Shropshire Council

Shropshire Council
Legal and Democratic Services
Shirehall
Abbey Foregate
Shrewsbury
SY2 6ND

Date: 3 February 2021
My Ref:
Your Ref:

Committee:
Audit Committee

Date: **Thursday, 11 February 2021**
Time: **1.30 pm**
Venue: **THIS IS A VIRTUAL MEETING - PLEASE USE THE LINK ON THE AGENDA TO LISTEN TO THE MEETING**

Members of the public will be able to listen to this meeting by clicking on this link:

www.shropshire.gov.uk/AuditCommittee11Feb21

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- You will need to download MS Teams (free) and click on the link to listen to the meeting if you are using a PC
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- Use the link at 1.30 pm on the day of the meeting and click on 'Join as Guest'
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You are requested to attend the above meeting.
The Agenda is attached

Claire Porter
Director of Legal and Democratic Services (Monitoring Officer)

Members of Audit Committee

Peter Adams (Chairman)
Ioan Jones
Chris Mellings
Brian Williams (Vice Chairman)
Michael Wood

Your Committee Officer is:
Michelle Dulson Committee Officer
Tel: 01743 257719 Email: michelle.dulson@shropshire.gov.uk

AGENDA

1 Apologies for Absence / Notification of Substitutes

2 Disclosable Pecuniary Interests

Members are reminded that they must not participate in the discussion or voting on any matter in which they have a Disclosable Pecuniary Interest and should leave the room prior to the commencement of the debate.

3 Public Questions

To receive any questions from the public, notice of which has been given in accordance with Procedure Rule 14. The deadline for notification for this meeting is 1.30pm on Tuesday 9 February 2021.

4 Members Questions

To receive any questions from Members, notice of which has been given in accordance with Procedure Rule 14. The deadline for notification for this meeting is 1.30pm on Tuesday 9 February 2021.

5 Second line assurance: Treasury Strategy 2021/22 (Pages 1 - 52)

The report of the Director of Finance, Governance and Assurance (Section 151 Officer) is attached.
Contact: James Walton (01743) 258915

6 Date and Time of Next Meeting

The next meeting of the Audit Committee will be held on the 4 March 2021 at 1.30pm.

Committee and Date	Item
Cabinet 8 February 2021 Audit Committee 11 February 2021 Council 25 February 2021	 Public

TREASURY STRATEGY 2021/22

Responsible Officer James Walton
e-mail: james.walton@shropshire.gov.uk Tel: (01743) 258915

1. Summary

1.1 The report proposes the Treasury Strategy for 2021/22 and recommends Prudential and Treasury Indicators for 2021/22 to 2023/24. The report is technical in nature but the key points to note are:-

- Borrowing is largely driven by the requirements of the approved Capital Programme. From 2011/12 the Council's borrowing requirement has been significantly reduced due to the Government changing the way in which it funds the Council's capital expenditure and providing capital grants rather than supported borrowing approval with on-going (as it was defined at the time) revenue support grant to meet the financing costs of the borrowing. Currently the approved borrowing requirement identified within the Capital Programme 2021/22 to 2023/24 is prudential borrowing of £118.909 million. In addition to this there is an anticipated prudential borrowing requirement for future prioritised schemes in the Capital Strategy 2021/22 to 2023/24 of £113.670 million.

- In late December 2017, CIPFA issued revised Prudential and Treasury Management Codes. As from 2019/20 all local authorities are required to prepare an additional report, a Capital Strategy report. The Council is continuing to develop both the Capital Strategy report and business cases for a number of large schemes linked to proposals set out in the Council's Finance Strategy. Any updates required as a result of future decisions will be reported accordingly.

- The Council's lending continues to be restricted to highly credit rated Banks, three Building Societies, Money Market Funds and Part Nationalised Institutions which meet Link Asset Services creditworthiness policy, other Local Authorities and the UK Government.

- The internal Treasury Team will continue to look for opportunities to make savings by actively managing the cash and debt portfolio in accordance with the Treasury Strategy.

- The bank rate was decreased to 0.10% in March 2020 as a direct consequence to the COVID-19 pandemic and the impact on global financial markets. As a consequence, we have seen investment yields supressed. We are unlikely to see any further bank rate increases from the Monetary Policy Committee (MPC) in the next two financial years. This will have a major impact on the investment income that the Council will receive during this period.

- Long term borrowing rates are expected to be higher than investment rates during 2021/22 therefore long term borrowing may be postponed in order to maximise savings in the short term. Currently the approved borrowing requirement identified within the Capital Programme 2021/22 to 2023/24 is prudential borrowing of £118.909 million. In addition to this there is an anticipated prudential borrowing requirement for future prioritised schemes in the Capital Strategy 2021/22 to 2023/24 of £113.670 million. Any changes to this requirement as a result of future decisions will be reported accordingly.

- The Council has agreed to offer to lend funds to Connexus Housing Ltd (which incorporates both South Shropshire Housing Association and the Meres & Mosses Housing Association) and Severnside Housing at an agreed rate. It has previously been agreed to offer to lend up to £10 million to each of these Housing Associations in order to support the building of affordable housing and shared office accommodation in Shropshire. For security purposes, each loan has been secured against existing assets held by or owned by the Housing Association. To date £9,770,000 has been drawn down by Connexus Housing Ltd and £10,000,000 by Severnside Housing.

- Following Council approval on 28th February 2019, Shropshire Council formed a Wholly Owned Local Housing Company, known as Cornovii Homes. An initial unsecured loan was approved and made to the Company of £1 million to provide funding for operating and set up costs. The Council has subsequently approved additional funding in the form of equity and a loan to facilitate land purchases and development costs. The loan element, totalling £14 million, is anticipated to be released to the Company over the financial years 2020/21 and 2021/22. In addition, a further £35 million revolving loan facility has been agreed.

2. Recommendations

2.1. Recommendations to Cabinet

Cabinet recommend that Council:-

a) Approve, with any comments, the Treasury Strategy for 2021/22.

b) Approve, with any comments, the Prudential Indicators, set out in Appendix 1, in accordance with the Local Government Act 2003.

c) Approve, with any comments, the Investment Strategy, set out in Appendix 2 in accordance with the MHCLG Guidance on Local Government Investments.

d) Approve, with any comments, the Minimum Revenue Provision (MRP) Policy Statement, set out in Appendix 3.

e) Authorise the Section 151 Officer to exercise the borrowing powers contained in Section 3 of the Local Government Act 2003 and to manage the Council's debt portfolio in accordance with the Treasury Strategy.

f) Authorise the Section 151 Officer to use other Foreign Banks which meet Link's creditworthiness policy as required.

2.2. Recommendations to Audit Committee

g) Audit Committee are asked to consider and endorse, with appropriate comment, the Treasury Strategy 2021/22.

2.3. Recommendations to the Council

h) Approve, with any comments, the Treasury Strategy for 2021/22.

i) Approve, with any comments, the Prudential Indicators, set out in Appendix 1, in accordance with the Local Government Act 2003.

j) Approve, with any comments, the Investment Strategy, set out in Appendix 2 in accordance with the MHCLG Guidance on Local Government Investments.

k) Approve, with any comments, the Minimum Revenue Provision (MRP) Policy Statement, set out in Appendix 3.

l) Authorise the Section 151 Officer to exercise the borrowing powers contained in Section 3 of the Local Government Act 2003 and to manage the Council's debt portfolio in accordance with the Treasury Strategy.

m) Authorise the Section 151 Officer to use other Foreign Banks which meet Link's creditworthiness policy as required.

REPORT

3. Risk Assessment and Opportunities Appraisal

3.1. The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998.

3.2. There are no direct environmental, equalities or climate change consequences arising from this report.

3.3. Compliance with the CIPFA Code of Practice on Treasury Management, the Council's Treasury Policy Statement and Treasury Management Practices and the Prudential Code for Capital Finance together with the rigorous internal controls will enable the Council to manage the risk associated with Treasury Management activities and the potential for financial loss.

4. Financial Implications

4.1 The financial implications arising from the Treasury Strategy are detailed in this report. The Council makes assumptions about the levels of borrowing and investment income over the financial year. Reduced borrowing as a result of capital receipt generation or delays in delivery of the capital programme will both have a positive impact of the council's cash position. Similarly, higher than benchmarked returns on available cash will also help the Council's financial position. For monitoring purposes, assumptions are made early in the year about borrowing and returns based on the strategies agreed by Council in the preceding February. Performance outside of these assumptions results in increased or reduced income for the Council.

4.2 As at 31 December 2020 the Council held £170 million in investments and borrowing of £304 million at fixed interest rates.

5. Climate Change Appraisal

5.1 The Council's Financial Strategy includes proposals to deliver a reduced carbon footprint for the Council, therefore the Treasury Team is working with the Council in order to achieve this. There are no climate change impacts arising from this report.

6. Background

6.1. 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, providing adequate liquidity initially before considering investment return.

6.2. 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. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

6.3. The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

6.4. Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day to day treasury management activities.

6.5. The Council defines its treasury management activities as "the management of the 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".

6.6. Revised reporting was required for the 2019/20 reporting cycle due to revisions of the MHCLG Investment Guidance, the MHCLG Minimum Revenue Provision

(MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy, to provide a longer-term focus to the capital plans and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011. The capital strategy is being reported separately.

