Report to:	**Audit, Best Value and Community Services Scrutiny Committee**
Date:	**24 June 2013**
By:	**Chief Operating Officer**
Title of report:	**Treasury Management – Stewardship Report 2012/13**
Purpose of report:	**To report on the County Council's Treasury Management activities for the year 2012/13.**

RECOMMENDATIONS:
(1) The Committee is recommended to note the treasury management performance in 2012/13; and
(2) That the Committee note the actual treasury and prudential indicators as contained within appendices B and C.

1. Introduction

1.1 The annual stewardship report reviews the Council's treasury management performance and is a requirement of the Council's reporting procedures as required by the Code of Practice for Treasury Management. It covers the treasury management activities and the actual prudential and treasury indicators for 2012/13.

2. Supporting Information

2.1 The County Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance. The County Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector and operates treasury management service in compliance with this Code. These require that the prime objective of the treasury management activity is the effective management of risk, and that its borrowing activities are undertaken in a prudent, affordable and sustainable basis and treasury management practices demonstrate a low risk approach. The Code requires the regular reporting of treasury management activities to:

- Forecast the likely activity for the forthcoming year (in the Annual Treasury Strategy Report); and
- Review actual activity for the preceding year (this Stewardship report).
- A mid year review.

2.2 This report sets out:

- A summary of the original strategy agreed for 2012/13 and the economic factors affecting this strategy (Appendix A).
- The treasury management activity during the year (Appendix B);
- The Prudential Indicators, which relate to the Treasury function and compliance with limits (Appendix C).

3. The economic conditions compared to our original Strategy for 2012/13

3.1 The original Strategy and the economic conditions prevailing in 2012/13 are set out in Appendix A which is attached to this report. 2012/13 continued the challenging environment of the previous years, with concerns over the economies of European countries and their impact on the UK economy. The main implications have been continuing counterparty risk and low investment returns.

4. The Treasury activity during the year on short term investments and borrowing

The Treasury Management Strategy

4.1 The strategy for 2012/13, agreed in January 2012, continued the prudent approach

and ensured that all investments were only to the highest quality rated banks and only up to a period of one year. A more prudent approach was adopted throughout 2012/13 because of the uncertainties in the market and all investments were able to be called without notice. The emphasis was to be able to react quickly if market conditions worsen.

Short term lending

4.2 The total amount received in short term interest for 2012/13 was £1.9m at an average rate of 0.62%. This was above the average of base rates in the same period (0.5%) but fell short of the aim to secure investment income of at least base rate plus 0.4% on the Council's general cash balances. This was against a backdrop of ensuring, so far as possible in the current financial climate, the security of principal and the minimisation of risk. This Council has continued to follow an extremely prudent approach with security and liquidity as the main criteria before yield.

Short term borrowing

4.3 No borrowing was undertaken on a short-term basis during 2012/13 to cover temporary overdraft situations.

Long term borrowing

4.4 Details of our long term borrowing are included in Appendix B of the report. The important points are:

- No new borrowing was undertaking during 2012/13. It was agreed to use "internal borrowing" to finance new capital investment
- The average interest rate of all debt at 31 March 2013 (£264.2m) was 5.20%.
- Although a proactive approach has been taken to repayment and restructuring of debt, no cost effective opportunities arose during the year.

5. Prudential Indicators and compliance with limits

5.1 The County Council is required by the CIPFA Prudential Code to report the actual prudential indicators after the end of each year. There are eight indicators which relate to treasury management and they are set out in Appendix C.

6. Conclusion

6.1 This report updates the Cabinet and fulfils the requirement to submit a stewardship report in the form prescribed in the Treasury Management Code of Practice. Short term lending has achieved returns better than base rate. However, the rate is below the aim to secure investment income of at least base rate plus 0.4% on the Council's general cash balances. This reflects the target which is to ensure so far as possible in the financial climate, the security of principal and the minimisation of risk.

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BACKGROUND DOCUMENTS

Cabinet- 26 January 2012 Treasury Management Strategy for 2012/13
13 November 2012 Treasury Management Half Year report 2012/13
29 January 2013 Treasury Management Strategy for 2013/14

Audit, Best Value and Community Services Scrutiny-
6 November 2012 Update on Treasury Management

CIPFA Prudential Code and Treasury Management in the Public Services- Code of practice
Local Government Act 2003 Local Government Investments guidance

Appendix A

A summary of the strategy agreed for 2012/13 and the economic factors affecting this strategy and amendments to this strategy in the year

1. Background information

1.1 Cabinet receive an annual Treasury Management Strategy report, normally in January or February, which sets out the proposed strategy for the year ahead. This strategy includes the limits and criteria for organisations to be used for the investment of cash surpluses and has to be approved by the County Council.

