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South Hams Audit Committee

South Hams District Council

Title:	**Agenda**
Date:	**Thursday, 6th September, 2018**
Time:	**2.00 pm**
Venue:	**Cary Room - Follaton House**
Full Members:	***Chairman*** Cllr Pearce ***Vice Chairman*** Cllr Pennington *Members:* Cllr Bramble, Cllr Holway, Cllr Brazil
Interests – Declaration and Restriction on Participation:	Members are reminded of their responsibility to declare any disclosable pecuniary interest not entered in the Authority's register or local non pecuniary interest which they have in any item of business on the agenda (subject to the exception for sensitive information) and to leave the meeting prior to discussion and voting on an item in which they have a disclosable pecuniary interest.
Committee administrator:	Member.Services@swdevon.gov.uk

N.B. Legal and financial officers will not, as a general rule, be present throughout all meetings, but will be on standby if required. Members are requested to advise Member Services in advance of the meeting if they require any information of a legal or financial nature.

MINUTES OF A MEETING OF THE AUDIT COMMITTEE HELD AT FOLLATON HOUSE, TOTNES ON THURSDAY 26 JULY 2018

Members in attendance * Denotes attendance ø Denotes apology for absence			
ø	Cllr I Bramble	*	Cllr J A Pearce (Chairman)
*	Cllr J Brazil	*	Cllr J T Pennington (Vice-Chairman)
ø	Cllr T R Holway		

Members also in attendance:
Cllr S A E Wright

Item No	Minute Ref No below refers	Officers and Visitors in attendance
All Items		Head of Paid Service; Section 151 Officer; Finance Community Of Practice Lead; Senior Specialist – Accountant; KPMG Representatives; and Senior Specialist – Democratic Services

A.9/18 **MINUTES**

The minutes of the meeting of the Committee held on 21 June 2018 were confirmed as a correct record and signed by the Chairman.

A.10/18 **URGENT BUSINESS**

The Chairman advised that she had no urgent items to be raised at this meeting.

A.11/18 **DECLARATIONS OF INTEREST**

Members and officers were invited to declare any interests in the items of business to be considered during the course of the meeting, but none were made.

A.12/18 **ANNUAL STATEMENT OF ACCOUNTS 2017/18**

The Committee considered a report that presented the audited Statement of Accounts and the audited Annual Governance Statement for the financial year ended 31 March 2018.

In introducing the report, officers informed that there had been minimal changes made to the Statement of Accounts and the Annual Governance Statement following the completion of the audit work. For clarity, it was confirmed that these changes that had been made primarily related to the presentation and format of these documents.

In discussion, the following points were raised:-

(a) Those Members in attendance reiterated their previous tributes to the achievements of the Finance Community Of Practice in meeting the requirement to publish the Council's Accounts a month earlier than in 2016/17;

(b) Since it was not directly evident in the Accounts, a Member questioned how he would be able to ascertain the total expenditure that the Council had spent on obtaining consultant advice. In reply, officers advised that the Council did not have a budget for external consultancy and such detail would be part of the business case for each specific project;

(c) In response to a request, officers agreed to write to colleagues at Devon County Council to gain a breakdown of the overseas equities asset allocation for pensions;

(d) A Member highlighted the comments in the Accounts relating to some of the repair and maintenance costs being incurred due to the vandalism of public conveniences. As part of the current pay on entry for using public conveniences proposals, officers confirmed that the potential for increased vandalism costs had been factored into the business case.

It was then:

RESOLVED

1. That the wording of the Letter of Representation (as set out in Appendix A of the presented agenda report) be approved;

2. That the audited Statement of Accounts for the financial year ended 31 March 2018 (as outlined in Appendix B of the presented agenda report) be approved; and

3. That the Annual Governance Statement post audit (as detailed in Appendix C of the presented agenda report) be approved.

A.13/18 **EXTERNAL AUDIT ISA260 REPORT 2017/18**

The Committee considered a report that had been produced by KPMG that was entitled: 'External Audit ISA260 Report 2017/18'.

The KPMG representatives introduced the report and wished to pay tribute to the Finance Community Of Practice for their support and timely responses to questions and issues raised.

In discussion, the following points were raised:-

(a) With regard to Housing Benefit controls, the Committee was reminded that the problems had now been resolved and reconciliations were up to date and reported to the Finance Community Of Practice Lead on a monthly basis;

(b) Members noted that the section of the KPMG report on Value for Money Arrangements focused on whether or not the Council had adequate arrangements in place as opposed to whether or not the authority had achieved value for money. As with all other local authorities, the representatives had identified that the delivery of a balanced budget was the key risk. Having considered all of the processes that the Council had put in place, the representatives were of the view that these were fit for purpose;

(c) A Member questioned the lack of reference in the report to those recent significant projects (e.g. One Council and the Local Authority Controlled Company) that had not materialised. In response, the representatives advised that the outcomes of such projects were considered and KPMG had recognised that the associated risks had been highlighted as part of the risk assessments for these projects. Furthermore, the representatives were satisfied that the Council had taken its decisions on these projects having weighed up all of those identified risks;

(d) As had been raised at the previous Committee meeting (Minute A.4/18 refers), a Member again expressed his surprise that there was a lack of reference in the report to the intrinsic links between the financial standing of West Devon Borough Council and the inevitable knock-on effects to this Council. In response, the Section 151 Officer informed that this point would be reflected in the strategic risk assessment report that would be presented to the Audit Committee meeting to be held on 11 October 2018.

In conclusion, the Committee recognised that the Council would soon be working with a new External Auditor and Members therefore wished to put on record their thanks and best wishes to KPMG and its representatives who had developed excellent working relationships with both Members and officers.

It was then:

RESOLVED

That the content of the ISA 260 Report for 2017/18 be noted.

(Meeting commenced at 10.00 am and finished at 10.50 pm)

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Chairman

Appendix B of this report contains exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act 1972

Committee:	**Audit Committee**
Date:	**6 September 2018**
Title:	**Activities to Support Economic Growth**
Portfolio Area:	**Cllr John Tucker, Leader of the Council, Assets**
Wards Affected:	**All**
Relevant Scrutiny Committee:	**Overview & Scrutiny Panel**
Date next steps can be taken:	**27 September 2018**
Authors:	**Darren Arulvasagam / Chris Brook** Business Development / Assets CoP Lead Darren.Arulvasagam@swdevon.gov.uk Chris.Brook@swdevon.gov.uk

Recommendations:

That the Audit Committee RECOMMEND to Executive to RECOMMEND to Council to:

1. **ADOPT the commercial property strategy; and**
2. **AGREE a total borrowing limit of £60m for the Commercial Property Strategy.**

1.0 Executive Summary

1.1 In July 2017, it was resolved that the Council deferred a decision regarding a commercial property acquisition strategy (26/13). At that time, the proposal was to acquire commercial property outside of the District. On 19th July 2018, Executive received a report entitled "Activities to Support Economic Growth", which proposed a revised strategy. Based on feedback received, an updated version of this strategy is shown in Appendix A.

