PREVENTING PROTECTING RESPONDING

TYNE & WEAR FIRE AND RESCUE AUTHORITY

MEETING: 22ND FEBRUARY 2010

SUBJECT: CAPITAL PROGRAMME 2010/2011 INCLUDING PRUDENTIAL INDICATORS AND TREASURY MANAGEMENT STRATEGY AND POLICY

JOINT REPORT OF THE CHIEF FIRE OFFICER, CLERK TO THE AUTHORITY, FINANCE OFFICER AND THE CHIEF EMERGENCY PLANNING OFFICER

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1. Introduction

1.1 The purpose of this report is to present for consideration and approval of Members, the Capital Programme for 2010/2011, including the Prudential Indicators and the Treasury Management Strategy and Policy.

2. Capital Resources

2.1 The Authority receives grant support towards borrowing costs through the Revenue Support Grant Settlement. The Authority is also able to supplement the capital programme with:-

- the ‘usable’ part of any capital receipt;
- a contribution from revenue resources;
- supported capital expenditure;
- specific capital grant;
- operating leases.

3. Capital Programme 2010/2011

3.1 Since the 2009/2010 Capital Programme was reported to Members on 25th January 2010 which included a provisional programme for 2010/2011, the capital requirements of the Authority for 2010/2011 have been reviewed by the Chief Fire Officer, through the Authority’s Asset Management Group and is reflected in the 2010/2011 Capital Programme at Appendix A.

Commitments from 2009/2010

3.2 A number of areas of potential slippage were brought to Members attention in the Third Review of the 2009/2010 Capital Programme, reported to members in January 2010. The expectation, however, is that these schemes will be fully spent within the current financial year, so the Capital Programme for 2010/2011 takes no account of slippage at this time.

New Starts

3.3 The Capital Programme for 2010/2011 includes provision of £1,254,328 to fund New Starts, in addition to £393,850 which is required to fund Continuing Projects. The proposed Capital Programme and Vehicle Replacement Programme for 2010/2011 are attached at Appendix A. Included within New Starts is provision for the following capital schemes:

IT Equipment:
- New and Replacement Hardware (£265,000) – includes ongoing hardware refresh of the Authority's PC, Server and associated infrastructure. This will assist in the ICT section's, "virtualisation" project and will provide opportunities to reduce the Authority's carbon footprint by reducing the number of servers. This should, in turn, lead to efficiency savings from 2011/2012 onwards.

Operational Equipment:
- Operational Equipment (£93,000) – includes provision for the purchase of Lighting and Foam equipment to provide the most up to date safety equipment for firefighters.

Estates:
- Non PFI Station Refurbishment (£275,000) – includes the conversion of existing open plan areas into single cellular study / rest areas. This will support the dignity and equality aspects required to attract and retain a greater number of female firefighters;
- Storage Facility for Aerial Ladder Platform at Gosforth (£201,000) – the procurement of the Aerial Ladder Platform (ALP) was reported to Authority in March 2009 and delivery is scheduled for 2010/2011. This scheme includes the construction of a purpose made facility to store the ALP at Gosforth Fire Station which has been identified as the best strategic location for this asset;
- Other schemes less than £100,000 (£135,650) – includes repairs to the roof structure at Birtley Fire Station, muster bay improvements at Hebburn Fire Station and refurbishment of gym facilities at West Denton Fire Station. Also includes a contribution to groundworks relating to the NEFRA project at Tynemouth, as reported to Members in June 2009.

Carbon Reduction Plan
- Carbon Reduction Plan (£199,678) – the Authority is working in partnership with the Carbon Trust and other FRAs to develop a Carbon Management Plan, as reported in the 2009/2010 Revenue Budget Third Review. The Plan identifies the Authority's target of reducing CO_2 emissions from normal business activities by 22% by March 2015 through changes in the Authority's estate, fleet, policy and behaviour.

- The Revenue Budget Third Review, reported to Members in January 2010, noted that a reserve of £600,000 will be established from the 2009/2010 Revenue Budget underspend to fund the cost of carbon reduction measures. It is intended that the costs arising from the Carbon Reduction Plan are met from this reserve. Investment in the Plan will

introduce efficiency savings when comparing future costs against the future costs of not undertaking the actions, however, increases in energy prices are likely to mean that cash releasing efficiency savings will not materialise.

Resourcing

3.4 It is proposed that the Capital Programme for 2010/2011 of £1,648,178 be resourced as follows:

- Revenue Contribution to Capital Outlay - £1,448,178 (of which £346,791 will be met from earmarked reserves);
- Fire Capital Grant - £200,000;
- Borrowing – nil.

3.5 With regard to the Vehicle Replacement Programme, option appraisal will be undertaken, where leasing finance is available, to determine whether leasing or outright purchase represents the best option on a value for money basis. Appropriate budget provision has been included within the Revenue Budget for 2010/2011.

Fire Capital Grant

3.6 As reported previously to Members, the Authority will receive a Fire Capital Grant allocation of £959,579 in 2010/2011. This grant represents new money and will not involve borrowing. With the exception of a requirement that the grant only be used for capital expenditure, the grant is not ringfenced.

3.7 Paragraph 3.4, above, identifies that a contribution of £200,000 from the 2010/2011 Fire Capital Grant allocation is required to contribute towards funding the 2010/2011 Capital Programme. The remainder of the grant will be transferred to a Capital Grants Reserve in order to meet the cost of future prioritised capital schemes.

Future Years

3.8 Appendix A includes an indicative Capital Programme for 2011/2012 and 2012/2013. As referred to at paragraph 3.1, the Chief Fire Officer has undertaken a review of the capital requirements for 2010/2011 and this included a review of the requirements for 2011/2012 and 2012/2013. The provision for future years will be kept under close review to consider any emerging priorities. This will ensure that the Authority's investment in its assets delivers best value for money. Further updates will be provided to Members through the normal quarterly monitoring process.

4. Prudential Framework for Local Authority Capital Expenditure

4.1 One of the principal features of the Local Government Act 2003 was to provide the primary legislative requirements to introduce a new prudential regime for the control of Local Authority capital expenditure. The regime relies upon both secondary legislation in the form of regulations, and a prudential code which has been published by the Chartered Institute of Public Finance and Accountancy (CIPFA).

4.2 Under the prudential framework, local authorities are free to borrow without specific government consent if they can afford to service the debt without extra government revenue support. The basic principle is that authorities are free to invest as long as their capital spending plans are affordable, sustainable and prudent. As a control mechanism, to ensure this occurs, all authorities must follow the Prudential Code published by CIPFA. This involves setting various prudential limits and indicators that must be approved by the Authority before the start of the relevant financial year as part of their budget setting process. The prudential indicators have been prepared and all matters specified in the code have been taken into account. Regular monitoring will take place during the year and, where appropriate, reports on the indicators will be made to the Authority as part of the quarterly capital review reports.

4.3 At this stage, it is not necessary to utilise the opportunities within the framework since the Authority is able to afford its capital programme through the use of Revenue Contributions and Fire Capital Grant to fund Capital Expenditure.

5. The Prudential Code and Prudential Indicators

5.1 The Local Government Act 2003 gives statutory backing to the CIPFA Prudential Code for Capital Finance. The regulations specify that it is this Code to which authorities must have regard when setting and reviewing their affordable borrowing limits. The Prudential Code was reported to Authority in March 2004.

CIPFA has issued a revised Prudential Code in 2009 with a number of indicators being removed from the Prudential Code and becoming part of the CIPFA Treasury Management in the Public Services Code of Practice.

The following indicators, previously included in the Prudential Code, now form part of the CIPFA Treasury Management in the Public Services Code of Practice but have been included alongside the Prudential Code indicators set out in Appendix B for ease of reference:

Indicator	Appendix B Reference
Upper limit on fixed interest rate exposure.	P10
Upper limit on variable interest rate exposure.	P11
Upper limit for the maturity structure of borrowing.	P12
Lower limit for the maturity structure of borrowing.	P12
Prudential limit for principal sums invested for periods longer than 364 days.	P13

All of the above indicators together with background information on these indicators and what they are seeking to assess, are detailed in Appendix B in full compliance with the revised code.

5.2 It should be noted that accounting regulations relating to the introduction of International Financial Reporting Standards (IFRS) are being introduced from 1st April 2010 that are likely to affect a number of the Authority's prudential indicators. In particular, changes to accounting standards for PFI schemes and leasing may require these assets to be brought onto the Authority's Balance Sheet. This will result in an increase to the Authority's capital financing requirement, authorised limit for external debt, and its operational boundary for external debt. These adjustments are technical in nature and a prudent amount has been added to all limits for 2010/2011 onwards to reflect these adjustments. This is in accordance with government and accounting guidance which has not yet been finalised and is therefore subject to further changes as necessary. It is considered likely that both the Authority's Authorised Limit for External Debt of £28.535 million and its Operational Boundary for External Debt of £23.535 million for 2009/2010 million will be exceeded as a result of these changes and the Authority is recommended to approve a revision to the Authorised Limit for External debt to £51.137 million and to its Operational Boundary for External Debt to £46.137 million.

5.3 In setting or revising the required Prudential Indicators, the Authority must have regard to a number of matters:

- affordability, e.g. implications for the precept;
- prudence, and sustainability;
- implications for external borrowing;
- value for money, e.g. option appraisal;
- stewardship of assets, e.g. asset management planning;
- service objectives and strategic planning;
- practicality, e.g. achievability of the planned capital investment.

5.4 To aid transparency, wherever possible, indicators for previous years are based on information contained in the published Balance Sheet of the Authority. The Code does not include any suggested limits or ratios, as these will depend on each Authority's circumstances. The indicators are not designed to make comparisons between Authorities.

5.5 In order to ensure that the Authority is in a position to set its prudential indicators for 2010/2011, the preparation of the Capital Programme for 2010/2011 has required estimates of capital expenditure to be prepared over a three year period through to 2012/2013.

6. The Annual Minimum Revenue Provision Statement

6.1 Regulations came into force on 31st March 2008 revoking secondary legislation relating to the requirement to make a Minimum Revenue Provision (MRP) to repay borrowing over time, and replacing it with a new regulation containing a duty for local authorities, each year, to determine for the current financial year, an amount of MRP that it considers prudent. CLG provided statutory guidance on the methodology to use, which local authorities 'must have regard to'.

