Police and Crime Commissioner for Surrey – Decision Making Record

Report Title:	**Prudential Indicators and Annual Minimum Revenue Provision Statement 2021/22**
Decision number:	**2022/003**
Author and Job Role:	**Kelvin Menon – Treasurer**
Protective Marking:	**OFFICIAL**

Summary

Under the CIPFA Prudential Code for Capital Finance the Prudential Indicators the Prudential Indicators should be reported on and reviewed at the mid-year point. This report seeks to satisfy that requirement.

Paragraph 4.7 in the accompanying report indicates that the indicators as set for 2021/22 are being complied with

Recommendation:

It is RECOMMENDED that the Police and Crime Commissioner notes the report and compliance with the Prudential Indicators for 2021/22

Signature:

Lisa Townsend

Date: 27th January 2022

All decisions must be added to the decision register.

Areas of consideration

Consultation

None

Financial implications

These are set out in the paper

Legal

None

Risks

Changes to capital program could impact the Prudential Indicators and so they will continue to be reviewed on a regular basis

Equality and diversity

.
None

Risks to human rights

None

2021/22 Mid-Year Treasury Management report to JAC

Required for:	*Joint Audit Committee Meeting January 2022*
Security Classification:	**Official**
Handling information if required:	N/A
Suitable for publication:	*Yes*
Title:	2021/22 Mid-Year Treasury Management report
Version:	N/A
Purpose:	To review the annual activity and performance of the treasury management function.
ACPO / Strategic Lead:	PCC CFO
National Decision Model compliance:	*Yes*
Date created:	6 January 2022
Date to be reviewed:	

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1. Introduction

Purpose of the Report:

1.1. The purpose of this report is to summarise the Treasury Management performance for the nine months to 31 December 2021.

1.2. The mid-year performance of the Treasury Management Service during 2021/22 is reported in line with CIPFA's Code of Practice on Treasury Management and the PCC's 202/21 Treasury Management Strategy Statement (TMSS).

1.3. The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that those charged with governance and scrutiny receive regular updates on treasury management activity.

1.4. The Police and Crime Commissioner for Surrey - 2021/22 Treasury Management Strategy Statement can be found on the Police and Crime Commissioner's website as follows; https://surrey-pcc.gov.uk/wp-content/uploads/2020/07/12.pdf

Terms of Reference:

1.5. As set out in the Joint Audit Committee's terms of reference, the JAC will provide advice and recommendations to the PCC in relation to the following area of Financial Reporting;

13. Ensure that an effective system of scrutiny is in place in respect of Treasury Management, strategy, policies and practices.

2. Treasury Management – Statutory Requirements

2.1. The legal status of the Treasury Management Code in England and Wales is derived from regulations issued under the Local Government Act 2003. The Capital Finance and Accounting Regulations 2003 explicitly require English authorities (now including policing bodies) to "have regard" to the Treasury Management Code.

2.2. The Treasury Management Code and the Prudential Code are closely linked and regard to the Prudential Code is required when setting limits to the level of affordable borrowing under section 3(5) of the 2003 Act.

2.3. Treasury Management is defined in the Prudential Code 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."*

2.4. The Local Government Finance Act 1992 sets a 'balanced budget requirement' whereby the budget for the financial year is calculated and council tax charges are set to meet the expenditure after taking into account other sources of income.

2.5. The Local Government Act 2003 requires local authorities (including policing bodies) to create and keep under review the limits of how much money they can afford to borrow. The processes that must be followed in setting these limits are described in the Prudential Code.

2.6. The 2003 England and wales Regulations place a duty to charge a 'minimum revenue provision' (MRP) to the revenue account, which is deemed to be prudent.

2.7. The Statutory Guidance on Local Authority Investments in England (MHCLG 2018) makes it clear that borrowing should never be done for the explicit purpose of making an investment return and that borrowing in advance of need purely in order to profit from the investment of the extra sums borrowed is against the principles of the statutory framework and the Prudential Code.