1.2 This Council has always adopted a prudent approach to its investment strategy and in the last few years, there have been regular changes to the list of the approved organisations used for investment of short term surpluses. This list is regularly reviewed to ensure that the Council is able to invest in the best available rates consistent with low risk; the organisations are regularly monitored to ensure that their financial strength and low risk has been maintained.

1.3 When the original strategy for 2012/13 was drawn up in January 2012, the money markets were still volatile with Banks reluctant to lend to each other. In this climate ensuring the security of investments continues to be difficult and extreme caution has to be taken on where surplus funds can be invested.

1.4 At the same time, the Treasury Management Policy Statement was agreed as unchanged for 2012/13.

East Sussex County Council defined its treasury management activities as:

"The management of the organisation's cash flows, its banking, money market and capital market transactions (other than those of the Pension Fund) the effective management of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

The County Council regards the successful identification, monitoring and management 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.

This authority 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 best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

2. Long term borrowing approach

2.1 County Council's past strategy was to borrow to support the Capital Programme and lend out other cash (rather than using internal borrowing). Historically this meant that the interest rate earned on cash balances was higher than the interest rate paid on loans from the Public Works Loans Board (PWLB). In the current financial climate, this interest rate differential has been removed. No new PWLB borrowing has taken place since January 2008 and is unlikely in the current climate unless long term PWLB rates reach a very low level (where the long term benefit would exceed the short term costs). The average rate of all debt at 31 March 2013 of £264.2m is 5.20% and has remained at the same level in 2012/13 as no new loans have been taken and no beneficial rescheduling of debt has been available

2.2 Our opportunity to restructure our debt has been significantly reduced since October 2010 as a result of the PWLB increasing all of its lending rates by 1% as part of the Government's Comprehensive Spending Review. However, it did not increase the rate of interest used for repaying debt so that not only the cost of our future borrowing has increased

but our opportunity to restructure our debt when market conditions allow has been significantly reduced.

3. Investment outlook

3.1 When the strategy was agreed in January of 2012, the advice given to us by our advisors, Sector, was that short term rates were expected to remain on hold for a considerable time. Economic forecasting remained troublesome with so many extermal influences weighing on the UK. There was consensus among analysts that the economy would remain weak and whilst there was still a broad range of views as to potential performance, they have all been downgraded throughout 2011. Key areas of uncertainty included:

- a worsening of the Eurozone debt crisis and heightened risk of the breakdown of the bloc or even of the currency itself;
- the impact of the Eurozone crisis on financial markets and the banking sector;
- the impact of the Government's austerity plan on confidence and growth and the need to rebalance the economy from services to exporting manufactured goods;
- the under-performance of the UK economy which could undermine the Government's policies that have been based upon levels of growth that inceasingly seem likely to be undershot;
- a continuation of high levels of inflation ;
- the economic performance of the UK's trading partners, in particular the EU and US, with some analysts suggesting that recession could return to both;
- stimulus packages failing to stimulate growth;
- elections due in the US, Germany and France in 2012 or 2013;
- potential for protectionism i.e. an escalation of the currency war / trade dispute between the US and China.

The overall balance of risks remained weighted to the downside. Lack of economic growth, both domestically and overseas, would impact on confidence putting upward pressure on unemployment. It would also further knock levels of demand which would bring the threat of recession back into focus.

3.2 Sector believed that the longer run trend is for gilt yields and PWLB rates to rise due to the high volume of gilt issuance in the UK, and the high volume of debt issuance in other major western countries.

3.3 Given the weak outlook for economic growth, Sector saw the prospects for any interest rate changes before mid-2013 as very limited. There was potential for the start of Bank Rate increases to be even further delayed if growth disappointed.

4. Strategy agreed for 2012/13

4.1 The strategy ensured that in the current economic climate a prudent approach was maintained. This would be achieved through investing with selected banks and funds which meet the Council's rating criteria. The emphasis would continue on security (protection of the capital sum invested) and liquidity (keeping money readily available for expenditure when needed) rather than yield. The strategy continued with this prudent approach and no change was proposed to change the revised strategy for 2011/12.