6.7. This strategy statement has been prepared in accordance with CIPFA's revised Code of Practice on Treasury Management. Accordingly, the Council's Treasury Strategy will be approved annually by full Council and there will also be a mid-year review report. In addition, treasury management update reports will be submitted quarterly to Directors and Cabinet. The aim of these reporting arrangements is to ensure that those with ultimate responsibility for the treasury management function appreciate fully the implications of policies and practices, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

6.8. In late December 2017, CIPFA issued a revised Treasury Management Code of Practice and a revised Prudential Code. These revisions particularly focused on non-treasury investments and the requirement for all local authorities to produce a detailed Capital Strategy as from 2019/20. The majority of these requirements are already included in an appendix to the Council's Financial Strategy, but this will now be included as a separate Capital Strategy report. This report will provide the following:-

- a high-level long-term 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

6.9. The aim of this capital strategy is to ensure that all elected members on the full council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

6.10. This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The capital strategy will show:

- The corporate governance arrangements for these types of activities;
- Any service objectives relating to the investments;
- The expected income, costs and resulting contribution;
- The debt related to the activity and the associated interest costs;
- The payback period (MRP policy);
- For non-loan type investments, the cost against the current market value;
- The risks associated with each activity.

Where a physical asset is being bought, details of market research, advisers used, (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

6.11. Attached in appendix 2 is the Council's Annual Investment Strategy which includes a list of additional responsibilities for the Section 151 Officer role following the issue of the revised Treasury Management Code of Practice and Prudential Code.

6.12. The revised codes have clarified CIPFA's position that there is a clear separation between treasury and non-treasury investments and on the role of the treasury management team. Accordingly, periodic reporting by the treasury management team to members will focus solely on treasury investments. If non treasury investments are considered, a separate report will be presented for approval and any changes required to Prudential indicators incorporated within an updated Treasury Strategy if necessary.

6.13. The Council will adopt the following reporting arrangements in accordance with the requirements of the Code:-

Area of Responsibility	**Council/Committee/Officer**	**Frequency**
Treasury Management Policy Statement	Full Council/Cabinet	As required
Treasury Strategy/Annual Investment Strategy/MRP Policy	Full Council/Cabinet	Annually before the start of the financial year
Capital Strategy	Full Council/Cabinet	Annually before the start of the financial year
Treasury Strategy/Annual Investment Strategy/MRP Policy – mid year report	Full Council/Cabinet	Mid year
Treasury Strategy/Annual Investment Strategy/MRP Policy – updates or revisions at other times	Full Council/Cabinet	As required
Annual Treasury Report	Full Council/Cabinet	Annually by 30 September after the end of the financial year
Quarterly Treasury Management Update Reports	Directors/Cabinet	Quarterly
Treasury Management Monitoring Reports	Reports prepared by Investment Officer to the Head of Treasury & Pensions who reports to the Section151 Officer	Monthly
Treasury Management Practices	Section 151 Officer	As required
Scrutiny of Treasury Strategy	Audit Committee	Annually before the start of the financial year
Scrutiny of the treasury management performance	Audit Committee	Half yearly

7. Treasury Strategy 2021/22

7.1. The Local Government Act 2003 and supporting Regulations requires the Council to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that capital investment plans are affordable, prudent and sustainable. This report incorporates the indicators to which regard should be given when determining the Council's Treasury Management Strategy for the next financial year.

7.2. As the Council is responsible for housing, Prudential Indicators relating to Capital Expenditure, financing costs and the Capital Financing Requirement will be split between the Housing Revenue Account (HRA) and the General Fund.

7.3. The Act also requires the Council to set out its Treasury Strategy for borrowing and to prepare an Annual Investment Strategy. This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

7.4. The proposed Strategy for 2021/22 in respect of the following aspects of the treasury management function is based upon the Section 151 Officer's view on interest rates, supplemented with leading market forecasts provided by the Council's Treasury Advisor, Link Asset Services.

7.5. The proposed strategy will focus on the following areas of treasury activity:-

- Treasury limits in force which will limit the treasury risk and activities of the Council.
- The determination of Prudential and Treasury Indicators.
- The current treasury position.
- Prospects for interest rates.
- Capital borrowing strategy.
- Policy on borrowing in advance of need.
- Debt rescheduling.
- Investment strategy.
- Capital plans.
- Creditworthiness policy.
- Policy on use of external service providers.
- The MRP strategy.
- Leasing.

7.6. It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This therefore means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from:-

- increases in interest charges caused by increased borrowing to finance additional capital expenditure, and

- any increase in running costs from new capital projects

are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

8. Treasury Limits for 2021/22 to 2023/24

8.1. It is a statutory requirement under Section 3 of the Local Government Act 2003 and supporting Regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Affordable Borrowing Limit". This authorised limit represents the legislative limit specified in section 3 of the Local Government Act 2003.

8.2. The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits.

8.3. Whilst termed an "Affordable Borrowing Limit", the capital plans to be considered for inclusion incorporate those planned to be financed by both internal/external borrowing and other forms of liability, such as credit arrangements. The Authorised Borrowing Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years and is the limit which the Council must not breach. All of the other Prudential Indicators are estimates only and can be breached temporarily but this is very rarely the case. If this did happen it would be reported to Members outlining the reasons for this temporary breach.

8.4. The Council are asked to approve these Prudential Indicators in Appendix 1.

9. Prudential & Treasury Indicators for 2021/22 to 2023/24

9.1. The Prudential Code and CIPFA Code of Practice on Treasury Management require the Council to set a number of Prudential and Treasury Indicators. Following the December 2017 publication of the revised CIPFA Treasury Management Code of Practice, there is no longer a requirement to include the prudential indicator showing the incremental impact on the Council tax / Housing rents of Capital Investment decisions, so this has been removed. In addition to the specified indicators, we have set further internal indicators for Treasury Management, regarding lower limits on interest rate exposure for both borrowing and investments.

9.2. It should be noted that these indicators should not be used for comparison with indicators from other local authorities. Use of them in this way would be likely to be misleading and counterproductive as other authorities Treasury Management policies and practices vary. The most important indicator is prudential indicator number 4 which specifies the authorised limit which cannot be breached under any circumstances. In the event that this indicator was breached a separate report would be brought to Council.

9.3. **Prudential Indicator 1** - The ratio of financing costs indicator shows the trend in the cost of financing capital expenditure as a proportion of the Authority's net revenue. This indicator also shows the ratio of the HRA financing costs to the HRA net revenue stream.

Prudential Indicator No. 1	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
	%	%	%	%
Non HRA ratio of financing costs (gross of investment income) to net revenue stream	9.0	7.6	9.0	8.3
Non HRA ratio of financing costs (net of investment income) to net revenue stream	8.5	7.2	8.5	7.8
HRA Ratio of financing costs to HRA net revenue stream	38.2	39.9	39.3	38.7

9.4. **Prudential Indicator 2** - A key indicator of prudence is that gross external borrowing should not, except in the short term, exceed the capital financing requirement (CFR). The capital financing requirement is the maximum we would expect to borrow based on the current capital programme. Compliance with the indicator will mean that this limit has not been breached. Gross borrowing includes debt administered on behalf of Telford and Wrekin Council, Magistrates Courts and Probation Service. It also includes the debt transferred from Oswestry Borough Council and North Shropshire District Council on the 1st April 2009. In accordance with the Code the HRA Capital Financing requirement has been calculated separately and has been updated due to the HRA reform which took place on the 28 March 2012.

Prudential Indicator No. 2	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Net Borrowing & Capital Financing Requirement:	**£ m**	**£ m**	**£ m**	**£ m**	**£ m**
Non HRA Capital Financing Requirement	386	383	419	436	494
HRA Capital Financing Requirement	85	85	95	105	115
Commercial activities/non-financial investments Capital Financing Requirement	10	17	63	101	98
Total CFR	**481**	**485**	**577**	**642**	**707**
Movement in CFR	**6**	**5**	**92**	**65**	**65**
Movement in CFR represented by					
Net financing need for the year (above)	11	8	65	79	59
Less MRP/VRP and other financing movements	-5	-3	27	-14	6
Movement in CFR	**6**	**5**	**92**	**65**	**65**
Gross Borrowing including HRA	308	304	366	455	519
Investments	157	160	150	140	130
Net Borrowing	**151**	**144**	**216**	**315**	**389**

9.5. **Prudential Indicator 3** - The estimated capital expenditure has been split between Non HRA and HRA and represents commitments from previous years to complete ongoing schemes, the expenditure arising from the proposed new schemes within the capital programme for 2020/21, and the estimated expenditure for 2021/22, 2022/23 and 2023/24. This indicator also includes details on the financing of capital expenditure.