6.2 The guidance recommends that authorities must submit to Authority an annual statement of its policy on making a MRP in respect of the following financial year and highlight which of the various options set out in the guidance will be followed.

6.3 The four options for calculating MRP which were set out in the guidance can be summarised as follows:

- Option 1 – Regulatory Method: applying the statutory formula set out in the 2003 Regulations before it was revoked in 2008.
- Option 2 – Capital Financing Requirement (CFR) Method: multiplying the CFR at the end of the preceding financial year by 4%.
- Option 3 – Asset Life Method: amortising expenditure over an estimated useful life for the relevant assets created. An assessment must be made of the asset life at the outset of the capital scheme and MRP is charged to revenue in either equal annual instalments or by an annuity method over the estimated life of the asset. The MRP charge will commence in the financial year following the one in which the asset comes into service.
- Option 4 – Depreciation Method: making charges to revenue in accordance with the standard rules for depreciation accounting for the particular asset being created or enhanced.

6.4 For 2010/2011, having considered all of the options available, it is proposed that the Authority uses Option 1 (the regulatory method) for government supported borrowing. This approach has been adopted since the new regulations were enacted and is a continuation of the method previously used by the Authority (under the existing regulations 28 and 29 of the Capital Finance Regulations and the Local Government Act 2003) where MRP is calculated with regard to the 'credit ceiling' of the authority. This takes into account all loan advances and repayments through the Authority's consolidated advances and borrowing pool with MRP being calculated at 4% of the opening 'credit ceiling' balance.

6.5 Option 1 is preferred as this option takes the formulae used by the government in calculating revenue support grant as its basis and therefore better reflects the actual funding provided by government.

6.6 The draft regulations also recommend consideration of two options for any future borrowing under the prudential system for which no government support is being given and is therefore self-financed. The Authority currently has no plans to undertake unsupported borrowing and, therefore at this stage, it is not proposed to include a proposed policy in relation to this category of borrowing.

6.7 In addition revised accounting guidelines to comply with IFRS are to be introduced for 2010/2011. The new standards will potentially have the effect of reclassifying operational leases, finance leases and PFI contracts. These proposed changes may affect a number of the Authority's prudential indicators. In particular, changes to accounting standards for PFI schemes and leasing may require these assets to be brought onto the Authority's balance sheet adjusting previous years' MRP payments. It is recommended that the MRP policy for both 2009/2010 and 2010/2011 be adjusted in accordance with paragraph 6.8 below and monitored to ensure that there will be no impact on the Council Tax Precept from revisions to accounting standards.

6.8 In summary, it is recommended that the Authority approves the following Annual Minimum Revenue Provision Statement for 2010/2011:

- For all government supported borrowing the Authority will adopt Option 1 as set out in the government’s guidance, which is a continuation of the basis upon which the Authority currently calculates MRP as set out in paragraph 6.3 above.

- For MRP payments in relation to finance leases and PFI contracts previously held off-balance sheet but now included on-balance sheet to comply with IFRS requirements, the amount of MRP to be made will be set to ensure that the finance charge and MRP for finance leases and on-balance sheet PFI schemes is equal to the rental or service charge payable in the income and expenditure account for the year, which writes down the balance sheet liability of those assets. The Authority will therefore follow CLG guidance which states:

  'IFRS requires these changes to be accounted for retrospectively, with the result that an element of the rental or service charge payable in previous years (and previously charged to the revenue accounts) will be taken to the balance sheet to reduce the liability. On its own, this change in the accounting arrangements would result in a one-off increase to the capital financing requirement, and an equal increase in revenue account balances. This is not seen as a prudent course of action, and guidance aims to ensure that authorities are in the same position as if the change had not occurred. It does this by recommending the inclusion in the annual MRP charge of an amount equal to the amount that has been

taken to the balance sheet to reduce the liability, including the retrospective element in the first year.'

Following the above, CLG guidance will ensure that, if the move to implement IFRS for the Fire Authority has the effect of bringing more PFI schemes and leases on balance sheet, there will be no effect on the charge to the revenue account and no impact on the Council Tax Precept arising from changes made to accounting standards that must be followed by the Authority.

7. Treasury Management

7.1 The Revised CIPFA Treasury Management Code of Practice 2009

The Fire and Rescue Authority's Treasury Management Code of Practice for 2010/2011 is fully informed and guided by it's lead authority, Sunderland City Council, which meets fully the requirements of the revised Treasury Management Code of Practice. Appendix E sets out these details for information. The Authority is recommended to adopt the new code as set out by the lead authority which it must approve formally in advance of the forthcoming year.

The attached Appendices (C and D) set out the Treasury Management Policy and Strategy Statements that are to be adopted by the Fire and Rescue Authority and it is recommended that:

- the Governance Committee is provided with a wider remit to carry out the role of scrutiny and review of all future Treasury Management reports and that arrangements are agreed and put in place in March to enable them to carry out this role.

7.2 In accordance with the Authority's Financial Regulations, all investment and borrowing is made on the Authority's behalf by Sunderland City Council. This ensures that the Fire and Rescue Authority benefits from beneficial interest rates achieved through pooling of resources.

7.3 The Treasury Management Strategy is a joint strategy with that of Sunderland City Council as cash balances, although accounted for separately, are pooled for the purposes of minimising borrowing costs and maximising investment returns.

7.4 Attached for approval at Appendices C and D are the Treasury Management Policy Statement and the detailed Treasury Management Strategy respectively which fully comply with the requirements of the revised Treasury Management in the Public Services: Code of Practice.

8. Recommendations

8.1 Members are requested to:

- approve the Capital Programme and Vehicle Replacement Programme for 2010/2011 as set out at Appendix A;
- approve the Annual Minimum Revenue Provision Statement set out in Section 6.
- approve the amendments to the Prudential Indicators for 2009/2010 in respect of the Authority's Authorised Limit for External Debt to £51.137 million and to its Operational Boundary for External Debt to £46.137 million.
- approve the Prudential Indicators for the years 2010/2011, 2011/2012 and 2012/2013 as set out in Appendix B;
- approve the adoption of the Revised Treasury Management Code of Practice as set out by the Lead Authority in Appendix E.
- approve the Treasury Management Policy set out at Appendix C;
- approve the Treasury Management Strategy for 2010/2011 as set out in Appendix D.

Appendix A

TYNE AND WEAR FIRE AND RESCUE AUTHORITY

CAPITAL PROGRAMME 2010/2011 TO 2012/2013

SUMMARY

Project Description	Gross Cost	Projected Expenditure to 31.3.10	Estimated Payments		
			2010/11	2011/12	2012/13
	£	£	£	£	£
FIRE SERVICE					
Continuing Projects	1,301,982	621,132	393,850	187,000	100,000
Projects Commencing 2010/2011 and Future Years	3,167,084	0	1,254,328	913,921	998,835
	4,469,066	621,132	1,648,178	1,100,921	1,098,835
EMERGENCY PLANNING	0	0	0	0	0
	4,469,066	621,132	1,648,178	1,100,921	1,098,835
VEHICLE REPLACEMENT PROGRAMME					
Fire Services-Vehicles	5,600,500	0	3,275,500	1,661,500	663,500
TOTAL CAPITAL EXPENDITURE	10,069,566	621,132	4,923,678	2,762,421	1,762,335

TYNE AND WEAR FIRE AND RESCUE AUTHORITY

CAPITAL PROGRAMME 2010/2011 TO 2012/2013

Project Description	Gross Cost	Projected Expenditure to 31.3.10	Estimated Payments		
			2010/11	2011/12	2012/13
	£	£	£	£	£
Continuing Projects					
Operational Equipment					
Breathing Apparatus Equipment	570,000	400,000	170,000	0	0
Estates					
Non PFI Sites BMS Energy Programme	232,132	121,132	111,000	0	0
Works arising from Stock Condition Survey	499,850	100,000	112,850	187,000	100,000
	1,301,982	621,132	393,850	187,000	100,000
Projects Commencing 2010/2011 and Future Years					
IT Equipment					
New and Replacement Hardware	555,000	0	265,000	140,000	150,000
Network & Comms Infrastructure Development	215,000	0	30,000	120,000	65,000
New Software & Supporting Systems	245,000	0	55,000	90,000	100,000
Operational Equipment					
Operational Equipment	254,600	0	93,000	80,500	81,100
Estates					
Non PFI Station Refurbishment	275,000	0	275,000	0	0
Storage Facilities at Gosforth for ALP	201,000	0	201,000	0	0
Appliance bay doors/lighting programme for all Stations	150,000	0	0	150,000	0
West Denton - General refurbishment/decoration	260,000	0	0	0	260,000
Other schemes (less than £100,000)	502,150	0	135,650	231,500	135,000
Carbon Management Plan	509,334	0	199,678	101,921	207,735
	3,167,084	0	1,254,328	913,921	998,835
	4,469,066	621,132	1,648,178	1,100,921	1,098,835

TYNE AND WEAR FIRE AND RESCUE AUTHORITY

CAPITAL PROGRAMME 2010/2011 TO 2012/2013

Project Description	Gross Cost	Estimated Payments To be leased		
		2010/11	2011/12	2012/13
	£	£	£	£
VEHICLE REPLACEMENT PROGRAMME				
SLIPPED FROM 2009/2010 PROGRAMME				
2 Operational Support Units	300,000	300,000		
1 Special Rescue Tender	200,000	200,000		
1 Aerial Ladder Platform	485,000	485,000		
2010/2011 PROGRAMME				
1 Staff Car	17,500	17,500		
1 Minibus	22,000	22,000		
1 Panel Van (small)	20,000	20,000		
2 Panel Vans (large)	50,000	50,000		
16 Vans/Cars (small)	136,000	136,000		
10 Vans/Cars (large)	120,000	120,000		
11 Water Tenders	1,925,000	1,925,000		
2011/2012 PROGRAMME				
5 Water Tenders	875,000		875,000	
1 Aerial Ladder Platform	600,000		600,000	
1 Staff Car	17,500		17,500	
3 vans/cars (small)	25,500		25,500	
2 Vans/Cars (large)	24,000		24,000	
1 Van/Car (specialist)	12,500		12,500	
1 Minibus	22,000		22,000	
3 Panel Vans (small)	60,000		60,000	
1 Panel Van (large)	25,000		25,000	
2012/2013 PROGRAMME				
4 Water Tenders	525,000			525,000
1 vans/cars (small)	8,500			8,500
9 Vans/Cars (large)	108,000			108,000
1 Minibus	22,000			22,000
	5,600,500	3,275,500	1,661,500	663,500

Appendix B

Prudential Indicators 2010/2011

Local Authorities are required to have regard to the Prudential Code when carrying out their duties under Part 1 of the Local Government Act 2003. The key objectives of the code are to ensure that the capital investment plans of Local Authorities are affordable, prudent and sustainable. A further key objective is to ensure that treasury management decisions are taken in accordance with good professional practice.

