DECISION-MAKER:		**AUDIT COMMITTEE**		
SUBJECT:		**REVIEW OF PRUDENTIAL LIMITS AND TREASURY MANAGEMENT MID-YEAR 2024/25**		
DATE OF DECISION:		**11 NOVEMBER 2024**		
REPORT OF:		**EXECUTIVE DIRECTOR ENABLING SERVICES & S151 OFFICER**		
CONTACT DETAILS				
Executive Direct	**Title:**	**Executive Director Enabling Services & S151 Officer**		
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STATEMENT OF CONFIDENTIALITY		
NOT APPLICABLE		
BRIEF SUMMARY		
The purpose of this report is to inform Audit Committee of the Treasury Management activities and performance for 2024/25 against the approved Prudential Indicators for External Debt and Treasury Management.		
RECOMMENDATIONS:		
It is recommended that Audit committee:		
	(i)	Notes the mid-year position for Treasury Management (TM) activities and Prudential Indicators.
	(ii)	Notes that the continued proactive approach to TM has led to reductions in borrowing costs and safeguarded investment income during the year.
REASONS FOR REPORT RECOMMENDATIONS		
1.	The Treasury Management Code requires public sector authorities to determine an annual TM Strategy and as a minimum, formally report on their treasury activities and arrangements to Audit Committee mid-year and after the year-end. This report fulfils that requirement and enables those tasked with implementing policies and undertaking transactions to demonstrate they have properly fulfilled their responsibilities and enable those with ultimate responsibility/audit of the TM function to scrutinise and assess its effectiveness and compliance with policies and objectives.	
2.	In addition to the formal reports to Audit Committee, from 1st April 2023 the 2021 Code introduced mandatory quarterly reporting of the TM prudential indicators and are included in the Financial Monitoring reports presented to Cabinet. The next update – based on quarter 2 and therefore the mid-year position will be presented in November 2024.	

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED		
3.	No alternative options are relevant to this report.	
DETAIL (Including consultation carried out)		
	CONSULTATION	
4.	Not applicable.	
	BACKGROUND	
5.	The Local Government Act 2003 introduced a system for borrowing based largely on self-regulation by local authorities themselves. The basic principle of the new system is that local authorities will be free to borrow if their capital spending plans are affordable, prudent and sustainable.	
6.	The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires that authorities report on the performance of the treasury management function at least twice a year (mid-year and at year end). It also requires that monitoring of the TM indicators should be reported quarterly (along with the other prudential indicators) as part of the council's general revenue and capital monitoring.	
7.	The Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The council's Capital Strategy, complying with CIPFA's requirement, along with the TM strategy was approved by full Council on 6 March 2024.	
8.	Overall responsibility for TM remains with the Council. No activity is without risk; the effective identification and management of risk are integral to the Council's TM objectives. The council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. This report covers treasury activity and the associated monitoring and control of risk.	
9.	This report:	
	a)	is prepared in accordance with the revised CIPFA TM Code and the revised Prudential Code;
	b)	presents details of capital financing, borrowing, debt rescheduling and investment transactions;
	c)	reports on the risk implications of treasury decisions and transactions;
	d)	gives details of the mid-year position on TM in 2024/25; and
	e)	confirms compliance with treasury limits and Prudential Indicators.
10.	The report and appendices highlight that:	
	a)	Borrowing activities have been undertaken within the approved borrowing limits and there has been full compliance with the approved Prudential Indicators.
	b)	Due to the increasing borrowing requirement the overall treasury strategy is to minimise both external borrowing and investments and to only borrow to the level of net borrowing requirement. The reasons for

