risk of losing some of its deposit or having it converted to equity in order to maintain the bank as a going concern., .

In the 15/16 policy a replacement liquidity option through bond funds was included within the treasury policy with allowable funds defined by credit rating and weighted average life (WAL.) Investing in senior secured bonds backed by collateral provides a protection against bail-in. In 2016/17 the secured lending was extended to include repurchase agreements.

Whilst the investment strategy has been amended to allow greater flexibility with investments any decision as to whether to utilise this facility will be made based on an assessment of risk and reward undertaken jointly between the Chief Finance Officer and LCC Treasury Management Team, and consideration of this forms part of the on-going meetings that take place throughout the year.

The legislative and regulatory background to treasury management activities requires the Commissioner to set out the use of "specified" and "non-specified" investments.

Specified Investments: The CLG Guidance defines specified investments as those:-

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and invested with one of:
  - the UK Government,
  - a UK local authority, parish council or community council, or
  - a body or investment scheme of "high credit quality".

The Commissioner defines "high credit quality" organisations as those having a credit rating of A+ or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher.

Non-Specified Investments are any investment that does not meet the definition of a specified investment. The Commissioner does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition of specified credit quality.

The Commissioner may lend or invest money using any of the following instruments:-

- interest-bearing bank accounts,
- fixed term deposits and loans,
- callable deposits where the Commissioner may demand repayment at any time (with or without notice),
- certificates of deposit,
- bonds, notes, bills, commercial paper and other marketable instruments, and
- shares in bond funds

Investments may be made at either a fixed rate of interest, or at a variable rate linked to a market interest rate, such as LIBOR, subject to the limits on interest rate exposures below.

On behalf of the Commissioner the county council's treasury management section prepares daily cash flow forecasts to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Commissioner's medium term financial plan and cash flow forecast.

The performance target on investments will remain as being above the average rate for 7 day notice money.

7. Minimum Revenue Provision (MRP) Strategy

The Commissioner is required to assess MRP for 2018/19 in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003.

The major proportion of the MRP will relate to the more historic debt liability that will continue to be charged in accordance with the Capital Financing Requirement method for MRP calculation. This option allows for the MRP to be calculated as 4% of the Capital Financing Requirement. The CFR is derived from the Balance Sheet and represent the value of the fixed assets, for which financing has not already been made. This method of calculation has been used by the Authority since the introduction of the MRP in 2004.

Unsupported borrowing reflected within the debt liability will be subject to MRP under the Asset life method, which will be charged over a period which is reasonably commensurate with the estimated useful life applicable to the nature of expenditure, using the equal annual instalment method. For example, capital expenditure on a new building, or on the refurbishment or enhancement of a building, will be related to the estimated life of that building. Estimated life periods will be determined under delegated powers.

As some types of capital expenditure incurred by the Commissioner are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the

main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

In summary it is proposed that the Commissioner continues to use the Capital Financing Requirement option as applied to all supported borrowing.

The Commissioner currently applies the Asset Life method (Equal Charge approach) to capital expenditure financed by unsupported borrowing and it is proposed that this option also be continued.

The capital programme contains a scheme for the replacement of Blackpool police station which will involve an additional MRP charge to cover the financing of the new asset. This charge will be deferred, using current capital financing regulations, until the asset becomes fully operational, when savings will be realised from the restructure of the existing facilities. Deferring the MRP will only be applied for the construction of new assets.

Prudential Indicators for 2018/19 to 2020/21 in respect of the Police and Crime Commissioner's Treasury Management Activities.

In accordance with its statutory duty and with the requirements of the Prudential Code for Capital Finance and the CIPFA Code for Treasury Management, every local authority produces each year a set of prudential indicators which regulate and control its treasury management activities.

The following table sets out the debt and investment-related indicators which provide the framework for the Commissioner's proposed borrowing and lending activities over the coming three years. These indicators will also be approved by members as part of the Capital Programme approval process along with other capital expenditure-related indicators, but need to be reaffirmed and approved as part of this Treasury Management Strategy.