4.2 It was recognised that movements within the money markets can happen with no notice and the Director of Corporate Resources would have to amend this strategy in order to safeguard Council funds. As in the past any such actions would be reported to the next Cabinet meeting.

4.3 It was not expected that any new external borrowing would be undertaken in 2012/13 however the limits set out in the Authorised Limit for Borrowing would allow such borrowing. External borrowing would only take place if the rates available were so low that the long term benefits would significantly exceed the short term cost.

4.4 Opportunities for cost effective repayment of existing debt and restructuring opportunities were to be constantly monitored and would be taken if and when they emerge.

4.5 Our policy gave some flexibility to borrow up to £16m in advance of future need. However, given the current interest climate, no external borrowing and certainly none in advance, was planned.

4.6 The County Council funds would be invested as follows:-

(A) UK Investment Without Government Equity Holding

Up to a maximum of £60m deposited up to a period of up to one year with any of the following: -

The current policy stance was overnight but the policy allowed changes to reflect market conditions if and when they improved.

Bank / Fund / Local Authority
Barclays Santander UK HSBC Nationwide Individual Treasury Type Money Market Funds (AAA rated) which invest in Government Securities only Individual Cash Type Money Market Funds (AAA rated) Another Local Authority (Equivalent to the low risk of investing with the Government but not formally rated)

Only banks which met the following minimum rating criteria for at least two of the designated agencies to be used.

Ratings Agency	Long Term	Short Term
Fitch	AA-	F1+
Moody	AA3	P-1
Standards and Poors	AA-	A-1+

(B) UK Investment With Government Equity Holding of minimum of 30%

30% was agreed as a minimum level of significant associated company influence. In practice it serves as a trigger to formally review our position.

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Up to a maximum of £60m deposited up to a period of up to three months with the following: -

The policy stance was overnight but the policy allowed changes to reflect market conditions if and when they improved.

Bank
Lloyds/HBOS Nat West/RBS

Only banks which met the following minimum rating criteria for at least two of the designated agencies were to be used. The banks would not be used if the UK Sovereign rating falls below AAA.

Ratings Agency	Long Term	Short Term
Fitch	A	F1
Moody	A2	P-1
Standards and Poors	A	A-1

The policy retained the ability to revert to some, or even extensive use of the Government's Debt *Management* Account Deposit Facility (DMADF) if market risk conditions tightened. Other very safe alternative investments would be explored if they become available.

It was continued to be recognised that movements within the money markets can happen with no notice and the Director of Corporate Resources would have to amend this strategy in order to safeguard Council funds. As in the past any such actions would be reported to the next Cabinet meeting.

4.7 The strategy going forward continued with the policy of ensuring minimum risk but will also need to deliver secure investment income of at least bank rate on the Council's cash balances. (The actual target is bank rate plus 0.4%). The reduction from bank rate plus 0.5% for 2011/12 reflected the lower rates available in the market on the change to more prudent investments.

4.8 Additional requirements under the Code of Practice require the Council to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information has been and will continue to be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Sovereign ratings, Credit Default Swaps, equity prices, the Sector security and liquidity model and the CIPFA National treasury risk model as well as media updates etc.) would be assessed when comparing the relative security of differing investment counterparties.

4.9 All Money Market Funds used would be monitored and chosen by the size of fund, rating agency recommendation, exposure to other Countries (Sovereign debt), weighted average maturity and weighted average life of fund investment and counterparty quality.

4.10 All of the investments were classified as Specified Investments. These investments were sterling investments of not more than one-year maturity with institutions deemed to be high credit quality or with the UK Government (Debt Management Account Deposit Facility). These were considered low risk assets where the possibility of loss of principal or investment income was small. The County Council does not have any Non Specified Investments which are more than one-year maturity or with institutions which have a lesser credit quality.