1.2 Following meetings of the Investment Group in 2018, officers put together a strategy for commercial property acquisitions and asset developments within the South Hams district, in line with the "Enterprise" corporate strategic aim of creating places for enterprise to thrive and business to grow.

1.3 The proposed strategy would have the following multiple objectives:

1.3.1 Support regeneration and the economic activity of the District

1.3.2 Enhance economic benefit

1.3.3 Grow business rate income

1.3.4 Assist with the financial sustainability of the Council as an ancillary benefit.

1.3.5 Help the Council continue to deliver and/or improve frontline services in line with the Council's adopted strategy & objectives

1.4 It is recommended that the borrowing limit for the Strategy is £60m, based on the independent borrowing advice shown in Exempt Appendix B which recommends a total borrowing limit of £75m for the whole of the Council's operations, based on the Council's specific financial status.

1.5 The Committee are asked to support this recommendation.

1.6 How each acquisition or development scheme is funded will be reviewed on a case by case basis. It is envisaged this will predominantly be funded through prudential borrowing or any other unallocated or available Council reserve or capital receipt, as determined by the Council's Capital Financing Requirement (CFR).

1.7 The nominated Investment Group Members will consider each and every proposal on its own merits and specifically how each proposal meets the Council's multiple objectives.

1.8 The proposed strategy and/or implementation can be updated or ceased at any point prior to the full budget of the strategy being expended (and the required funding being borrowed), if Members determine that market conditions have deteriorated enough to make it financially unattractive.

1.9 It is anticipated that to fully implement the strategy, i.e. expend the full £60m could take upto 5 years to complete. Borrowing will not be undertaken in advance of need and only on a project by project basis. It is not currently expected that more than half of this sum would be committed before the end of this council year.

1.10 Projects and their outcomes will be kept under constant review by the Investment Group.

2.0 **Background**

2.1 In July 2017, it was resolved that the Council deferred a decision regarding a commercial property acquisition strategy (26/13). At that time, the proposal was to acquire commercial property outside of the District. On 19th July 2018, Executive received a report entitled "Activities to Support Economic Growth", which proposed a revised strategy.

2.2 Based on subsequent feedback received, an updated version of this strategy is shown in Appendix A. It includes both commercial property acquisition as well as funding of commercial development on Council land.

2.3 This proposal is in line with the "Enterprise" corporate strategic aim of creating places for enterprise to thrive and business to grow.

2.4 In the period between now and the original July 2017 proposals, there have been changes to the rules and guidance around what Councils can in, using prudential borrowing.

2.5 The MHCLG (Government) guidance on Investments has stated that Councils will need to disclose several recommended indicators in their treasury management strategies going forward, for reports published after 1 April 2018. The indicators that need to be disclosed after 1 April 2018 include an indicator on proportionality. This indicator assesses the amount of debt an Authority holds in relation to its Net Service Expenditure (NSE). The purpose of this indicator is to allow the reader to assess how proportional a Council's borrowing is, in relation to its Net Service Expenditure.

2.6 The Council has obtained independent advice on the amount of borrowing that would be acceptable for the District Council, based on the Council's own financial status. This advice is confidential is therefore treated as an exempt appendix as it is the intellectual property of a third party. The indicators themselves will be public information when they are published. The advice has been analysed in order to inform the recommendations within this report and the Borrowing Strategy (and appropriate limits) for the Council within the Medium Term Financial Strategy. Members can view this advice in Exempt Appendix B. As a result of this advice, it is recommended that the Council does not agree borrowing above £75m – with £60m for this strategy and a further maximum of £15m for any other borrowing requirement.

2.7 There are no Government guidelines on what is an acceptable level of proportionality (the proportion of borrowing as a factor of the Council's Net Service Expenditure) and it is for each Council to assess this level themselves. Proportionality is considered in the advice shown in Exempt Appendix B.

2.8 The Council will consider proportionality on a case by case basis for each borrowing decision as part of the decision making process, with information provided to the Investment group, the s151 officer, the Head of Paid Service and the Leader of the Council.

2.9 Investment in District, for the stated aims of this strategy, funded through borrowing is entirely consistent with all published guidance for Councils. Legal counsel has been undertaken as part of this process. The legal powers by which the Council can implement this strategy have been confirmed.

3 Commercial Aquisitions

3.0 The recommended strategy shown in Appendix A has been devised to give the Council, through delegated powers to the Investment Group, a clear set of criteria by which to appraise opportunities that arise.

3.1 Officers will provide the Investment Group with a set of data, such as that which is included in Appendix C (example decision template) and an indicative cash flow for each project under investigation. These would inform Members and aid their decision making on whether to proceed or not.

3.2 In parallel, the Council's Senior Leadership Team (SLT) are required to approve any bid or development. Any project will be subject to Due Diligence and Legal Searches and occasionally other data as need arises.

3.3 For acquisitions, assuming the bid remains as per that authorised at the time of sign off, the final sign off prior to exchange and payment of deposit (typically 10%) is made by; Chairman of the Investment Group, the Leader of the Council, S151 officer and Head of Paid Service. If the Leader is also the chair of the Investment Group, the Group will agree an alternate.

3.4 This process of delegated authority (1st stage for the Investment Group to bid on a purchase and 2nd stage for the 4 persons in 3.3 to formally approve to exchange and complete on a purchase) is required because there is often very little time (a number of days) to secure a bid on a property, especially if it is off market. Off market bids avoid price inflation caused by competing bidders.

3.5 The Investment Group should be aware that they will be required to process information similar to that in Appendix C in a very quick timeframe so as to provide their decision. They will also be asked to attend meetings on similarly short notice. These meetings may be held virtually to expedite decision making and substitutes can be nominated by the relevant parties, subject to discussion at the next Investment Group meeting.

4 Commercial Development

4.0 Commercial development in the context of this report refers to the development of commercial property on Council owned land, such as (by way of example only); the construction of a health and wellbeing clinic in Dartmouth.

4.1 There are multiple projects being worked on by officers that meet the criteria set out in the strategy and it is proposed that the Investment Group and scheme of delegation be used to facilitate timely and critical appraisal and ultimately approval of these proposals, including the granting of associated leases in excess of 15 years (which ordinarily would need to be a Full Council decision).

4.2 The information provided to the Investment Group will be similar for development projects, except that there will be additional risk analysis presented to include the construction phase of projects.

5 What might success look like?

5.0 The adoption of this strategy will facilitate inward investment in South Hams, promoting and fostering business development. This will help achieve the "enterprise" corporate objective.

