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Dear Councillor

SOUTH HAMS COUNCIL - THURSDAY, 29TH MARCH, 2018

I refer to the agenda for the above meeting and attach papers in connection with the following item(s).

Agenda No	Item
4.	**Waste Review** (Pages 1 - 12)
5.	**Treasury Management Strategy** (Pages 13 - 58)

Yours sincerely

Darryl White
Senior Specialist – Democratic Services

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The appendices to this report are considered exempt under paragraph 3 of schedule 12A of the Local Government Act 1972 in that it concerns the financial or business affairs of the Council. The public interest has been assessed and it is considered that, the public interest is better served by non-disclosure to the press and public.

Report to: **Council**

Date: **29 March 2018**

Title: **Frontline Services (Waste & Cleansing Procurement)**

Portfolio Area: **Commercial Services**

Wards Affected: **All**

Relevant Scrutiny Committee: **Council**

Urgent Decision: **N** Approval and clearance obtained: **Y**

Date next steps can be taken: Immediately

Author: **Helen Dobby & Jane Savage on behalf of the Waste Board** Role: **Group Leader (Commercial Services) & Commissioning Manager (Waste)**

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Recommendations:

1. It is **RECOMMENDED** that the Council note the progress of the project and endorse the view of the Frontline Services (Waste Procurement) Project Board to continue to the next stage of the competitive dialogue process for waste collection, recycling and cleansing services.

1. Executive summary

1.1. Members requested that key decisions during the procurement process be brought before Council. The procurement process goes through a number of stages – Outline Solutions, Detailed Solutions and Final Solutions. This report deals with the Outline Solutions Stage.

1.2. Bids have been received and evaluated for the Outline Solution Stage and proposals have been assessed as offering better quality against current service.

The appendices to this report are considered exempt under paragraph 3 of schedule 12A of the Local Government Act 1972 in that it concerns the financial or business affairs of the Council. The public interest has been assessed and it is considered that, the public interest is better served by non-disclosure to the press and public.

1.3. Appendix B contains further information from the submissions and outlines any potential savings, and service design improvements contained within the bids.

1.4. It should be noted that if the Council approve Recommendation 1, the procurement process will continue to the Detailed Solutions Stage and a further report will be brought before Council in July 2018.

1.5. West Devon are legally required to test services in line with the Public Contract Regulations 2015. In order for South Hams to properly test service costs in the marketplace detailed solution information will be required.

2. **Background**

2.1 Members requested that key decisions during the procurement process be brought before Council. This report deals with the Outline Solutions Stage and the Board have based the recommendation on whether it is of benefit to both South Hams and West Devon Councils to continue with the procurement process. It should be noted that if Recommendation 1 is approved, the procurement process will continue to the Detailed Solutions Stage and a further report will be brought before Council in July 2018. Detailed solutions expand upon the specific detail of service benefits to the Council based upon a more thoroughly costed service solution rather than the indicative costs given at outline stage.

2.2 At the current stage of the procurement process an endorsement of the recommendation does not commit South Hams District Council to outsource the services. It does however recognise that the process is currently competitive and allows bidders to proceed to Detailed Stage. West Devon Borough Council are committed to continue with the process to be compliant with Public Contract Regulations 2015. Broadly costed parameters have been submitted at this outline stage and Detailed Stage solutions would offer more in-depth analysis of quality and cost in July 2018.

2.3 To ensure commercial confidentiality of bids and maintain the integrity of the procurement process, actual costings cannot be disclosed in this report. The Project Board have considered both service price and the quality of service offered by the bidders.

2.4 Following the Special Council meetings for West Devon and South Hams on the 31 October 2017, a number of recommendations were agreed which allowed for a Notice to be placed in the European Journal (OJEU) to invite suitable candidates to bid for the recycling and waste collection, street cleansing and public toilet cleaning services in both Council areas.

2.5 These respective reports set out the key objectives for the services as well as defining 'red lines' for service delivery. The market place was asked to cost the current service design as well as to provide optimum service solutions designed to meet the required objectives as detailed in the report. The optimum service solutions included the need to work towards the Devon aligned service. This is in line with the Waste and Resource Management Strategy for Devon to which the Council is committed.

2.6 To ensure legal compliance in West Devon the procurement must be completed in time for a service commencement date of the 1st April 2019. South Hams are testing the market within the same timeframe to take advantage of a shared procurement, which has potential advantages for both Councils, in terms of procurement costs and economies of scale.

2.7 Recommendations at key points in the procurement process will come from the Frontline Services (Waste Procurement) Project Board who have access to all procurement information. It was requested that key gateway decisions during the process be brought before Council for consideration.

2.8 The latest Board Highlight Report is attached as Appendix A. This and previous Highlight Reports can be reviewed by all Members at: http://is.swdevon.lan/members-west-devon/messages-from-officers/ . Please note the highlight Reports are not available to the general public. In summary, these reports set out progress to date, milestone activity, budget position, and the main project risks. The current position is summarised in the following paragraphs.

2.9 Detailed contract documents were developed by the waste working groups which included setting out the specific requirements of the two Councils and has produced detailed baseline data for both.

2.10 All bidders scored highly enough at the selection stage to be invited to take part in the next stage of the process, which was to submit Outline Solutions. The bidders understand the scale, scope and size of contract which we are procuring and the importance of each Council's identity. They are major market forces and have existing footholds in the South West – they are either already involved in, or have an interest in neighbouring South West contracts which are due to come to market shortly. As such our positioning and procurement timing should allow for a fully competitive testing of the market in relation to our services.

2.11 The process is divided into 3 parts, Outline Stage, Detailed Stage and Final Stage. This report deals with the Outline Stage where evaluation is based on 60% cost and 40% quality and whether solutions offer an advantage, in particular a financial advantage, over the current means of delivery.

2.12 Bidders were asked to provide bids on the basis of the services being split into 3 Lots:

- Lot 1 West Devon's waste and cleansing services
- Lot 2 South Hams' waste and cleansing services
- Lot 3 Both Councils' waste and cleansing services

3. Evaluation of Outline Solutions

3.1 All proposals have been assessed as offering better quality against current service design.

3.2 To ensure a like for like comparison, proposals have been evaluated against current service costs taking into account considerations, such as depot usage, income from recyclables and customer support. At this stage due to the procurement methodology, exact specification of services cannot be determined as this would be refined during later dialogue stages and therefore the comparison of pricing against existing costings cannot be finalised but based on the solutions offered so far. However, an indication of current delivery costs against those proposed are shown in Appendix B. For commercial reasons, exact costings cannot be disclosed in this report but have been fully considered by the Project Board.

3.3 It should be noted that net costs for the provision of waste and cleansing services have risen in recent years, not least due to the introduction of the National Living Wage, fluctuations in the global recyclable materials markets including Chinese import restrictions and a national shortage of HGV drivers.

3.4 The next stage of the procurement involves a second round of dialogue with bidders to discuss optimum solutions for each Council after which invitations to submit Detailed Solutions will be issued.

4. Options available and consideration of risk

4.1 There is no material risk to the Council of continuing to the next stage of the procurement process and, if the recommendation is approved, a further recommendation on whether to continue with the process will come before Council in July.

4.2 There is a risk if West Devon choose not to endorse Recommendation 1 as failure to continue with the procurement process and award a contract by April 2019 would result in the Council being non-compliant with the Public Contract Regulations 2015.

4.3 All Devon districts have committed to move towards the Devon Aligned Service. Any delay may incur additional costs and the Council would miss out on opportunities that the aligned service could provide such as improvements to the customer, increase in recycling rate and income, increased opportunities for partnership working and cost reductions, and positive environmental impacts.

4.4 At this stage it is not necessary to make decisions such as opting for less frequent residual collections. However it is worth noting that any savings that can be achieved from this option will not be fully realised if a decision is made after the procurement process is concluded.

5. Proposed Way Forward

5.1. It is proposed that Council endorses the view of the Board to continue to the next stage of the competitive dialogue process for waste collection, recycling and cleansing services.

5.2. This recommendation fits with the corporate priorities of Environment, Infrastructure and Resources.

6. **Implications**

Implications	Relevant to	Details and proposed measures to address

	proposals Y/N	
Legal/Governance	Y	The Council has a duty to arrange for collection and disposal of household waste. The legislative framework is to be found in the Environmental Protection Act 1990, Waste Framework Directive 2008, and Controlled Waste Regulations 2012. The procurement process is compliant with the Public Contract Regulations 2015. Any change in policy will need to be communicated to bidders so that they can consider the impact on their pricing strategy.
Financial	Y	Financial implications are set out in Appendix B.
Risk	Y	The risks are set out at section 4 of this report.
Comprehensive Impact Assessment Implications		
Equality and Diversity	N	Not applicable
Safeguarding	N	Not applicable
Community Safety, Crime and Disorder	N	Not applicable
Health, Safety and Wellbeing	N	Not applicable
Other implications	N	None

Supporting Information

Appendices:

Appendix A: Project Board Highlight Report February 2018 - **Exempt**
Appendix B: Outline Solutions Stage Council Position - **Exempt**

Background Papers:
Council Report 31 October 2017

Approval and clearance of report

Process checklist	Completed
Portfolio Holder briefed	**Yes**
SLT Rep briefed	**Yes**
Relevant Exec Director sign off (draft)	**Yes**
Data protection issues considered	**Yes**
If exempt information, public (part 1) report also drafted. (Cabinet/Scrutiny)	

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Report to:	**Council**
Date:	**29th March 2018**
Title:	**2018/19 Treasury Management Strategy**
Portfolio Area:	**Support Services – Councillor S Wright**
Wards Affected:	**All**

Relevant Scrutiny Committee: **Overview and Scrutiny Panel**

Urgent Decision:	**N**	Approval and clearance obtained:	**Y**

Date next steps can be taken: Full Council

Authors: Lisa Buckle Role: **Strategic Finance Lead (S151 Officer)**

Contact: **Email Lisa.buckle@swdevon.gov.uk 01803 861413**

Recommendations: That the Council approve:-

1. The prudential indicators and limits for 2018/19 to 2020/21 contained within Appendix A of the report.

2. The Minimum Revenue Position (MRP) statement contained within Appendix A which sets out the Council's Policy on MRP.

3. The Treasury Management Strategy 2018/19 and the treasury prudential indicators 2018/19 to 2020/21 contained within Appendix B.