5. The economy in 2012/13 – Commentary from Sector (Treasury Management Advisors) in May 2013.

5.1 The financial year 2012/13 continued the challenging investment environment of previous years, namely low investment returns and continuing heightened levels of counterparty risk. The original expectation for 2012/13 was that Bank Rate would start gently rising from quarter 4 2014. However, economic growth in the UK was disappointing during the year due to the austerity programme, weak consumer confidence and spending, a lack of rebalancing of the economy to exporting and weak growth in our biggest export market - the European Union (EU). The coalition Government maintained its tight fiscal policy stance against a background of warnings from two credit rating agencies that the UK could lose its AAA credit rating. The key to retaining this rating will be a return to strong economic growth in order to reduce the national debt burden to a sustainable level, within the austerity plan

timeframe. Weak UK growth resulted in the Monetary Policy Committee increasing quantitative easing (QE) by £50bn in July to a total of £375bn. Bank Rate therefore ended the year unchanged at 0.5% while CPI inflation fell from 3% at the start of the year to end at 2.8% in March, with a fall back to below 2% pushed back to quarter 1 2016.

5.2 The EU sovereign debt crisis was an ongoing saga during the year with first Greece and then Cyprus experiencing crises which were met with bailouts after difficult and fraught negotiations.

5.3 Gilt yields oscillated during the year as events in the ongoing Eurozone debt crisis ebbed and flowed, causing corresponding fluctuations in safe haven flows into / out of UK gilts. This, together with a further £50bn of QE in July and widely expected further QE still to come, combined to keep PWLB rates depressed for much of the year at historically very low levels.

5.4 The Funding for Lending Scheme, announced in July, resulted in a flood of cheap credit being made available to banks and this has resulted in money market investment rates falling sharply in the second half of the year. However, perceptions of counterparty risk have improved after the ECB statement in July that it would do “whatever it takes” to support struggling Eurozone countries. This has resulted in some return of confidence to move away from only very short term investing.

The treasury management activity during the year

1. Short term lending interest rates

1.1 Base interest rate remained at 0.5% throughout 2012/13. The rate is the lowest ever rate and the rate has remained unchanged for the longest period on record. The last change was over four years ago in March 2009.

1.2 There have been continued uncertainties in the markets during the year to date as set out in Section 5 of Appendix A.

1.3 Additional market information including Sovereign ratings, Credit Default Swaps, equity prices, the Sector security and liquidity model and the CIPFA National treasury risk model as well as media updates etc have been used to assess the relative security of differing investment counterparties.

1.4 The strategy for 2012/13, agreed in January 2012, continued the prudent approach and ensured that all investments were only to the highest quality rated banks and only up to a period of one year. No changes to this Strategy have been required but a more prudent approach has been adopted because of the uncertainties in the market. Investments in all banks continued to be on call (overnight only).

1.5 The total amount received in short term interest for 2012/13 was £1.9m at an average rate of 0.62%. This was above the average of base rates in the same period (0.5%) but fell short of the aim to secure investment income of at least base rate plus 0.4% on the Council's general cash balances. This is against a backdrop ensuring, so far as possible in the financial climate, the security of principal and the minimisation of risk.

1.6 The reason for the reduction in return from June was because of the transfer of our investment in Money Market Funds (MMFs) from "Cash Type" to "Treasury Type" which has funds in Government Securities only and into the safe haven of the Government's Debt Management Account Deposit Facility (DMADF). The interest rate received on all MMFs has reduced during the year and the "Treasury Type" MMFs and the DMADF rates received are less than received on "Cash Type" MMFs. The reason for these changes was the continued major concerns in the market due to the problems with European countries and the Euro and these have been set out in Paragraphs 5.1 to 5.4 of Appendix A. The changes to the investments held comply with our Treasury Management Strategy and this Council has continued to follow an extremely prudent approach with security and liquidity as the main criteria before yield.

1.7 Although Santander UK and Barclays are listed as Banks which could be used for investments, their ratings fell for two out of the three Credit Rating Agencies below the criteria set in the last two months of 2011 and now do not meet the criteria set for any of the three Rating Agencies. Nationwide is also listed but their ratings also do not meet the requirements of our Strategy for any of the three Rating Agencies. HSBC does meet our criteria but show little interest in the short term market. All of these Banks were not used for investment in 2012/13.