5.1 Whilst acquisition opportunities cannot be forecast, it is anticipated that one or two commercial acquisitions may meet the Council's criteria within a year of approval. Likely spend may therefore be between £2-6m, generating a net income (after borrowing and acquisition costs) of £20k-£60k per annum (equivalent of a 1% yield after borrowing, management, maintenance and capital repayment costs).

5.2 Over a two year horizon, it is anticipated that commercial development should have started on one or more of the Council's sites. As a guide, each development may cost in the order of £5m - £10m.

5.3 Over a three – five year horizon, developments will have been concluded and entered the operational / income phase. As a guide, a 1% net yield (after borrowing, management, maintenance and capital repayment costs) may be a reasonable assumption for development income, but there will be a variation between projects.

5.4 It should be reiterated that the income derived from commercial development and some commercial acquisitions will be secondary to the economic and social benefit they will bring to South Hams and the strategy anticipates that outcome.

5.5 Investment Group Members may opt to accept a net yield return of less than 1% if the benefits of job creation or safeguarding, tourism, town centre regeneration, business rate growth or effective asset utilisation are deemed more important by the Investment Group than a purely financial return.

5.6 For illustrative purposes only, an example of how the borrowing requirements may add up to £75m are shown in Appendix D.

6 Options available and consideration of risk

6.0 The overall objectives of this strategy are set out below:

6.0.1 To support regeneration and the economic activity of the District

6.0.2 To enhance economic benefit & business rates growth

6.0.3 To assist with the financial sustainability of the Council as an ancillary benefit.

6.0.4 To help the Council continue to deliver and/or improve frontline services in line with the Council's adopted strategy & objectives

6.1 South Hams District Council is a business rates pilot area for 2018/19, which sets out economic objectives of the pilot area. This strategy would help deliver these objectives. Each acquisition or development will be assessed on its fit with meeting the objectives stated above, on a case by case basis.

6.2 If the Council decides not to adopt the strategy as proposed, it should still be able to deliver some of its development ambitions, utilising the existing Council approval routes and committees. What will be far more challenging will be to deliver on the commercial acquisition element of the strategy, as that is almost impossible to do in a timely manner without a scheme of delegation in place.

6.3 Research shows that where Councils undertake this activity, there is an increasing level of delegation, enabling them to move quickly when properties come to market. This is implicit within the adopted and recommended strategy.

6.4 Members could opt to follow, amend or reject the recommendations.

6.5 Legal counsel has been undertaken as part of this process. The legal powers by which the Council can implement this strategy set out in Section 8.0.

6.6 The strategy looks to mitigate risks by setting specific criteria for purchases and necessary due diligence must be completed before officers and the Investment Group recommend any purchase.

6.7 It should be recognised that there is an inherent tension between some of the objectives of this strategy. For example, a decision to purchase or develop business units to lease to tenants will help achieve the first two objectives. However, if the tenant defaults on its rent payments, the third objective would be at risk.

6.8 In contrast, purchasing a commercial building with an existing very strong tenant, could be seen to meet the first two objectives of the strategy less well, but would expose the Council to less financial risk.

6.9 Officers, working with their specialist advisors in the market will sift opportunities and only present to the Investment Group, things that meet the Strategy closely. They will then lead the Investment Group into debate over the specific benefits and risks of each opportunity before the Investment Group make a decision. In this way, risk will be transparent through the process.

7 Proposed Way Forward

7.1 This report will be discussed at Executive and then Council later in September, where any comments raised by the Overview & Scrutiny Panel or Audit Committee can be considered.

7.2 Full Council will consider the borrowing limit for this Strategy as part of the Medium Term Financial Strategy on September 27th 2018. It is envisaged in December 2018, Council will consider approving a revised Treasury Management Strategy which would increase the borrowing limits of the Council (depending on the recommendations from the various bodies), to facilitate implementation of this strategy. As part of this report, the Council will also include the new proportionality indicators to address the Government guidance issued in February 2018.

8 Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/ Governance	Y	Advice on the relevant powers and appropriate vehicles for delivering these proposals has been sought from external specialist advisers and legal counsel. Legal counsel opinion has been obtained which sets out the various powers available to the Council, which supports the Council's proposed strategy as described in this report. This proposal is consistent with the Council's powers to borrow and invest under the Local Government Act 2003 and section 1 Localism Act 2011 (the general power of competence) and / or section 120 Local Government Act 1972 (power to acquire land). The Council is empowered to buy pursuant to section 120 of the Local Government Act 1972. Section 1 of the Local Government Act 2003 provides a power to the Council to borrow for the purposes of any enactment. Disposal of any of the acquired properties will have to be undertaken in accordance with the provisions of section 123 Local Government Act 1972. In order to lawfully implement the acquisition strategy, each proposal (including the funding strategy for purchases) should be reviewed as part of a decision to purchase or sell, and tested for value for money, and regulatory compliance. There is an overriding duty toward prudent management of risk, and officers, including the Council's section 151 officer owe a fiduciary duty in relation to given transactions. There is a duty on the Council to have regard to Statutory Guidance on Local (the New Guidance) Government Investments. As such, as part of the due diligence, officers consideration of each particular investment will need to include consideration of all the legal circumstances of the particular case. Appendix B of this report is exempt from publication because it contains confidential information provided to the Council as defined in Paragraph 3 of Schedule 12A to the Local Government Act 1972. The public interest test has been applied and it is considered that the public interest lies in not disclosing this report at this time because it contains commercially sensitive information which could prejudice the Council if such information was disclosed at this time.
Financial	Y	The Council will purchase assets, or develop existing assets and hold these directly on its balance sheet and therefore the direct costs of purchase and acquisition or development can be capitalised. This will include costs such as stamp duty, legal fees, construction, planning, due diligence and agency fees. When individual purchase decisions or asset developments are made, a bespoke business case will be produced alongside a package of due diligence information to support the decision

		making process. The delegated authorities approving a purchase will need to be satisfied that any proposed acquisition not only delivers best value but also meets the criteria contained within the Commercial Property Strategy and has proper regard to how the acquisition or development meets the Council's multiple objectives of the strategy. Any PWLB borrowing to fund the acquisition of commercial property is not secured on the property acquired. PWLB borrowing rates are fixed for the term of the loan. Individual borrowing decisions will be taken prudently in line with the Council's treasury management strategy and by officers within that function. The Council will need to approve a revised Treasury Management Strategy which would increase the borrowing limits of the Council (depending on the recommendations from the various bodies), to facilitate implementation of the strategy. 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.
Risk	Y	The security risk is that the capital value of an acquired or developed property falls. Whilst this would have an effect on the Council's balance sheet, this loss will be realised if the Council chooses to sell the property and incurs a capital loss. The liquidity risk is the risk of failure of a tenant within one of the acquired or developed properties. The yield risk is that the ancillary income derived from the assets will alter during the life of the asset. This will be actively managed; with specialist agents commissioned to manage the asset and its tenants. Properties will only be acquired if they have a minimum of 5 years unexpired lease term and are located in areas deemed to be attractive for future lettings / sales, limiting the risk to the Council's portfolio. The Council already owns and operates a property estate valued at circa £75m. It therefore has experience of managing such an estate and can act as an intelligent client to fulfil the proposed strategy, with the aid of commissioned property experts. The cost of these experts has been included in the financial projections from this strategy.
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	Not Applicable