4. The Investment Strategy 2018/19 Appendix C and the detailed criteria included in Appendix D and the counter party list in Appendix E

5. To invest £500,000 into CCLA Local Authority Property Fund (LAPF) and £1 million into the CCLA Diversified Income Fund as per Appendix H.

6. To externally borrow from the PWLB for the Leisure Investment as set out in Section 5.

1. Executive summary

This report seeks approval of the proposed Treasury Management and Investment Strategies together with their associated prudential indicators.

Good financial management and administration underpins the entire strategy. The budget for investment income for 2018/19 has been set at £123,000. This remains the same as the 2017/18 budget.

The following changes have been made to 2018/19 Treasury Management Strategy,

- **Country and sector limits** – the Council has the opportunity to lift the restriction to only use UK registered banks. This limit has been widened to allow the use of approved counterparties from countries with a minimum sovereign credit rating of AA- (see Appendix C).

- **Counterparty list** – following the opportunity to lift the restriction to only use UK registered banks, the Council's suggested counterparty list has been included in Appendix E.

- **CCLA Property Investment Funds** – the Council's list of investment vehicles has been updated to allow the future use of CCLA Property Investment Funds. This will be the Council's only Non-Specified Investment and a limit of £2 million has been set for this asset class. There is a recommendation to invest £1.5 million into CCLA as per Appendix H.

- **Capital Strategy** - In December 2017, CIPFA issued revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities will be required to prepare an additional Capital Strategy report. Details of what this report is intended to provide can be found at point 2.2 of this report. The Council will produce a Capital Strategy in 2018/19.

- **Prudential Indicators** – the estimates of the incremental impact of capital investment decisions on council tax indicator has been removed from the revised 2017 Prudential Code. However, the Council is retaining this as a local indicator to support Member decision making.
  The Council's prudential indicators have been revised to reflect the current schedule of borrowing for the leisure investment (see Appendix A).

- **Asset Class** – the current approach means the Council is just dealing with money market instruments, plus the potential to invest in the property fund (CCLA), so there is not much asset diversification currently.

2. Background
The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's risk appetite on investments, providing adequate liquidity initially before considering investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses.
CIPFA defines treasury management as:

"The management of the local authority's borrowing, 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."

2.1 Reporting requirements

The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

Prudential and treasury indicators and treasury strategy (this report) - The first, and most important report covers:
- The capital plans (including prudential indicators);
- A minimum revenue provision (MRP) policy
- The treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- An investment strategy (the parameters on how investments are to be managed).

A mid year treasury management report – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision.

An annual treasury report – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Scrutiny - The above reports are required to be adequately scrutinised before being recommended to the Council. The reports are presented to the Executive prior to being recommended to Council. The Strategy for 18-19 was considered by the Executive on 15th March and the Audit Committee on 22nd March. It is within the Terms of Reference of the Audit Committee to scrutinise the Treasury Management Strategy. This report was published before the meeting of the Audit Committee on 22nd March. The Treasury Management Strategy was recommended to Council by the Executive on 15th March.

2.2 Capital Strategy

In December 2017, CIPFA issued revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities will be required to prepare an additional Capital Strategy report, which is intended to provide the following:-

- A high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- An overview of how the associated risk is managed
- The implications for future financial sustainability arising from longer term capital objectives

The aim of this report is to ensure that all elected members on the full council fully understand the overall strategy, governance procedures and risk appetite entailed by the Capital Strategy.
The Capital Strategy will include capital expenditure, investments and liabilities and treasury management in sufficient detail to allow all members to understand how stewardship, value for money, prudence, sustainability and affordability will be secured.

2.3 Treasury Management Strategy for 2018/19

The strategy for 2018/19 covers two main areas:

Capital issues
- The capital plans and the prudential indicators;
- The minimum revenue provision (MRP) policy.

Treasury management issues
- The current treasury position;
- Treasury indicators which limit the treasury risk and activities of the Council;
- Prospects for interest rates;
- Policy on borrowing in advance of need;
- The investment strategy;
- Creditworthiness policy; and
- Policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, MHCLG MRP Guidance, the CIPFA Treasury Management Code and MHCLG Investment Guidance.

It is noted that MHCLG released revised Investment and MRP Guidance on 2nd February and the Council will adopt any relevant changes in an updated Strategy during the 2018/19 financial year.

2.4 Training

The CIPFA Code requires the responsible officer to ensure that Members with responsibility for treasury management receive adequate training in treasury management. This training has recently been widened to include Non-Treasury Investment. Treasury management training will be organised for Members during the 2018-19 financial year.

The training needs of treasury management officers are periodically reviewed. Officers received training on 31st January 2018.

2.5 Treasury management advisors

The Council uses Link Asset Services, Treasury solutions as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

3. Outcomes/outputs

The budget for investment income for 2018/19 has been set at £123,000. This remains the same as the 2017/18 budget. However an income target of an extra £25,000 has been set for 2018/19.

4. Options available and consideration of risk

In order to maximise investment returns the Council needs to be able to either increase our investment portfolio which could potentially mean increasing the risk factor or maintain the current list of Counter Party’s but further increase the limit we can invest in each to avoid using those with the lowest rate of return.

5. Borrowing for the Leisure Investment

The Council has modelled its Balance Sheet position for 31/3/18 and future years, in order to inform the decision as to how to structure the borrowing for the Leisure Investment. The purpose of the modelling was to identify the capacity of the Council to utilise an element of internal borrowing rather than all external borrowing through the Public Works Loans Board (PWLB).

In terms of the Council's capacity to borrow internally, the level to which the Council could do this has been assessed at between £3 million to £4 million, based on current modelling and forecasting.

In July 2016 (Minute 33/16) the Council agreed to undertake prudential borrowing of £6.337 million for the new leisure contract, with a further £1.5 million of prudential borrowing for a loan facility being subject to a business case.

The leisure investment in 2017/18 is just under £1 million, with the main investment occurring in 2018/19, and a smaller residual element in 2019/20.

The Council is being reimbursed by the Leisure contractor for the borrowing costs of the Leisure Investment and this income has already been factored into the MTFS (Medium Term Financial Strategy). Therefore if the Council did use internal borrowing for some of the Leisure investment, the saving is the difference between what it would cost the Council to borrow externally (currently around 2.5%) and the loss of income on investments (up to 1%).

So if the Council internally borrowed £3 million for the Leisure Investment, this could save up to £45,000 per annum initially (£3 million at 1.5% saving). Obviously when interest rates rise, the saving becomes less - as this borrowing is over a 24 year period, being the remaining period of the contract term.

The recommendation of the S151 Officer is for the Council to take out external borrowing with the PWLB for all of the leisure investment on a 24 year term (the remaining period of the contract and estimated life of the asset). The current interest rate would be around 2.5%.

Over a 24 year period this would give more flexibility to the Council to internally borrow for other projects in the future, which would be considered in their own right. This would also protect against future interest rate rises over the next 24 years and ensure that Leisure is a self-financing stand alone investment project.

6. New changes affecting the Treasury Management activities

International Financial Reporting Standard 9 – Financial Instruments

From 1 April 2018, new accounting rules will apply to investments, as the Local Authority Accounting Code adopts International Financial Reporting Standard 9 *Financial Instruments*. IFRS 9 was devised to correct the weaknesses in accounting practices that contributed to the global financial crisis. In particular it:

- changes the default accounting treatment for investments from one where gains and losses in value are not recognised as income or expenditure until an investment matures or is disposed of to one where income or expenditure is recognised as gains and losses arise
- changes the model for impairment loss allowances from one based on incurred losses to one based on expected losses

The first of these changes is particularly relevant and would affect a CCLA investment. Where these investments are based on buying shares in funds (such as CCLA), the 1 April 2018 changes in accounting rules will require fair value movements to be debited/credited to revenue as they arise. This is explained further in Appendix H.

There is a risk that if losses arise on this investment, it would result in a charge against revenue in the year it arose and could not be stored up to be offset against potential future gains. Developments in this area will be monitored carefully over the next few months.