Treasury Management Prudential Indicators	**2017/18 (Revised) £000**	**2018/19 £000**	**2019/20 £000**	**2020/21 £000**
1. Adoption of the Revised CIPFA Code of Practice on Treasury Management	Adopted for all years			
2. Authorised limit for external debt - A prudent estimate of external debt, which includes sufficient headroom for unusual cash movements.				
Borrowing	43,000	63,000	76,000	75,000
Other long-term liabilities	1,000	1,000	1,000	1,000
TOTAL	44,000	64,000	77,000	76,000
3. Operational boundary for external debt - A prudent estimate of debt, but no provision for unusual cash movements. It represents the estimated maximum external debt arising as a				

consequence of the Commissioner's current plans.				
Borrowing	40,000	45,000	51,000	49,000
Other long-term liabilities	500	500	500	500
TOTAL	40,500	45,500	51,500	49,500

4. Gross Debt / Capital Financing Requirement Indicator

	2017/18 (Rev) £m	2018/19 £m	2019/20 £m	2020/21 £m
Capital Financing Requirement	60.017	65.129	72.254	70.561
Estimated Gross Debt	37.949	43.061	50.186	48.493
Debt to CFR (%)	63.2	66.1	69.5	68.7

This is a measure of prudence.
The fact that gross debt is less than the capital financing requirement is taken as an indicator borrowing has only been made for capital purposes.

5. Upper limit for fixed interest rate exposure				
Upper limit of borrowing at fixed rates	100%	100%	100%	100%
Upper limit of investments at fixed rates	100%	100%	100%	100%
6. Upper limit for variable rate exposure				
Upper limit of borrowing at variable rates	75%	75%	75%	75%
Upper limit of investments at variable rates	100%	100%	100%	100%
7. Upper limit for total principal sums invested for over 364 days (per maturity date as a percentage of total investments.)	50%	50%	50%	50%

8. Maturity structure of Debt	**Upper Limit %**	**Lower Limit %**
Under 12 months	70	-
12 months and within 24 months	60	-
24 months and within 5 years	65	-
5 years and within 10 years	80	-
10 years and above	90	10

2017/18 (Rev)	2018/19	2019/20	2020/21

9. **Ratio of financing costs to revenue stream**	0.94%	1.02%	1.40%	*1.52%*
10. **Estimate of impact of capital investment on council tax**		£31.53	£28.13	£20.01
11. **Estimate of impact of capital investment on council tax NET of revenue contributions to capital**		£0.72	£3.58	£4.62

Decision Required

The Commissioner is asked to approve the treasury management strategy for 2018/19, including

f) Treasury management prudential indicators

g) The borrowing strategy

h) The investment strategy

i) The MRP strategy

j) To formally adopt the updated policy statement at Appendix A

Appendix A

Treasury Management Policy Statement

The Police and Crime Commissioner's financial regulations require him to create and maintain a treasury management policy statement, stating the policies, objectives and approach to risk management of his treasury activities, as a cornerstone for effective treasury management.

Definition
The Police and Crime Commissioner defines his treasury management activities as: the management of the Commissioner's investments and cash flows, his 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.

Risk management
The Commissioner regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of his treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

Value for money
The Commissioner acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. He 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.

Borrowing policy
The Commissioner aims to fund its capital expenditure in a cost effective manner. This will involve using short term and variable rate loans when these are seen as being the most beneficial strategy. However consideration will be given to the long term funding needs and the stability to budgets that fixed interest loans provides. The Commissioner will also constantly evaluate debt restructuring opportunities of the existing portfolio.

The Commissioner will set an affordable borrowing limit each year in compliance with the *Local Government Act 2003*, and will have regard to the *CIPFA Prudential Code for Capital Finance in Local Authorities* when setting that limit. He will also set limits on its exposure to changes in interest rates and limits on the maturity structure of its borrowing in the treasury management strategy report each year.

Investment policy
The Commissioner's primary objectives for the investment of his surplus funds are to protect the principal sums invested from loss, and to ensure adequate liquidity so that funds are available for

expenditure when needed. The generation of investment income to support the provision of services is an important, but secondary, objective.

The Commissioner will have regard to the Communities and Local Government Guidance on Local Government Investments and will approve an investment strategy each year as part of the treasury management strategy. The strategy will set criteria to determine suitable organisations with which cash may be invested, limits on the maximum duration of such investments and limits on the amount of cash that may be invested with any one organisation.