It should be noted that accounting regulations relating to the introduction of International Financial Reporting Standards (IFRS) are being introduced that may affect a number of the Authority's prudential indicators. In particular, changes to accounting standards for PFI schemes and leasing may require these assets to be brought onto the Authority's balance sheet, increasing the Authority's capital financing requirement, authorised limit for external debt and operational boundary for external debt. These adjustments are technical in nature and authorities are being consulted on the measures required. A prudent amount has been added to all limits to reflect these potential adjustments, however, as guidance has not yet been finalised should any of the Authority's prudential indicators be exceeded as a result these changes they will be reported to Authority at the next meeting following the change.

The indicators that must be taken into account are shown below:

P1 The actual capital expenditure that was incurred in 2008/2009 and the estimates of capital expenditure to be incurred for the current and future years that are recommended for approval are:

	Capital Expenditure				
	2008/2009 £000 Actual	**2009/2010 £000 Estimate**	**2010/2011 £000 Estimate**	**2011/2012 £000 Estimate**	**2012/2013 £000 Estimate**
Fire and Rescue Service	1,866	2,710	1, 648	1,101	1,099
Emergency Planning Unit	0	0	0	0	0
Total Spend	**1,866**	**2,710**	**1,648**	**1,101**	**1,099**

The provision for capital expenditure from 2009/2010 onwards is based on the Capital Programme 2010/2011, reported to Authority on 22nd February 2010.

P2 Estimates of the ratio of financing costs to net revenue stream for the current and future years, and the actual figures for 2008/2009 are:

Ratio of financing costs to net revenue stream				
2008/2009 Actual	**2009/2010 Estimate**	**2010/2011 Estimate**	**2011/2012 Estimate**	**2012/2013 Estimate**
0.66%	1.87%	2.35%	2.89%	2.93%

The estimates of financing costs include current commitments and the proposals in this capital report. The forecast shows an increase in anticipated ratios for 2010/2011 onwards as a result of the current economic downturn, leading to lower interest rates on investments. It should be noted that ratios will vary depending on the interest rates obtained on investments and the level of investments.

The level of financing costs is considered to be affordable and has been taken into account when assessing the Medium Term Financial Strategy (please see the report on the Revenue Budget 2010/2011 elsewhere on today's agenda).

P3 Estimates of the end of year capital financing requirement for the Authority for the current and future years and the actual capital financing requirement as at 31 March 2009 are:

Capital financing requirement				
31/03/09 £000 Actual	**31/03/10 £000 Estimate**	**31/03/11 £000 Estimate**	**31/03/12 £000 Estimate**	**31/03/13 £000 Estimate**
18,427	45,401	46,234	46,487	46,728

The Capital Financing Requirement measures the Authority’s underlying need to borrow for a capital purpose. In accordance with best professional practice, Sunderland City Council, on the Authority’s behalf, does not associate borrowing with particular items or types of expenditure. The Authority has an integrated Treasury Management Strategy, which has been prepared in accordance with the CIPFA Code of Practice for Treasury Management. There are, at any point in time, a number of cash flows, both positive and negative, and the treasury position in terms of its borrowings and investments is managed in accordance with the approved treasury management strategy and practices. In day to day cash management, no distinction can be made between revenue cash and capital cash. External borrowing arises as a consequence of all the financial transactions taking account of the Authority’s needs, and not simply those arising from capital spending. In contrast, the capital financing requirement reflects the Authority’s underlying need to borrow for a capital purpose. The substantial increase in the Capital Financing Requirement at 31/03/10 reflects potential changes arising from compliance with new accounting standards relating to IFRS (these are detailed in section 5.2 of the main report).

P4 CIPFA's Prudential Code for Capital Finance in Local Authorities includes the following as a key indicator of prudence:

> "In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that net external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years."

The Authority had no difficulty meeting this requirement in 2008/2009, nor is any difficulty envisaged for the current or future years. This view takes into account current commitments, existing plans, and the proposals in this report.

P5 In respect of its external debt, it is recommended that the Authority approves the following authorised limits for its total external debt gross of investments for the next three financial years and agrees to amend the previously agreed limit for the current year as it is considered likely that the Authority's Authorised Limit for External Debt for 2009/2010 of £28.535 million will be exceeded as a result of accounting changes relating to the incorporation of IFRS requirements. The Authority is recommended to approve a revision in the Authorised Limit for External Debt in 2009/2010 to £51.137 million in the light of these changes.

The limits separately identify borrowing from other long term liabilities such as finance leases. The Authority is asked to approve these limits and to delegate authority to the Finance Officer, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal and best value for money for the Authority. Any such changes made will be reported to the Authority at its next meeting following the change. The figures below have been calculated by reference to the overall Authorised Limit for Sunderland City Council which covers all separate bodies, including the Fire and Rescue Authority, which is subject to the Prudential Code

	Authorised Limit for External Debt			
	2009/2010	**2010/2011**	**2011/2012**	**2012/2013**
	£000	**£000**	**£000**	**£000**
Borrowing	26,069	26,987	27,279	27,536
Finance Lease	68	62	56	50
Other long term liabilities	25,000	26,000	27,000	28,000
Total	51,137	53,049	54,335	55,586

The Finance Officer reports that these authorised limits are consistent with the Authority's current commitments, existing plans and the proposals in this report on the Capital Programme for capital expenditure and financing, and with its approved treasury management policy statement and practices. The Finance Officer confirms that they are based on the estimate of most likely, prudent but not worst case scenario, with, in addition, sufficient headroom over and above

this, to allow for operational management, for example unusual cash movements. Risk analysis and risk management strategies have been taken into account; as have plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes.

In taking its decisions on the Revenue Budget and Capital Programme for 2010/2011, the Authority is asked to note that the authorised limit determined for 2010/2011, will be the statutory limit determined under section 3(1) of the Local Government Act 2003.

P6 The Authority is also asked to approve the following operational boundary for external debt for the same time period. The proposed operational boundary for external debt is based on the same estimates as the authorised limit but reflects directly the estimate of the most likely, prudent but not worst case scenario, without the additional headroom included within the authorised limit to allow, for example, for unusual cash movements, and equates to the maximum of external debt projected by this estimate. The operational boundary represents a key management tool for in year monitoring. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified.

The Authority is also asked to delegate authority to the Finance Officer, within the total operational boundary for any individual year, to effect movement between the separately agreed figures for borrowing and other long term liabilities, in a similar fashion to the authorised limit. Any such changes will be reported to the Authority at its next meeting following the change.

The operational boundary limit will be closely monitored and a report will be made to Authority if it is exceeded at any point. In any financial year, it is generally only expected that the actual debt outstanding will approach the operational boundary when all of the long-term borrowing has been undertaken for that particular year and will only be broken temporarily as a result of the timing of debt rescheduling. It is considered likely that the Authority's set operational boundary for 2009/2010 of £23.535 million will be exceeded as a result of accounting changes relating to the incorporation of IFRS requirements and the Authority is recommended to approve a revision in the operational boundary for external debt in 2009/2010 to £46.137 million in the light of these changes.

	Operational boundary for external debt			
	2009/2010 £000	**2010/2011 £000**	**2011/2012 £000**	**2012/2013 £000**
Borrowing	21,069	21,987	22,279	22,536
Finance Lease	68	62	56	50
Other long term liabilities	25,000	26,000	27,000	28,000
Total	46,137	48,049	49,335	50,586

P7 The Authority's actual external debt at 31 March 2009 was £18.394 million (calculated on the basis that all Authority debt is classed as external), comprising £18.326 million borrowing and £0.068 million in respect of a finance lease. The Authority does not plan to take out any long term liabilities but has

included an element for this in its calculation of the operational and authorised boundaries to allow flexibility over future financing. It should be noted that actual external debt is not directly comparable to the authorised limit and operational boundary, since the actual external debt reflects the position at one point in time and allowances need to be made for cash flow variations.

P8 The estimate of the incremental impact of new capital decisions proposed in the Revenue Budget report, over and above capital investment decisions that have previously been taken by the Authority are:

For the Band D Council Tax Precept		
2010/2011	**2011/2012**	**2012/2013**
£0.05	£0.21	£0.33

The estimates show the revenue effect of all capital expenditure arising from all schemes commencing in 2010/2011 and the following two financial years. The impact on the Band D Council Tax Precept detailed above takes account of estimated government grant funding through the Revenue Support Grant and the Authority's share of the nationally pooled Non – Domestic Rates.

These forward estimates are not fixed and do not commit the Authority. They are based on the Authority's existing commitments, current plans and the capital plans detailed in Appendix A. The cumulative effect of full-year debt charges will have an additional impact of £0.44 in 2013/2014. There are no known significant variations beyond this timeframe that would result from past events and decisions or the proposals in the budget report.

P9 Sunderland City Council, on the Authority's behalf, has adopted the CIPFA Code of Practice for Treasury Management in the Public Services. This original 2001 Code was adopted on 20th November 2002 by the full Council and the revised Code (see Appendices C & D in this report) will be adopted on 3rd March 2010.

P10 It is recommended that the Authority sets an upper limit on its fixed interest rate exposures of £90 million in 2010/2011, £115 million in 2011/2012 and £120 million in 2012/2013.

P11 It is further recommended that the Authority sets an upper limit on its variable interest rate exposures of £50 million in 2010/2011, £60 million in 2011/2012 and £60 million in 2012/2013.