MiFIDII

The Markets in Financial Instruments Directive (MiFID) is the framework of European Union (EU) legislation for:

- investment intermediaries that provide services to clients around shares, bonds, units in collective investment schemes and derivatives (collectively known as 'financial instruments')
- the organised trading of financial instruments

MiFID applied in the UK from November 2007, and was revised by MiFID II, which took effect in January 2018, to improve the functioning of financial markets in light of the financial crisis and to strengthen investor protection. MiFID II extended the MiFID requirements in a number of areas including:

- new market structure requirements
- new and extended requirements in relation to transparency
- new rules on research and inducements
- new product governance requirements for manufacturers and distributers of MiFID 'products'
- introduction of a harmonised commodity position limits regime

Part of the new legislation required bodies whom perform complex investments to be deemed/classified as professional investment bodies.

Those bodies who decided not to be classified (opt up) or did not met the requirements to be classified as a professional investment body would be deemed as retail investors. Retail investors are limited on the types of investments they could make, some Money Market Funds would be unavailable to retail investors.

To ensure that the Council could continue to invest in the current manner, the Council opted up to be classed as a professional body. This 'professional body status' has been accepted in all cases of parties with whom the Council currently invests.

7. Proposed Way Forward

It is recommended for the Council to approve the Treasury Management and Investment Strategy.

8. Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/Governance	Y	The elements set out in paragraph 2.2 cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the CIPFA Treasury Management Code, the Department for Communities and Local Government (DCLG) Investment Guidance and the DCLG MRP Guidance. It is within the Terms of Reference of the Audit Committee to scrutinise the Treasury Management Strategy.
Financial	Y	Good financial management and administration underpins the entire strategy. The budget for investment income for 2018/19 is £123,000. A stretched income target of a further £25,000 is being set. As at 31/3/17 (Balance Sheet position), the Council had £29.175 million in investments. See comments in Appendix H regarding the investment of £1.5 million into CCLA.

Risk	Y	The security risk is the risk of failure of a counterparty. The liquidity risk is that there are liquidity constraints that affect the interest rate performance. The yield risk is regarding the volatility of interest rates/inflation. The Council has adopted the CIPFA Code Of Practice for Treasury Management and produces an Annual Treasury Management Strategy and Investment Strategy in accordance with CIPFA guidelines. The Council engages a Treasury Management advisor and a prudent view is always taken regarding future interest rate movements. Investment interest income is reported quarterly to SLT and the Executive as part of budget reports
Comprehensive Impact Assessment Implications		
Equality and Diversity	N	N/a
Safeguarding	N	N/a
Community Safety, Crime and Disorder	N	N/a
Health, Safety and Wellbeing	N	N/a
Other implications	N	none

<u>Supporting Information</u>

Appendices:

Appendix A - The Capital Prudential indicators 2018/19 to 2020/21.
Appendix B - The Treasury Management Strategy 2018/19
Appendix C – The Investment Strategy
Appendix D - Treasury Management Practice (TMP 1) – Credit and Counterparty Risk Management
Appendix E – Counterparty List as at 16th February 2018
Appendix F - Treasury Management Scheme of delegation
Appendix G - Glossary of Terms Appendix
Appendix H – CCLA Investment Options
Appendix I – LAPF Factsheet (CCLA Option)
Appendix J – DIF Brochure (CCLA Option)

Background Papers:

Executive: 9/03/17 - TMS & Annual Investment Strategy 2017-18
Executive: 07/12/17 - TMS (Mid Year Update)
Executive: 15/3/18 – Treasury Management Strategy 2018-19

Process checklist	**Completed**
Portfolio Holder briefed	**Yes**
SLT Rep briefed	**Yes**
Relevant Exec Director sign off (draft)	**Yes**
Data protection issues considered	**Yes**
If exempt information, public (part 1) report also drafted. (Committee/Scrutiny)	**N/a**

APPENDIX A

THE CAPITAL PRUDENTIAL INDICATORS 2018/19 – 2020/21

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist Members' overview and confirm capital expenditure plans.

Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts:

Capital expenditure	2016/17 Actual £'000	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000
Total	**3,023**	**3,413***	**7,492**	**2,464**	**410**

*Note – This figure is £2,415,000 as per the Council report on 9 February 2017, plus £0.998 million for Leisure Investment in 17/18. In July 2016 (Minute 33/16) the Council agreed to undertake prudential borrowing of £6.337 million for the new leisure contract, with a further £1.5 million of prudential borrowing for a loan facility being subject to a business case. The remaining leisure investment occurs in 18/19 and 19/20.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital expenditure	2016/17 Actual £'000	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000
Total	3,023	3,413	7,492	2,464	410
Financed by:					
Capital receipts	665	877	1,111	TBA	TBA
Capital grants	1,166	613	700	TBA	TBA
Reserves (including New Homes Bonus Reserve)	1,192	925	744	TBA	TBA
Net financing need for the year (This is the prudential borrowing required for capital investment in Leisure)	Nil	998	4,937	TBA	TBA

The Council's borrowing need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). It is essentially a measure of the Council's underlying need to borrow. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each assets life.

In July 2016 (Minute 33/16) the Council agreed to undertake prudential borrowing of £6.337 million for the new leisure contract. There is predicted to be £1 million of Leisure investment in 2017/18 (this is shown in the movement in CFR). The remaining leisure investment occurs in 18/19 and 19/20.

The Council is asked to approve the CFR projections below:

	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Capital Financing Requirement (CFR)					
Total CFR	- 98	900	5,797	5,676	5,396
Movement in CFR	Nil	998	4,897	-121	-280
Movement in CFR represented by:					
Net Financing need for the year	Nil	998	4,937	159	Nil
Less MRP and other financing movements	Nil	Nil	-40	-280	-280
Net borrowing requirement	Nil	998	4,897	-121	-280

Minimum revenue provision (MRP) policy statement

Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2003 states that 'A local authority shall determine for the current financial year an amount of minimum revenue provision which it considers to be prudent'. The provision is made from revenue in respect of capital expenditure financed by borrowing or credit arrangements.

With all options MRP should normally commence in the financial year following the one in which expenditure was incurred. Regulation 28 does not define 'prudent'. However MRP guidance has been issued, which makes recommendations to authorities on the interpretation of that term. Authorities are legally obliged to 'have regard' to the guidance.

The first recommendation given by the guidance is to prepare, before the start of each financial year, an annual statement of the policy on making MRP in respect of that financial year and submit this to Full Council for approval. The guidance aims to ensure that the provision for the repayment of borrowing which financed the acquisition of an asset should be made over a period bearing some relation to that over which the asset continues to provide a service.

The MRP policy to be adopted is as below:-

Borrowing	MRP Methodology
Leisure Investment	**Asset Life Method** MRP is charged using the Asset Life method – based on the estimated life of the asset. (For the Leisure investment, MRP will be charged over the 25 years – therefore 4% per annum). This option provides for a reduction in the borrowing need over approximately the asset's life.

Affordability prudential indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

Ratio of financing costs to net revenue stream

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream. It is calculated by dividing investment income and interest received by the Council's Net Budget Requirement.

	2016/17	2017/18	2018/19	2019/20	2020/21
	Actual	Estimate	Estimate	Estimate	Estimate
Ratio of net financing cost to net revenue stream.	(1.8)%	(1.1)%	1.0%	4.1%	4.3%

This is a surplus in 16/17 and 17/18 but it becomes a net financing cost from 2018/19 onwards.

APPENDIX B

TREASURY MANAGEMENT STRATEGY (BORROWING)

Introduction

The capital expenditure plans set out in Appendix A provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

The Council's treasury portfolio position at 31 March 2017, with forward projections are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
External Debt					
Debt at 1 April	Nil	Nil	Nil	6,300	6,300
Expected change in debt					
Debt at 31 March	Nil	Nil	6,300	6,300	6,300
CFR	-98	900	5,797	5,676	5,396
Under/(over) borrowing	-98	900	-503	-624	-904
Investments					
Total Investments at 31 March	29,175	30,000	30,000	30,000	30,000
Net (Investment)/Debt	(29,175)	(30,000)	(23,700)	(23,700)	(23,700)

Treasury Indicators: Limits to borrowing activity

The Operational Boundary – This is the limit beyond which external debt is not normally expected to exceed. This is the maximum level of external debt for cash flow purposes.

Operational Boundary	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Borrowing	5,000,000	9,000,000	10,000,000	10,000,000
Other long term liabilities	-	-	-	-
Total	5,000,000	9,000,000	10,000,000	10,000,000

The Authorised Limit for External Debt – A further key prudential indicator represents a control on the overall level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by Full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. This provides headroom over and above the operational boundary for unusual cash movements. This is the maximum amount of money that the Council could afford to borrow.

1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although no control has yet been exercised.

2. ***The Council is asked to approve the following Authorised Limit:***

Authorised limit	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Borrowing	10,000,000	14,000,000	15,000,000	15,000,000
Other long term liabilities	-	-	-	-
Total	10,000,000	14,000,000	15,000,000	15,000,000

Prospects for interest rates

The Council has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives our central view.

	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Bank rate	0.50%	0.75%	0.75%	1.00%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.50%
5yr PWLB rate	1.90%	2.00%	2.10%	2.10%	2.20%	2.30%	2.30%	2.40%	2.40%	2.50%	2.50%	2.60%	2.60%
10yr PWLB rate	2.50%	2.50%	2.60%	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%
25yr PWLB rate	2.80%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB rate	2.60%	2.70%	2.80%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%

As expected, the Monetary Policy Committee (MPC) delivered a 0.25% increase in Bank Rate at its meeting on 2 November. This removed the emergency cut in August 2016 after the EU referendum. The MPC also gave forward guidance that they expected to increase Bank rate only twice more by 0.25% by 2020 to end at 1.00%. The Link Asset Services forecast as above includes increases in Bank Rate of 0.25% in May and November 2018, November 2019 and August 2020.