Supporting Information

Appendices:
Appendix A – Recommended Commercial Property Strategy & Criteria
Appendix B – Exempt Appendix B South Hams Benchmarking Report
Appendix C – Example of decision template to be presented to the Investment Group
Appendix D – Illustrative Borrowing Requirements for SHDC

Background Papers:
- "Activities to Support Economic Growth presented to Executive, July 2018
- "Commercial Property Acquisition Strategy", presented to Council, July 2017
- Statutory Guidance On Local Government Investments (3rd Edition) https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/678866/Guidance_on_local_government_investments.pdf
- Proposed Changes To The Prudential Framework Of Capital Finance https://www.gov.uk/government/consultations/proposed-changes-to-the-prudential-framework-of-capital-finance

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Appendix A – SHDC Commercial Property Strategy

Overall Objectives:
The Council's commercial property strategy has multiple objectives as stated below:

- To support regeneration and the economic activity of the District
- To enhance economic benefit & business rates growth
- To assist with the financial sustainability of the Council as an ancillary benefit
- To help the Council continue to deliver and/or improve frontline services in line with the Council's adopted strategy & objectives.

Desired Outcomes:

The following outcomes are desired by the application of this strategy. Each acquisition or development opportunity will be assessed on its fit with meeting the objectives stated above and should deliver one or more of the following outcomes (benefits):

- ✓ Job creation or safeguarding
- ✓ Health & Wellbeing
- ✓ Town centre regeneration
- ✓ Tourism / Increased footfall
- ✓ Business rate growth
- ✓ Improved asset utilisation
- ✓ A minimum Net yield of 1%

This strategy will be achieved by acquisitions and developments within the South Hams District. This will include the focussed acquisition of existing commercial property assets and the development of new properties which are to be let to third parties.

Risk

- The risks of acquiring property may be mitigated through the acquisition of assets with secure, long income streams, although this risk will be weighed up against the social and economic benefits of acquisitions to support commerce and trade in the District
- Acquisitions are to be made in a careful and controlled manner, with specific analysis of risk criteria carried out in the 'due diligence' stage prior to the completion of each purchase
- The portfolio will be relatively risk-averse, targeting tenants of strong financial standing and minimum unexpired lease terms of four years at the date of acquisition. However, these criteria will be considered on a case by case basis and can be outweighed in order to meet the strategy objectives

Location:

- Wherever opportunities arise within the District, in order to acquire good properties which deliver the Council's multiple objectives stated above and are deemed an acceptable risk.

Tenant mix:

- Where possible, a mix of tenants will be sought to create a balanced portfolio
- The final decision over the appropriateness of any tenant would be reviewed at the time of acquisition
- SHDC owns a significant number of commercial units already within the District, mainly smaller units and tenants with relatively low credit ratings. This reflects the historic policy of supporting small start-ups which has proved successful and continues to be. Newer acquisitions are likely to be for larger units which may have single tenant occupancy.

Lease length:

- A minimum 4 years unexpired (mean unexpired term for multi-let properties) is preferable, however this is flexible if it helps achieve the strategy objectives
- For multi-let properties, a mix of lease expiry dates are preferred, thereby limiting void risk (unless the property is purchased with a view to re-development)
- Properties would preferably be let to sound tenants on leases with a preference for 'Full Repairing and Insuring' leases for single occupiers and through internal repair obligations and a service charge for multi-let properties. There may be overriding economic reasons to move away from this position and these will be considered on a case by case basis.

For all of the above:
The final decision over the definition of "good", "secure", "strong", "long", "careful", "controlled", "acceptable", "balanced" and "risk-averse" will be agreed between the property acquisition advisers (including legal due diligence) and the individuals delegated with the responsibility to conclude the acquisition of the properties. This discretion will be based on both the risk to the capital value of the asset and its' fit with the strategy objectives.

Yield:

- The Council will only acquire properties where the running cost does not require Council subsidy. Per acquisition, a minimum net yield (an ancillary benefit) of 1.0% is to be sought, after acquisition, management, maintenance, capital repayment and funding costs. However, the Council may opt to accept a net yield return of less than 1% if the benefits of job creation or safeguarding, tourism, town centre regeneration, business rate growth or effective asset utilisation are deemed more important than a purely financial return.

Value & Cost:

- Acquisitions and development initiatives will be funded using predominantly borrowing or any other unallocated or available Council reserve or capital receipt.
- The Executive and Council will consider the borrowing limit for the Strategy as part of the Medium Term Financial Strategy in September 2018. It is envisaged in December 2018, Full Council will need to approve a revised Treasury Management Strategy which would increase the borrowing limits of the Council (depending on the recommendations from the various bodies), to facilitate implementation of this strategy. As part of this report, the Council will also include the new proportionality indicators to address the Government guidance issued in February 2018.
- Larger lot sizes are favoured - smaller size properties have disproportionately higher management costs and expose the Council to greater property void risks, but the economic and trade benefits of buying smaller units may outweigh this.
- Acquisition costs are forecast not to exceed 7% (Stamp Duty Land Tax (SDLT) / Legal / Agents / Due Diligence). These costs are to be contained within the overall strategy budget

Funding:

- This is to be secured on a case by case basis on the most commercially advantageous terms available predominantly through borrowing or any other unallocated or available Council reserve or capital receipt
- The term will not exceed the expected remaining life of the property, but as a rule, the Council wishes to secure borrowing over a maximum 50 year term. Capital repayments will seek to repay a minimum of 50% of the capital value of any acquired property.

Tax Implications:

- Due to the Council holding the asset, it is not anticipated that there will be any corporation tax or income tax implications from this strategy
- Some properties may be VAT elected, meaning VAT must be charged to tenants. This will be dealt with on a case by case basis and will be covered by the due diligence connected with that acquisition. The Council is able to charge and recover VAT
- Capital Gains Tax would not apply to assets sold from Council ownership. This position may change if a company were to be used to hold the acquired asset.