P12 It is recommended that the Authority sets upper and lower limits for the maturity structure of its borrowings, consistent with Sunderland City Council's policy, as follows:

Amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate at the start of the period:

	Upper limit	Lower limit
under 12 months	40%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and above	100%	0%

P13 It is proposed that the Fire and Rescue Authority funds may be invested for over 364 days within the limits set by the Sunderland City Council as set out in the Treasury Management Strategy.

The objective of the Code is to provide a framework for local authority capital finance that will ensure for individual local authorities that:

(a) capital expenditure plans are affordable

(b) all external borrowing and other long term liabilities are within prudent and sustainable levels

(c) treasury management decisions are taken in accordance with professional good practice

and that in taking decisions in relation to (a) to (c) above the local authority is

(d) accountable, by providing a clear and transparent framework.

Further, the framework established by the Code should be consistent with and support:

(e) local strategic planning

(f) local asset management planning

(g) proper option appraisal.

In exceptional circumstances the objective of the Code is to provide a framework that will demonstrate that, where there is a danger of not ensuring the above, the Authority can take timely remedial action.

Appendix C

Treasury Management Policy Statement

CIPFA recommends that the Authority's Treasury Management Policy Statement adopts the following form of words to define the policies and objectives of its treasury management activities:

- The Authority defines its treasury management activities as: The management of the Authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

- The Authority regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.

- The Authority acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

Authority is requested to formally approve this statement.

Appendix D

Treasury Management Strategy Statement

1. Introduction

1.1 The Authority has customarily considered an Annual Treasury Management Strategy Statement under the requirement of the CIPFA Code of Practice on Treasury Management. The 2003 Prudential Code for Capital Finance in Local Authorities introduced new requirements for the manner in which capital spending plans are to be considered and approved, including the development of an integrated Treasury Management Strategy.

1.2 The revised CIPFA Treasury Management in the Public Services Code of Practice and Prudential Code still require due regard to be had to the Prudential Indicators set out in Appendix B, when determining the Authority's Treasury Management Strategy.

Borrowing Strategy

1.3 The suggested borrowing strategy for 2010/2011 in respect of the following aspects of the treasury management function is based upon the Finance Officer's views on interest rates, supplemented with leading market forecasts provided by the Authority's treasury adviser. The strategy covers:

- the past and current treasury position including interest rates;
- the borrowing requirement for 2010/2011;
- an economic forecast, including the outlook for interest rates;
- capital borrowings and borrowing strategy for 2010/2011;
- debt rescheduling.

The Borrowing Strategy is set out in paragraphs 2 to 6 inclusive.

Annual Investment Strategy

1.4 The Annual Investment Strategy comprises:

- investment objectives;
- security of capital: the use of credit ratings and other market intelligence;
- investments defined as capital expenditure;
- provision for credit related losses;
- past performance and current position;
- outlook and proposed investment strategy for 2010/2011;
- end of year report.

The Annual Investment Strategy is set out at paragraphs 7 to 14.

BORROWING STRATEGY

2. The Past and Current Treasury Position including Interest Rates

2.1 Interest Rates 2009/2010

2.1.1 Interest rates have varied only slightly during the current financial year, with the largest movement being in the 10 year period which has moved up 0.88%. Both the shorter and the longer periods show a slight decrease from the start of the year, as shown in the table below:

Loan Type	31st March 2009 %	20th January 2010 %	Difference %
7 Day Notice	0.50	0.25	(0.25)
1 Month	0.96	0.41	(0.55)
PWLB - 1 Year	0.83	0.93	0.10
5 Year	2.56	3.13	0.57
10 Years	3.38	4.26	0.88
25 Years	4.28	4.57	0.29
50 Years	4.58	4.49	(0.09)

The Bank of England Base Rate was reduced from 1.00% to 0.50% on 5th March 2009 where it has remained.

2.1.2 Shorter-term interest rates –The Bank of England is expected to resist increasing the Base Rate for as long as possible to help build up momentum in economic growth for the UK. It is forecast to increase by 0.25% in September 2010 and end the financial year at 1.50%. The risk to this scenario is judged to be that these projected increases will be delayed.

2.1.3 Longer-term interest rates – Public Works Loan Board (PWLB) rates have remained relatively flat throughout 2009/2010. The 1 year PWLB has remained around 1%, while the 25 year and 50 year have hovered around 4.50%.

2.2 Long-term Borrowing 2009/2010

2.2.1 As part of the Treasury Management Policy and Strategy Statement, which was included in the February 2009 Capital Programme report to Authority, a benchmark rate of 4.00% was set for all long-term borrowing to be undertaken in 2009/2010.

2.2.2 Long-term borrowing of £5.6 million was required to be replaced in 2008/2009 as a result of 11.75% redeemable stock maturing in November 2008. As PWLB rates were forecast to fall during 2009/2010, a decision was taken not to replace this borrowing at that time.

There was a further possible borrowing requirement of £20.0 million due to four 'Lenders Option Borrowers Option' loans (LOBO's) that

were due to rollover in 2009/2010 (details shown below). With a LOBO the lender has the option to vary the rate on the rollover date and this can either be accepted at the new rate or alternatively it can repay the loan. The lenders have not exercised their option to vary the rate in respect of these loans so far in 2009/2010, and these loans will continue to the next rollover period.

Start Date	Lender	Amount £m	Period (Years)	Rate %	Rollover Date	Rollover Period
29/09/06	Dexia	5.0	60	4.32	29/09/09	Every 3 Years
21/10/03	Barclays	5.0	40	4.50	21/10/09	Every 6 Months
03/02/06	Dexia	5.0	60	4.37	03/02/10	Every 3 Years
22/02/06	Dexia	5.0	60	4.38	22/02/10	Every 3 Years

2.2.3 The Treasury Management Strategy for 2009/2010 included provision for debt rescheduling as follows: "to secure further early debt redemption when (and if) appropriate opportunities arise. Consequently market conditions will be closely monitored to identify and take advantage of any such opportunities".

In January 2009, £30.0 million of PWLB loans (with an average rate of 4.20%) were prematurely repaid as part of a debt rescheduling exercise. This was considered opportune as investment rates were averaging 1.80% (and were projected to fall further as the Bank Base Rate was cut to help protect the economy from the recession). Investments were therefore used to temporarily finance this transaction as the net premium involved was very advantageous, being almost cost neutral. The aim was then to replace the loans in 2009/2010 in a range of tranches at various maturity periods over the short to medium term to mitigate against any interest rate risk in the future. All replacement loans were taken out with regard to the Authority's target borrowing rate of 4% or below, thus reducing the overall interest charged to the Authority.

These loans have now been replaced and are shown in the table below:

Date	Lender	Loan No	Amount £'m	Period (Years)	Rate %	Difference from Benchmark of 4%
18/06/09	PWLB	495591	5.0	3.0	2.32	1.68
18/06/09	PWLB	495595	5.0	4.0	2.73	1.27
22/06/09	PWLB	495612	5.0	9.0	3.67	0.33
30/06/09	PWLB	495648	5.0	10.0	3.71	0.29
10/08/09	PWLB	495784	4.0	8.5	3.65	0.35
10/08/09	PWLB	495785	4.0	11.5	3.99	0.01
13/10/09	PWLB	496090	2.0	18.5	3.99	0.01
Total			**30.0**			
13/10/09	PWLB	496090	3.0	18.5	3.99	0.01
Total Borrowed			**33.0**			

The £33 million replacement borrowing from the PWLB was at an average rate of 3.414%.
A total of £30 million of these loans (with an average rate of 3.356%) were to replace the £30 million of PWLB that was prematurely repaid at an average rate of 4.2%. This will result in annual savings of £252,200 per annum for at least the next 3 years.
The remaining £3 million borrowed (at 3.99%) was to partly replace the £5.6m 11.75% stock which matured in November 2008 and this will result in annual savings of £232,800.
Interest rates will continue to be monitored to determine the optimum time to replace the remaining £2.6 million loan stock with new PWLB borrowings. The direct impact on the Authority is that borrowing costs will reduce, as the average cost of borrowing which the Authority forms part of, will reduce in 2010/2011.

On 12th January 2010 a further rescheduling exercise was undertaken when £24.0 million of PWLB loans with an average rate of 4.2% were prematurely repaid, which was almost cost neutral, incurring a minimal cost of £288. These loans are shown below:

Date	Lender	Loan No	Amount £m	Period (Years)	Rate %	Premium / (Discount) £
12/01/10	PWLB	490872	4.0	45.0	4.15	(46,699)
12/01/10	PWLB	490873	4.0	46.0	4.15	(47,065)
12/01/10	PWLB	491674	3.0	46.0	4.20	(5,908)
12/01/10	PWLB	491675	3.0	47.0	4.20	0
12/01/10	PWLB	491676	3.0	48.0	4.20	0
12/01/10	PWLB	491695	3.0	48.0	4.30	60,144
12/01/10	PWLB	491876	4.0	47.0	4.25	39,816
Total Repaid			**24.0**			**288**

This action was considered opportune as investment rates were averaging 0.8% and the average interest payable on the PWLB loans was on average 4.2%, it was therefore considered prudent and appropriate to repay certain higher interest rated PWLB loans using investments to temporarily finance this transaction as the net premium involved was very advantageous, being almost cost neutral. This will result in annual savings of £817,000. The aim is then to replace the loans in 2010/2011 or in future years by replacing the debt on a lower term or with variable rate debt prior to securing lower long term rates at some point in the future, depending upon the financial market outlook. Again this debt rescheduling exercise opportunity is geared to reducing total interest payments and the Authority will benefit from reduced interest payments during 2010/2011 as a result.

It is intended to temporarily fund the loans repaid by the use of investments as the current return on investments is much lower than the 4.2% interest that was being paid on these loans.

The Treasury Management team will continue to monitor market conditions and will secure further early debt redemption when and if

appropriate opportunities arise. Any rescheduling undertaken will be reported to the Authority as part of the current treasury management reporting procedure.