Prudential Indicator No. 3	**2019/20 Actual**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**	**2023/24 Estimate**
	£ m	**£ m**	**£ m**	**£ m**	**£ m**
Non HRA Capital expenditure	46.5	63.2	114.2	112.4	72.8
HRA Capital expenditure	6.0	5.9	20.1	19.8	14.0
Commercial activities/non-financial investments	6.7	4.3	35.4	30.0	0.0
Total Capital expenditure	**59.2**	**73.4**	**169.7**	**162.2**	**86.8**
Financing of capital expenditure					
Capital receipts	2.2	8.3	15.9	5.0	0.0
Capital grants	37.0	47.8	56.7	61.9	3.0
Other Contributions	3.7	7.9	24.5	0.1	0.0
Major Repairs Allowance	3.7	3.5	1.0	3.8	0.0
Revenue	3.6	1.4	4.3	3.0	1.0
Net financing need for the year	**9.0**	**4.5**	**67.3**	**88.4**	**82.8**
Commercial activities/non-financial investments	**2019/20 Actual**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**	**2023/24 Estimate**
	£ m	**£ m**	**£ m**	**£ m**	**£ m**
Capital expenditure	6.7	4.3	35.4	30.0	0.0
Financing Costs	0.2	0.2	1.1	0.9	0.0
Net financing need for the year	**6.5**	**4.1**	**34.3**	**29.1**	**0.0**
Percentage of total net financing need	97%	96%	97%	97%	100%

9.6. **Prudential Indicator 4 which must not be breached** - The authorised limit is the borrowing limit set for Shropshire Council and includes the HRA borrowing. This indicator shows the maximum permitted amount of outstanding debt for all purposes. It includes three components:

1. The maximum amount for capital purposes;
2. The maximum amount for short term borrowing to meet possible temporary revenue shortfalls;
3. The maximum permitted for items other than long term borrowing i.e. PFI & leasing.

Prudential Indicator No. 4	2021/22	2022/23	2023/24
External Debt	**£ m**	**£ m**	**£ m**
Authorised Limit for External Debt:			
Borrowing	615	630	689
Other long term liabilities	96	92	98
Commercial activities/ non-financial investments	46	39	0
Total	**757**	**761**	**787**

9.7. The HRA debit limit is as follows:

Prudential Indicator	2020/21	2021/22	2022/23	2023/24
	£ m	**£ m**	**£ m**	**£ m**
HRA CFR	85	95	105	115

9.8. **Prudential Indicator 5 –** The more likely outcome for the level of external debt is shown in the operational boundary which the Council is required to set. This is calculated on the same basis as prudential indicator number 4, however, this is the limit which external debt is not normally expected to exceed.

Prudential Indicator No. 5	2021/22	2022/23	2023/24
External Debt	**£ m**	**£ m**	**£ m**
Operational Boundary:			
Borrowing	500	559	622
Other long term liabilities	96	92	98
Commercial activities/ non-financial investments	46	39	0
Total	**642**	**690**	**720**

9.9. **Prudential Indicator 6** - The estimated external debt is based on the capital programme for 2020/21.

Prudential Indicator No. 6	2019/20 Actual	2020/21 Estimate
Actual External Debt	**£ m**	**£ m**
Borrowing	308	304
Other long term liabilities	102	98
Total	**410**	**402**

9.10. **Prudential Indicator 7** - The Prudential Code requires the Council to set interest rate exposure limits for borrowing and investments.

Prudential Indicator No. 7* Internal Indicator No. 1 ** No. 7^ Internal Indicator No. 2 ^^	**2021/2022**	**2022/2023**	**2023/2024**
Borrowing Limits			
	£ m	**£ m**	**£ m**
Upper Limit for Fixed Interest Rate Exposure *	615	630	689
Upper Limit for Variable Interest Rate Exposure ^	308	315	345
Lower Limit for Fixed Interest Rate Exposure **	307	315	344
Lower Limit on Variable Interest Rate Exposure ^^	0	0	0

These indicators seek to control the amount of debt exposed to fixed and variable interest rates. Variable rate debt carries the risk of unexpected increases in interest rates and consequently increases in cost. The upper limit for variable rate exposure has been set following advice from Link, however, this limit is never likely to be reached due to authority's objective to have no more than 25% of outstanding debt at variable interest rates.

Upper limit for fixed rate exposure
Calculation: A maximum of 100% of the Authorised Limit (£615m in 2021/22) exposed to fixed rates is consistent with the Authority's objective to have a long term stable debt portfolio.

Upper limit for variable rate exposure
Calculation: For efficient management of the debt portfolio it is considered prudent by Link to permit up to 50% (£308m in 2021/22) of the Authorised Limit to be borrowed at variable interest rates.

Lower limit for fixed rate exposure
Calculation: Upper limit for fixed rate exposure less the maximum permitted borrowing at variable interest rates

Lower limit for variable rate exposure
Calculation: To be consistent with the Authority's objective to have a long term stable portfolio all of the debt portfolio could be at a fixed rate therefore the lower limit for variable rate exposure should be nil.

Prudential Indicator No. 8* Internal Indicator No. 3 ** No. 8^ Internal Indicator No. 4 ^^	2021/22	2022/23	2023/24
Investment Limits			
	£ m	**£ m**	**£ m**
Upper Limit for Fixed Interest Rate Exposure *	250	250	250
Upper Limit for Variable Interest Rate Exposure ^	250	250	250
Lower Limit for Fixed Interest Rate Exposure **	0	0	0
Lower Limit on Variable Interest Rate Exposure ^^	0	0	0

These indicators seek to control the amount of investments exposed to fixed and variable interest rates. Variable rate investments are subject to changes in interest rates, but have a higher degree of liquidity and action can be taken at short notice in response to interest rate changes.

Upper limit for fixed rate exposure
Calculation: Maximum amount of fixed rate investments in order to maintain a stable investment portfolio.

Upper limit for variable rate exposure
Calculation: For the purposes of efficient portfolio management in response to interest rate conditions a maximum potential exposure to variable rates of £250m in 2021/22 is recommended.

Lower limit for fixed rate exposure
Calculation: A lower limit of zero is locally set so as to enable full advantage to be taken of market conditions.

Lower limit for variable rate exposure
Calculation: A lower limit of zero is locally set so as to enable full advantage to be taken of market conditions.

9.11. **Prudential Indicator 9** - The upper and lower limit for the maturity structure of borrowings is detailed below.

Prudential Indicator No. 9	**Upper Limit**	**Lower Limit**
Maturity Structure of Fixed/Variable Rate Borrowing 2021/22*	**%**	**%**
Under 12 months	15	0
12 months & within 24 months	15	0
24 months & within 5 years	45	0
5 years to 10 years	75	0
10 years to 20 years	100	0
20 years to 30 years	100	0
30 years to 40 years	100	0
40 years to 50 years	100	0
50 years and above	100	0

- **The internal limit is to have no more than 15% of total outstanding debt maturing in any one financial year. This is to ensure that the risk of having to replace maturing debt at times of high interest rates is controlled.**

9.12. **Prudential Indicator 10** - The Council is required to set maximum levels for investments over 365 days for both the internal treasury team and an external fund manager if appointed.

Prudential Indicator No. 10	**2021/22**	**2022/23**	**2023/24**
Investment Limits			
	£m	£m	£m
Upper Limit for Total Principal Sums Invested for over 365 days:			
Externally Managed (if appointed)	30	30	30
Internally Managed	70	70	70
Shrewsbury Shopping Centres	60	70	80

Rationale: The limit for the external cash fund manager has been set at £30 million in the event that an external manager is appointed. The limit for the internal treasury team has been set in order for the authority to potentially take advantage of more stable returns going forward. This includes the lending to date to local housing associations and future lending to Cornovii Homes. A separate limit of £60 million is included for the investment in units held within the JPUT for the Shrewsbury Shopping Centres. This limit is higher than the gross capital investment cost of £53.1m as it includes headroom for any future capital investment requirements.

10. Current Treasury Position

10.1 The Council's treasury position at 31 December 2020 is set out below:-

Outstanding debt for capital purposes	Actual £m
Long-term fixed rate PWLB	254.4
Long term fixed rate – Market	49.2
Total	**303.6**

Investments	£m
Internally managed - long term (1 Year)	15.0
- short term cash flow	155.4
Total	**170.4**

11. Prospects for Interest Rates

11.1. The Council retains the services of Link Asset Services as adviser on treasury matters and part of the service provided is to help the Council to formulate a view on interest rates. The following table gives the latest Link central view:-

Link's interest rate forecast as at December 2020

Link Group Interest Rate View 9.11.20

These Link forecasts have been amended for the reduction in PWLB margins by 1.0% from 26.11.20

	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
5 yr PWLB	0.80	0.80	0.80	0.80	0.80	0.90	0.90	0.90	0.90	0.90	1.00	1.00	1.00	1.00
10 yr PWLB	1.10	1.10	1.10	1.10	1.10	1.20	1.20	1.20	1.20	1.20	1.30	1.30	1.30	1.30
25 yr PWLB	1.50	1.50	1.60	1.60	1.60	1.60	1.70	1.70	1.70	1.70	1.80	1.80	1.80	1.80
50 yr PWLB	1.30	1.30	1.40	1.40	1.40	1.40	1.50	1.50	1.50	1.50	1.60	1.60	1.60	1.60

Link's current interest rate view is that Bank Rate will: -

- remain at its current level of 0.1% until March 2024.

The effect on interest rates for the UK is expected to be as follows:-

Short-term interest rates (investments)

11.2. The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it has left Bank Rate unchanged at its subsequent meetings to date, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected in the forecast table above as economic recovery is expected to be only gradual and, therefore, prolonged.

These forecasts were based on an assumption that a Brexit trade deal would be agreed by 31 December 2020, as this has now occurred these forecasts do not need to be revised. Investment returns are likely to remain exceptionally low during 2021/22 with little increase in the following two years.