Investment and borrowing rates

Investment returns are likely to remain low during 2018/19 but to be on a gently rising trend over the next few years.

- Borrowing interest rates increased sharply after the result of the general election in June and then also after the September MPC meeting when financial markets reacted by accelerating their expectations for the timing of Bank Rate increases. Since then, borrowing rates have eased back again. Apart from that, there has been little general trend in rates during the current financial year. The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times when authorities will not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt;

- There will remain a cost of carry to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost – the difference between borrowing costs and investment returns.

Borrowing Strategy

In July 2016 (Minute 33/16) the Council agreed to undertake prudential borrowing of £6.337 million for the new leisure contract, with a further £1.5 million of prudential borrowing for a loan facility being subject to a business case.

There is predicted to be £1 million of Leisure investment in 2017/18 (this is shown in the movement in CFR). The remaining leisure investment occurs in 18/19 and 19/20.

Treasury management limits on activity

There are two related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. However if these are set to be too restrictive they will impair the opportunities to reduce costs/improve performance.

The indicators are:

- Upper limits on fixed interest rate exposure – This covers a maximum limit on fixed interest rates.
- Upper limits on variable interest rate exposure – This covers a maximum limit for variable interest rates.

The Council is asked to approve the following treasury indicators and limits:

Interest rate Exposures	2018/19	2019/20	2020/21
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	50%	50%	50%
Limits on fixed interest rates: Debt only	12,500,000	12,500,000	12,500,000
Limits on variable interest rates: Debt only	2,500,000	2,500,000	2,500,000
Maturity Structure of fixed interest rate borrowing 2018/19			
		Lower	**Upper**
Under 12 months		0%	10%
12 months to 2 years		0%	10%
2 years to 5 years		0%	30%
5 years to 10 years		0%	50%
10 years and above		0%	100%

Policy On Borrowing In Advance Of Need

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Borrowing in advance will be made within the constraints that:

- The Council would not look to borrow more than 18 months in advance of need.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

If the Council had to borrow temporarily for cash flow purposes only in an emergency, then the S151 Officer, under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks. A report will subsequently be reported to Council. In all other circumstances, approval to borrow money will always be a decision that can only be made by Full Council and a full report will be brought to Members.

Municipal Bond Agency

It is possible that the Municipal Bond Agency will be offering loans to local authorities in the future. The Agency hopes that the borrowing rates will be lower than those offered by the Public Works Loan Board (PWLB). This Authority may make use of this new source of borrowing as and when appropriate.

APPENDIX C

Investment policy

The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectorial Guidance Notes 2017 ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, then return.

In accordance with the above guidance from the CLG and CIPFA, and in order to minimise the risk to investments, the Council applies minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

Ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

Investment instruments identified for use in the financial year are listed in appendix D under the 'specified' and 'non-specified' investments categories. Counterparty limits will be as set through the Council's treasury management practices – schedules.

Creditworthiness policy

This Council applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit Watches and credit Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands

- Yellow 5 years *
- Dark pink 5 years for Enhanced money market funds (EMMFs) with a credit score of 1.25
- Light pink 5 years for Enhanced money market funds (EMMFs) with a credit score of 1.5
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No colour not to be used

** Please note: the yellow colour category is for UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt –see appendix D.*

The Link Asset Services' creditworthiness service uses a wider array of information than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored weekly. The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services' creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on any external support for banks to help support its decision making process.

Country and sector limits

The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA-.

Investment strategy

In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

Investment returns expectations. Bank Rate is forecast to stay flat at 0.50% until quarter 4 2018 and to rise to 1.25% by quarter 1 2021.
Bank Rate forecasts for financial year ends (March) are:

- 2017/18 0.50%
- 2018/19 0.75%
- 2019/20 1.00%
- 2020/21 1.25%

The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year are as follows:

- 2017/18 0.40%
- 2018/19 0.60%
- 2019/20 0.90%
- 2020/21 1.25%

The overall balance of risks to these forecasts is currently probably slightly skewed to the upside and are dependent on how strong GDP growth turns out, how quickly inflation pressures rise and how quickly the Brexit negotiations move forward positively.

Investment treasury indicator and limit - total principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Council is asked to approve the treasury indicator and limit: -

Maximum principal sums invested > 365 days			
£m	**2018/19**	**2019/20**	**2020/21**
Principal sums invested > 365 days	£6m	£6m	£6m

Icelandic bank investments

The Council placed a deposit of £1,250,000 on 25th September 2008 with the Heritable Bank which is a subsidiary of Landsbanki, one of the Icelandic Banks that was affected by the world economic crisis. Of this amount £1,227,517 (98%) has already been repaid to the Council by the Administrators. As at today, the Council has £22,483 frozen in the Heritable Bank.

At the time the deposit was placed, the risk rating of Heritable was 'A' (long term deposits) and F1 (short term deposits). Both ratings indicated low risk and were within the deposit policy approved by the Council. Heritable Bank is registered in Scotland with an address in Edinburgh. Heritable Bank Plc is authorised and regulated by the Financial Services Authority and is on the FSA Register. The bank's shares are owned by Icelandic bank, Landsbanki.

Administrators have kept the bank trading and are winding down the business over a period of years. The Administrators have paid fifteen dividends amounting to 98% of the original deposit. The timescale for receiving the final amount outstanding has not been confirmed. The administrators estimate that the return to all unsecured creditors is now between 98-100 pence in the pound.

End of year investment report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

APPENDIX D

Treasury Management Practice (TMP1) – Credit and Counterparty Risk Management

Specified investments – These investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. These are considered low risk assets where the possibility of loss of principal or investment income is small. These would include sterling investments which would not be defined as capital expenditure with:

1. The UK Government (such as the Debt Management Account deposit facility, UK treasury bills or a gilt with less than one year to maturity).
2. Supranational bonds of less than one year's duration.
3. A local authority
4. Pooled investment vehicles (such as money market funds) that have been awarded a high credit rating by a credit rating agency.
5. A body that is considered of a high credit quality (such as a bank or building society)

Non-specified investments: These are any investments which do not meet the Specified Investment criteria.

CCLA Property Fund investment will be the Council's only Non-Specified Investment and there is a limit of £2 million for this asset class.

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories.The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

	Minimum credit criteria / colour band	**Max % of total investments / £ limit per institution**	**Max. maturity period**
DMADF – UK Government	N/A	100%	6 months
Money Market Funds	AAA	£6 million	Liquid
Ultra Short Dated Bond Funds	AAA	£6 million	T + 2
Local authorities	N/A	£6 million	5 years
Property Investment Funds – CCLA	N/A	£2 million	No fixed maturity date but will generally be up to 7 years

Term deposits with banks and building societies	Yellow	£6 million (£7 million for Lloyds plc – see note)	Up to 5 years
	Purple		Up to 2 years
	Blue		Up to 1 Year
	Orange		Up to 1 Year
	Red		Up to 6 months
	Green		Up to 100 days
	No Colour		Not for use
The Council is not recommending using the following investment vehicles and this is reflected by showing 0% against the limit per institution.			
UK Government gilts	AAA	0%	Yellow (5 years)
UK Government Treasury bills	AAA	0%	6 months
Bonds issued by multilateral development banks	AAA	0%	Yellow (5 years)
CDs or corporate bonds with banks and building societies	Yellow	0%	Up to 5 years
	Purple		Up to 2 years
	Blue		Up to 1 year
	Orange		Up to 1 year
	Red		Up to 6 months
	Green		Up to 100 days
	No colour		Not for use

SPECIFIED INVESTMENTS:

All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum 'high' rating criteria where applicable

	Minimum 'High' Credit Criteria	Use
Debt Management Agency Deposit Facility	-	In-house
Term deposits – local authorities	-	In-house
Term deposits – banks and building societies	Green	In-house

Term deposits with nationalised banks and banks and building societies

	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
Lloyds Bank plc*	Blue	In-house	£7 million	Up to 1 year
Other UK part nationalised banks	Blue	In-house	£6 million	Up to 1 year

Collective Investment Schemes structured as Open Ended Investment Companies (OEICs): -		
1. Government Liquidity Funds	MMF Rating	In-house
2. Money Market Funds	MMF Rating	In-house
3. Ultra Short Dated Bond Funds	EMMF	In-house