2.2.4 There are nine market Lender's Option / Borrower's Option (LOBO) loans totalling £39.5 million. Of these £34.5 million were converted from stepped rate loans (i.e. loans where the interest rate was fixed for an initial period, and then rose to an agreed higher rate) to flat rate loans (sometimes known as vanilla LOBO's) where the interest rate remains the same throughout the period of the loan. The rescheduling of these LOBO's had the following effects:

- Lengthening the period of the loan resulting in a lower interest rate;
- Reducing volatility levels by lengthening the 'roll-over' period from every six months to every three years.

The one unchanged LOBO detailed below, stepped up to the higher rate of 4.50% from the initial rate of 2.55% on 23rd April 2007.

Start Date	Lender	Amount £m	Period (Years)	Rate %	Fixed Period	Roll Over Period
21/10/03	Barclays	5.0	40	4.5	23/04/07	Every 6 months

The last 'roll-over' date (21st October 2009) has now passed without the lender requesting a change in the rate of interest. The Lender still has the option at the end of each 'roll-over' period to vary the interest rate and has the option to accept the new rate or repay the loan at that point.

The Treasury Management team will continue to monitor this loan for an opportunity to renegotiate the loan in a similar manner to the other LOBO's.

2.3 Current Portfolio Position

The treasury portfolio position for Sunderland City Council which the Fire and Rescue Authority forms part of, at 22nd January 2010 is:

		Principal (£m)	Total (£m)	Average Rate (%)
Borrowing				
Fixed Rate Funding	PWLB	107.5		
	Market	24.5		
	Other	0.4	132.4	3.95
Variable Rate Funding	PWLB	0.0		
	Market	15.0		
	Temporary/ Other	30.9	45.9	1.70
Total Borrowing			**178.3**	**3.37**
Total Investments	In House		**164.3**	**1.93**
Net Debt			**14.0**	

There is currently a difference between gross debt and net debt (after deducting cash balances), of £14.0 million.

2.4 There are a number of risks and benefits associated with having both a large amount of debt whilst at the same time having a considerable amount of investments.

Benefits of having a high level of Investments are;

- liquidity risk – having a large amount of investments means that the Authority is less at risk should money markets become restricted or less available.- this mitigates against liquidity risk;
- interest is received on investments which helps the Authority to address its Strategic Priorities;
- the Authority has greater freedom in the timing of its borrowing as it can afford to wait until the timing is right rather than be subject to the need to borrow at a time when interest rates are not advantageous.

Risks associated with holding a high level of Investments are;

- the Counterparty risk – institutions can not repay the Authority investment placed with them;
- interest rate risk – the rate of interest earned on the investments will be less than that paid on debt, thus causing a loss to the Authority.

The Authority has mitigated these risks by formulating its Treasury Management Policy that incorporates both a Borrowing Strategy and an Annual Investment Strategy and has also taken prudent action to redeem debt early using investments temporarily to the benefit of the Authority by saving on interest charges particularly over the past two financial years.

3. Borrowing Requirement 2010/2011

3.1 Future Borrowing Requirement

The future borrowing requirement for Sunderland City Council which the Fire and Rescue Authority forms part of, at 22nd January 2010 is:

		2010/11 £m	**2011/12 £m**	**2012/13 £m**
1.	Unsupported Capital Borrowing (potential)	0.0	0.0	0.0
2.	Replacement borrowing (PWLB)	26.5	0.0	5.0
3.	Replacement borrowing (Market)	0.0	0.0	0.0
4.	Market LOBO replacement (potential)	10.0	19.5	20.0
TOTAL – KNOWN (2+3)		**26.5**	**19.5**	**25.0**
TOTAL – POTENTIAL (1+4)		**24.0**	**29.5**	**35.0**

4. The Outlook for Interest Rates

4.1 Sector Treasury Services are appointed treasury advisers and part of their service is to assist in formulating a view on interest rates.

4.2 **Economic Forecasts**
Set out below, are a number of current city forecasts for short-term or variable (the Bank of England Base Rate) and longer fixed interest rates.

4.2.1 **Survey of Economic Forecasts**
The table below shows the HM Treasury – December 2009 summary of forecasts of 23 City and 12 academic analysts for Q4 2009 and Q4 2010. Forecasts for 2010 to 2013 are based on 31 forecasts in the last quarterly forecast (January 2010):

Bank Rate Forecast		Quarter ended		Annual Average Bank Rate			
	Actual %	Q4 2009 %	Q4 2010 %	Average 2010 %	Average 2011 %	Average 2012 %	Average 2013 %
Median	0.50	0.50	1.30	0.70	1.80	3.00	3.70
Highest	0.50	0.50	2.00	1.30	3.30	4.30	4.60
Lowest	0.50	0.50	0.50	0.50	0.50	1.00	1.40

4.2.2 Sector's interest rate forecast of 11th January 2010 is set out below:

	2009/10	2010/11				2011/12				2012/13			
	Mar 2010 %	Jun 2010 %	Sept 2010 %	Dec 2010 %	Mar 2011 %	Jun 2011 %	Sept 2011 %	Dec 2011 %	Mar 2012 %	Jun 2012 %	Sept 2012 %	Dec 2012 %	Mar 2013 %
Bank Rate	0.50	0.50	0.75	1.00	1.50	2.25	2.75	3.25	3.50	3.75	4.25	4.25	4.50
PWLB 5yr	3.05	3.20	3.30	3.40	3.60	3.85	4.15	4.55	4.60	4.80	4.80	4.85	4.85
PWLB 10 yr	4.00	4.05	4.15	4.30	4.45	4.60	4.80	4.90	5.00	5.10	5.10	5.15	5.15
PWLB 25y	4.55	4.65	4.70	4.80	4.90	5.00	5.05	5.10	5.20	5.30	5.30	5.35	5.35
PWLB 50yr	4.60	4.70	4.75	4.90	5.00	5.10	5.15	5.20	5.30	5.40	5.40	5.45	5.45

4.2.3 Capital Economics interest rate forecast of 5th November 2009 is set out below

	2009/10	2010/11				2011/12		
	Mar 2010 %	Jun 2010 %	Sept 2010 %	Dec 2010 %	Mar 2011 %	Jun 2011 %	Sept 2011 %	Dec 2011 %
Bank Rate	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
PWLB 5yr	2.35	2.15	2.15	2.15	2.15	2.15	2.15	2.15
PWLB 10 yr	3.45	3.15	2.65	2.65	2.65	2.65	2.65	2.65
PWLB 25y	3.85	3.75	3.75	3.75	3.75	3.75	3.75	3.75
PWLB 50yr	4.15	4.05	4.05	4.05	4.05	4.05	4.05	4.05

4.2.4 UBS interest rate forecast of January 2010 is set out below

	2009/10	2010/11				2011/12		
	Mar 2010 %	Jun 2010 %	Sept 2010 %	Dec 2010 %	Mar 2011 %	Jun 2011 %	Sept 2011 %	Dec 2011 %
Bank Rate	0.50	0.50	0.75	1.00	1.50	2.00	2.50	3.00
PWLB 5yr	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
PWLB 10 yr	3.90	4.05	4.40	4.75	4.90	5.15	5.40	5.40
PWLB 25y	4.45	4.65	5.00	5.15	5.40	5.65	5.90	5.90
PWLB 50yr	4.55	4.75	5.10	5.25	5.50	5.75	6.00	6.00

4.3 Economic Background

4.3.1 Introduction

- The global credit crunch,of August 2007 almost led to the near collapse of the world banking system in September 2008. This then had the effect of pushing most of the major economies of the world into a very sharp recession in 2009, which was accompanied by a dearth of lending from banks anxious to rebuild their weakened balance sheets. Many governments were forced to recapitalise and rescue their major banks with the consequence that most central banks around the world agreed to cut their central bank rates to between 0.10% – 1.00% in order to help counter the ensuing world recession.
- The long awaited start of growth eventually came through in quarter 3 of 2009 in the US and the EU. However, there was

disappointment that the UK failed to emerge from recession until quarter 4. Figures released on 26th January 2010 showed that the UK emerged from the recession in Quarter 4 of 2009, but only by the slenderest of margins, by 0.1%. This shows that the recovery is still quite fragile.

- Inflation has plunged in most major economies and is currently not seen as being a problem for at least the next two years due to the large output gaps and high unemployment which will have the effect of curbing wage growth. In many countries there have been widespread pay freezes in 2009 and these are likely to be persistent for some time.
- Most analysts think that there still needs to be a radical world rebalancing of excess savings rates by cash rich Asian and oil based economies and excess consumption rates in Western economies if the world financial system is to avoid a potential repeat of this type of financial crisis in the future.
- Most major economies have resorted to an expansion of fiscal stimulus packages in order to encourage a quicker exit from recession. This, together with expenditure on direct support provided to ailing banks, has led to a significant increase in government debt levels which will take many years to repay.

4.3.2 **Two growth scenarios**

- The main issue with the world economy at the moment is 'how quickly will the major world economies recover' however opinion by financial experts and economists is divided as detailed below: This division of opinion is also reflected in the views of Capital Economics and UBS in the tables above which set out their views on interest rates projected into the future..

4.3.3 **Strong recovery**

- This is a normal cyclical recovery which will be strong in the major world economies. The US still has potential to add further fiscal stimulus in 2010 to ensure that strong recovery continues after the current round of stimulus measures end. Growth in the EU is likely to be strong in 2010 and is likely to not require such help from EU governments.
- The forecast suggests that UK GDP growth will almost get back to the long term average of about 2.5% by 2011 but growth is likely to peak in the first half of 2010 as inventory rebuilding and stimulus measures begin to fade and some fiscal contraction occurs later in the year.
- In addition it is suggested that the economy will rebalance with strong growth in exports and import substitution helped by strong recovery in the EU and the rest of the world.
- Sterling has depreciated by 25% since reaching its peak in 2007 and is expected to remain weak, which benefits manufacturing industry and exports.
- Consumer spending – only a minimal recovery is expected due to a steady increase in the savings ratio from +5.6% in 2009 to about +8% in 2011 as consumers reduce debt and/or build up cash savings. Consumer spending will also be low due to the fact that

both earnings/incomes will be held down by pay freezes or below inflation increases and increases expected in general taxation.