2. Long term borrowing

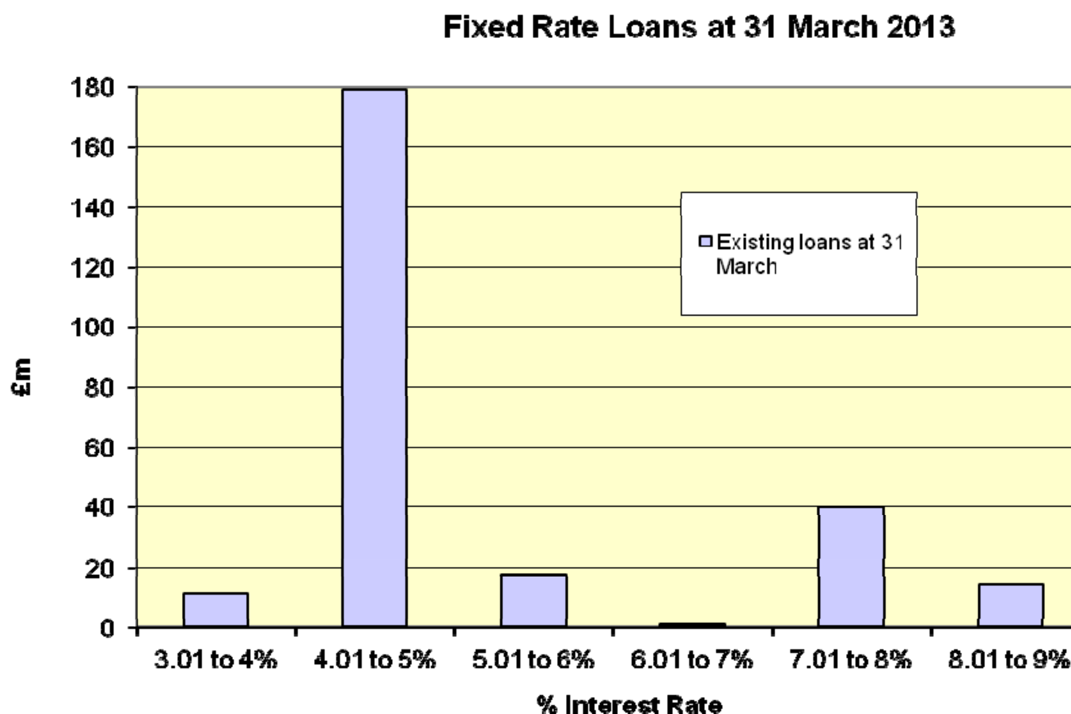
2.1 The County Council has had a strategy to borrow to support the Capital Programme and lend out other cash (rather than using internal borrowing). Historically this meant that the interest rate earned on cash balances was higher than the interest rate paid on loans from the Public Works Loans Board (PWLB). In the current financial climate, this interest rate differential has been removed. The cost of new borrowing is now well in excess of the rate achievable on our investments. No new PWLB borrowing has taken place since January 2008 and is unlikely in the current climate unless long term PWLB rates reach a very low level (where the long term benefit would exceed the short term costs).

2.2 The average interest rate of all debt at 31 March 2013 of £264.2m was 5.20% and was unchanged from the previous year.

2.3 Opportunities for cost effective repayment of existing debt and restructuring opportunities were constantly monitored but none emerged in the first six months of the year.

2.4 In the autumn of last year, the Department of Communities and Local Government asked local authorities to make a return to enable them to benefit from a small reduction in all of the PWLB rates for new loans. The PWLB "certainty rate" as it has been named reduced PWLB borrowing rates by 0.20% for most local authorities from November 2012. A return was submitted to keep our options open but despite this reduction, East Sussex did not borrow as the long term benefit did not exceed the short term costs.

The range of interest rates payable in all of the loans is illustrated in the graph below:



3. Short term borrowing

3.1 No borrowing was undertaken on a short-term basis during 2012/13 to date to cover temporary overdraft situations.

4 Treasury Management Advisers

4.1 The Strategy for 2012/13 explained that the County Council uses Sector as its treasury management consultant on a range of services which include:

- Technical support on treasury matters, capital finance issues and advice on reporting;
- Economic and interest rate analysis;
- Debt services which includes advice on the timing of borrowing;
- Debt rescheduling advice surrounding the existing portfolio;
- Generic investment advice on interest rates, timing and investment instruments;
- Credit ratings from the three main credit rating agencies and other market information;
- Assistance with training on treasury matters

Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remained with the Council. This service remains subject to regular review.

4.2 Sector is the largest provider of Treasury Management advice services to local authorities in the UK and they claim to be the market leading treasury management service provider to their clients. The advice has been and will continue to be monitored regularly to ensure a continued excellent advisory service.