Long-term interest rates (borrowing)

11.3. The 50 year PWLB rate is expected to rise gradually to reach 1.5% by the end of June 2022. It is expected to continue rising gradually to reach 1.6% by the end of June 2023. There is scope for it to move around the central forecast by + or – 0.25%. The 25 year PWLB rate is also expected to rise slightly to reach 1.7% by the end of June 2022 and 1.8% by the end of June 2023. The 10 year PWLB rate is expected to rise gradually to 1.1% by the end of March 2022. Again further gradual rises are expected in 2023/24. The 5 year PWLB rate is also expected to rise gradually from 0.8% to 0.9% by the end of March 2022 and to 1.0% by the end of June 2023. The PWLB rates and forecasts shown above take into account the review of PWLB margins over gilt yields. Subsequently, all forecasts have been reduced by 1%.

11.4. Borrowing interest rates fell to historically very low rates as a result of the COVID-19 crisis and the quantitative easing operations of the Bank of England. Gilt yields up to 6 years have been negative during most of the first half of 20/21.

11.5. In November, the Chancellor announced the conclusion to the review into PWLB rates; the rates offered by the PWLB were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which intended to purchase assets primarily for yield in its three year capital programme.

12. Borrowing Strategy

12.1. The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council’s reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

12.2. The approved borrowing requirement identified within the Capital Programme 2021/22 to 2023/24 is prudential borrowing of £118.909 million. In addition to this there is an anticipated prudential borrowing requirement for future prioritised schemes in the Capital Strategy 2021/22 to 2023/24 of £113.670 million. The Council will adopt a pragmatic approach to changing circumstances when considering new borrowing if required in the future. Consideration will be given to the following:-

i) As long term borrowing rates are expected to be higher than investment rates and look likely to be for the next couple of years or so all new external borrowing may be deferred in order to maximise savings in the short term. The running down of investments also has the added benefit of reducing exposure to interest rate and credit risk. However, in view of the overall forecast for long term borrowing rates to increase over the next few years, consideration will also be given to weighing up the short term advantage of internal borrowing against potential long term costs if the opportunity is missed for taking loans at long term rates which will be higher in future years.

ii) Temporary borrowing from the money markets or other local authorities.

iii) PWLB variable rate loans for up to 10 years.

iv) Long term fixed rate market loans (including loans offered by the Municipal Bond Agency) at rates below PWLB rates for the equivalent maturity period.

v) Short term PWLB rates are expected to be cheaper than longer term borrowing therefore borrowing could be undertaken in the under 10 year period early on in the financial year when rates are expected to be at their lowest. This will also have the added benefit of spreading debt maturities away from a concentration in longer dated debt.

vi) If it was felt that there was a significant risk in a sharp fall in long and short term rates then long term borrowings will be postponed. If it was felt there was a significant risk of a sharp rise in long and short term rates then the portfolio position would be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

12.3. Delegated authority is sought for the Section 151 Officer to exercise the borrowing powers contained in the Local Government Act 2003 to manage the debt portfolio.

13. External versus internal borrowing

13.1. The Prudential Code requires the Council to explain its policy on gross and net debt. The Council currently has gross debt of £304 million and net debt (after deducting cash balances) of £134 million. The next financial year is expected to see the Bank Rate remain at 0.10% and potentially remaining at this rate for next two financial years. As borrowing rates are expected to be higher than investment rates this would indicate that value could best be obtained by avoiding new external borrowing and using internal cash balances to finance new capital expenditure. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. This is referred to as internal borrowing and maximises short term savings. This is subject to change as the country navigates its way through and out of the coronavirus pandemic.

13.2. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

13.3. The Council has examined the potential for undertaking early repayment of some external debt in order to reduce the difference between its gross and net debt positions. However, the introduction by the PWLB of significantly lower rates for repayments than for new borrowing means that large premiums would be incurred, and such levels of premiums cannot be justified on value for money grounds.

13.4. Against this background caution will be adopted with the 2021/22 treasury operations. The Section 151 Officer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to Members at the next available opportunity.

14. Policy on borrowing in advance of need

14.1. 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 value for money can be demonstrated and that the Council can ensure the security of such funds.

14.2. In determining whether borrowing will be undertaken in advance of need the Council will:-

- Ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need.
- Ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered.
- Evaluate the economic and market factors that might influence the manner and timing of any decision to borrow.
- Consider the merits and demerits of alternative forms of funding.
- Consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.
- Consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balance and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

15. Debt Rescheduling

15.1. Consideration will be given to the potential for making savings by running down investment balances to repay debt prematurely as short-term rates on investments are likely to be lower than rates currently paid on debt. However, this will need careful consideration in the light of premiums that may be incurred by such a course of action. The proposals for debt rescheduling are a continuation of the existing policy and such transactions will only be undertaken:-

- in order to generate cash savings at minimum risk.
- to help fulfil the strategy set out above.
- in order to enhance the balance of the long-term portfolio by amending the maturity profile and/or volatility of the portfolio.

15. Investment Strategy

15.1. The MHCLG and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy.

15.2. The Council is required, under CIPFA's Treasury Management Code of Practice, to formulate an Annual Investment Strategy (Appendix 2). This outlines the Council's approach to:-

- Security of capital
- Creditworthiness policy
- Monitoring of credit ratings
- Specified and Non Specified Investments
- Temporary Investments

15.3 The Council's investment priorities are the security of capital and the liquidity of its investments. The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk as outlined in the Annual Investment Strategy.

15.4 The Council are asked to approve the Investment Strategy set out in Appendix 2.

16. Minimum Revenue Provision (MRP) Statement

16.1 The Council is required to pay off an element of the accumulated general fund capital spend each year (the CFR) through a revenue charge (the Minimum Revenue Provision - MRP) although it is also allowed to undertake additional voluntary payments if required. MHCLG regulations have been issued which require the full Council to approve an MRP Statement in advance of each year. Council are asked to approve the Minimum Revenue Provision Statement set out in Appendix 3.

17. Leasing

17.1. In the past the Council has used operating leases to finance the purchase of vehicles and equipment. The Section 151 Officer will assess the relative merits of operating and finance leases on a case by case basis and enter into the most advantageous. Schools I.T equipment will continue to be internally financed by borrowing against a small fund set against school balances with schools repaying their borrowing over a period of 3 years.

18. Lending to Housing Associations

18.1. As previously approved by full Council, the Council has offered to lend funds to Connexus Housing Ltd (which incorporates South Shropshire Housing Association and the Meres & Mosses Housing Association) and Severnside Housing at an agreed rate.

18.2. It has been agreed that the interest rate charged will depend on the period over which the loan is to be taken and that it will be linked to the applicable PWLB rate plus an administration fee. It has been agreed to offer to lend up to £10 million to each of these Housing Associations in order to support the building of affordable housing and shared office accommodation in Shropshire. For security purposes, each loan has been secured against existing assets held by or owned by the Housing Association. Officers have sought advice from Wragge & Co who have confirmed that the Council has the power to lend funds to Housing Associations under the Housing Act 1996 and have drawn up the legal documentation relating to the loan agreement. To date £9,770,000 has been drawn down by Connexus Housing Ltd and £10,000,000 by Severnside Housing.

18.3. Following Council approval on 28th February 2019, Shropshire Council formed a Wholly Owned Local Housing Company, known as Cornovii Homes. An initial unsecured loan to the Company of £1 million was also approved to provide funding for operating and set up costs. The Council has subsequently approved funding in the form of equity and a loan to facilitate land purchases and development costs. The loan element, totalling £49 million broken down in two agreements of £14 million and £35 million; is anticipated to be released to the Company over the next few financial years.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)
Treasury Management Practices

Treasury Strategy 2020/21 (Council 27 February 2020)

Treasury Strategy 2020/21 Mid-Year Review (Council 17 December 2020)

Financial Strategy Report 2021/22 to 2025/26 (Cabinet 14 December 2020)

Shrewsbury Shopping Centres Report (Council 14 December 2017)

Cornovii Initial loan approval paper, (Council 28 February 2019)

Cabinet Member : David Minnery, Portfolio Holder for Finance

Local Member

N/A

Appendices:

1 – Prudential Indicators

2 – Council's Annual Investment Strategy

3 – Minimum Revenue Provision Policy Statement

Prudential Indicators

Prudential Indicator	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
	%	%	%	%
Non HRA ratio of financing costs to net revenue stream	9.0	7.6	9.0	8.3
HRA ratio of financing costs to HRA net revenue stream	38.2	39.9	39.3	38.7

Prudential Indicator	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
	%	%	%	%
Non HRA ratio of financing costs (net of investment income) to net revenue stream	8.5	7.2	8.5	7.8

Prudential Indicator	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Net Borrowing & Capital Financing Requirement:	**£ m**	**£ m**	**£ m**	**£ m**	**£ m**
Non HRA Capital Financing Requirement	386	383	419	436	494
HRA Capital Financing Requirement	85	85	95	105	115
Commercial activities/non-financial investments Capital Financing Requirement	10	17	63	101	98
Total CFR	**481**	**485**	**577**	**642**	**707**
Movement in CFR	**6**	**5**	**92**	**65**	**65**
Movement in CFR represented by					
Net financing need for the year (above)	11	8	65	79	59
Less MRP/VRP and other financing movements	-5	-3	27	-14	6
Movement in CFR	**6**	**5**	**92**	**65**	**65**
Gross Borrowing (including HRA)	308	304	366	455	519
Investments	157	160	150	140	130
Net Borrowing	**151**	**144**	**216**	**315**	**389**