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

A Guide to Money Market Funds	
Definition	A pool of cash managed by an independent fund management company. Frequently these are well known banks or investment houses
Investment	Investors purchase units (shares) of the fund which are held on their behalf in a custody account.
Returns	Returns in line with either 7-day or 1-month LIBID are targeted by most funds.
Liquidity	The funds are very liquid. Shares can be purchased and sold on the same day if necessary and without penalty. Deals are subject to a cut-off time which varies from manager to manager but can be as late as 2pm.
Variety	Two types of classes exist – 1) Stable Net Asset Value (SNAV) – the most common variety. Prices are fixed and interest is credited to investors in the form of a dividend. 2) Accumulating Net Asset Value (ANAV) – interest is credited to the shares and the price rises to reflect the return achieved.
Accounting	Purchases of MMF shares do not score as capital expenditure. Sales do not score as capital receipts.
Legality	Local authorities are permitted to invest in sterling denominated funds with an AAA credit rating and domiciled in the EU.
Regulation	UK-based Funds are regulated by the Financial Services Authority. Those domiciled in other EU zones (the majority) are regulated via the Undertakings for Collective Investment in Transferable Securities (UCITS) Code. The Code lays down strict common standards of investment and management.
Portfolio holdings	Cash is invested in a selection of high quality, high liquidity securities including: time deposits, certificates

	of deposit, short-dated gilts, corporate bonds and notes, commercial paper etc.
Credit rating	Local authorities are empowered to place funds in investment schemes with a high credit rating. Money Market Funds fall into this category and are all rated by one or more of the three rating agencies. Credit Quality – measures the financial strength of the fund (not the manager) and the probability of it defaulting.
Risk management	The funds eligible for local authority investment score highly on credit quality and low volatility. All have an AAA rating which means that the chances of default are considered minimal. 1) Rating requirements – in order to maintain an AAA rating fund managers must adhere to requirements specified by the rating agencies. These include: • A maximum exposure to any one counterparty (concentration ratio) between 5% & 10% • A maximum weighted average maturity (WAM) for the entire fund – typically 60 days • A minimum level of overnight investments to ensure high liquidity • A lower limit on quality of investment counterparty 2) Ring fencing – monies received from share purchases are invested in financial instruments by the managing organisation. Deposits/security investments are held in custody by a non-related company that specialises in custody services. Counterparty exposure of the fund (and of the investor) is to the underlying securities and not to the management company.
Exposure limits	In view of the funds' low concentration ratios; quality of asset holdings; maximum WAM and ring-fencing arrangements, counterparty risk is spread widely. MMFs possess the same status as external fund managers operating cash/gilt funds for local authorities. They should have their own counterparty limit which can be considerably greater than that accorded to individual investment counterparties.

COUNTERPARTY LIST

APPENDIX E

Counterparty as at 16th Feb 2018		Fitch Rating						Moody's Ratings				S&P Ratings			
United Kingdom		Long Term		Short Term	Viability	Support		Long Term		Short Term		Long Term		Short Term	Suggested Duration
	Collateralised LA Deposit*														Y - 60 mths
	Debt Management Office														Y - 60 mths
	Multilateral Development Banks														Y - 60 mths
	Supranationals														Y - 60 mths
	UK Gilts														Y - 60 mths
Banks	Abbey National Treasury Services	PW	A	F1			1	SB	Aa3		P-1				R - 6 mths
Banks	Bank of Scotland PLC	SB	A+	F1	a		5	SB	Aa3		P-1	PO	A	A-1	R - 6 mths
Banks	Barclays Bank PLC	PW	A	F1	a		5	NO	A1		P-1	SB	A	A-1	R - 6 mths
Banks	Close Brothers Ltd	SB	A	F1	a		5	SB	Aa3		P-1				R - 6 mths
Banks	Goldman Sachs International Bank	SB	A	F1				SB	A1		P-1	SB	A+	A-1	R - 6 mths
Banks	HSBC Bank PLC	SB	AA-	F1+	a+		1	NO	Aa3		P-1	SB	AA-	A-1+	O - 12 mths
Banks	Lloyds Bank Plc	SB	A+	F1	a		5	SB	Aa3		P-1	PO	A	A-1	R - 6 mths
Banks	Santander UK PLC	PW	A	F1	a		2	SB	Aa3		P-1	SB	A	A-1	R - 6 mths
Banks	Standard Chartered Bank	SB	A+	F1	a		5	SB	A1		P-1	SB	A	A-1	R - 6 mths
Banks	Sumitomo Mitsui Banking	SB	A	F1			1	SB	A1		P-1	SB	A	A-1	R - 6 mths
Banks	UBS Ltd.	SB	AA-	F1+			1	SB	A1		P-1	SB	A+	A-1	O - 12 mths
Building Societies	Coventry Building Society	SB	A	F1	a		5	SB	A2		P-1				R - 6 mths
Building Societies	Leeds Building Society	SB	A-	F1	a-		5	SB	A3		P-2				G - 100 days
Building Societies	Nationwide Building Society	NO	A+	F1	a		5	SB	Aa3		P-1	SB	A	A-1	R - 6 mths
Building Societies	Skipton Building Society	SB	A-	F1	a-		5	SB	Baa1		P-2				G - 100 days
Building Societies	Yorkshire Building Society	SB	A-	F1	a-		5	SB	A3		P-2				G - 100 days
Nationalised and Part Nationalised Banks	National Westminster Bank	PW	BBB+	F2	bbb+		5	PW	A2		P-1	PO	BBB+	A-2	B - 12 mths
Nationalised and Part Nationalised Banks	Royal Bank of Scotland Group Plc	SB	BBB+	F2	bbb+		5	SB	Baa3		P-3	SB	BBB-	A-3	B - 12 mths
Nationalised and Part Nationalised Banks	The Royal Bank of Scotland Plc	SB	BBB+	F2	bbb+	PW	5	NW	A2	NW	P-1	SB	BBB+	A-2	B - 12 mths

Key

Watches and Outlooks		Duration	
SB	Stable Outlook	Yellow - Y	60 Months
NO	Negative Outlook	Blue - B	12 Months
NW	Negative Watch	Orange - O	12 Months
PO	Positive Outlook	Red - R	6 Months
PW	Positive Watch	Green - G	100 Days
EO	Evolving Outlook		
EW	Evolving Watch		

APPENDIX F

Treasury Management Scheme of Delegation

Full Council:

- Receiving and reviewing reports on treasury management policies, practices and activities
- Approval of annual strategy
- Approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices
- Budget consideration and approval
- Approval of the division of responsibilities
- Receiving and reviewing regular monitoring reports and acting on the recommendations
- Approving the selection of external service providers and agreeing terms of appointment

The treasury management role of the Section 151 Officer:

- Recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- Submitting regular treasury management policy reports
- Submitting budgets and budget variations
- Receiving and reviewing management information reports
- Reviewing the performance of the treasury management function
- Ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- Ensuring the adequacy of internal audit, and liaising with external audit
- Recommending the appointment of external service providers
- To ensure that members with responsibility for treasury management receive adequate training in treasury management.
- Te review the training needs of treasury mangement officers periodically

GLOSSARY OF TERMS

Basis Point
1/100th of 1%, i.e., 0.01%

Base Rate
Minimum lending rate of a bank or financial institution in the UK

Benchmark
A measure against which the investment policy or performance of a fund manager can be compared

Bill of Exchange
A financial instrument financing trade

Callable Deposit
A deposit placed with a bank or building society at a set rate for a set amount of time. However, the borrower has the right to repay the funds on pre-agreed dates, before maturity. This decision is based on how market rates have moved since the deal was agreed. If rates have fallen, the likelihood of the deposit being repaid rises, as cheaper money can be found by the borrower

Cash Fund Management
Fund management is the management of an investment portfolio of cash on behalf of a private client or an institution, the receipts and distribution of dividends and interest, and all other administrative work in connection with the portfolio

Certificate of Deposit (CD)
Evidence of a deposit with a specified bank or building society repayable on a fixed date. They are negotiable instruments and have a secondary market; therefore the holder of a CD is able to sell it to a third party before the maturity of the CD

Commercial Paper
Short-term obligations with maturities ranging from 2 to 270 days issued by banks, corporations and other borrowers. Such instruments are unsecured and usually discounted, although some may be interest bearing

Corporate Bond
Strictly speaking, corporate bonds are those issued by companies. However, the term is used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies

Counterparty
Another (or the other) party to an agreement or other market contract (e.g., lender/ borrower/writer of a swap, etc)

CPI
Consumer Price Index – calculated by collecting and comparing prices of a set basket of goods and services as bought by a typical consumer, at regular intervals over time.

CDS
Credit Default Swap – a swap designed to transfer the credit exposure of fixed income products between parties. The buyer of a credit swap receives credit protection, whereas the seller of the swap guarantees the credit worthiness of the
product. By doing this, the risk of default is transferred from the holder of the fixed income security to the seller of the swap

Derivative
A contract whose value is based on the performance of an underlying financial asset, index or other investment, e.g., an option is a derivative because its value changes in relation to the performance of an underlying stock.