2.8. The MHCLG Statutory Guidance on Local Government Investments (MHCLG, 2018) stresses the prudent investment strategy order of security, liquidity and yield.

- First and foremost, ensure the security of principal sums invested, i.e. ensure we get back the full investment.
- Then ensure the liquidity needed i.e. funds are available when needed by considering the length of an investment.
- Only when the above two conditions are satisfied should the yield or return on investment be considered.

2.9. The Treasury Management Code recommends that the PCC should, as a minimum, report:

- An annual **Treasury Management Strategy Statement** (TMSS) before the start of the year
- An annual **Capital Strategy**
- An **Annual Report** on Treasury Management Activities, Performance and Non-Compliance
- A **Mid-Year Report** on Treasury Management Activities, Performance and Non-Compliance
- Treasury Management **Prudential Indicators** including borrowing limits

2.10. Adherence to the above legislation aims to ensure the PCC for Surrey have comprehensive policies and practices in place for the effective management and control of their treasury management activities, including the effective management and control of risk.

3. Treasury Management Mid-Year Report to 31 December 2021

3.1. The treasury management function is carried out by Surrey County Council (SCC) under a service level agreement. Under this agreement the following treasury management transactions were undertaken in 2021/22 and hence includes up to 31 December 2021.

3.2. The Council account for the Surrey Police and Crime Commissioner's cash balances they manage as short-term borrowing, the balance of which was £18.5m as at 31 December 2021.

3.3. There was no significant change in the Capital Financing Requirement which was within approved limits along with other Prudential Indicators.

Short Term Lending

3.4. In accordance with agreed policy, surplus cash was lent on a daily basis to SCC. The following loans were made during the period to 31 December 2021.

2020-2021 Full year		2021-2022 Quarters 1-3
£27.401m	Average Investment	£32.339m
253	Number of Loans	190
£47K	Total Interest Received	£26k
0.31%	Average Interest Earned Q1	0.10%
0.14%	Average Interest Earned Q2	0.10%
0.13%	Average Interest Earned Q3	0.13%
0.10%	Average Interest Earned Q4	
0.16%	Total Average Interest Earned	0.11%

The average rate of return for the year 2020-21 was 0.17% and the average rate of return for the first three quarters of the year 2021-22 was 0.11% based upon an average investment of £32.3m and is above the average London Inter-Bank BID rate (formerly Local Authority 7 day rate) for the same period of -0.07%. Appendix 1 shows the interest rate received with appendix 2 showing the actual interest received.

Appendix 3 shows that investment balances started to fall from 2016/17 due to the use of reserves to fund the budget and the reduction in capital receipts received. Interest income received also falls in 2016/17 but fluctuates due to an increase in interest rates for 2018/19 and then a sharp decrease in 2020/21 due to Covid.

3.5. The primary consideration governing the Surrey County Council's Strategy is to invest its funds prudently and to have regard to the security and liquidity of its investments before seeking optimal rate of return or yield and to strike a balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the aim is to achieve a total return that is equal or higher than the prevailing rate of inflation in order to maintain the spending power of the sum invested. No sums were invested for more than one year during 2021-22 up to 31 December 2021.

3.6. The weighted average return on all investments the council received in the quarter to 30 September 2021 was 0.02%. This compared to the average Bank of England (BoE) base rate of 0.10% for the same period. SCC currently pay with higher of; the London Inter-Bank BID rate, the Bank of England Rate or the SCC rate.

3.7. Ultra-low short-dated cash rates (which have been a feature since March 2020 when Bank Rate was cut to 0.1%) have resulted in the return on sterling low volatility net asset value money market funds (LVNAV MMFs) being close to zero even after some managers have temporarily waived or lowered their fees. At this stage net negative returns are not the central case of most MMF managers over the short-term, and fee cuts or waivers should result in MMF net yields having a floor of zero, but the possibility cannot be ruled out.

3.8. The Bank of England increased the Base Rate from 0.10% to 0.25% on 16 December 2021.

3.9. Interest rates on many investments are now so low that there is a risk going forward that for some short-term deposits could exceed the interest that could be earned.