Prudential Indicator	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
	£ m	£ m	£ m	£ m	£ m
Non HRA Capital expenditure	46.5	63.2	114.2	112.4	72.8
HRA Capital expenditure	6.0	5.9	20.1	19.8	14.0
Commercial activities/non-financial investments	6.7	4.3	35.4	30.0	0.0
Total Capital expenditure	**59.2**	**73.4**	**169.7**	**162.2**	**86.8**
Financing of capital expenditure					
Capital receipts	2.2	8.3	15.9	5.0	0.0
Capital grants	37.0	47.8	56.7	61.9	3.0
Other Contributions	3.7	7.9	24.5	0.1	0.0
Major Repairs Allowance	3.7	3.5	1.0	3.8	0.0
Revenue	3.6	1.4	4.3	3.0	1.0
Net financing need for the year	**9.0**	**4.5**	**67.3**	**88.4**	**82.8**
Commercial activities/non-financial investments	**2019/20 Actual**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**	**2023/24 Estimate**
	£ m	**£ m**	**£ m**	**£ m**	**£ m**
Capital expenditure	6.7	4.3	35.4	30.0	0.0
Financing Costs	0.2	0.2	1.1	0.9	0.0
Net financing need for the year	**6.5**	**4.1**	**34.3**	**29.1**	**0.0**
Percentage of total net financing need	97%	96%	97%	97%	100%

Prudential Indicator	2021/22	2022/23	2023/24
External Debt	£ m	£ m	£ m
Authorised Limit for External Debt:			
Borrowing	615	630	689
Other long term liabilities (PFI)	96	92	98
Commercial activities/ non-financial investments	46	39	0
Total	**757**	**761**	**787**

Prudential Indicator	2020/21	2021/22	2022/23	2023/24
	£ m	£ m	£ m	£ m
HRA CFR	85	95	105	115

Prudential Indicator	2021/22	2022/23	2023/24
External Debt	£ m	£ m	£ m
Operational Boundary:			
Borrowing	500	559	622
Other long term liabilities (PFI)	96	92	98
Commercial activities/ non-financial investments	46	39	0
Total	**642**	**690**	**720**

Prudential Indicator	2019/20 Actual	2020/21 Estimate
External Debt	£ m	£ m
Borrowing	308	304
Other long term liabilities (PFI)	102	98

Total	410	402

Prudential Indicator	2021/22	2022/23	2023/24
Borrowing Limits	**£ m**	**£ m**	**£ m**
Upper Limit for Fixed Interest Rate Exposure	615	630	689
Upper Limit for Variable Interest Rate Exposure	308	315	345
Lower Limit for Fixed Interest Rate Exposure	307	315	344
Lower Limit on Variable Interest Rate Exposure	0	0	0

Prudential Indicator	2021/22	2022/23	2023/24
Investment Limits	**£ m**	**£ m**	**£ m**
Upper Limit for Fixed Interest Rate Exposure	250	250	250
Upper Limit for Variable Interest Rate Exposure	250	250	250
Lower Limit for Fixed Interest Rate Exposure	0	0	0
Lower Limit on Variable Interest Rate Exposure	0	0	0

Prudential Indicator	Upper Limit	Lower Limit
Maturity Structure of Fixed/Variable Rate Borrowing During 2021/22 **	**%**	**%**
Under 12 months	15	0
12 months & within 24 months	15	0
24 months & within 5 years	45	0
5 years & within 10 years	75	0
10 years & within 20 years	100	0
20 years & within 30 years	100	0
30 years & within 40 years	100	0
40 years & within 50 years	100	0
50 years and above	100	0

**** Internal limit is to have no more than 15% of total outstanding debt maturing in any one financial year.**

Prudential Indicator	2021/22	2022/23	2023/24
Investment Limits			
	£m	£m	£m
Upper Limit for Total Principal Sums Invested for over 365 days:			
Externally Managed (if appointed)	30	30	30
Internally Managed	70	70	70
Shrewsbury Shopping Centres	60	70	80

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The Council's Annual Investment Strategy

The Council's investment policy has regard to the MHCLG Guidance on Local Government Investments and the CIPFA Treasury Management Code of Practice which requires the Council to formulate a strategy each year regarding the investment of its revenue funds and capital receipts. Authorities are required to take the guidance into account under the terms of section 12 of the Local Government Act 2003.

In accordance with the above guidance from the MHCLG 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.

The income and expenditure flow of the Council is such that funds are temporarily available for investment. Under the Annual Investment Strategy the Council may use, for the prudent management of its treasury balances, any of the investments highlighted under the headings of **Specified Investments** and **Non-Specified Investments** as detailed on the attached table (Appendix 2A).

Creditworthiness Policy

The Council uses the creditworthiness service provided by its treasury advisor, 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. In addition, in line with the Treasury Management Code of Practice, it does not rely solely on the current credit ratings of counterparties but also uses the following overlays:-

- Credit watches and credit outlooks from credit rating agencies.
- Credit Default Swap (CDS) spreads to give an 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 duration of investments and are therefore referred to as durational bands. The Council is satisfied that this service gives the required level of security for its investments. It is also a service which the Council would not be able to replicate using in house resources.

The selection of counterparties with a high level of creditworthiness will be achieved by a selection of institutions down to a minimum durational band with Link's weekly credit list of worldwide potential counterparties. The Council will therefore use counterparties within the following durational bands:-

- Yellow – 5yrs e.g. AAA rated Government debt, UK Gilts, Collateralised Deposits
- Dark Pink – 5 years for Ultra-Short Dated Bond Funds or Enhanced Money Market Funds with a credit score of 1.25 (Not currently used)
- Light Pink - 5 years for Ultra-Short Dated Bond Funds or Enhance Money Market Funds with a credit score of 1.5 (Not currently used)
- Purple - 2yrs (Council currently has maximum of 1 year)
- Blue - 1 year (only applies to nationalised or part nationalised UK Banks)
- Orange - 1 year
- Red - 6 months
- Green – 100 days
- No colour – not to be used

The Link Asset Services creditworthiness service uses ratings from all three agencies and uses a wider array of information than just primary credit ratings to determine creditworthy counterparties. By using this approach and applying it to a risk weighted scoring system, it does not give undue over reliance to just one agency's ratings.

Monitoring of Credit Ratings

All credit ratings will continue to be monitored continuously and formally updated monthly if any changes are required. The Council is alerted to interim changes in ratings from all three agencies by Link Asset Services.

If a counterparty's or investment scheme's rating is downgraded with the result that it no longer meets the Council's minimum criteria, the further use of that counterparty will be withdrawn immediately. If a counterparty is upgraded so that it fulfils the Councils criteria, its inclusion will be considered for approval by the S151 Officer.

In addition to credit ratings the Council will be advised of information in movements in CDS against the iTraxx benchmark and other market data on a daily basis via the Passport website. Extreme market movements may result in the downgrade of an institution or the removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition the Council will monitor the financial press and also use other market data and information e.g. information on external support for banks.

UK banks – ring fencing

The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as "ring-fencing". Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank, (RFB), will be focused on lower risk, day-to-day core transactions, whilst more complex and "riskier" activities are required to be housed in a separate entity, a non-ring-fenced bank, (NRFB). This is intended to ensure that an entity's core activities are not adversely affected by the acts or omissions of other members of its group.

While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Council will continue to assess the new-formed entities in the same way that it does others and those with sufficiently high ratings, (and any other metrics considered), will be considered for investment purposes.

The Council currently has investments with HSBC, Barclays & Lloyds. HSBC and Lloyds are classified as ring fenced banks and Barclays as non ring fenced. All these institutions appear on Link Asset Services approved lending list and meet the council's creditworthiness criteria.

Country Limits

It is recommended that the Council will only use approved counterparties from the UK and from other countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies). It is recommended that UK institutions continue to be used unless the sovereign credit rating falls below A. Following the problems with Icelandic Banks lending is currently restricted to the UK which currently has a sovereign credit rating of AA and Sweden which has the highest possible sovereign rating of AAA. The S151 Officer has delegated authority to revert back to placing investments in countries with a minimum sovereign credit rating of AA- in line with Link's revised creditworthiness policy if required.

Security of Capital

The Council's current policy is to not place investments with any Foreign banks. The only exception to this is a call account set up with the Swedish bank, Handlesbanken, but this is a highly credit rated institution and the sovereign rating of Sweden is AAA as stated above. Funds are also repayable immediately if required. Following approval of the S151 Officer, lending to AAA rated Money Market Funds has also recommenced. Lending to other Foreign banks which comply with Link's creditworthiness policy may be considered again but only with the express approval of the S151 Officer.
In addition, in order not to solely rely on an institution's credit ratings there have also been a number of other developments which require separate consideration and approval for use:

Part Nationalised banks in the UK effectively take on the creditworthiness of the Government itself i.e. deposits made with them are effectively being made to the Government. This is because the Government owns significant stakes in the banks and this ownership is set to continue. Link are still supportive of the Council using these institutions with a maximum 12 month duration. For this reason Royal Bank of Scotland (RBS) and National Westminster Bank which are part of the RBS Group are included on the approved counterparty list.