DMADF
Deposit Account offered by the Debt Management office, guaranteed by the UK government

ECB
European Central Bank – sets the central interest rates in the EMU area. The ECB determines the targets itself for its interest rate setting policy; this is to keep inflation within a band of 0 to 2%. It does not accept that monetary policy is to be used to manage fluctuations in unemployment and growth caused by the business cycle

EMU
European Monetary Union

Equity
A share in a company with a limited liability. It generally enables the holder to share in the profitability of the company through dividend payments and capital gain

Fed.
Federal Reserve Bank of America – sets the central rates in the USA

Floating Rate Notes
Bonds on which the rate of interest is established periodically with reference to short-term interest rates

Forward Deal
The act of agreeing today to deposit funds with an institution for an agreed time limit, on an agreed future date, at an agreed date

Forward Deposits
Same as forward dealing (above)

FSA (Financial Services Authority)
Body responsible for overseeing financial services

Fiscal Policy
The Government policy on taxation and welfare payments

Gilt
Registered British Government securities giving the investor an absolute commitment from the government to honour the debt that those securities represent

Gilt Funds
Pooled fund investing in bonds guaranteed by the UK government

Money Market Fund (MMF)
A well rated, highly diversified pooled investment vehicle whose assets mainly comprise of short term instruments. It is very similar to a unit trust, however in a MMF

Monetary Policy Committee (MPC)
Government body that sets the bank rate (commonly referred to as being base rate). Their primary target is to keep inflation within plus or minus 1% of a central target of 2.5% in two year's time from the date of the monthly meeting of the Committee. Their secondary target is to support the Government in maintaining high and stable levels of growth and employment

Open Ended Investment Companies
A well diversified pooled investment vehicle, with a single purchase price, rather than a bid/offer spread

Other Bond Funds
Pooled funds investing in a wide range of bonds

Reverse Gilt Repo
This is a transaction as seen from the point of view of the party which is buying the gifts. In this case, one party buys gifts from the other and, at the same time and as part of the same transaction, commits to resell equivalent gifts on a specified future date, or at call, at a specified price

Retail Price Index (RPI)
Measurement of the monthly change in the average level of prices at the retail level weighted by the average expenditure pattern of the average person

Sovereign Issues (Ex UK Gilts)
Bonds issued or guaranteed by nation states, but excluding UK government bonds

Supranational Bonds
Bonds issued by supranational bodies, e.g., European investment bank. These bonds – also known as Multilateral Development Bank bonds – are generally AAA rated and behave similarly to gilts, but pay a higher yield ("spread") given their relative illiquidity when compared with gilts

Term Deposit
A deposit held in a financial institution for a fixed term at a fixed rate

Treasury Bill
Treasury bills are short term debt instruments issued by the UK or other governments. They provide a return to the investor by virtue of being issued at a discount to their final redemption value

WARoR
Weighted Average Rate of Return is the average annualised rate of return weighted by the principal amount in each rate

WAM
Weighted Average Time to Maturity is the average time, in days, till the portfolio matures, weighted by principal amount

WATT
Weighted Average Total Time is the average time, in days, that deposits are lent out for, weighted by principal amount

APPENDIX H

Briefing Note on CCLA Investment Options

Recommendation:

It is recommended to Council:

1. That the total sum of £1,500,000 from the Council's treasury management funds is invested in CCLA's (CCLA Investment Management Limited's) Local Authorities Property Fund (LAPF) and its Diversified Income Fund (DIF) as detailed in section 4.1 of this Appendix H.

1.0 Executive Summary

1.1 This report sets out the rationale for the recommendation of investing £1m into the CCLA DIF and £0.5m into the CCLA LAPF.

1.2 Combined, these investments could generate an additional £51k pa in additional investment income, based on current interest rates. In the first year the entry costs to the fund would need to be absorbed so this benefit won't start be realised until the second year e.g. 2019/20 onwards.

2.0 Background

CCLA – Investment Services for Churches, Charities & Local Authorities

2.1. A variety of investment instruments are available to the Local Authority market. In addition to the notice accounts and fixed term deposits available from UK and overseas banks, it is also possible for the Council to invest, for example, in UK Government Gilts, bond funds and property funds. These alternative instruments would either require the Council to tie up its cash for significantly longer periods, thus reducing liquidity, or would carry a risk of loss of capital if markets go down. The Council's policy in the past, therefore, has been not to invest in these slightly more risky and less liquid forms of investment.

2.2. However, a variety of factors suggest that now may be an appropriate time to reconsider that approach, e.g.:

(a) The perception of increased risk in bank deposits.

(b) A growing UK economy that could support a more positive outlook for other forms of investment.

(c) A challenging budget outlook that would benefit from the influx of additional investment income.

2.3. Officers have therefore considered a variety of different forms of investment and have concluded that investment in to CCLA represents a balanced investment opportunity, splitting investment in to CCLA's two funds – the LAPF, which invests in UK Property and the DIF, which invests in global distributed investments. The latter pays dividends earned from revenue income generated from cash, AAA or BBB short-dated bonds and diverse investments in things such as energy / renewables, aircraft leasing, student accommodation, care homes, and some property.

2.4. **LAPF**

The CCLA (Churches, Charities and Local Authorities) Local Authority Property Fund has been specifically set up for local authorities, and currently has investments of over £933 million, with over 166 local authority investors including 9 county councils, 7 metropolitan councils/London boroughs and over 40 unitary and district councils. Devon County Council, Plymouth City Council, West Devon Borough Council and four Devon town councils are invested in the Fund. The fund own and operate 62 commercial properties across the UK, across various sectors with many having blue-chip tenants. By investing in this fund, South Hams would be able to diversify is risk exposure across the UK and multiple property types and sectors, generating a yield significantly higher than that generated by current treasury management investments, which averaged around 0.6% in the past 12 months.

2.5. The income yield over the course of the investment is likely be around 4-5%, significantly above the rates available for term deposits with banks. The income yield will vary from year to year, but tends to be within a fairly narrow range – the 12 months to Dec 2017 averaged a net income (after management costs) of 4.58%. A £500k investment would have the potential to yield £21k additional investment income in its first full year to help offset the budget pressures facing the Council.

2.6. However, there are risks that should not be discounted. The capital value of property can go down as well as up, and therefore the capital redeemed at the end of the investment could be less than the sum initially invested. There are also charges that would need to be met; there is a bid offer spread of 8.3%, so the initial value of the fund will be lower than the initial amount invested. The Annual Management Charge is 0.65% of the net asset value of the Fund and is charged against income before any income distribution is made. These factors combined mean that any investment needs to be held for a minimum of 5 years, and capital growth would need to be around 2% per year to ensure that the capital redeemed at the end of the investment is at least equal to the initial amount invested. The investment can be redeemed at any time, but it may take 3 to 4 months from the time that the redemption request was made for CCLA to liquidate sufficient holdings in order to return the funds. If the Council only invested £500k, in normal market conditions it is likely that this could be returned to the Council within one month of the request.

2.7 It should be noted that the charges above are similar to those that the Council would incur if it were to buy residential property. Stamp duty on an investment property is 5%, whilst agents fees on disposal, legal fees on acquisition and disposal and ongoing management fees for the property would equate (or even exceed) the above costs. The management charge of 0.65% is lower than most typical investment bonds / pension funds, which typically charge 0.75% as an annual fee.

2.8. Appendix A shows a CCLA LAPF Fact Sheet. Further details about CCLA can be found at www.ccla.co.uk Investments into this fund do not count as capital expenditure and dividends are treated as revenue income. The Council could invest and then sell at a later date and this means not only does the Council obtain regular returns (Paid quarterly), it also has the potential to benefit from an increase in "capital" value.

2.9. The potential return of 4.58% is approximately 7.6 times higher than the forecast treasury management return. In 2017/18, the average current return achieved was approx. 0.6%.

2.10 **DIF**

The DIF is a newer fund and is available to a wider pool of investors (whereas the LAPF is only available to Local Authorities). It was launched in late 2016 and so far has £74m in managed funds. There are 10 Local Authority investors, including one county and four boroughs / districts. The minimum investment is £1m and on average the fund has generated a dividend yield, after management costs of 3%.

2.11 The lower return is due to the inherent lower risk appetite of the fund, with strict rules in place to ensure that at any time ,the maximum exposure to equities is 40%. Due to the nature of the investors, Churches, Charities & Local Authorities, all investments are closely scrutinised to ensure no investor would be embarrassed by inappropriate acquisitions or investments. The fund place a significant proportion of its managed funds in short dated bonds and cash instruments, meaning that withdrawals from the scheme are more liquid than the LAPF fund. With this in mind, the bid/offer spread is far lower, at 0.44%.

2.12 Like the LAPF, the scheme accepts revenue investments and on exit, revenue will be returned to the local authority. All dividends are paid as revenue income. This is one of the fundamental reasons why the CCLA investment is being proposed, and why CCLA is popular with Local Authorities as an investment opportunity.

2.13 A minimum £1m investment would generate annual returns of c£30k based on the current 3% yield, after the initial cost of acquisition. Appendix B shows a CCLA DIF Brochure. Further details about CCLA can be found at www.ccla.co.uk

2.14 In 2017/18 the average return on investments was 0.6%.The DIF yield of 3% is 5 times higher.

3.0 **Options available and consideration of risk**

3.1. Members could opt to follow the recommendation or invest a higher or lower sum. Alternatively, Members could opt to pursue an alternative investment strategy. Investment into the LAPF should only be considered if the investment can be maintained for a medium – long term, i.e. 5 years minimum. If the investment needs to be liquidated before that timeframe, it is highly possible that the sum returned would be less than the sum originally invested.

3.2. The DIF is not subject to the same bid/offer spread and therefore is more liquid as the LAPF and therefore this investment will be easier to liquidate if the Council choose to divest. Based on this difference and taking a balanced risk approach, it is recommended that Members agree to invest £1m into the DIF (averaging 3% dividend yield pa) and £0.5m into the LAPF (averaging a 4.58% dividend yield).Assuming dividend rates stay roughly stable, investing at these sums would generate an additional £51k pa for the Council.

3.3. The Council has for many years adopted a very cautious and prudent approach to treasury management. Lending has only been made to banks and building societies which have strong credit limits and meet the criteria set by the Council, using information published by the three major credit rating agencies. This policy has been maintained in the knowledge that putting security before liquidity or yield does impact on the income being generated from these investments.

3.4. Officers have consulted with two other local authorities who have already invested into the LAPF and one who has invested in the DIF. All suggested they were very happy to recommend investment.

3.5. The DIF itself is inherently more liquid than the LAPF as it reflects the underlying assets not being solely invested in property, there are established markets for equities and bonds.