3.10. The cost to the PCC for the services of Surrey County Council for 2020/21 was £20,746 and is expected to remain at a similar level for 2021/22.

Other Investment Activity

3.11. The definition of investments in the CIPFA's revised Treasury Management Code now covers all financial assets well as other non-financial assets which are held primarily for financial return. Surrey Police does not currently hold any non-treasury investments.

Short Term Borrowing

3.12. No short term external borrowing was undertaken during 2020/21 or up to 31 December 2021, all cash balances were lent overnight allowing us the flexibility to draw on our own resources.

Long Term Borrowing

3.13. An external loan with PWLB was taken out on 11 March 2019 to support the Building the Future (BtF) project. This loan was for £15.635m with a loan method of

Equal Instalments of Principle (EIP) running over 30 years to 11 March 2049 with an interest rate of 2.34%.

3.14. The PCC also has historical internal borrowing of £7.830m relating to capital expenditure incurred prior to 01 April 2008 and a further £10.815m since which is being repaid over periods of 5-30 years. Use of internal resources in lieu of borrowing by the PCC continues to be the most cost effective means of funding capital expenditure. This also lowers the overall treasury risk by reducing both external debt and temporary investments.

3.15. No new external borrowing was taken in the first nine months of 2021/22.

3.16. Further external borrowing may be required over the next few years and is currently at the planning stage to fund the proposed capital programme and (BtF) going forward. The PCC has various options for financing borrowing, this is likely to be achieved through a mixture of internal and Public Work Lending Board (PWLB) borrowing. The PWLB remains the preferred source of borrowing given the transparency and control that its facilities continue to provide. The main objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required.

Future Borrowing Requirements

3.17. The latest 2021/22 capital programme currently indicates approximately £8m external borrowing may be required before the end of 2021/22. This is under regular review and further borrowing in the future is highly likely.

Surrey County Council

3.18. Surrey County Council's treasury management officers monitor cash flow on behalf of the PCC and aggregate this with their own cash flow, before making appropriate investments on behalf of both organisations. Accordingly there was no requirement for the PCC of Surrey to deal with brokers or bankers during 2020/21 or since up to 31 December 2021.

Value for Money

3.19. The PCC is committed to achieving value for money in treasury management. Actual returns on investment appear low, however this is partly due to the low rates available during the current economic climate and is also offset against the competitively low cost of the treasury management service provided by SCC.

4. Treasury Management & Prudential Indicators to 31 December 2021

4.1. **Prudence Limits.** The PCC must ensure that net external borrowing does not, except in the short term, exceed the total capital financing requirement in the preceding year.

No.	Indicator	ACTUAL	BUDGET	FORECAST	
		2020/21 £'000	**2021/22 £'000**	**2021/22 £'000**	

1	**Borrowing and the capital financing requirement**	✓	✓	✓	☐
	Investments	(12,680)	(14,239)	(11,301)	a
	External borrowing	0	18,099	8,027	b
	External borrowing requirement/investment(-)	**(12,680)**	**(3,274)**	(3,274)	a+b
	CFR	**26,547**	**43,493**	33,153	
	External borrowing > CFR?	NO	NO	NO	
	Management action required	None	None	None	

4.2. Capital Expenditure Limits. These indicators assume that external borrowing will be used but do not commit the PCC to that level of spend or a particular method of financing.

No.	Indicator	ACTUAL	BUDGET	FORECAST
		2020/21 £'000	**2021/22 £'000**	**2021/22 £'000**
1	**Total Capital Expenditure**	13,325	19,277	19,844

No.	Indicator	ACTUAL	BUDGET	FORECAST
		2020/21 £'000	**2021/22 £'000**	**2021/22 £'000**
2	**Capital Financing Requirement (CFR)**	26,547	43,493	33,153

4.3. External Debt Limits. All treasury management activities undertaken during the year to date in 2021/22 comply fully with the CIPFA Code of Practice and the Surrey Police approved Treasury Management Strategy. Compliance with specific investment limits, the authorised borrowing limit and operational boundary for external debt, as demonstrated below:

No.	Indicator	ACTUAL	ORIGINAL ESTIMATE	REVISED FORECAST
		2020/21 £'000	**2021/22 £'000**	**2021/22 £'000**
1	**Authorised Limit**	32,122	52,627	40,115

2	**Operational Boundary**	29,202	47,842	36,468
3	**Actual External Debt**	14,563	14,042	14,042
3	**Total Long Term Debt (Internal & External)**	26,547	43,493	33,153

4.4. Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not considered a compliance failure. Total debt did not exceed the operational boundary in any period during 2021/22 for the period to 31 December 2021.

4.5. Maturity Structure of Borrowing. This indicator is set to control exposure to refinancing risk and the following table illustrates the length of time that current actual fixed rate borrowing is maturing.

No.	Indicator	ACTUAL	ORIGINAL ESTIMATE	REVISED FORECAST
3	**Treasury Management Debt Maturity**	**2020/21**	**2021/22**	**2021/22**
	26-30 years	100%	100%	100%

4.6. **Principal Sums Invested for Periods Longer than one year.** Surrey Police have no investment sums planned or actual that exceed 364 days.

4.7. **Prudential Indicator Compliance.** All of the indicators for the 2021/22 period to 31 December 2021 were compliant. The following table shows the current year compliance against the Prudential Indicators set for 2021/22. Only those indicators where boundaries are set are shown below:

Category	Indicator	Definition	2021/22 Indicator Set	2021/22 Indicator Actual	Compliant	Notes
Prudence	Borrowing and the Capital Financing Requirement	Borrowing must not exceed the Capital Financing Requirement (CFR) in the current year	Borrowing £13.640m CFR £35.449m	Actual Borrowing £14.042m Actual + Planned Borrowing = £21.801m Planned Net Debt £10.500m CFR £33.153m	Yes	External Borrowing is less than CFR
External Debt	Authorised Limit	Authorised Limit for External Debt	£40.115m	Actual External Debt £14.042m Total Debt including planned borrowing £21.801m	Yes	Borrowing is less than limit
Operational Boundary	Level of debt required for the capital program	Must not exceed level set	£36.468m	£33.153m	Yes	Borrowing is less than limit
Treasury	Upper Limit on Variable Rate exposure	Proportion of investments at variable rate	0% to 100%	0% to 100%	Yes	No specific limit set allows flexibility for investments
Treasury	Upper Limit on Fixed Interest Exposure	Proportion of Investments at fixed rate	0% to 100%	0% to 100%	Yes	No specific limit allows flexibility for investments
Treasury	Principle sums invested for more than 364 days	Maximum that can be invested for more than 364 days	0%	0%	Yes	No investments made lasting longer than 364 days
Treasury	Maturity Structure of Borrowing	Limits on maturity of loans	0% to 100%	0% to 100%	Yes	No specific limit allows flexibility for borrowing decisions to achieve best value

5. Conclusions

5.1. The PCC has complied with relevant statutory and regulatory stipulations, which require the PCC to identify the levels of risk associated with its treasury management activities.

5.2. During the nine months to 31 December 2021 the PCC complied with legislative and regulatory requirements.

5.3. The Chief Finance Officer confirms compliance with the approved TMSS for 2021/22 and that a prudent investment approach has been followed with priority given to security and liquidity of amounts invested over actual yield achieved.

5.4. Risk management considerations:

Associated risks have been considered and adequate control measures implemented. All Treasury Management activity is carried out in accordance with the approved Treasury Management Strategy Statement, which aims to minimise risk to ensure the PCC principal sums are safeguarded. Maximising income is considered secondary to this main aim.

If the PCC does not review annual performance of treasury management activity in line with the CIPFA Treasury Management Code of Practice there is a risk that poor management of public funds could occur and go unnoticed, resulting in censure from the auditors and reputational damage as a consequence.