Local Authorities are not credit rated but where the investment is a straightforward cash loan, statute suggests that the credit risk attached to local authorities is an acceptable one (Local Government Act 2003 s13). Local Authorities are therefore included on the approved list.

The total permitted investment in any one organisation at any one time varies with the strength of the individual credit rating. For the highest rated and Part

Nationalised Institutions the maximum amount is currently limited to £20m. Any changes to the maximum limit must be approved by the S151 Officer.

MHCLG Investment Guidance

Guidance from the MHCLG requires Councils to give priority to the security and portfolio liquidity of investments over yield whilst still aiming to provide good returns. This is in line with the Council's current practice and it is recommended that the policy should be reaffirmed.

The guidance also requires Councils to categorise their investments as either "specified" or "non-specified" investments.

(i) Specified Investments

Specified investments are deemed as "safer" investments and must meet certain conditions, ie they must :-

- be denominated in sterling
- have less than 12 months duration
- not constitute the acquisition of share or loan capital

- either: be invested in the UK government or a local authority
or a body or investment scheme with a "high" credit quality.

The Council is required to specify its creditworthiness policy and how frequently credit ratings should be monitored. It must also specify the minimum level of such investments.

Of the investments currently authorised by the Council, deposits in the Debt Management Office Account and with other Local Authorities automatically qualify as specified investments as they are of less than 12 months duration and are denominated in sterling.

The classification of the other investments is dependent on the counterparty having high credit quality in line with Link's creditworthiness policy. The Council is alerted to any changes in an institutions credit rating by Link Asset Services.

(ii) Non Specified Investments

These are any investments which do not meet the specified investment criteria outlined above. The Council is required to look at non-specified investments in more detail. It must set out:

- procedures for determining which categories of non-specified investments should be used
- the categories deemed to be prudent
- the maximum amount to be held in each category

The Strategy must also set out procedures for determining the maximum period for committing funds.

It is recommended that the following procedure be adopted for determining which categories of non-specified investments should be used:

- the Cabinet/Council should approve categories on an annual basis
- advice should be provided by the S151 Officer

- priority should be given to security and portfolio liquidity ahead of yield

It is recommended that for specified investments the range of maximum limits is set between £5m and £20m for the internal treasury team. For non specified investments it is recommended that the limit for the internal treasury team should be restricted to £70m of the total investment portfolio (excluding the Shrewsbury Shopping Centre acquisition). Any changes to the maximum limits must be approved by the S151 Officer.

Temporary Investment Strategy

The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it has left Bank Rate unchanged. It is felt that the bank rate will remain at its current level of 0.10% for the next several years. This view is based on the latest forecasts obtained by the Authority's treasury advisor, Link Asset Services.

If an external fund manager is appointed in 2021/22 they would also have to adhere to the authorised specified and non-specified investments on the attached table. They would also have to comply with the Council's Annual Investment Strategy and their agreement must stipulate guidelines and other limits in order to contain and control risk.

The market is continually monitored for opportunities to lock in to higher, longer term rates in order to bring some stability to the returns going forward and add value. However, based on the interest rate assumptions outlined above, we do not expect to lock into longer term deals unless exceptionally attractive rates are available which make longer term deals worthwhile.

For the cash flow generated balances, we will seek to utilise instant access accounts, Money Market Funds and short dated deposits (1-3 months) in order to benefit from the compounding of interest.

The present strategy is to diversify investments so as to spread risk over a range of investment types and periods and provide the opportunity to enhance returns. Due to the current lending restrictions in place diversification has been some what reduced due to the reduction in the number of institutions which we can lend to, however, by taking this course of action the credit risk has been reduced. The portfolio as at 31 December 2020 is set out in paragraph 10.1 of the Treasury Strategy 2021/22 report. Performance of the in-house operation will continue to be monitored on a monthly basis by your officers in conjunction with the treasury advisor.

All investments will continue to be made in accordance with the Local Government Act 2003, and with those institutions on the authorised lending list. The credit status of institutions on the approved list is monitored continuously.

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

Policy on the use of external service providers

The Council currently uses Link Asset Services, as its external treasury management advisers. The Council recognises that the responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon our external service providers. The Council 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 review.

Scheme of Delegation

Full Council

- Approval of Treasury Strategy.
- Receiving and reviewing reports on treasury management policies, practices and activities including the Annual Treasury Report and Mid-Year Strategy Report.
- Budget consideration and approval

Cabinet

- Receiving & reviewing Treasury Strategy, Mid-Year Strategy Report, Annual Treasury Report and Quarterly Treasury Management Update Reports

Audit Committee

- Reviewing the treasury management policy and procedures and making recommendations to the responsible body.
- Receiving & reviewing Treasury Strategy, Mid Year Report, Annual Treasury Report.

Role of the Section 151 Officer

The role of the S151 Officer in relation to treasury management is as follows:-

- Recommending clauses, treasury management policy/practices for approval, reviewing the same regularly and monitoring compliance.
- Approval of segregation of responsibilities.
- Approval of the Treasury Policy Statement and Treasury Management Practices.
- 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.

The above list of specific responsibilities of the s151 Officer in the 2017 Treasury Management Code has not changed. However, implicit in the changes in both Codes, is a major extension of the functions of this role, especially in respect of non-financial investments:-

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long term timeframe.
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority
- ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following*:* -
    - *Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;*
    - *Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;*
    - *Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;*
    - *Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;*
    - *Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.*

Pension Fund Cash

The Council complies with the requirements of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 and does not pool pension fund cash with its own balances for investment purposes.

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LOCAL GOVERNMENT INVESTMENTS (England)

SPECIFIED INVESTMENTS

All investments listed below must be sterling-denominated.

Investment	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum Credit Criteria	Capital Expenditure?	Circumstance of use	Maximum period
Term deposits with the UK government (e.g. DMO Account) or with local authorities (i.e. local authorities as defined under Section 23 of the 2003 Act) with maturities up to 1 year	No	Yes	High security although most LAs not credit rated.	No	In-house and by external fund manager	1 year
Term deposits with credit-rated deposit takers (banks and building societies), including callable deposits, with maturities up to 1 year	No	Yes	Yes – Minimum colour band green	No	In-house and by external fund manager	1 year
Certificates of Deposit issued by credit-rated deposit takers (banks and building societies) up to 1 year. *Custodial arrangement required prior to purchase*	No	Yes	Yes – Minimum colour band green	No	In house buy and hold and External fund managers	1 year
Banks nationalised by high credit rated (sovereign rating) countries – non UK	No	Yes	Minimum Sovereign Rating AA-	No	In house and external fund managers	1 year

Investment	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / 'High' Credit Rating criteria	Capital Expenditure?	Circumstance of use	Maximum period
UK Nationalised & Part Nationalised banks	No	Yes	Yes – Minimum colour band green	No	In House and external managers	1 year
Government guarantee (explicit) on all deposits by high credit rated (sovereign rating) countries	No	Yes	Yes – Minimum Sovereign Rating AA- / UK Sovereign Rating	No	In house and external fund managers	1 year
Bonds issued by multilateral development banks (Euro Sterling Bonds as defined in SI 2004 No 534) **Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government e.g. National Rail** *Custodial arrangement required prior to purchase* Gilt Funds and Bond Funds (including Ultra-Short Dated Bond Funds)	No No No	Yes Yes Yes	AAA UK sovereign rating AAA	No No No	In-House on a buy and hold basis after consultation/advice from Link also for use by External fund manager In House and by external fund managers	1 year 1 year
Gilts : up to 1 year *Custodial arrangement required prior to purchase*	No	Yes	Govt-backed UK Sovereign Rating	No	In House on a buy and hold basis and for trading by external fund manager subject to the guidelines and parameters agreed with them	1 year

Investment	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / 'High' Credit Rating criteria	Capital Expenditure?	Circumstance of use	Maximum period
Money Market Funds (CNAV), Enhanced Money Market Funds (LVNAV & VNAV) & Government Liquidity Funds (including CCLA Fund)	No	Yes	Yes AAA rated & UK sovereign rating. Enhanced MMFs minimum colour Dark Pink/Light Pink & AAA rated	No	In-house and by external fund managers subject to the guidelines and parameters agreed with them	the period of investment may not be determined at the outset but would be subject to cash flow and liquidity requirements. Deposits are repayable at call.
Treasury bills [*Government debt security with a maturity less than one year and issued through a competitive bidding process at a discount to par value*] *Custodial arrangement required prior to purchase*	No	Yes	Govt-backed UK Sovereign Rating	No	In House or external fund managers subject to the guidelines and parameters agreed with them	1 year

Monitoring of credit ratings:
All credit ratings will be monitored continuously and formally updated on a monthly basis if required. If a counterparty or investment scheme is downgraded with the result that it no longer meets the Council's minimum credit criteria, the use of that counterparty / investment scheme will be withdrawn.
Any intra-month credit rating downgrade which the Council has identified that affects the Council's pre-set criteria will also be similarly dealt with.

LOCAL GOVERNMENT INVESTMENT (England)

NON-SPECIFIED INVESTMENTS

All investments listed below must be sterling-denominated (with the exception of the WME US dollar account).