3.6. In the Members' Budget Survey, 58% supported an investment, with 16% undecided.

4.0 Proposed Way Forward

4.1. It is proposed that if the Council approve this report's recommendations, officers invest the £500,000 into CCLA LAPF and £1m into CCLA DIF after 1 April 2018. These investments would be monitored as part of the treasury management function, but it is anticipated that the investment would be left to generate income for a minimum of five years. Balancing the investment across these two funds will help create a more diversified, risk managed fund for the Council in addition to the other funds it already manages.

5.0 Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/ Governance	Y	The Treasury Management Strategy Statement (TMSS) for 2018/19, set out the Council's investment priorities as being: • Security of capital; • Liquidity; and • Yield.

		The Council aims to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with highly credit rated financial institutions, using our suggested creditworthiness approach, including a minimum sovereign credit rating, and Credit Default Swap (CDS) overlay information. The Treasury Management Strategy is risk averse with no investments allowed for a period of more than a year and very high credit rating are required together with a limit of £3m per counterparty. The TMSS has been updated accordingly for the recommended CCLA investments. Agreeing to invest in the CCLA fund requires Council approval.
Financial	Y	An investment in to CCLA will represent an increased risk of loss of capital in comparison to the use of term deposits with banks and building societies. Such an investment has the potential to provide a significant increase in investment income that could contribute towards the predicted budget gaps highlighted in the Medium Term Financial Strategy. If there is a downward valuation in the CCLA investment in 2018/19, the decrease would be an expense to the Income and Expenditure Account of the Council, as the Available for Sale Reserve is not available in 18/19, due to a change in the Accounting Code of Practice. This could be significant, for example a 10% drop in the valuation of the £1.5 million investment at the year end would mean a charge to the Income and Expenditure Account of £150,000 in that year. Therefore this would affect the 'bottom line' of the Council adversely by £150,000. This is due to IFS9 as explained in Section 6 of the covering report.

		The converse is true - in that if the valuation increased, a gain would be realised in the Income and Expenditure Account. So the Council would see extra income in its Revenue Outturn for that year.
Risk	Y	The security risk is the risk of failure of a counterparty. The liquidity risk is that there are liquidity constraints that affect interest rate performance. The yield risk is regarding the volatility of interest rates/inflation. The Council has adopted the CIPFA Code Of Practice for Treasury Management and produces an Annual Treasury Management Strategy and Investment Strategy in accordance with CIPFA guidelines. The Council engages a Treasury Management advisor and a prudent view is always taken regarding future interest rate movements. See the risk of fluctuations in the valuation of the investment in the 'financial' section. Investment interest income is reported quarterly to SLT and the Executive.
Comprehensive Impact Assessment Implications		
Equality and Diversity	N	N/A
Safeguarding	N	N/A
Community Safety, Crime and Disorder	N	N/A
Health, Safety and Wellbeing	N	N/A
Other implications	N	N/A

<u>Supporting Information</u>

Appendices:
Appendix I – CCLA LAPF Fund Fact Sheet
Appendix J – CCLA DIF Brochure

The Local Authorities' Property Fund

Fund Fact Sheet – 31 December 2017

Investment objective

The Fund aims to provide investors with a high level of income and long-term capital appreciation.

Investment policy

The Fund is an actively managed, diversified portfolio of UK commercial property. It will principally invest in UK commercial properties, but may invest in other assets.

Suitability

The Fund is suitable for the long-term funds of any local authority seeking exposure to UK commercial property.

Independent Governance

The trustee is the Local Authorities' Mutual Investment Trust (LAMIT) a body controlled by members and officers appointed by the Local Government Association, the Convention of Scottish Local Authorities, the Northern Ireland Local Government Officers' Superannuation Committee and investors in the Fund.

Who can invest?

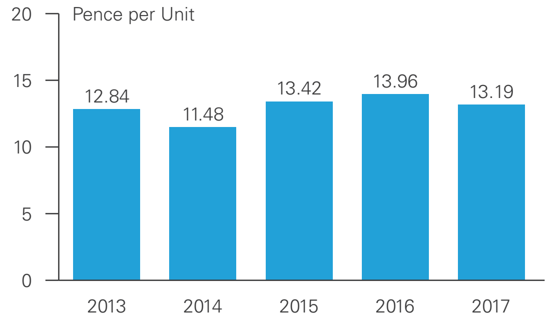
Any local authority in England, Wales, Scotland and Northern Ireland.

Income

Gross dividend yield	4.58%*
AREF/IPD™ Other Balanced Property Fund Index yield	3.58%
Official Bank Rate	0.50%

* Based upon the net asset value and historic gross annual dividend of 13.7122p

Rolling 12 month distributions to 31st March:



Unique accounting advantages

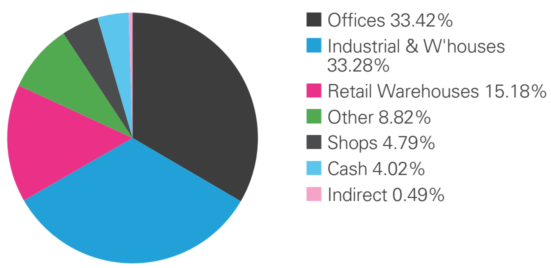
Unlike other property fund investments or even direct property purchases, investment in the Fund does not count as capital expenditure for English or Scottish local authorities. Dividends are treated as revenue but the General Fund is protected from fluctuations in the unit price. The investment is treated as an available for sale financial asset.

Fund update

The prime focus of our investment strategy is on asset selection and management. We try to identify assets which, through active management, can make a significant contribution to total returns and to the income payment to investors. We also bias the subsector weightings to reflect our view of their relative attractiveness. At present, this means a relatively high weighting to industrial and office assets and a relatively low weighting to retail, with no shopping centre or supermarket holdings.

The Fund has continued to enjoy a strong inflow of new money. Reflecting these cash receipts and the wish to avoid a drag on returns from unwanted cash holdings, the focus of activity has been on acquisitions; five properties have been bought. These include two hotels, one on the outskirts of the City of London, the other in Brighton. The initial yields on both are under 4%, but rents are RPI based and the leases are long, 31 years in both cases. We have also bought three industrial warehouse investments, in Milton Keynes, Northampton and Bolton. Total expenditure has amounted to £127m, with another purchase expected to complete shortly. There was one sale, of a small retail asset, the proceeds were materially above valuation. Rent reviews made a positive contribution to income but these were being offset by the temporary rental loss from refurbishment work, such as in Kingsway. At the end of the quarter the void rate was 7.6%, similar to the level at the end of September and significantly below that of the market.

Asset allocation



The Fund has credit facilities which, at quarter end, were not utilised.

Discrete year total return performance (net)

12 months to 31 December	2017	2016	2015	2014	2013
The Local Authorities' Property Fund	+9.68%	+2.12%	+14.09%	+19.50%	+8.92%
Benchmark	+10.58%	+3.66%	+12.97%	+17.34%	+9.25%

Annualised total return performance (net)

Performance to 31 December 2017	1 year	3 years	5 years
The Local Authorities' Property Fund	+9.68%	+8.52%	+10.71%
Benchmark	+10.58%	+9.00%	+10.67%

Benchmark AREF/IPD™ Other Balanced Property Fund Index. Net performance shown after management fees and other expenses. Past performance is no guarantee of future returns. Source: CCLA

Top ten property holdings – total 37.28%

London, Kingsway
London, Goodman's Yard
London, Stockley Park, Longwalk
London, Beckton Retail Park
Bracknell, The Arena
Elstree, Centennial Park
Bristol, Gallagher Retail Park
Brighton, West Street
Cambridge, Cambridge Science Park
Bolton, Wingates Industrial Estate

Key facts

Total fund size	£931m
Current borrowing	£0m
Number of holdings	62

	Income units
Offer (buying) price	319.44p (xd)
Net asset value	299.24p (xd)
Bid (selling) price	294.60p (xd)

Launch date	18 April 1972
Unit types	Income
Minimum initial investment	£25,000
Minimum subsequent investment	£10,000
Dealing day	Month end valuation day*
Sedol & ISIN numbers	0521664, GB0005216642
Dividend payment dates	End January, April, July & October
Annual management charge (taken 100% from income)	0.65%

* Instructions for the issue or redemption of units must be received by CCLA no later than 5pm on the business day prior to the Valuation Date. If the valuation day is a bank holiday, the dealing day will be the previous working day. Units are only realisable on each monthly dealing date and redemptions may not be readily realisable; a period of notice not exceeding six months may be imposed for the redemption of units.

Tax reclaims should be addressed to: Glynis Free, Specialist Repayment Team 7 South, Ty - Glas, Cardiff, CF14 8HR.
Telephone 03000 580618, 9.30am - 1pm.

Risk Warning

This document is a financial promotion and is issued for information purposes only. It does not constitute the provision of financial, investment or other professional advice. CCLA have not considered the suitability of this investment against your individual needs and risk tolerance. To ensure you understand whether our product is suitable, please read the Fund Factsheet document and the Scheme Particulars. We strongly recommend you seek independent professional advice prior to investing. Investors should consider the following risk factors identified as specific to the Fund before investing: Counterparty/Tenant/Credit Risk (financial institution/tenants may not pay), Market Risk (investment value affected by market conditions), Operational Risk (general operational risks), Expiry/Maturity Profile (timing of maturity of tenancies), Liquidity Risk (investment in non-readily realisable assets), Interest Rate risk (changes to interest rate affecting income), Concentration Risk (need for diversification and suitability of investment), Business Risk (possibility of lower than anticipated profits). Please see the Fund Scheme Particulars for further details.