5.5. There are no equality or Human Right implications arising from this report

5.6. Relevant legislation and guidance has been complied with in the delivery of the Treasury Management activities.

6. Decisions Required

6.1. The Chief Finance Officer invites the Joint Audit Committee Members to review the 2021-22 Treasury Management Mid-year Report and recommend for approval by the PCC.

7. Attachments / Background Papers

7.1. Appendix 1 - **Interest Rates Received**
7.2. Appendix 2 - **Actual Interest Amounts Received**
7.3. Appendix 3 - **Average Investment Balances**
7.4. Appendix 4 - **Economic Update**
7.5. Appendix 5 - **Regulatory Update**
7.6. Appendix 6 - **PWLB certainty rates**
7.7. Background sources detailing compliance requirements:

- The PCC for Surrey's Treasury Management Strategy Statement
- CIPFA Treasury Management in Public Services Code: Guidance Notes for Local Authorities including Police and Fire Authorities (2018 Edition)
- CIPFA The Prudential Code for Capital Finance in Local Authorities: Guidance Notes for Practitioners (2018 Edition)
- MHCLG MRP Guidance and Investment Guidance
- Local Government Finance Act 1992
- Local Government Act 2003 (England and Wales)
- The Capital Finance and Accounting Regulations 2003
- International Financial Reporting Standards (IFRS) in the Code of Practice on Local Authority Accounting in the United Kingdom (2021/22 Edition)