- House price recovery is expected to persist helped by a low Bank Base Rate for a prolonged period. House prices are expected to rise by about 6% in 2010, and 3% in 2011. Mortgage approvals are anticipated to rise back to the level of around 75,000-80,000 per month and this scale of increase is needed to ensure a continuation of a trend of rising house prices.
- CPI inflation was expected to peak at 2.5% in early 2010 after the rise in VAT in January but then to fall to a low of roughly 1.5% in early 2011 and to stay below 2% for the rest of 2011.
- The current MPC attitude is one of restraint and seeking to avoid increasing Bank Base rates for as long as possible to secure economic recovery, the aim being to try to ensure that growth is achieved and well established before Bank Base rates gets back to the level of 4%–5% before the next cyclical recession and that all assets purchased through Quantitative Easing measures have been sold off by then. The first Bank Base Rate increase is expected in Q3 2010.
- A change of Government in 2010 with a more aggressive fiscal stance could delay the timing of Bank Base Rate increases.
- The UK fiscal deficit is 6.4% of GDP, about £90bn, which is expected to fall at £11bn per annum, over the next eight years at currently planned rates. This is similar to the peak deficit of 7% experienced in the 1990s which was remedied to a surplus of 1.6% in the space of 6 years helped by strong, steady economic growth of 3% per annum and supported by loose government monetary policy that compensated for the fiscal squeeze.

The major risk to this scenario would be a lack of supply of bank credit. However, it is felt that the Bank of England is on alert to ensure that this does not happen and would continue various measures to assist the expansion of credit.

4.3.4 Weak Recovery

- The current economic cycle is not a normal business cycle but a balance sheet driven cycle. Over borrowing by banks, corporates and consumers are focused on shrinking their levels of borrowing to more viable and affordable levels and this balance sheet adjustment will take several years to effect. Repayment of debt will therefore act as a major impetus to the required increase in demand in the economy. Consequently, there will only be weak economic recovery over the next few years after the initial sharp inventory rebuilding and is forecast to reach only 1.5% maximum growth by 2011.
- Fiscal contraction will further dampen economic recovery driven by a strong political agenda to accelerate cuts in government and public expenditure together with increases in taxation expected after the general election in 2010.
- The consumer savings ratio will rise so as to eliminate over borrowing and to insure against people losing their jobs during the

present economic downturn. This will depress consumer expenditure which is the main driver of the UK economy thus limiting expected growth.

- Growth will also be hampered by a reduced supply of credit from weakened banks compounded by weak demand for credit.
- The eventual reversal of Quantitative Easing will take cash out of the economy and further reduce demand in the economy.
- Unemployment is likely to rise to near 3 million in 2010 and take some years to subside due to expected weak growth. High unemployment will reduce tax income and increase expenditure on benefits and the costs of local authority services.
- Inflation will not be a threat for several years as the current 6% output gap will take until 2014 to be corrected.
- However, deflation is considered a risk for some years to come as both falls in manufacturing prices over the last 12 -18 months and the impact of wage deflation will still have to feed through to the economy.
- CPI inflation will rise up to over 2% in early 2010 but will then be on a strong downward trend to about -1% in 2011.
- There is no need for the MPC to change the Bank Base Rate from 0.5% in 2010 or 2011 and possibly for the next 5 years as they will need to counter the fiscal contraction that will dampen demand in the economy over this period.
- Long term PWLB rates will fall from current levels to nearer 4% in 2010 due to the weak economic recovery and minimal inflation highlighted above so that the real rate of return (net of inflation) on long dated gilts is considered appropriate at these low levels

4.3.5 Economic summary and review

- At the current time it is difficult to have confidence as to exactly how strong the UK economic recovery will prove to be. Both the above scenarios are founded on large conflicting assumptions and research.
- The Authority's treasury advisers have adopted a more moderate view between these two scenarios which is reflected in the economic forecast set out in 4.2.2. and is based upon the following views:
  - The risk that long-term gilt yields and PWLB rates will rise markedly are considered high.
  - There are large uncertainties in both scenarios due to the major difficulties of forecasting the following areas:
    - degree of speed and severity of fiscal contraction after the general election;
    - timing and amounts of the reversal of Quantitative Easing;
    - speed of recovery of banks' profitability and balance sheet imbalances;
    - changes in the consumer savings ratio;
    - rebalancing of the UK economy towards exporting and substituting imports.

In summary, the overall balance of risks is weighted to the downside, with the view that the pace of economic growth disappoints and Bank Rate increases are delayed and / or lower than presently forecast.

There is also a risk that a double dip recession could occur.

4.4 Base Rate Forecast

Sector has advised that they expect the Bank Base Rate to steadily increase over the next three financial years from its current level of 0.50% to 1.50% by March 2011 and to 4.50% by March 2013.

4.5 Long-term PWLB Rates

With regard to the PWLB interest rates, the shorter periods are more influenced by the Base Rate whereas the longer periods are more sensitive to inflation, both actual and expected. Sector is forecasting the PWLB rates to steadily increase throughout 2010/2011 across all periods. The 5 years PWLB is forecast to be 3.6% by March 2011 and the 25 year and 50 year to be around the 5.0% mark.

5. Capital Borrowings and Borrowing Strategy for 2010/2011

5.1 Money markets will no doubt become more volatile in the lead up to the General Election. The Finance Officer will monitor the interest rate market and adopt a pragmatic approach to any changing circumstances, reporting any decisions to Authority as part of established reporting procedures for Treasury Management.

5.2 Sensitivities of the Forecast

5.2.1 The main sensitivities of the forecast are likely to be the two scenarios below. Authority officers, in conjunction with treasury advisers, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- If it was felt that there was a significant risk of a sharp rise in long and short term borrowing rates, perhaps arising from a greater than expected increase in world economic activity, then the portfolio position will be re-appraised with the likely action that further fixed rate funding would be drawn whilst interest rates were still relatively cheap.

- If it was felt that there was a significant risk of a sharp fall in long and short term borrowing rates, for example if growth rates remained low or were weakening, then long term borrowings would be postponed, and any rescheduling from fixed rate funding into variable or short rate funding would be considered.

The Finance Officer, taking account of the advice from the Authority's treasury adviser considers a benchmark financing rate of 4.50% for any further long-term borrowing for 2010/2011 to be appropriate. With

long-term interest rate forecasts set to remain around their current levels that level is considered appropriate as the long-term borrowing rate benchmark limit for 2009/2010.

5.2.2 If long term rates do not fall then consideration will be given to utilising some investment balances to fund the borrowing requirement in 2010/2011. In addition, the Authority may not need to borrow further depending upon the evaluation and progress of various capital schemes. However the need to adapt to changing circumstances will be required, and flexibility will be retained to adapt to such changes.

The Finance Officer, taking advice from the Authority's treasury advisers will continue to monitor rates closely, and whilst implementing the borrowing strategy, will adopt a pragmatic approach in identifying the low points in the interest rate cycle at which to borrow.

6. Debt Rescheduling

6.1 The reasons for any rescheduling of debt will include:

- the generation of cash savings at minimum risk;
- in order to help fulfil the Treasury Management Strategy; and
- in order to enhance the balance of the long-term portfolio (by amending the maturity profile and/or the balance of volatility).

In previous years debt rescheduling has achieved significant savings in interest charges and discounts and these interest savings have been secured for many years to come. However, changes to the PWLB rules in 2007, in respect of replacement loans significantly impacted upon the potential for debt rescheduling unless significant changes in interest rates are forecast or occur. Such has been the case in the latter part of 2008 and in 2009.

The latest interest rate projections for 2010/2011 show short term borrowing rates will be considerably cheaper than longer term rates. As such there are likely to be significant opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of their short term nature and the likely cost of refinancing those short term loans, once they mature, compared to the current rates of longer term debt in the existing debt portfolio. Any such rescheduling and repayment of debt is likely to lead to a reduction in volatility in the Authority's maturity profile as in recent years there has been a skew towards longer dated PWLB. The Authority is keeping a watching brief on market conditions in order to secure further early debt redemption when, and if, appropriate opportunities arise. The timing of all debt repayment is crucial. The timing of all borrowing and investment decisions inevitably includes an element of risk, as those decisions are based upon expectations of future interest rates. The policy to date has been very firmly one of risk spread and this will be continued.

6.2 There has been much discussion as to whether the size of spread between long term PWLB repayment and new borrowing rates should be revised (downwards) in order to help local authorities currently dissuaded from using investment cash balances to repay long term borrowing and thereby reduce counterparty and interest rate risk exposure. This has also been highlighted in recent government consultations which emphasise that Authorities must not borrow to on-lend and in a recent Debt Management Office (DMO) / PWLB consultation document options were suggested to revise the methodology used to calculate the early repayment rate. The consultation period ended in January 2010 and developments will be monitored to assess if there is any merit in amending the strategy if significant changes are introduced.

6.3 Any rescheduling undertaken will be reported to Authority, as part of the agreed treasury management reporting procedure.

ANNUAL INVESTMENT STRATEGY

7. Introduction

7.1 The Authority has regard to the Government Guidance on Local Government Investments and the Chartered Institute of Public Finance and Accountancy's (CIPFA's) Treasury Management in Public Services: Code of Practice and Cross Sectoral Guidance Notes (CIPFA TM Code).

7.2 Completion of an Annual Investment Strategy is a requirement under the Government's Guidance on Local Government Investments. The Annual Investment Strategy states which investments the Authority may use for the prudent management of its treasury balances during the financial year under the headings of 'Specified Investments' and 'Non-Specified Investments'. Under the prudential code and Government Guidance of Local Government Investments it is possible to use non-specified investments as approved investments. Non-specified investments are for greater than one year (up to a maximum of 5 years), this can present a higher risk than investments for shorter periods.

7.3 This Strategy sets out:

- the procedures for determining the use of each class of investment (advantages and associated risk), particularly if the investment falls under the category of "non-specified investments";
- the maximum periods for which funds may be prudently committed in each class of investment;
- the amount or percentage limit to be invested in each class of investment;
- whether the investment instrument is to be used by the Authority's in-house officers and/or by the Authority's appointed external fund managers, (if used); and, if non-specified investments are to be used in-house, whether prior professional advice is to be sought from treasury advisers;
- the minimum amount to be held in short-term investments (i.e. one which the Authority may require to be repaid or redeemed within 12 months of making the Investment).