		this are to reduce credit risk, take pressure off the Council's lending list and avoid the cost of carry existing in the current interest rate environment. Throughout the period, capital expenditure levels, market conditions and interest rate levels were monitored to minimise borrowing costs over the medium to longer term and to maintain stability.
	c)	CIPFA's Treasury Management in the Public Services Code of Practice and associated guidance notes define treasury management investments as investments that arise from the organisation's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required for use in the course of business. As reported previously SCC holds £27M in the CCLA property fund which was reviewed following the revised CIPFA guidance, and it still meets our medium term investments objectives. This will remain under review in conjunction with our TM advisors. For further details on the funds' performance see Appendix 2, paragraphs 37 to 43.
	d)	Total TM investment returns for 2024/25 are currently forecast at £2.7M and during the period April to September achieved an average return of 4.78%.
	e)	The differential between debt costs and investment earnings continued to widen, resulting in the continued use of internal resources in lieu of borrowing as the most cost-effective means of financing capital expenditure. The average rate for repayment of debt, (the Consolidated Loans & Investment Account Rate – CLIA), is forecast at 3.11% this is higher than last year (2.98%) but is in line with strategy due to new borrowing being taken at higher rates than maturing debt and previous new borrowing. Borrowing is deferred until it is actually required to minimise costs unless a good opportunity was to present itself. It is the intention to continue to monitor both short term and long term markets during 2024/25 whilst there is so much volatility in markets.
	f)	Since 2012, the Council has pursued a strategy of internal borrowing – minimising external borrowing by running down its own investment balances and only borrowing short term to cover cash flow requirements. This has both reduced the credit risk exposure and saved the Council money in terms of net interest costs. Net interest costs being the difference between interest received on investments and interest payable on borrowing
	g)	In achieving interest rate savings, the Council is exposed to interest rate risk by taking out variable debt. This was and continues to be financially favourable in current markets but does mean that close monitoring of the markets is required to ensure that the Council can act quickly should the situation begin to change, for example, during the last 2 years we have borrowed £60M long term to introduce some certainty into the loan portfolio in a volatile interest environment.
	h)	Forecast net loan debt will increase during 2024/25 from £330M to £468M (£138M) as detailed in Appendix 2, paragraph 1. This increase is largely due to the assumption at this stage that Exceptional Financial Support (EFS) will be used to its maximum and

funded through borrowing. This borrowing requirement will reduce in the event we do not utilise the full EFS allocation or use other capital resources e.g. capital receipts generated by the ADDP programme, to part fund EFS.

Actual debt charges for the year for borrowing (excluding HCC transferred debt and PFI schemes) is forecast at £12.08M at an average interest rate of 3.11%

11. Appendix 1 summarises the economic outlook and events in the context of which the Council operated its treasury function during 2024/25 to date.

12. Appendix 2 summarises treasury activity during the year and covers:

- Borrowing Requirement and Debt Management
- Investment Activity
- Non – Treasury Investments

COMPLIANCE WITH PRUDENTIAL INDICATORS

13. It can be confirmed that the Council has complied with its Prudential Indicators for 2024/25, approved by Council on 6 March 2024.

14. In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of TM activity during 2024/25. None of the Prudential Indicators has been breached and a prudent approach has been taken in relation to investment activity with priority being given to security and liquidity over yield. The table below summarises the Key Indicators, further details can be seen in appendix 4.

15. ***Table1: Key Prudential Indicators***

Indicator	**Limit**	**Actual at 30/9/2024**
Authorised Limit for external debt	£810M	£370M
Operational Limit for external debt	£690M	£370M
Maximum external borrowing year to date	£750M	£317M
Limit of fixed interest debt	100%	99%
Limit of variable interest debt	50%	1%
Limit for long term investments	£30M	£28M

RESOURCE IMPLICATIONS

<u>Capital/Revenue</u>

16. The capital and revenue implications are considered as part of the quarterly financial monitoring reports and MTFS updates.

17. The interest cost of financing the long term and short term loan debt is charged corporately to the Income and Expenditure account and is forecast to be £12.08M in 2024/25, of which £6.75M relates to the HRA. This is lower than originally budgeted mainly due to no new long term borrowing being taken to date as we continued to make use of internal balances and used short term borrowing as they provided value for money and minimised loan costs as long term debt rates are expected to fall later in year.