8. Contact Details

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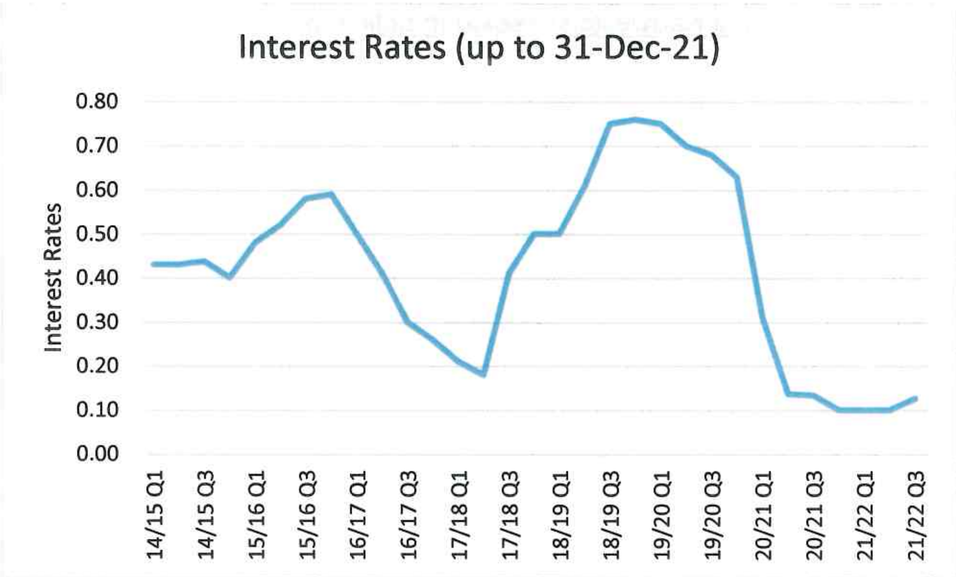
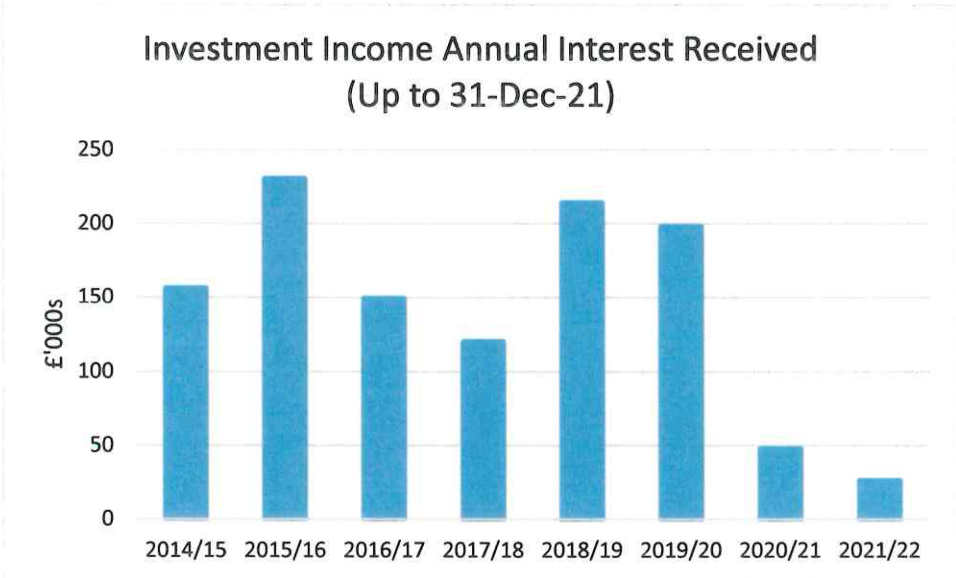
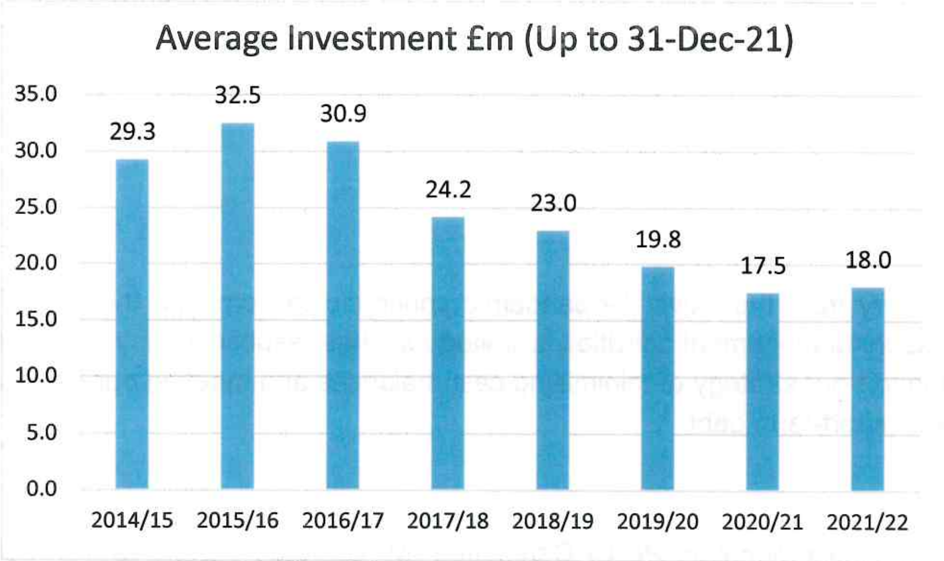
APPENDIX 1 - Interest Rates Received



APPENDIX 2 - Actual Interest Amounts Received



APPENDIX 3 - Average Investment Balances


Average Investment £m (Up to 31-Dec-21)
35.0
30.0
25.0
20.0
15.0
10.0
5.0
0.0
29.3
32.5
30.9
24.2
23.0
19.8
17.5
18.0
2014/15
2015/16
2016/17
2017/18
2018/19
2019/20
2020/21
2021/22

APPENDIX 4 - Economic Update

Economic Update

Economic recovery from the Covid-19 pandemic continued to dominate the year. The impact on Treasury Management activities is limited as it has resulted in very low interest rates which support our strategy of minimising cash balances and meeting our borrowing requirement with short-term debt.

The Bank of England's Monetary Policy Committee (MPC) voted 7-2 on 4th November 2021 to leave the Bank Rate unchanged at 0.10% and made no changes to its Quantitative Easing programme at £895 billion, due to finish by the end of this year. The Bank of England Monetary Policy Committee voted again **on 16 December to increase the Bank of England base rate to 0.25%** from 0.1%. The rise came despite concerns that the Omicron variant might derail the economy by triggering consumers to spend less.