Exit Strategy:

- The Council is not looking to actively trade commercial property within the first 5 years of ownership of any acquired property, however this is flexible if required to meet this strategy's objectives
- If it is determined that the most prudent action is to sell an individual asset, this will be considered on a case by case basis and will be acted upon in consultation with the 'Investment Group' Chair, Leader, S151 officer and Head of Paid Service
- It is proposed that all properties will be held as Council Assets. This may change if the Council were to set-up a trading company and it was found to be commercially advantageous for such a vehicle to hold the asset
- It is important to note that there would be early repayment charges if borrowing used to acquire a commercial property were to be repaid before the end of the loan term. However, Public Works Loan Board (PWLB) lending is not secured against property, so would not inhibit the asset being traded during the loan period. An alternative asset could be purchased (& held) with any sale receipt.

Governance Arrangements:

Acquisitions & Developments

Acquisitions and developments must conform to the adopted commercial property strategy. Any deviation from the agreed strategy will require Council approval.

Specialists will be commissioned to act on behalf of the Council to source suitable properties and manage the acquisition due diligence process.

Delegated authority to be given to the Head of Paid Service, in consultation with the S151 officer, Leader of the Council and Chair of the 'Investment Group' (or their deputy). Each receive one vote to proceed with purchase. In the event of a split decision, the S151 officer has the casting vote.

The Council will consider proportionality on a case by case basis for each acquisition as part of the decision making process, with information provided to the Investment Group Members, the s151 officer, the Head of Paid Service and the Leader of the Council.

Before a final decision to proceed with a development or acquisition is made, local ward members will be briefed and be able to share their views with the Investment Group.

The 'Investment Group' will determine its chair and will receive details of potential purchases from the Assets CoP. They will vote on whether to bring a potential purchase decision to the Head of Paid Service.

The same governance arrangements will be used to approve capital expenditure relating to any development projects and the subsequent granting of leases in excess of 15 years as recommended by the Assets CoP Lead, on a project by project basis.

Running / Review
If the management of the acquired assets cannot be managed in-house by existing resources, it will be outsourced to property professionals. The cost of this management is to be deducted before calculating the net yield. The Investment Group to receive regular reporting to confirm portfolio composition and performance. Regular reporting to Audit Committee as required.

Disposal
Once acquired, decisions relating to the ownership of any acquired properties will be dealt with in-line with the Council's constituted scheme of delegation.

Disposal will be considered if the portfolio breaches the approved strategy. Decisions to be made in consultation with the 'Investment Group' Chair, Leader of the Council, S151 officer and Head of Paid Service.

Resources:
The work to filter, appraise and recommend investment and development opportunities will be undertaken within the Assets CoP. This will be supplemented by specific consultant advice as required and associated costs built into the business case for each project. The Assets CoP has strong relationships with a number of local and national consultants who will be required to support the projects. Examples of this include (but are not limited to): CCD Properties (development specialists), Arcadis (building technical due diligence), Womble Bond Dickinson (legal due diligence) and Savills (commercial property investment advice).

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APPENDIX C: EXAMPLE DECISION TEMPLATE - TRANSACTION REVIEW

CRITERIA	SCORE [RAG]	NOTES
Location[1]		Well located commercial estate, in XYZ Town
Property Condition[2]		Subject to Technical Due Diligence (TDD) – initial appraisal suggests some need for Capital Expenditure going forward, say £XXX within 5 years
Credit Rating of Tenant[3]		Multi- let building with a range of tenants and corresponding tenant strength. Better than average for this location and mix. (Dun and Bradstreet reports will be obtained to give a credit rating)
Length of Lease[4]		Some leases greater than 5 years, a few as long as 10.
Gross Yield[5]		5.42% (assuming fully occupied). This reflects the demand in this sector of the market
Management & Maintenance Costs[6]		Will be outsourced as currently is the case.
Conformity to MHCLG Guidelines[7]		Within District and therefore within the Council's strategy
Any Specific Problems Identified[8]		The amount of Capital Expenditure that is needed on the building needs understanding in greater detail, after the bid process.

Key to Specific Factors:

1. Location: Population of Catchment area, economic vibrancy of town, known or anticipated market demand, proximity to Motorway, or major A road, proximity to other similar properties (town centre/out-of-town).

2. Property Condition: Date of construction & any imminent or significant refurbishment (forecast capital spend), modernization requirements.

3. Credit Rating of Tenant(s): Dun & Bradstreet Credit Rating, annual accounts.

4. Length of Lease: No. of unexpired years, break points, bank guarantees, rent reviews.

5. Gross Yield: After any head rent (Leasehold only), **Net Yield:** After maintenance, management, insurance, interest, capital repayments, acquisition costs

6. Management & Maintenance Costs: No. of tenants, ease of in-house management, probable on-going property maintenance requirements.

7. Conformity to MHCLG Guidelines [04/2018] : Especially with respect to location: i.e. Within District / Devon / LEP Area

8. Any Specific Problems Identified, following legal & technical Due Diligence. E.g. Anomalies in Title Deed, restrictive Use Classes, local competition, construction, or refurbishment incomplete.

Property Details and Address	
Owner	Unknown
Tenant Details	XYZ Tenants
Purchase Price	£3,500,000 (bid price to be agreed with agent, but no higher than this figure)
Probable Exchange Date	Date to be inserted
Probable Completion Date	Date to be inserted
Net Annual Rental Income *Based on full occupancy	Rent payable: £203,166 <u>Less</u> Interest repayments on PWLB borrowing (99,243) MRP on Annuity basis (36,786) (Capital repayment on borrowing) Repairs and Maintenance allowance (20,317) (10% of rent) Net Rental Income per annum: £46,820 (Note this falls to £34,000 if One Unit is vacant)
Amount to be Borrowed: (Purchase Price plus 7%)	£3,745,000 (£3,500,000 + 7%)
Gross Yield (based on rent of £203,166)	Gross Yield of 5.42% Net Yield of 1.25%
Loan Period & Interest Rate:	50 years Interest rate TBC
Confirmation of Useful Life of the Building (for loan length purposes and MRP calculations)	TBC
Details of acquisition costs	Stamp Duty Land Tax £164,500 Consultant 1: £17,500 Consultant 2: £10,000 (estimate) Consultant 3: £13,000 (estimate) Estimated Costs £205,000
How the property meets the Council's multiple objectives under the Council's strategy	Economic Regeneration – refurbished building and improved building stock leading to; Business Growth In line with the Member approved strategy of being within the District.
Debt Proportionality considerations	Debt of £3.745 million represents a multiplier of XYZ of the Council's Net Cost of Services of £XYZ million.
Lease expiry details:	Ranges from 6 months to 10 years.
Tenant Strength details: (D & B rating)	Ranges: 5A1 – N1
Guarantor's details: (D & B rating)	There is no Guarantor.