Prudential Indicators which relate to the Treasury function and compliance with limits

1.1 The County Council is required by the Prudential Code to report the actual prudential indicators after the end of each year. There are eight indicators which relate to treasury management and they are set on an annual basis and monitored, they comprise:-:

- Operational and authorised borrowing limits which includes short term borrowing (paragraph 1.2 below)
- Interest rate exposure (paragraph 1.3 below)
- Interest rate on long term borrowing (paragraph 1.4 below)
- Maturity structure of debt (paragraph 1.5 below)
- Maturity structure of investments (paragraph 1.6 below)
- Compliance with the Treasury Management Code of Practice (paragraph 1.7 below)
- Interest on investments (paragraph 1.8 below)
- Capital Financing Requirement and Minimum Revenue Provision (paragraph 1.9 below)

1.2 **Operational and authorised borrowing limits.**

The tables below sets out the estimate and projected capital financing requirement and long-term borrowing in 2012/13

	CAPITAL FINANCING REQUIREMENT	**2012/13**	**2012/13**	**2012/13**
		Estimate **£m**	**Revised Estimate** **£m**	**Estimated Actual** **£m**
	Capital financing requirement at 1 April 2012	352	391	391
ADD	Financing of new assets	19	21	-
LESS	Provision for repayments of debt	-13	-16	-16
		-------	-------	-------
	Capital financing requirement at 31 March 2013	**358**	**396**	**378**
ADD	Net borrowing for next year	16	19	
		-------	-------	
	Operational boundary	**374**	**415**	
ADD	Short term borrowing	20	20	Nil
		-------	-------	
	Authorised limit	**394**	**435**	

	ACTUAL BORROWING	**2012/13**
		Actual **£m**
	Long term borrowing at 1 April 2012	264.2
	No new borrowing in 2012/13	
	Long term borrowing at 31 March 2013	**264.2**

The Capital Financing Requirement includes PFI Schemes and Finance Leases.

The revision of the Authorised Limit for 2012/13 from £394m to £435m reflected the move to International Financial Reporting Standards (IFRS) and previously agreed Private Finance Initiative (PFI) contracts and some leases (being reclassified as finance leases instead of operating leases) coming onto the County Council Balance Sheets as long term liabilities.

This new accounting treatment impacted on the Authorised Limit, which was approved by Cabinet on 26 January 2012.

The Operational boundary for borrowing was based on the same estimates as the authorised limit. It reflected directly the authorised borrowing limit estimate without the additional amount for short term borrowing included to allow, for example, for unusual cash movements. The Operational boundary represents a key management tool for in year monitoring and long term borrowing control.

The Authorised limit was consistent with the County Council's current commitments, existing plans and the proposals for capital expenditure and financing, and with its approved treasury management policy statement and practices. It was based on the estimate of most likely, prudent but not worst case scenario, with in addition sufficient headroom (short term borrowing) over and above this to allow for day to day operational management, for example unusual cash movements or late receipt of income. Risk analysis and risk management strategies were taken into account as were plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes.

The Authorised limit is the "Affordable Borrowing Limit" required by S3 of the Local Government Act 2003 and must not be breached. The Long Term borrowing at 31st March 2013 of £264m is under the Operational boundary and Authorised limit set for 2012/13. The Operational boundary and Authorised limit have not been exceeded during the year.

1.3 **Interest rate exposure**

The County Council continued the practice of seeking to secure competitive fixed interest rate exposure for 2012/13. To provide flexibility however it set limits on our variable rate exposure in case that became a more effective approach. There are figures for both borrowing and lending and a combined borrowing and lending table.

Borrowing	2012/13 Estimate	2012/13 Actual
Fixed Rate Exposure		
Upper Limit	100%	100%
Lower Limit *	54%	
Variable Rate Exposure		
Upper Limit	46%	0%
Lower Limit *	0%	

(* assumes all new borrowing is variable)

Lending		
Fixed Rate Exposure		
Upper Limit	100%	70%
Lower Limit	0%	
Variable Rate Exposure		
Upper Limit	100%	30%
Lower Limit	0%	

Borrowing and Lending combined		
Fixed Rate Exposure		
Upper Limit	100%	84%
Lower Limit	28%	
Variable Rate Exposure		
Upper Limit	100%	16%
Lower Limit	0%	

In 2012/13, borrowing has continued to be at a fixed rate. The County Council has no variable rate loans. Our lending has been both at fixed rates (to Banks and the Debt Management Office (DMO)) and variable rates (to Money Market Funds).