HMRC interest rates are linked to the Bank of England base rate and as a consequence of the change in base rate, HMRC interest rates on late payments are set to increase from 27 December 2021 for quarterly instalment payments and 4 January 2022 for non-quarterly instalment payments whereas repayment interest rates will remain unchanged.

Over the next year the MPC will be doing a delicate balancing act of weighing combating inflation being higher for longer against growth being held back by supply shortages (pushing prices up and holding back production directly), labour shortages, surging fuel prices and tax increases. Some of those could potentially be at least partially offset by consumers spending "excess savings" accumulated during the pandemic. However, it is also possible that more affluent people may be content to hold onto elevated savings and investments and, therefore, not support the economic recovery to the extent that the MPC may forecast. It is uncertain whether a broad-based increased in wages is possible given the pressures on businesses.

The MPC's forward guidance on its intended monetary policy on raising Bank Rate versus selling (quantitative easing) holdings of bonds is as follows: -

1. Raising Bank Rate as "the active instrument in most circumstances".
2. Raising Bank Rate to 0.50% before starting on reducing its holdings.
3. Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.
4. Once Bank Rate had risen to at least 1%, it would start selling its holdings.

Forecasts by the Bank showed inflation under-shooting the 3 years ahead 2% target (1.95%), based on market expectations of Bank Rate hitting 1% in 2022. This implies that rates don't need to rise to market expectations of 1.0% by the end of next year. Investors have priced in multiple rises in Bank Rate to 1% by 2024. While advisors indicate the Bank Rate will rise, it is by a lesser extent than expected by markets.

Household spending, the driver of the recovery to date, is under pressure from a combination of retail energy price rises, the end of government support programmes and soon, tax rises. Government spending, the other driver of recovery, will slow considerably as the economy is taken off life support.

Inflation rose to 3.2% in August. A combination of factors will drive this to over 4% in the near term. While the transitory factors affecting inflation, including the low base effect of 2020, are expected to unwind over time, the MPC has recently communicated fears that these transitory factors will feed longer-term inflation expectations that require tighter monetary policy to control. This has driven interest rate expectations substantially higher

COVID-19 vaccines. These are the game changers which boosted confidence that life in the UK could largely return to normal during the summer after a third wave of the virus threatened to overwhelm hospitals in the spring. With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is plenty of pent-up demand and purchasing power stored up for services in hard hit sectors like restaurants, travel and hotels. The big question is whether mutations of the virus could develop which render current vaccines ineffective, as opposed to how quickly vaccines can be modified to deal with them and enhanced testing programmes be implemented to contain their spread.

APPENDIX 5 – Regulatory Update

Revision to CIPFA Codes

In February 2021 CIPFA launched two consultations on changes to its Prudential Code and Treasury Management Code of Practice. These followed the Public Accounts Committee's recommendation that the prudential framework should be further tightened following continued borrowing by some local authorities for investment purposes although this did not apply to Surrey Police. In June, CIPFA provided feedback from this consultation.

In September CIPFA issued the revised Codes and Guidance Notes in draft form and opened the latest consultation process on their proposed changes which include:

- Clarification that local authorities must not borrow in order to invest primarily for financial return;
- The requirement to categorise investments for Treasury purposes, commercial

purposes and for service delivery purposes (Surrey Police do not undertake any for commercial purposes);

- The introduction of Investment Management Practices (IMP's) by which local authorities will need to start monitoring their non-treasury investment portfolios;
- The requirement to assess the proportionality of non-treasury investments in the authorities overall financial capacity; and
- Some revisions in the prudential indicators, including the inclusion of the liability benchmark to measure the need to borrow.

These revisions, if implemented as drafted, are not expected to have a significant impact on Surrey Police's activities but may increase the reporting requirements in respect of non-treasury investments and other items.

APPENDIX 6 - PWLB certainty rates

The graph below illustrates the general trends in PWLB interest rates for the six months to September 2021.