8. Investment Objectives

8.1 All investments will be in pounds sterling. The general policy objective for this Authority is the prudent investment of its treasury balances. The Authority's investment priorities are in order of importance:

(A) The **security** of capital;
(B) The **liquidity** of its investments and then
(C) The Authority aims to achieve the **optimum yield** on its investments but this is commensurate with the proper levels of security and liquidity.

9. Security of Capital: The Use of Credit Ratings

9.1 Sovereign Credit Ratings

One of the recommendations of the Code is that local authorities set limits for the amounts of investments that can be placed with institutions based in foreign countries. Previously investment criteria was based upon the individual credit ratings for institutions. It is therefore recommended that sovereign ratings are applied in the Counterparty criteria as set out in Annex 1.

9.2 Counterparty Criteria and Other Market Intelligence and Information

The Authority takes into account not only the credit ratings issued by all three credit rating agencies (Fitch, Moody's and Standard & Poor's), but also, all available market data and intelligence, the level of government support to financial institutions and advice from its Treasury Management advisors and has done so for many years.

Set out in Annex 1 is the detailed criteria that will be used, subject to approval, in determining the level of investments that can be invested with each counterparty or institution. Where a counterparty is rated differently by any of the 3 rating agencies, the lowest rating will be used to determine the level of investment.

9.3 Monitoring of Credit Ratings:

- All credit ratings are monitored on a daily basis. The Authority has access to all three credit ratings agencies and is alerted to changes through its use of the Sector Treasury Services credit worthiness service.

- If a counterparty's rating is downgraded with the result that it no longer meets the Authority's minimum criteria, the Authority will cease to place funds with that counterparty. The Authority will also immediately inform its external fund manager(s), if used, to cease placing funds with that counterparty.

- If a counterparty's rating is downgraded with the result that, their rating is still sufficient for the counterparty to remain on the Approved Lending List, then the counterparty's authorised investment limit will be reviewed accordingly. A downgraded credit rating may result in the lowering of the counterparty's investment limit and vice versa. The Authority will also immediately inform its external fund manager(s), if used, of any such change(s).

- If fund managers are employed by the Authority, the Authority will establish with its fund manager(s) their credit criteria and the frequency of their monitoring of credit ratings so as to be satisfied as to their adherence to the Authority's policy.

9.4 Post Credit Crunch Developments

Since the credit crunch crisis there have been a number of developments which require separate consideration and which also help inform the Annual Investment Strategy.

9.4.1 Nationalised / Part Nationalised Banks

In order to stabilise the UK banking system, the UK Government nationalised some banks (Northern Rock and Bradford & Bingley) and took a major shareholding in others (Royal Bank of Scotland (RBS - 84% stake) and Lloyds (43% stake)). These investments by the Government will be managed on a commercial basis by a new arm's-length company, 'UK Financial Investments Limited' (UKFI), which is wholly owned by the Government. Its overarching objectives will be to protect and create value for the taxpayer as shareholder, with due regard to financial stability and acting in a way that promotes competition.

On 1st January 2010 Northern Rock was split into two separate entities; Northern Rock Plc and Northern Rock Asset Management. Northern Rock Plc is the "good bank", according to the Government, and will be regulated by the FSA. It is this bank which will hold local authority deposits. Previously Fitch assigned an Individual Rating of F to Northern Rock, which reflected that this bank had failed and is now owned by the Government. However, since the split of the bank on 1st January 2010 Fitch have not issued an individual or support rating and are currently reviewing their ratings in relation to Northern Rock.

The Government by taking such a large stake in RBS and Lloyds, together with the support packages listed below, have demonstrated their determination not to let these banks fail. As a result of this the Governments AAA rating will be applied to these counterparties with a counterparty limit of £40 million in line with our the credit criteria set out in Annex 1.

9.4.2 UK Banking System - Support Packages

The UK Government has not given a blanket guarantee on all deposits but has underlined its determination to ensure the security of the UK banking system by supporting eight named banks with a £500bn support package. Whilst no blanket guarantee is in place this represented a very significant financial commitment which has been accompanied by further statements of intent should a worsening scenario emerge. It is proposed to continue to lend to these eight banks and building societies within the UK, applying a credit rating of AA to these counterparties in recognition of their participation in the Governments support package. As a result of this it is proposed to apply to these counterparties a counterparty limit of £30 million in line with our credit criteria set out in Annex 1.

On 13th October 2008, the UK Government announced a further measure known as the Credit Guarantee Scheme. This scheme forms part of the Government's measures announced on 8th October 2008 to ensure the stability of the financial system and to protect savers, depositors, businesses and borrowers. In summary these measures are intended to:

- provide sufficient liquidity in the short term;
- make available new capital to UK banks and building societies to strengthen their resources, permitting them to restructure their finances, while maintaining their support for the real economy; and,
- ensure that the banking system has the funds necessary to maintain lending in the medium term.

As previously stated this Credit Guarantee Scheme is not a blanket guarantee by the UK Government on all deposits but it has underlined the Government's determination to ensure the security of the UK banking system by supporting the banking system with a £500bn support package.

In April 2009 the government introduced it's Asset-backed Securities Guarantee Scheme. The assets eligible for the 2009 Scheme will be residential mortgage-backed securities (RMBS) backed by residential mortgages over property in the UK. HM Treasury will keep the scope of the 2009 Scheme under review. The 2009 Scheme forms part of the Government's measures, announced on 19 January 2009, to support lending in the UK economy, and represents an extension of the 2008 Credit Guarantee Scheme for unsecured debt issuance by UK incorporated banks and building societies (the "2008 Scheme").

In summary, the 2009 Scheme is intended to:

- improve banks' and building societies' access to wholesale funding markets
- help support lending to creditworthy borrowers
- promote robust and sustainable markets over the long term
- protect the taxpayer.

9.4.3 Other Countries

Other countries have also signalled their support for their domestic banks through the provision of very significant financial support and guarantees similar to those provided by the UK Government in relation to its banks.

9.4.4 Sovereign Ratings

The sovereign credit rating of a particular country would take precedence over the individual credit ratings for the banks covered by that guarantee. However a judgement is necessary as to whether to rely on the blanket guarantees to authorise lending to these banks and for which countries they are prepared to do so. The Authority,

after consultation with it's Treasury Advisers has decided to only include countries with a minimum sovereign credit rating of AA+. Furthermore, when determining which country to include, other information will considered such as the Gross Domestic Product (GDP) for that country as well as it's economic outlook, and the strength of it's financial system.

10. Investments Defined as Capital Expenditure

10.1 The acquisition of share capital or loan capital in any body corporate is defined as capital expenditure under Section 16(2) of the Local Government Act 2003. Such investments have to be funded out of capital or revenue resources and are classified as 'non-specified investments'.

10.2 A loan or grant by this Authority to another body for capital expenditure by that body is also deemed by regulation to be capital expenditure by the Authority. It is therefore important for the Authority to clearly identify if the loan has been made for policy reasons or if it is an investment for treasury management purposes. The latter will be governed by the framework set by the Authority for 'specified' and 'non-specified' investments.

10.3 The Authority will not use (or allow any external fund managers it may appoint to use), any investment, which will be deemed as capital expenditure.

11. Provisions for Credit Related Losses

11.1 If any of the Authority's investments appear at risk of loss due to default, (i.e. a credit-related loss, and not one resulting from a fall in price due to movements in interest rates), then the Authority will make revenue provision of an appropriate amount in accordance with proper accounting practice or any prevailing government regulations, if applicable.

12. Past Performance and Current Position

12.1 During 2009/2010 the Authority did not employ any external fund managers, all funds being managed by the in-house team.

The performance of the fund managed by Sunderland City Council's in-house Treasury Management team is shown below and compares this with the previous years performance:

	2008/09 Return %	2008/09 Benchmark %	2009/10 Return % Year to date	2009/10 Benchmark % Year to date
Performance	5.06	3.60	1.90	0.35

12.2 During 2009/2010 the Authority will continue to review the optimum arrangements for the investment of its funds.

13. Outlook and Proposed Investment Strategy 2010/2011

13.1 Based on its cash flow forecasts, the Authority, together with the City Council anticipates its fund balances in 2010/2011 are likely to range between £150 million and £230 million which represents a cautious approach and provides for funding being received in excess of the level budgeted for and also for unexpected and unplanned levels of slippage and underspending. However in 2010/2011, if short-term interest rates fall materially below long-term rates, it is possible that some investment balances may be used to fund some long-term borrowing or used for debt rescheduling. Such funding is wholly dependent upon market conditions and will be assessed and reported to Authority if and when the appropriate conditions arise.

13.2 The Authority is not committed to any investments, which are due to commence in 2010/2011, (i.e. it has not agreed any forward deals).

13.3 Activities likely to have a significant effect on investment balances are:

- Capital expenditure during the financial year, (dependent upon timing), will affect cash flow and short term investment balances;
- Any slippage in capital expenditure from, and to, other financial years will also affect cash flow, (no slippage has been taken into account in current estimates);
- Any unexpected capital receipts or income;
- Timing of new long-term borrowing to fund capital expenditure;
- Possible funding of long-term borrowing from investment balances (dependent upon appropriate market conditions).

13.4 The minimum amount of overall investments that Sunderland City Council will hold in short-term investments (less than one year) is £50 million. As it has decided to restrict most of its investments to term deposits, it will maintain liquidity by having a minimum of 40% of these short-term investments maturing within 6 months.

13.5 A maximum limit of £100 million is to be set for Sunderland City Council's in-house non-specified investments over 364 days up to a maximum period of 2 years. This amount has been calculated by reference to Sunderland City Council's cash flows, including the potential use of earmarked reserves. The Finance Officer will monitor long-term investment rates and identify any investment opportunities if market conditions change. This will enable the Authority to invest balances available from sources such as the Strategic Investment Reserve, Schools, the Insurance Reserve and balances from any slippage of the capital programme.

13.6 The type of investments to be used by the in-house team will be limited to term deposits and interest bearing accounts and will follow the criteria as set out in Annex 1.