1.4 **Interest rate on long term borrowing**

The rate of interest taken on new long term borrowing will be monitored as the following targets have been set.

- Rate taken on borrowing is within 0.25% of lowest point for set loan period (i.e. 45-50 years) during the year

- Rate taken is within lowest eighth of rates available for set loan period (i.e. 45-50 years) during the year

No new borrowing has been taken in 2012/13.

1.5 **Maturity structure of debt**

The Council has set upper and lower limits for the maturity structure of its borrowings as follows.

	Lower limit	Upper limit	Actual at 31.3.2013
Under 12 months	0%	25%	5%
12 months and within 24 months	0%	40%	2%
24 months and within 5 years	0%	60%	13%
5 years and within 10 years	0%	80%	8%
10 years and within 20 years	0%	80%	14%
20 years and within 30 years	0%	80%	18%
30 years and within 40 years	0%	80%	25%
40 years and above	0%	80%	15%

The County Council has not exceeded the limits set in 2012/13.

In addition, two targets have monitored the maturity structure of our debt. Not more than £20m of debt should mature in any financial year and not more than 15% to mature in any two consecutive financial years. New borrowing has been undertaken giving due consideration to the debt maturity profile, ensuring that an acceptable amount of debt is due to mature in any one financial year. This helps to minimise the authority's exposure to the risk of having to replace a large amount of debt in any one year or period when interest rates may be unfavourable. The bar chart in the attached Annex shows the maturity profile.

There has been a change to the reporting arrangements under the Treasury Management Code of Practice regarding the maturity structure of debt. The next possible call date has replaced the final maturity date to report when the debt expires on our market loans. This has increased the amount in certain earlier years and reduced the amount in later years in our comparisons and in one year (2016/17) has exceeded the maximum of £20m of debt in any one year. It does not exceed the other limit of not more than 15% to mature in any two consecutive financial years. In practice, based on previous experience of market loans both for East Sussex and with other local authorities the loan is unlikely to be called.

1.6 **Maturity structure of investments**

From 1 April 2004, the Investment Guidance issued by the Officer of Deputy Prime Minister, allowed local authorities the freedom to invest for more than for one year. All investments over one year were to be classified as Non-Specified Investments. The County Council had taken advantage of this freedom in previous years. No Non-Specified Investments are held

within our overall portfolio of investments and in line with our prudent approach in our strategy, no new long term investments (over 364 days) have been taken in 2012/13.

1.7 Compliance with the Treasury Management Code of Practice

East Sussex County Council has adopted the CIPFA *Code of Practice for Treasury Management in the Public Services.*

1.8 Interest on investments

1.8.1. The table below sets out the average monthly rate received on our investments and compares it to the Bank of England Base rate to reflect both the interest rates available in the market and limitation in the use of counterparties.

Month	Amount £000	Monthly rate	Margin over Base rate	Margin against Base plus 0.4%
April	213.7	0.83%	0.33%	-0.07%
May	215.5	0.81%	0.31%	-0.09%
June	177.6	0.67%	0.17%	-0.23%
July	159.8	0.57%	0.07%	-0.33%
August	156.5	0.57%	0.07%	-0.33%
September	151.1	0.58%	0.08%	-0.32%
October	153.1	0.57%	0.07%	-0.33%
November	148.4	0.57%	0.07%	-0.33%
December	154.6	0.59%	0.09%	-0.31%
January	153.8	0.59%	0.09%	-0.31%
February	120.5	0.52%	0.02%	-0.38%
March	133.5	0.53%	0.03%	-0.37%
Total for 2012/13	**1.938.1**	**0.62%**	**0.12%**	**-0.28%**

1.8.2. The total amount received in short term interest for the year was £1.9m at an average rate of 0.62%. This was above the average of base rates in the same period (0.5%) but below the aim to secure investment income of at least base rate plus 0.4% on the Council's general cash balances whilst ensuring, so far as possible in the financial climate, the security of principal and the minimisation of risk. This Council has continued to follow an extremely prudent approach with security and liquidity as the main criteria before yield.