Investment	(A) Why use it? (B) Associated risks?	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum credit rating	Capital Expen-diture?	Circumstance of use	Max % of overall investments	Maximum maturity of investment
Certificates of Deposit with credit rated deposit takers (banks and building societies) with maturities greater than 1 year *Custodial arrangement required prior to purchase*	(A) tradable more liquid than fixed term deposits (B) (i) 'Market or interest rate risk' : Yield subject to movement during life of CD which could negatively impact on price of the CD. (ii) Although in theory tradable, are relatively illiquid.	No	Yes	UK Sovereign rating	No	In house on a buy and hold basis after consultation/advice from Link & external cash fund manager(s) subject to the guidelines and parameters agreed with them.	50%	*Suggested limit :* Average duration in the portfolio not to exceed 5 years
Collateralised deposit	Deposits are backed by collateral of AAA rated local authority	No	Yes	UK Sovereign rating	No	In house & External Manager	25%	*5 years*
UK government gilts with maturities in excess of 1 year *Custodial arrangement required prior to purchase*	(A)((i) Excellent credit quality. (ii)Very Liquid). (iii) If held to maturity, known yield (rate of return) per annum ~ aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk (B) (i) 'Market or interest rate risk' : Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e. potential for capital loss.	No	Yes	UK Sovereign rating	NO	In house on a buy & hold basis following advice from Link and for trading by external cash fund manager subject to the guidelines and parameters agreed with them	50%	*Suggested limit :* Average duration in the portfolio not to exceed 5 years

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Investment	(A) Why use it? (B) Associated risks?	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum credit rating **	Capital Expen-diture?	Circumstance of use	Max % of overall investments	Maximum maturity of investment
Term deposits with UK government, other Local Authorities, and credit rated deposit takers (banks and building societies) including callable deposits with maturities greater than 1 year	(A)(i) Certainty of rate of return over period invested. (ii) No movement in capital value of deposit despite changes in interest rate environment. (B) (i) Illiquid : as a general rule, cannot be traded or repaid prior to maturity. (ii) Return will be lower if interest rates rise after making the investment. (iii) Credit risk : potential for greater deterioration in credit quality over longer period	No	No	Minimum colour band purple	NO	In-House For trading by external cash fund manager subject to the guidelines and parameters agreed with them	£40 million 50%	*Suggested limit:* 3 years
Sovereign bond issues ex UK Government Gilts: any maturity	(A) (i) Excellent credit quality. (ii) Liquid. (iii) If held to maturity, known yield (rate of return) per annum – aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk (B) (i) "Market or interest rate risk" : Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e. potential for capital loss	No	Yes	AAA	No	For trading by external cash fund manager only subject to the guidelines and parameters agreed with them	50%	*Suggested limit:* 5 years
Bonds issued by multilateral development banks (Euro-Sterling Bonds) or issued by a financial institution guaranteed by UK government Custodial arrangement required prior to purchase	(A) (i) Excellent credit quality. (ii) Liquid. (iii) If held to maturity, known yield (rate of return) per annum – aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk (B) (i) "Market or interest rate risk" : Yield subject to movement during life of bond which could negatively impact on price of the bond i.e. potential for capital loss	Yes	Yes	AAA	No	In house on a buy and hold basis after consultation/advice from Link. Also for use by external fund managers	10% 50%	5 years

Investment	(A) Why use it? (B) Associated risks?	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum credit rating **	Capital Expen-diture?	Circumstance of use	Max % of overall investments	Maximum maturity of investment
Corporate Bonds & Corporate Bond funds (the use of these investments would constitute capital expenditure although this is currently under review)	(A)(i) Excellent credit quality. (ii) Liquid. (iii) If held to maturity, known yield (rate of return) per annum – aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk (B)(i) “Market or interest rate risk” : Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e. potential for capital loss	Yes	Yes	Minimum Sovereign rating AA-	Yes	To be used by external fund managers only	50%	*Suggested limit:* *5 years*
Jersey Property Unit Trust (JPUT)	Required to facilitate the acquisition of the Shrewsbury Shopping Centres via a Jersey based Property Unit Trust – required only subject to full Council approval of the acquisition method on 14th December 2017.	No	No	No Minimum Credit rating – assets held within the fund to undergo annual valuation to determine value of Units within the Trust.	Yes	In House use following specialist technical and legal advice.	£60m	*5 years*
Pooled property funds – including CCLA Local Authorities Property Fund	Enhanced return but increased risk, only to be used following advice from Link	No	Yes	No Minimum Credit rating need to assess underlying assets within fund following advice taken from Link	No	In House Use & External Fund managers following advice from Link	20%	*5 years*
Floating Rate notes	(A)(i) Rate of return tied to some measure of current interest rates, so when interest rates are expected to go up they offer protection to investors against such rises (ii) In some circumstances may have access to banks which meet minimum credit criteria but generally don’t take small fixed term deposit cash amounts (B)(i) Credit quality : if financial health of issuer deteriorates, investors will demand a greater yield and the price of the bond will fall	Yes	Yes	Minimum Colour band green	No	In House Use & External Fund managers following advice from Link	10%	*3 years*
US Dollar Deposits (WME Only)	US dollar account to be utilised as a part of West Mercia Energy prudent management of income and expenditure, ensuring that ongoing US dollar commitments can be hedged, thus extinguishing any adverse risk of	No	Yes	Minimum Colour band green	No	West Mercia Energy Only	N/A	*3 Months*

	exposure to movements in the exchange rate and guaranteeing a known cashflow for West Mercia Energy. The account is only to be used for this purpose and not for the purpose of speculative or trading transactions.							

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Appendix 3

The Council's Annual Minimum Revenue Provision Statement

Statutory Requirements

The Council is required by statute to set aside a minimum revenue provision (MRP) to repay external debt. The calculation of the minimum revenue provision (MRP) is as per the *Local Authority (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414].* In regulation 28, detailed rules were replaced with a simple duty for an authority to make an amount of MRP which it considers to be "prudent".

The broad aim of a prudent provision is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant. The guidance includes four options (and there are two alternatives under Option three) for the calculation of a prudent provision.

There is no requirement to charge MRP where the Capital Financing Requirement (CFR) is nil or negative at the end of the preceding financial years. There is also no requirement to charge MRP on the Housing Revenue Account share of the CFR.

The legislation recommends that before the start of each financial year the Council prepares a statement of its policy on making MRP in respect of that financial year and submits it to the Full Council for approval.

Policy for Calculation of Prudent Provision

The options for the calculation of a Prudent Provision are detailed in appendix 3(a) to this report. Authorities must always have regard for the guidance and the decision on what is prudent is for the authority to conclude, taking into account detailed local circumstances, including specific project timetables and revenue-earning profiles.

Following a review of the MRP policy from 2018/19 the prudent provision for Supported Borrowing has been calculated based on the expected useful life of the asset on an annuity calculation basis.

Option 3a - Asset life method (Unsupported Borrowing) - equal instalment method will continue to be used for unsupported borrowing agreed prior to 2018/19 and specific treatment for PFI Assets and assets held under Finance Leases and long-term capital loans. For any approved unsupported borrowing from 2018/19 the prudent provision will be calculated on an annuity basis linked to the expected useful life of the asset for consistency with the Supported Borrowing calculation, Option 3b.

Supported Borrowing

From 2016/17 the approach for calculating the MRP was on a straight line (equal instalments) calculation basis on the remaining asset life of the assets linked to the borrowing. An analysis of the average remaining asset life of the assets financed from previous supported borrowing, determined the average remaining life to be around 45 years and this was used as the basis of calculation.

From 2018/19 Council approved to adopt the annuity calculation method for supported borrowing whilst retaining the link to the average remaining useful life of the assets it was used to finance. The annuity calculation method results in lower MRP payments in the early years, but higher payments in later years. This method has the advantage of linking MRP to the flow of benefits from an asset where these are expected to increase in later years.

CIPFA puts forward the following reasons for using the annuity method in CIPFA's "The Practitioner's Guide to Capital Finance in Local Government" (2008) which states:

- The annuity method provides a fairer charge than equal instalments as it takes account of the time value of money, whereby paying £100 in 10 year's time, is less of a burden than paying £100 now.
- The schedule of charges produced by the annuity method results in a consistent charge over an asset's life, taking into account the real value of the amounts when they fall due.
- The annuity method is a prudent basis for providing for assets that provide a steady flow of benefits over their useful life.

For 2018/19 and onwards the Council has adopted the annuity-based calculation on a 45-year basis.

Unsupported Borrowing - Asset Life Method

For new borrowing under the Prudential system for which no Government support is being given and is therefore self-financed (unsupported borrowing) the MRP has been calculated in accordance with Option 3 Asset Life Method. Option 3 is to make provision over the estimated life of the asset for which the borrowing is undertaken.

Freehold land cannot properly have a life attributed to it, so for the purposes of Option 3 it should be treated as equal to a maximum of 50 years. But if there is a structure on the land which the authority considers to have a life longer than 50 years, that same life estimate may be used for the land.

To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate. For energy efficiency schemes the payback period of scheme is used as the basis for calculating the period over which MRP is calculated.

This method is a straightforward calculation of MRP for unsupported borrowing which calculates MRP based on asset life.

Provision for debt under Option 3 will normally commence in the financial year following the one in which the expenditure is incurred. But the guidance highlights an important exception to the rule. In the case of a new asset, MRP would not have to be charged until the asset came into service and would begin in the financial year following the one in which the asset became operational. This “MRP holiday” would be perhaps two or three years in the case of major projects, or possibly longer for some complex infrastructure schemes, and could make them more affordable.