Disclosure

Investment in the Fund is for Eligible Local Authorities only. Past performance is not an indicator of future performance. The value of investments and the income derived from them may fall as well as rise. Investors may not get back the amount originally invested and may lose money. Any forward-looking statements are based upon our current opinions, expectations and projections. We undertake no obligations to update or revise these. Actual results could differ materially from those anticipated. Investments in the Fund and the Fund itself are not covered by the Financial Services Compensation Scheme (FSCS). However, the Manager may pay fair compensation on eligible claims arising from its negligence or error in the management and administration of the Fund. The Fund is an Alternative Investment Fund and an Unregulated Collective Investment Scheme established under a Scheme approved by H M Treasury under Section 11 of the Trustee Investments Act 1961 and is subject to provisions of a Trust Deed dated 6 April 1972 and a supplemental Trust Deed dated 13 September 1978. The Fund operates as an open-ended Fund under Part IV of the schedule to the Financial Services and Markets Act 2000 (Exemption) Order 2001. CCLA Fund Managers Limited (registered in England No. 8735639 at the office below) is authorised and regulated by the Financial Conduct Authority and is the manager of the Local Authorities Property Fund.

Senator House | 85 Queen Victoria Street | London | EC4V 4ET | Freephone: 0800 022 3505 | www.ccla.co.uk

DIVERSIFIED INCOME FUND

Designed to provide an attractive immediate income with rising income and higher capital values over time

CCLA

DIVERSIFIED INCOME FUND

Designed to provide an attractive immediate income with rising income and higher capital values over time.

The need for an alternative to cash deposits

Interest rates are expected to remain at very low levels for the foreseeable future. In contrast, inflation is forecast to rise, the increase accelerated by the sharp fall in the value of the pound. For cash investors higher inflation permanently reduces the real value of both income and capital.

Even in a less damaging environment cash is a poor choice for longer term investments. Returns are limited to the repayment of the original investment and a modest income which fluctuates in line with short term interest rates and which can never truly grow.

As well as poor returns cash investors also face higher risks following the introduction of the Bank Recovery and Resolution Directive. In times of crisis there is now the risk of 'bail-in', with the threat both to income and capital.

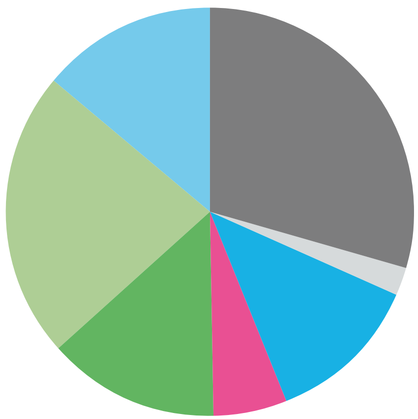
Investors seeking stronger returns therefore have to look beyond cash deposits – but which assets should they choose? History shows us that asset choice is the most important contributor to long-term performance and so making the wrong choice can have unexpected and unwanted effects on values. For those investors seeking improved returns and for whom risk control is essential, the prudent path is to take a portfolio approach, holding not one, but many assets and actively changing the blend to reflect evolving conditions.

A carefully constructed diversified portfolio spreads risk efficiently by investing in a range of assets whose characteristics complement each other, creating a balance of risk and return no single asset class fund can give. The result is that for any given level of return, volatility – the exposure to the day to day fluctuations in values – is consistently lower. The Diversified Income Fund has been structured with this lower volatility as one of its key aims.

The asset universe – a wide range of opportunity

The Fund can invest in a wide range of assets, actively changing the allocation to reflect the expected economic environment. The list of available assets is long and varied and includes conventional choices such as property and equities in the UK and overseas but the less common too, such as infrastructure, with three main areas of focus – civil (toll roads, ports and similar), social (such as care and nursing homes, doctors' surgeries and student accommodation), environmental and energy-related (including new forms of energy generation and efficiency, forestry and renewables). These should provide an attractive income and when combined with holdings in equities and bonds, a powerful source of risk diversification.

ASSET ALLOCATION



Source: CCLA as at 31 March 2017

An attractive income, rising over time

The only true sources of a growing income are real assets such as equities and property which are directly linked to rising activity in the economy. In contrast, income from fixed interest investments does not change whilst yields on cash can vary but do not rise on a consistent basis. The key to achieving an attractive and dependable income is therefore to combine the right asset mix with top quality individual holdings which are themselves able to support higher income payments in the future.

Responsible investment, an integral part of the process

We avoid companies with high governance risks because poor governance can destroy value and cause lasting reputational damage for all concerned. We seek to avoid investing in companies with the poorest governance, whilst in others, where we identify risks, we work to reduce them. We support these policies with an active voting programme. We believe that responsible investment supports returns and reduces the risks which conventional financial analysis cannot see.

A pooled fund approach, the sensible choice

Using a pooled fund has a number of important advantages for investors. It brings a consistent approach to fund management across all the assets in the portfolio, ensuring that structure, strategy and tactics are always consistent. Within the portfolio costs are better controlled, whilst charges are kept down. Administration is efficient with a single investment report providing transparency to reporting that multiple asset exposures simply do not have.

ABOUT THE FUND

Objective

The Fund aims to provide income and the potential for capital growth over the long-term from an actively managed diversified portfolio.

Distribution dates

Income will be distributed quarterly at the end of February, May, August and November to investors holding units on the last day of the preceding December, March, June and September.

Minimum subscription

The minimum initial investment is £1 million. The minimum additional investment is £25,000.

Fees

The Annual Management Charge (AMC) is 0.60%, the estimated Ongoing Charges Figure (OCF) is 0.75%. For investors which acquire units before the 31st March 2018 there will be a discount of 0.15% on the AMC which expires on the 31st March 2019.

The OCF includes our fees and is the total cost of managing your investments.

Spread

The Fund has no entry or exit charges and is single priced with a dilution levy. The rate or amount of the dilution levy will depend on the mix of assets in the relevant sub-fund and the transaction costs applying to them. In respect of the Fund, the estimated dilution levy charged by the ACS Manager based on future projections will be between 0% and 1.5% of the price of a unit, this charge arising on all deals. It is therefore not possible to predict the dilution levy accurately. In such circumstances if a dilution levy is not made then this may restrict the future growth of the sub-fund(s).

Dealing

Daily. Settlement proceeds will usually be paid within two working days after trade date.

Structure

The Fund is a sub-fund of the CCLA Authorised Contractual Scheme (ACS) and is a NURS.

The CCLA Authorised Contractual Scheme is an FCA regulated tax transparent fund which has been constituted as a co-ownership scheme. As a consequence of this the Fund will be treated as tax transparent for the purpose of income and/or gains by the relevant tax authorities. Each investor should take appropriate professional advice as to the tax treatment of their investment in the Fund.

A NURS is a Non-UCITS Retail Scheme, in accordance with the FCA Rules, an authorised fund which is neither a UCITS scheme nor a qualified investor scheme.

Depositary and Custodian

HSBC Bank Plc, 8 Canada Square, London EC14 5HQ

ACS Manager

CCLA Fund Managers Limited, Senator House, 85 Queen Victoria Street, London EC4V 4ET.

Investment Manager

CCLA Investment Management Limited, Senator House, 85 Queen Victoria Street, London EC4V 4ET.

Eligible Investors

As the Fund is an ACS, it is only marketable to Eligible Investors.

These are investors who are UK tax resident and also one of the following:

(a) A professional ACS investor (being a person who is a professional client for the purpose of the Markets in Financial Instruments Directive);

(b) A large ACS investor (being a person who in exchange for units makes a payment of not less than £1 million or contributes property with a value of not less than £1 million);

(c) A person who already properly holds units in the Fund.

In addition to the above, there is currently only one sub-fund which is principally targeted at local authorities, public sector organisations and charities who meet the eligibility criteria. Since only gross paying units are available, investors must be able to receive income payments gross.

Investment in the Fund is for Public Sector Eligible Investors only and may not be suitable for all investors. If you are in any doubt about the suitability of the Funds to your needs you should seek appropriate professional advice.

Past Performance is not an indicator of future performance. The value of investments and the income derived from them may fall as well as rise. Investors may not get back the amount originally invested and may lose money. Any forward looking statements are based upon our current opinions, expectations and projections. We undertake no obligations to update or revise these. Actual results could differ materially from those anticipated.

The Fund is authorised in the United Kingdom and regulated by the Financial Conduct Authority as an Alternative Investment Fund and a NURS established under a Scheme approved by H M Treasury under Section 11 of the Trustee Investments Act 1961 and is subject to provisions of a Trust Deed dated 2 December 2016. The Fund operates as an open-ended Fund under Part IV of the schedule to the Financial Services and Markets Act 2000 (Exemption) Order 2001.

Investments in the Fund and the Fund are covered by the Financial Services Compensation Scheme (FSCS). However, the Manager may also pay fair compensation on eligible claims arising from its negligence or error in the management and administration of the Fund.

CCLA Investment Management Limited is the manager of the Diversified Income Fund.

CCLA

www.ccla.co.uk

CCLA, Senator House, 85 Queen Victoria Street, London EC4V 4ET

Client Service Freephone: 0800 022 3505

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