1.8.3. The reason for the reduction in return from June was because of the transfer of our investment in Money Market Funds (MMFs) from "Cash Type" to "Treasury Type" which has funds in Government Securities only and into the safe haven of the Government's Debt Management Account Deposit Facility (DMADF). The interest rate received on all MMFs have reduced during the year and the "Treasury Type" MMFs and the DMADF rates received are less than received on "Cash Type" MMFs. The reason for the changes was the continued major concerns in the market due to the problems with European countries and the Euro and these have been set out in Paragraphs 5.1 to 5.4 of Appendix A. The changes to the investments held comply with our Treasury Management Strategy and this Council has continued to follow an extremely prudent approach with security and liquidity as the main criteria before yield.

1.9 Capital Financing Requirement and Minimum Revenue Provision (MRP)

The Council's Borrowing Need (the Capital Financing Requirement)

The prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of Council's underlying borrowing need.

The Council was asked to approve the CFR projection below:

CFR including appropriate balances and MRP charges for PFI Schemes and Finance Leases.

	2012/13 Likely Actual	**2013/14 Estimate**	**2014/15 Estimate**
	£m	**£m**	**£m**
Total CFR	**394**	**397**	**401**
Movement in CFR	3	3	4

Movement in CFR represented by			
Net financing need for the year (above)	19	19	19
MRP/VRP and other financing movements	-16	-16	-15
Movement in CFR	**3**	**3**	**4**

The Council is required to pay off an element of the accumulated General Fund capital spend each year through a revenue charge (the Minimum Revenue Provision – MRP). The Capital Financing Requirement and Minimum Revenue Provision will not be exceeded in 2012/13.

Minimum Revenue Provision (MRP) Statement

1.10 The statutory requirement for local authorities to charge the Revenue Account each year with a specific sum for debt repayment has been replaced with a more flexible statutory guidance and a variety of options is provided to councils to replace the existing Regulations, so long as there is a prudent provision.

1.11 The statutory duty is that a local authority shall determine for the financial year an amount of minimum revenue provision (MRP) that it considers to be prudent. This replaces the previous prescriptive requirement that the minimum sum should be 4% of the Council's Capital Financing Requirement (CFR).

1.12 To support the statutory duty the Government also issued a guidance, which required that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start the financial year to which the provision will relate. The Council are therefore legally obliged to have regard to this MRP guidance in the same way as applies to other statutory guidance such as the CIPFA Prudential Code, the CIPFA Treasury Management Code and the CLG guidance on Investments.

1.13 The MRP guidance offered four options under which MRP might be made, with an overriding recommendation that the County Council should make prudent provision to redeem its debt liability over a period which is commensurate with that over which the capital expenditure is estimated to provide benefits (i.e. estimated useful life of the asset being financed).

1.14 The move to International Financial Reporting Standards (IFRS) involved Private Finance Initiative (PFI) contracts, aftercare/restoration of closed landfill sites, and some leases (being reclassified as finance leases instead of operating leases) coming onto the County Council Balance Sheets as long term liabilities. This new accounting treatment impacted on the Capital Financing Requirement with the result that an annual MRP provision will be required.

1.15 The policy recommended for adoption from 1 April 2012 retained the key elements of the policy previously approved but now incorporates the IFRS changes (re PFI and finance leases) and the consequential updated Government Guidance. The policy adopted for 2012/13 is therefore as follows:-

1.16 For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy has been:

- Based on based on the non-housing CFR, i.e., The Council currently set aside a Minimum Repayment Provision based on basic MRP of 4% each year to pay for past capital expenditure and to reduce its CFR.

1.17 From 1 April 2008 for all unsupported borrowing the MRP policy has been:

- Asset Life Method – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option will be applied for any expenditure capitalised under a Capitalisation Direction).

- Asset Life Method (annuity method) The Council will also be adopting the annuity method, - MRP calculated according to the flow of benefits from the asset, and where the principal repayments increase over the life of the asset. The policy is being adopted as a result of any PFI's assets coming on the balance sheet and any related MRP will be equivalent to the "capital repayment element" of the annual service charge payable to the PFI Operator and for finance leases, MRP will also be equivalent to the "capital repayment (principal) element" of the annual rental payable under the lease agreement.

Under both methods, the Council has the option to charge more than the statutory MRP each year through a Voluntary Revenue Provision (VRP).

Annex