18.	In addition, interest earned on temporary balances invested externally is credited to the Income and Expenditure account. Forecast income is now £2.54M, slightly higher (£0.31M) than originally budgeted £2.23M.
19.	The expenses of managing the council's loan debt consist of brokerage and internal administration charges. These are pooled and borne by the HRA and General Fund proportionately to the related loan debt. Debt management expenses for 2024/25 are forecast to be £0.25M.
20.	A sustained favourable variance of £0.94M, due to reduced capital financing costs and higher investment returns has been transferred to the centrally held contingency to help reduce the reliance on Exceptional Financial Support (EFS), as agreed by Cabinet on 29th October 2024.
21.	To cover future risk of any loss on the CCLA pooled property fund due to the expectation that statutory override will cease in 2026/27, £0.80M has transferred to the Investment Risk Reserve, with a further transfer of £0.40M to be made in 2024/25. Further detail can be found in Appendix 2 paragraphs 37 to 43.
22.	On 10th April 2024 amended legislation and revised statutory guidance were published on Minimum Revenue Provision (MRP). The majority of the changes take effect from the 2025/26 financial year, although there is a requirement that for capital loans given on or after 7th May 2024 sufficient MRP must be charged so the outstanding CFR in respect of the loan is no higher than the principal outstanding less the Expected Credit Loss (ECL) charge for the loan. The regulations also require that local authorities cannot exclude any amount of their CFR from their MRP calculation unless by an exception set out in law. Capital receipts cannot be used to directly replace, in whole or part, the prudent charge to revenue for MRP (there are specific exceptions for capital loans and leased assets). The MRP policy is reviewed and updated annually, and our TM advisors have offered to carry out an MRP health check to ensure that the policy complies with the updated guidance, provides a prudent level of MRP and identify any opportunities to recalculate the annual charge.
Property/Other	
23.	There are no specific property implications arising from this report.
LEGAL IMPLICATIONS	
Statutory power to undertake proposals in the report:	
24.	Local Authority borrowing is regulated by Part 1, of the Local Government Act 2003, which introduced the new Prudential Capital Finance System. From 1 April 2004, investments are dealt with, not in secondary legislation, but through guidance. Similarly, there is guidance on prudent investment practice, issued by the Secretary of State under Section 15(1)(a) of the 2003 Act. A local authority has the power to invest for "any purpose relevant to its functions under any enactment or for the purposes of the prudent management of its financial affairs". The reference to the "prudent management of its financial affairs" is included to cover investments, which are not directly linked to identifiable statutory functions but are simply made in the course of treasury management. This also allows the temporary investment of funds borrowed for the purpose of expenditure in the reasonably near future; however, the speculative procedure of borrowing purely in order to invest and make a return remains unlawful.

<u>Other Legal Implications</u>:	
25.	None.
RISK MANAGEMENT IMPLICATIONS	
26.	Not Applicable
POLICY FRAMEWORK IMPLICATIONS	
27.	Not applicable. It should be note that the Statement of Accounts has been prepared in accordance with the CIPFA Code of Practice on Local Authority Accounting in the UK 2024/25.

KEY DECISION?	~~Yes~~/No
WARDS/COMMUNITIES AFFECTED:	NONE

<u>SUPPORTING DOCUMENTATION</u>

Appendices	
1.	2024/25 Economic Background
2.	Treasury Activity during 2024/25
3.	Southampton Benchmarking 30th September 2024
4.	Compliance with Prudential Indicators
5.	Glossary of Treasury Terms

Documents In Members' Rooms	
1.	None.

Equality Impact Assessment	
Do the implications/subject of the report require an Equality and Safety Impact Assessments (ESIA) to be carried out.	~~Yes~~/No
Privacy Impact Assessment	
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.	~~Yes~~/No

Other Background Documents

Equality Impact Assessment and Other Background documents available for inspection at:

Title of Background Paper(s)		Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	The Medium Term Financial Strategy, Budget Capital Programme 2024/25 to 2028/29 – reported to Council 6 March 2024	