Exit Strategy	Buying to hold in the long term. Demand in the sector for units of this size is high and it is anticipated that the estate will be run as is for the foreseeable, with a gradual leaving and replacement of tenants.
Option to Tax the property for VAT	No action to date (but will be Opted to Tax)
Insurance - Date added to Council's Insurance cover	Separate Insurance cover would be procured for the building.
Assets CoP Summary & Recommendation	At this stage there is a question mark over the quantum of capital expenditure required and over what timescale. This will be clarified should the Council's bid be successful (and the bid will be subject to TDD). The expectation is that tenants will leave over time, to be replaced by new ones, so there will be times when the estate is not full. It would be suggested that over the long term one unit being empty might be the norm at any one time. Management of the estate would need to be outsourced, as would the service charge element. The price is reflective of the market, but will make achieving the Council's portfolio target a challenge, and there may be a re-balance of the value of the estate in the short to medium term. This needn't be a concern unless the Council wishes to liquidate the asset at that point.
S151 / Finance CoP Summary & Recommendation	A bid is supported up to £3.5m (just below 0.94% net yield if one property is vacant). The Capital Expenditure requirements need understanding (assumed to be £100K). Note the Net Rental Income per annum falls to £34,000 if One Unit is vacant.
Legal Summary & Recommendation	TBC

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Appendix D - Illustrative Borrowing Requirements - SHDC

Commercial Property Acquisitions		
Acquisition 1	5,000,000	Example Only
Acquisition 2	250,000	Example Only
Acquisition 3	250,000	Example Only
Sub-Total Acquisitions	**5,500,000**	
Commercial Developments		
Project 1	5,000,000	Example Only
Project 2	6,700,000	Example Only
Project 3	780,000	Example Only
Project 4	9,310,000	Example Only
Project 5	5,000,000	Example Only
Project 6	24,700,000	Example Only
Project 6	2,350,000	Example Only
Project 7	660,000	
Sub-Total Developments	**54,500,000**	
TOTAL Acquisition & Development	**60,000,000**	
Other Borrowing Requirements		
Community Led Housing*	6,500,000	Example - Short term (2 Years) only to cover construction
Community Housing Affordable Rental	1,500,000	Long term borrowing for affordable rent (1st scheme example)
Leisure Fusion contract	5,500,000	Contractual Commitment
Leisure - Totnes	1,500,000	Based on delegated authority to fund Totnes improvements
Sub Total 'Other'	**15,000,000**	
TOTAL	**75,000,000**	

*GROSS REQUIREMENT, before any sales receipts

Borrowing already taken out (shown in Yellow)	5,500,000

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Report to:	**Audit Committee**
Date:	**6 September 2018**
Title:	**Annual Treasury Management Report 2017/18**
Portfolio Area:	**Support Services – Councillor S Wright**
Wards Affected:	**ALL**

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

Author:	Lisa Buckle	Role:	**Finance Community of Practice Lead**
	Sarah Adams		**Specialist Accountant**

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

Recommendations:

That the Audit Committee:

1. **Approves the actual 2017/18 prudential and treasury indicators in this report; and**

2. **Notes the Annual Treasury Management report for 2017/18.**

1. Executive summary

Income from investments this year was £140,126 which is £17,126 higher than the budget of £123,000 at an average return of 0.29%. The comparable performance indicator (Benchmark) is the average 7-day LIBID rate which was 0.21%. Therefore the Council achieved 0.08% return on investments over the benchmark for 17/18.

2. Background

Introduction

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2017/18. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

Treasury management is defined as:

"The management of the local authority's 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 "

During 2017/18 the minimum reporting requirements were that the full Council should receive the following reports:

- An annual treasury strategy in advance of the year (Executive 09/03/17 – E73/16)
- A mid-year (minimum) treasury update report (Executive 07/12/17 – E47/17)
- An annual review following the end of the year describing the activity compared to the strategy (this report)

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee before they were reported to the full Council. Member training on treasury management issues will be undertaken during 2018/19 in order to support members' scrutiny role.

The Economy and Interest Rates

During the calendar year of 2017, there was a major shift in expectations in financial markets in terms of how soon Bank Rate would start on a rising trend. After the UK economy surprised on the upside with strong growth in the second half of 2016, growth in 2017 was disappointingly weak in the first half of the year which meant that growth was the slowest for the first half of any year since 2012. The main reason for this was the sharp increase in inflation caused by the devaluation of sterling after the EU referendum, feeding increases into the cost of imports into the economy. This caused a reduction in consumer disposable income and spending power as inflation exceeded average wage increases. Consequently, the services sector of the economy, accounting for around 75% of GDP, saw weak growth as consumers responded by cutting back on their expenditure. However, growth did pick up modestly in the second half of 2017. Consequently, market expectations during the autumn, rose significantly that the MPC would be heading in the direction of imminently raising Bank Rate. The minutes of the MPC meeting of 14 September indicated that the MPC was likely to raise Bank Rate very soon. The 2 November MPC quarterly Inflation Report meeting duly delivered by raising Bank Rate from 0.25% to 0.50%. The 8 February MPC meeting minutes then revealed another sharp hardening in MPC warnings on a more imminent and faster pace of increases in Bank Rate than had previously been expected.
Market expectations for increases in Bank Rate, therefore, shifted considerably during the second half of 2017-18 and resulted in **investment rates** from 3 – 12 months increasing sharply during the spring quarter.

PWLB borrowing rates increased correspondingly to the above developments with the shorter term rates increasing more sharply than longer term rates. In addition, UK gilts have moved in a relatively narrow band this year, (within 25 bps for much of the year), compared to **US treasuries**. During the second half of the year, there was a noticeable trend in treasury yields being on a rising trend with the Fed raising rates by 0.25% in June, December and March, making six increases in all from the floor. The effect of these three increases was greater in shorter terms around 5 year, rather than longer term yields.

The **general election** on 8 June had relatively little impact on financial markets.

Overall Treasury Position as at 31 March 2018

At the beginning and the end of 2017/18 the Council's treasury position was as follows:

Investments	31 March 2017 Principal	Return for 2016/17	31 March 2018 Principal	Return for 2017/18
	£	%	£	%
Short term - fixed	17,000,000	0.49	22,600,000	0.32
Money Market Funds	12,175,000	0.34	20,140,000	0.26
Heritable Bank	22,483	-	22,483	-
Total	**29,197,483**		**42,762,483**	

NOTE: The timing and complexities of schemes such as the Localisation of Business Rates Retention (retention of business rates growth above the baseline) can impact on the year end positions.

The following is a list of our investments at 31 March 2018.