Prior to 2018/19 the Council adopted the Option 3a Straight Line calculation for unsupported borrowing. From 2018/19 Council approved to adopt the Option 3b annuity calculation method for new unsupported borrowing whilst retaining the link to the average remaining useful life of the assets it was used to finance. The annuity calculation method results in lower MRP payments in the early years, but higher payments in later years. This method has the advantage of linking MRP to the flow of benefits from an asset where these are expected to increase in later years.

The authority can still make voluntary extra provision for MRP in any year.

Adjustment A

This is an accounting adjustment to the MRP calculation that ensures consistency with previous capital regulations. Once calculated, the amount remains constant within the MRP calculations.

Between 2016/17 and 2017/18 the adjustment A was not included in the MRP calculation but continues to be a legitimate part of the calculation under the 2003 Regulations (Regulation 28) and can therefore continue to be used to reduce the supported borrowing CFR for MRP purposes. It has been considered to be prudent to include the Adjustment A value from 2018/19 onwards to calculate the CFR value. For Shropshire the fixed Adjustment A calculation is £4,446,483.75

PFI Assets and Assets Held Under Finance Leases

For assets under on-balance sheet PFI contracts and finance leases, the annual principal payment amount in the PFI or finance lease model is used as the MRP payment amount, with no additional charges above those within the contract.

Long Term Capital Loans

The Council has made available a small number or capital loans to Housing Associations and Village Halls, financed from the Councils balances. The annual repayments of principal amounts are treated as capital receipts and set aside in the Capital Adjustment Account in place of a revenue MRP charge.

Housing Revenue Account MRP

As at 31/03/21 the HRA CFR is £94.8m, this includes the £83.35m transferred to the Council as part of housing self-financing. In managing the HRA debt and considering the HRA business plan there is no mandatory requirement to make provision in the HRA for annual MRP payments. However, the Council will make annual voluntary provision for debt repayment in the HRA based on affordable levels in the HRA against the need for investment and delivering services in the HRA. The annual level of provision will be determined annually as part of the closure of the HRA.

2021/22 Annual MRP Statement

Appendix 3(b) provides the MRP statement for the 2021/22 financial year.

Capital Receipts Set Aside

The current regulations, Local Authority (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414] state that the minimum revenue provision is calculated using the previous year's closing Capital Financing Requirement for supported borrowing.

In 2009/10 Shropshire Council got DCLG approval to allow the new council to voluntarily set aside capital receipts as at 1st April 2009 to reduce the CFR and consequently reduce the MRP charge for 2009/10. This approach was discussed with our Treasury Advisors and External Auditors and was approved by Members in a report to Council in December 2009.

As the extent of new borrowing is not subject to any limitation the sum of capital receipts set aside are still available to support capital expenditure in future years. This will increase the CFR to its previous level and the MRP charge in future years will increase, but not beyond the level had the saving not been generated in 2009/10. Thus, the saving in MRP is therefore temporary, albeit very helpful to the short-term financial position.

As the full level of capital receipts set aside were not required to finance capital expenditure between 2009/10 and 2019/20, a balance was retained as set aside as at the end of each financial year to enable a further MRP saving in the following financial years. In the 2021/22 MRP Statement it has been assumed all the capital receipts retained as set aside as at 31 March 2021 to reduce the CFR will be offset by an increase in the CFR in 2021/22 from capital expenditure incurred in 2021/22. In the event that the level of capital expenditure in 2021/22 to be financed from the capital receipts set aside is below the level of capital receipts set aside, it is proposed to retain the balance in capital receipts as set aside in order to achieve a further MRP saving in 2022/23. This will be reported for approval as part of the Capital Outturn report 2020/21.

Appendix 3(a): Options for Prudent Provision

Option 1: Regulatory Method (Supported borrowing)
MRP is equal to the amount determined in accordance with the former regulations 28 and 29 of the 2003 Regulations, as if they had not been revoked by the 2008 Regulations. For the purposes of that calculation, the Adjustment A should normally continue to have the value attributed to it by the authority in the financial year 2004-05. However, it would be reasonable for authorities to correct any perceived errors in Adjustment A, if the correction would be in their favour.

Option 2: CFR Method (Supported borrowing)
MRP is equal to 4% of the non-housing CFR at the end of the preceding financial year without any adjustment for Adjustment A, or certain other factors which were brought into account under the previous statutory MRP calculation.

Option 3: Asset Life Method (Unsupported borrowing)
Where capital expenditure on an asset is financed wholly or partly by borrowing or credit arrangements, MRP is to be determined by reference to the life of the asset. There are two main methods by which this can be achieved, as described below. Under both variations, authorities may in any year make additional voluntary revenue provision, in which case they may make an appropriate reduction in later years' levels of MRP.

(a) Equal Instalment Method
MRP is the amount given by the following formula:

$$\frac{\mathbf{A - B}}{\mathbf{C}}$$

Where:
A is the amount of the capital expenditure in respect of the asset financed by borrowing or credit arrangements
B is the total provision made before the current financial year in respect of that expenditure
C is the inclusive number of financial years from the current year to that in which the estimated life of the asset expires.

For the purpose of the above formula in the initial year of making the MRP the variable "C" should be given the maximum values set out in the following table:

Expenditure Type	Maximum value of "C" in initial year
Expenditure capitalised by virtue of a direction under s16(2)(b)	"C" equals 20 years
Regulation 25(1)(a) Expenditure on computer programs	"C" equals the value it would have for computer hardware
Regulation 25(1)(b) Loans and grants towards capital expenditure by third parties	"C" equals the estimated life of the assets in relation to which the third-party expenditure is incurred
Regulation 25(1)(c) Repayment of grants and loans for capital expenditure	"C" equals 25 years, or the period of the loan, if longer
Regulation 25(1)(d) Acquisition of share or loan capital	"C" equals 20 years
Regulation 25(1)(e)	"C" equals the estimated life of the assets

Expenditure on works to assets not owned by the authority	
Regulation 25(1)(ea) Expenditure on assets for use by others	“C” equals the estimated life of the assets
Regulation 25(1)(f) Payment of levy on Large Scale Voluntary Transfers (LSVTs) of dwellings	“C” equals 25 years

(b) Annuity Method

MRP is the principal element for the year of the annuity required to repay over the asset life the amount of capital expenditure financed by borrowing or credit arrangements. The authority should use an appropriate interest rate to calculate the amount. Adjustments to the calculation to take account of repayment by other methods during the repayment period (e.g. by the application of capital receipts) should be made as necessary.

Option 4: Depreciation Method (Unsupported borrowing)

MRP is to be equal to the provision required in accordance with depreciation accounting in respect of the asset on which expenditure has been financed by borrowing or credit arrangements. This should include any amount for impairment chargeable to the Income and Expenditure Account.

For this purpose, standard depreciation accounting procedures should be followed, except in the following respects.

(a) MRP should continue to be made annually until the cumulative amount of such provision is equal to the expenditure originally financed by borrowing or credit arrangements. Thereafter the authority may cease to make MRP.

(b) On disposal of the asset, the charge should continue in accordance with the depreciation schedule as if the disposal had not taken place. But this does not affect the ability to apply capital receipts or other funding sources at any time to repay all or part of the outstanding debt.

(c) Where the percentage of the expenditure on the asset financed by borrowing or credit arrangements is less than 100%, MRP should be equal to the same percentage of the provision required under depreciation accounting.

Appendix 3(b): Minimum Revenue Provision Statement 2021/22

	£
Supported Borrowing - Asset Life (45 years)	
General Fund	
Closing CFR 2019/20	192,303,897
Proposed use of capital receipts voluntarily set aside to be applied in 2020/21	6,755,638
Adjustment A	(4,446,484)
Less transfer of asset from GF to HRA	(325,000)
	194,288,051
Less LGR (98) Debt	(56,819)
	194,231,232
Less MRP 2020/21	(2,507,761)
Add Back LGR (98) Debt	56,819
CFR for Supported Borrowing MRP Calculation	**191,780,290**
Add Back Adjustment A	4,446,484
Closing CFR 31/03/21 - Supported Borrowing (GF)	**196,226,774**
Housing Revenue Account	
Closing CFR 2019/20	84,804,619
Add transfer of asset from GF to HRA	325,000
Less MRP 2020/21 (none budgeted as per HRA MRP policy)	0
	85,129,619
Closing CFR 31/03/21 - Supported Borrowing (GF&HRA)	**281,356,393**
Unsupported Supported Borrowing – Asset Life (based on individual assets)	
Unsupported Borrowing brought forward	83,124,527
Add profiled prudential borrowing 2020/21	7,942,157
Less MRP – 2019/20	(2,146,444)
Closing CFR 31/03/21 - Unsupported Supported Borrowing	**88,920,240**
Closing CFR (GF&HRA) 31/03/21 - Borrowing Requirement	**370,276,633**
Additional items included:	
Village Hall Loans	278,462
Housing Association Loans	16,638,369
	387,193,465
Summary MRP	
MRP 2021/22 at on Annuity Basis at 45 year life from 2018/19	2,546,770
LGR (98) Debt MRP	12,740
Prudential Borrowing MRP	2,446,439
Total MRP 2021/22	**5,005,949**

N.B. The above excludes the CFR and MRP charges in relation to the on-balance sheet PFI schemes and finance leases.

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