Fixed Term Deposits

Counterparty	Fixed to	£	Interest Rate
Barclays Bank plc	03/05/2018	2,500,000	0.49%
Barclays Bank plc	19/09/2018	3,500,000	0.64%
Nationwide BS	06/04/2018	5,000,000	0.32%
Nationwide BS	19/06/2018	1,000,000	0.47%
Lloyds TSB Bank Plc	04/07/2018	5,000,000	0.60%
Lloyds TSB Bank Plc	02/08/2018	1,000,000	0.60%
Debt Management Office (See Note * below)	19/04/2018	1,600,000	0.25%
Debt Management Office (See Note * below)	19/04/2018	3,000,000	0.25%

*Note

These investments were taken out on 15th February and 15th March respectively (when the direct debit income from council tax and business rates was received) and were for a short term period. The current counter-party limits were already reached for Barclays, Nationwide and Lloyds. The investment was structured to mature on the day that the precepts were due to be paid to the major precepting authorities.

The Council's current counterparty limit is £6 million (£7 million for Lloyds plc).

Money Market Funds

Amount	Investment	Interest rate
£6,000,000	Standard Life (Ignis)	0.29%
£2,140,000	Deutsche	0.20%
£6,000,000	BlackRock	0.25%
£6,000,000	LGIM	0.28%

The Strategy for 2017/18

The expectation for interest rates within the treasury management strategy for 2017/18 anticipated that Bank Rate would remain at 0.50% until quarter 2 2019 and then increase to 0.75% in December 2018.

There would also be gradual rises in medium and longer term fixed borrowing rates during 2017/18 and the two subsequent financial years. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

The Borrowing Requirement and Debt

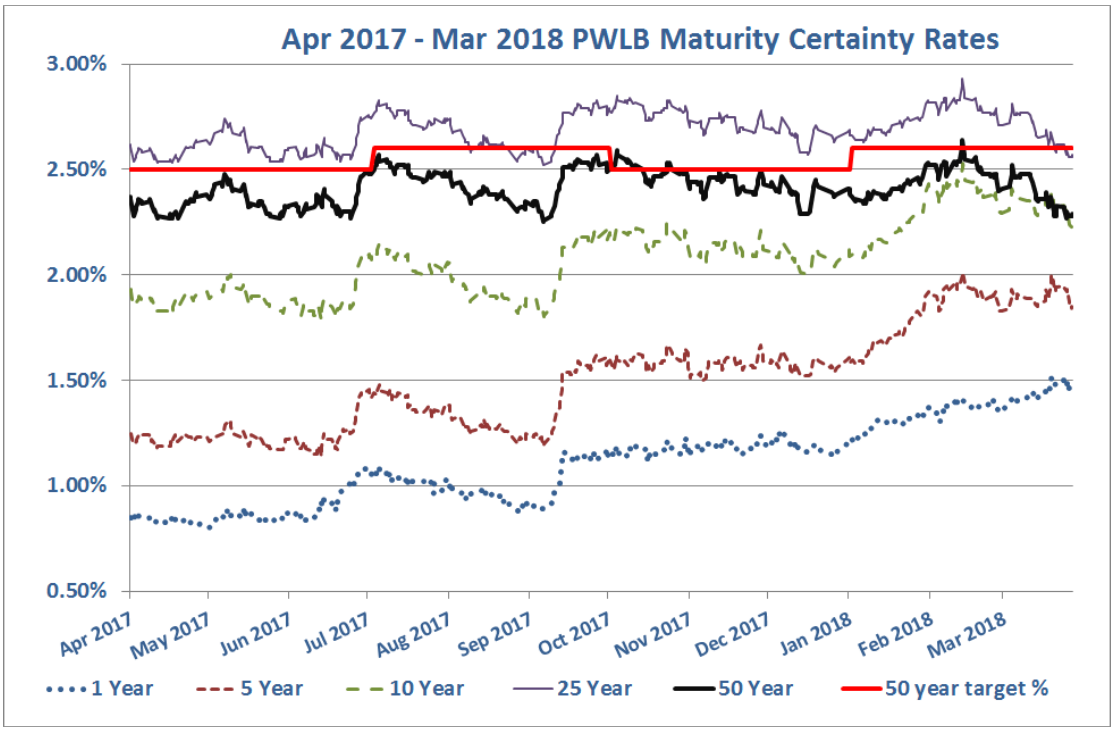
The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR).

	31-Mar-17 Actual	31-Mar-18 Budget	31-Mar-18 Actual
CFR General Fund (£m)	-98	2,502	646

NOTE: The budgeted position of £2.5m included borrowing for Leisure Investment which happened after 31 March 2018. The cost of the Leisure Investment is being reimbursed to the Council by the Leisure contractor.

Borrowing Rates in 2017/18

PWLB borrowing rates - the graph below shows, for a selection of maturity periods, the average borrowing rates, the high and low points in rates, spreads and individual rates at the start and the end of the financial year.



Investment Rates in 2017/18

Investments rates for 3 months and longer have been on a rising trend during the second half of the year in the expectation of Bank Rate increasing from its floor of 0.25%, and reached a peak at the end of March. Bank Rate was duly raised from 0.25% to 0.50% on 2 November 2017 and remained at that level for the rest of the year.

Investment Outturn for 2017/18

Investment Policy – the Council's investment policy is governed by MHCLG guidance, which has been implemented in the annual investment strategy approved by the Council on 21 March 2017 (revised 5 December 2017 – CM46). This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data, (such as rating outlooks, credit default swaps, bank share prices etc.

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Income from investments this year was £140,126 which is £17,126 higher than the budget of £123,000 at an average return of 0.29%. The comparable performance indicator (Benchmark) is the average 7-day LIBID rate which was 0.21%. Therefore the Council achieved 0.08% return on investments over the benchmark for 17/18.

Other Issues 2017/18

1. Revised CIPFA Codes

In December 2017, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued a revised Treasury Management Code and Cross Sectoral Guidance Notes, and a revised Prudential Code.

A particular focus of these revised codes was how to deal with local authority investments which are not treasury type investments e.g. by investing in purchasing property in order to generate income for the Authority at a much higher level than can be attained by treasury investments. One recommendation was that local authorities should produce a new report to members to give a high level summary of the overall capital strategy and to enable members to see how the cash resources of the Authority have been apportioned between treasury and non-treasury investments. Officers will report to members when the implications of these new codes have been assessed as to the likely impact on the Authority.

2. Markets in Financial Instruments Directive II (MiFID II)

The EU set the date of 3 January 2018 for the introduction of regulations under MIFID II. These regulations govern the relationship that financial institutions conducting lending and borrowing transactions will have with local authorities from that date. This has had little effect on South Hams District Council apart from having to fill in forms sent by each institution dealing with the Authority and for each type of investment instrument we use, apart from for cash deposits with banks and building societies.

3. Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/Governance	Y	Statutory powers are provided by the Local Government Act 1972 Section 151 and the Local Government Act 2003
Financial	Y	Income from Treasury Management activities amounted to £140,126 in 2017/18. Consideration of the Annual Treasury Report forms an essential component of the Council's systems for public accountability. It also provides a platform for future investment planning.
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 Members.
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

Supporting Information

Appendices:

Appendix A – Lending list as at 29 March 2018
Appendix B - Prudential and Treasury Indicators 2017/18

Background Papers:

Annual treasury strategy in advance of the year (Executive 09 March 2017 – E73/16)
A mid-year treasury update report (Executive 07 December 2017 – E47/17)

APPENDIX A

Counterparty as at 29th March		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	SB	A	F1			1	SB	Aa3		P-1				R - 6 mths
	Bank of Scotland PLC	SB	A+	F1	a		5	SB	Aa3		P-1	PO	A	A-1	R - 6 mths
	Barclays Bank PLC	PW	A	F1	a		5	NW	A1		P-1	SB	A	A-1	R - 6 mths
	Close Brothers Ltd	SB	A	F1	a		5	SB	Aa3		P-1				R - 6 mths
	Goldman Sachs International Bank	SB	A	F1				NO	A1		P-1	SB	A+	A-1	R - 6 mths
	HSBC Bank PLC	SB	AA-	F1+	a+		1	NW	Aa3		P-1	SB	AA-	A-1+	O - 12 mths
	Lloyds Bank Plc	SB	A+	F1	a		5	SB	Aa3		P-1	PO	A	A-1	R - 6 mths
	Santander UK PLC	PW	A	F1	a		2	SB	Aa3		P-1	SB	A	A-1	R - 6 mths
	Standard Chartered Bank	SB	A+	F1	a		5	SB	A1		P-1	SB	A	A-1	R - 6 mths
	Sumitomo Mitsui Banking Corporation	SB	A	F1			1	SB	A1		P-1	SB	A	A-1	R - 6 mths
	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
	Leeds Building Society	SB	A	F1	a-		5	SB	A3		P-2				G - 100 days
	Nationwide Building Society	SB	A+	F1	a		5	SB	Aa3		P-1	PO	A	A-1	R - 6 mths
	Skipton Building Society	SB	A-	F1	a-		5	SB	Baa1		P-2				G - 100 days
	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
	Royal Bank of Scotland Group Plc	SB	BBB+	F2	bbb+		5	SB	Baa3		P-3	SB	BBB-	A-3	B - 12 mths
	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 B

PRUDENTIAL AND TREASURY INDICATORS 2017/18

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

Capital Expenditure

This prudential Indicator is a summary of the Council's capital expenditure.

Capital Expenditure	2016/17 Actual £000	2017/18 Estimate £000	2017/18 Actual £000
Total	**3,023**	**5,015**	**4,179**

The table below summarises the financing of the Council's capital programme. Any shortfall of resources would result in a funding need (borrowing).

Capital Expenditure	2016/17	2017/18	2017/18
	Actual £000	**Estimate £000**	**Actual £000**
Total	**3,023**	**5,015**	**4,179**
Financed by:			
Capital receipts	665	877	1,212
Capital grants	1,166	613	1,079
Reserves	1,192	418	1,144
New Homes Bonus	0	507	0
Net financing need for the year	**0**	**2,600**	**744**

NB. Please note that the estimate for 2017-18 represents the approved capital programme for that year. However, actual capital spend includes not only expenditure on projects within that capital programme, but also expenditure on schemes carried forward from previous capital programmes.

NOTE: The estimate for 2017/18 included estimates for Leisure Investment which mostly happened after 31 March 2018. The cost of the Leisure Investment is being reimbursed to the Council by the Leisure contractor.

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 if the figure is greater than zero.

The Capital Financing Requirement estimate for 2017/18 was increased by £2.6 million in July 2016 (Minute 33/16) to reflect the new leisure contract. Note: No prudential borrowing occurred in 2017/18.

	2016/17	2017/18	2017/18
	Actual £000	**Estimate £000**	**Actual £000**
Total CFR	-98	2,502	646
Movement in CFR	Nil	2,600	744
Explained by:			
Minimum Revenue Provision	Nil	Nil	Nil
Change in underlying need to borrow	-	2,600	744

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 receipt of net 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	2017/18
	Actual	**Estimate**	**Actual**
Ratio of net financing cost to net revenue stream. This is a net cost.	(1.5)%	(0.5)%	(1.7)%

Estimates of the incremental impact of capital investment decisions on council tax

This indicator calculates the notional cost of the impact of lost investment income on the Council Tax, from spending capital resources.

The 2017/18 estimate of the impact on council tax (this is a notional indicator) included borrowing for Leisure Investment which happened after 31 March 2018. The cost of the Leisure Investment is being reimbursed to the Council by the Leisure contractor.

Incremental impact of capital investment decisions on the band D council tax (Notional cost as explained above)

	2016/17 Actual £	2017/18 Estimate £	2017/18 Actual £
Future incremental impact of capital investment decisions on the band D Council tax (Notional cost)	0.15	2.23	0.19

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	2016/17 £	2017/18 £
Borrowing	2,000,000	5,000,000
Other long term liabilities	-	-
Total	2,000,000	5,000,000

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.

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.

Authorised limit	**2016/17**	**2017/18**
	£	**£**
Borrowing	7,000,000	10,000,000
Other long term liabilities	-	-
Total	7,000,000	10,000,000

The Authorised Limit was increased in 2017/18 to reflect the proposed borrowing for the new leisure contract.

Meeting Date	Work Programme for Audit Committee 2018/19
11 October 2018	i) Six monthly update – Strategic Risk Assessment; ii) Six monthly update – Strategic Debt review; iii) Internal Audit Charter & Strategy; iv) Update on Progress on the 2018/19 Internal Audit Plan (to include Finance Procedure Rules Review); v) Constitution Review: Part 2; vi) KPMG Annual Audit Letter and Closure of the Audit Letter; and vii) Pensions Strategy and Treasury Management update (for information).
31 January 2019	i) KPMG Annual Grant Certification Letter; and ii) Update on progress on the 2018/19 Internal Audit Plan.
21 March 2019	i) Grant Thornton - External Audit Plan 2018/19; ii) Grant Thornton – Interim Audit Report 2018/19; iii) Treasury Management update (for information); iv) 2019/20 Internal Audit Plan; v) Draft Budget Book 2019/20; vi) Cost Methodology for Shared Services 2018/19; vii) Review of Council Constitution; viii) Update on Progress on the 2018/19 Internal Audit Plan; ix) Six monthly update – Strategic Risk Assessment; and x) Six monthly update – Strategic Debt review.

To be considered for programming: Civica / IT: Lessons Learnt (Minute O&S.6/18 refers)

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