13.7 The Finance Officer, in conjunction with the treasury adviser Sector Treasury Services, and taking into account the minimum amount to

be maintained in short-term investments will continue to monitor investment rates closely and to identify any appropriate investment opportunities that may arise.

13.8 The Authority will also agree strict investment limits and investment criteria with any external fund managers it may appoint. These external fund managers will work to the following parameters:

- The institutions on the Approved Lending list of the external manager must correspond to those agreed with Sunderland City Council (i.e. only institutions on Sunderland City Council's Approved Lending List to be included as shown in Annex 1);
- they will be allowed to invest in term deposits, Certificates of Deposit (CD's) and government gilt securities;
- An investment limit of £3 million per institution (per manager);
- A maximum limit of 50% fund exposure to government gilts;
- A maximum proportion of the fund invested in instruments carrying rates of interest for periods longer than 364 days shall not exceed 50%. Again, it is proposed to only recommend the use of fixed term deposits up to a maximum of 2 years.

13.9 The details regarding the types of investment and the time periods to be permitted for investments are detailed in the Approved Lending List (Annex 1) and also with reference to the Lending List Criteria set out in (Annex 1).

13.10 It is further proposed that:

- Delegated authority continue to be given to the Finance Officer, to vary the Lending List Criteria and Lending List itself should circumstances dictate, on the basis that changes be reported to Authority retrospectively, in accordance with normal Treasury Management reporting procedures.

14. End of Year Report

14.1 At the end of the financial year, the Authority will prepare a report on its investment activity as part of its Annual Treasury Report.

Annex 1a

LENDING LIST CRITERIA

Counterparty Criteria

The criteria takes into account not only the individual institution's credit ratings issued by all three credit rating agencies (Fitch, Moody's and Standard & Poor's), but also all available market data and intelligence, the level of government support and advice from its Treasury Management advisors.

Set out below are the criteria to be used in determining the level of funds that can be invested with each institution. Where an institution is rated differently by the rating agencies, the lowest rating will determine the level of investment.

Fitch / S&P's Long Term Rating	Fitch Short Term Rating	S&P's Short Term Rating	Moody's Long Term Rating	Moody's Short Term Rating	Maximum Deposit £m	Maximum Duration
AAA	F1+	A1+	Aaa	P-1	40	2 Years
AA+	F1+	A1+	Aa1	P-1	40	2 Years
AA	F1+	A1+	Aa2	P-1	30	364 days
AA-	F1+ / F1	A1+ / A-1	Aa3	P-1	20	364 days
A+	F1	A-1	A1	P-1	10	364 days
A	F1 / F2	A-1 / A-2	A2	P-1 / P-2	10	364 days
A-	F1 / F2	A-2	A3	P-1 / P-2	5	6 months
Local Authorities (limit for each local authority)					40	364 Days

Where the UK Government holds a shareholding in an institution the UK Government's credit rating of AAA will be applied to that institution to determine the amount the Authority can place with that institution.

The Code of Practice for Treasury Management in the Public Services recommends that consideration should also be given to country, sector, and group limits in addition to the individual limits set out above, these new limits are as follows:

Country Limit

At present, only UK institutions are included on the approved Lending List. It is proposed that only countries with a minimum sovereign credit rating of AA+ by all three rating agencies will be considered for inclusion on the Approved Lending List.

It is also proposed to set a limit of £30 million for all countries except for the UK provided they meet the above criteria. A separate limit of £250 million will be applied to the United Kingdom and is based on the fact that the government has done and is willing to take action to protect the UK banking system.

Country	Limit £m
UK	250
Non UK	30

Sector Limit

The Code recommends a limit be set for each sector in which the Authority can place investments. These limits are set out below:

Sector	Limit £m
Central Government	250
Local Government	250
UK Banks	250
UK Building Societies	150
Foreign Banks	0

Group Limit

Where institutions are part of a group of companies e.g. Lloyds Banking Group, Santander and RBS, then total limit of investments that can be placed with that group of companies will be determined by the highest credit rating of a counterparty within that group, unless the government rating has been applied. This will apply provided that:

- the government's guarantee scheme is still in place;
- the UK continues to have a sovereign credit rating of AAA; and
- that market intelligence and professional advice is taken into account.

Current group limits are set out in Annex 1b.

Annex 1b

Approved Lending List

	Fitch				Moody's			Standard & Poor's			
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength Rating	L Term	S Term	Limit £m	Max Deposit Period
UK	AAA	F1+			Aaa			AAA		250	364 days
Lloyds Banking Group (see Note 1)										**Group Limit 40**	
Lloyds Banking Group plc	AA-	F1+	C	1	A1	-	-	A	A-1	40	364 days
Lloyds TSB Bank Plc	AA-	F1+	C	1	Aa3	P-1	C-	A+	A-1	40	364 days
Bank of Scotland Plc	AA-	F1+	C	1	Aa3	P-1	D+	A+	A-1	40	364 days
Royal Bank of Scotland Group (See Note 1)										**Group Limit 40**	
Royal Bank of Scotland Group plc	AA-	F1+	D/E	1	A1	-	-	A	A-1	40	364 days
The Royal Bank of Scotland Plc	AA-	F1+	D/E	1	Aa3	P-1	C-	A+	A-1	40	364 days
National Westminster Bank Plc	AA-	F1+	-	1	Aa3	P-1	C-	A+	A-1	40	364 days
Ulster Bank Ltd	A+	F1+	E	1	A2	P-1	D-	A	A-1	40	364 days
Santander Group *										**Group Limit 30**	
Santander UK plc	AA-	F1+	B	1	Aa3	P-1	C-	AA	A-1+	30	364 days
Abbey National Treasury Services plc	AA-	F1+	-	-	Aa3	P-1	-	-	-	30	364 days
Alliance and Leicester plc	AA-	F1+	B	1	Aa3	P-1	E+	AA	A-1+	30	364 days
Barclays Bank plc *	AA-	F1+	B	1	Aa3	P-1	C	AA-	A-1+	30	364 days
HSBC Bank plc *	AA	F1+	B	1	Aa2	P-1	C+	AA	A-1+	30	364 days
Nationwide BS *	AA-	F1+	B	1	Aa3	P-1	C-	A+	A-1	30	364 days
Standard Chartered Bank *	A+	F1	B	1	A2	P-1	C+	A+	A-1	30	364 days
Clydesdale Bank / Yorkshire Bank **	AA-	F1+	C	1	A1	P-1	C-	A+	A-1	10	364 days
Co-Operative Bank Plc	A-	F2	B/C	3	A2	P-1	D+	-	-	5	6 months
Northern Rock	A+	-	-	-	-	-	-	A	A-1	10	364 days

	Fitch				Moody's			Standard & Poor's			
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength Rating	L Term	S Term	Limit £m	Max Deposit Period
Top 10 Building Societies (by asset size)											
Nationwide BS (see above)											
Yorkshire BS	A-	F2	B/C	3	Baa1	P-2	D+	A-	A-2	0	
Coventry BS	A	F1	B	3	A3	P-2	C-	-	-	5	6 Months
Chelsea BS ***	BBB+	F2	C	3	Baa3	P-3	E+	-	-	0	
Skipton BS	A-	F2	B/C	3	Baa1	P-2	D+	-	-	0	
Leeds BS	A	F1	B/C	3	A2	P-1	C+	-	-	10	364 Days
West Bromwich BS ***	BBB-	F3	C/D	3	Baa3	P-3	E+	-	-	0	
Principality BS ***	BBB+	F2	C	3	Baa2	P-2	D-	-	-	0	
Newcastle BS ***	BBB-	F3	C/D	3	Baa2	P-2	D-	-	-	0	
Norwich and Peterborough BS ***	BBB+	F2	C	3	Baa2	P-2	D	-	-	0	

Notes

Note 1 Nationalised / Part Nationalised
The counterparties in this section will have the UK Government's AAA rating applied to them thus giving them a credit limit of £40 million for a maximum period of 364 days

* Banks / Building Societies which are part of the UK Government's Credit Guarantee scheme
The counterparties in this section will have a AA rating applied to them thus giving them a credit limit of £30 million for a maximum period of 364 days

** The Clydesdale Bank (under the UK section) is owned by National Australia Bank

*** These will be revisited and used only if they meet the minimum criteria (ratings of A- and above)

Any bank which is incorporated in the United Kingdom and controlled by the FSA is classed as a UK bank for the purposes of the Approved Lending List

Appendix E

Adoption of the revised CIPFA Treasury Management Code of Practice 2009

1. INTRODUCTION

1.1 The CIPFA Code of Practice on Treasury Management in Local Authorities was revised in 2009 in the light of the default on investments to Icelandic banks in 2008. The revised Code requires that a report be submitted to the Authority, board or other appropriate body, setting out four amended clauses which should be formally passed in order to approve adoption of the new version of the Code of Practice and Cross-Sectoral Guidance Notes.

1.2 The revised Code also includes an amended version of the Treasury Management Policy Statement (TMPS) incorporating a revised definition of treasury management activities (please see Appendix C). The Code sets out various requirements, incorporated into the Treasury Management Strategy Statement, which have been summarised in section 7.1 of the report

2. RESOLUTIONS

2.1 CIPFA recommends that all public service organisations adopt, as part of their standing orders, financial regulations, or other formal policy documents appropriate to their circumstances, the following four clauses.

1. The Authority will create and maintain, as the cornerstones for effective treasury management:
   - a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities;
   - suitable Treasury Management Practices (TMP's), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities These will cover the following Treasury Management activities:
     - TMP1 Risk management;
     - TMP2 Performance management;
     - TMP3 Decision making and analysis;
     - TMP4 Approved instruments, methods and techniques;
     - TMP5 Organisation, clarity and segregation of responsibilities, and dealing arrangements;
     - TMP6 Reporting arrangements and management information arrangements;
     - TMP7 Budgeting, accounting and audit arrangements;
     - TMP8 Cash and cash flow management;
     - TMP9 Money laundering;
     - TMP10 Training and qualifications;

- TMP11 Use of external service providers;
- TMP12 Corporate governance.

The content of the policy statement and TMP's will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of this organisation. Such amendments will not result in the organisation deviating from the Code's key principles.

2. The Authority will receive reports on treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMP's.

3. The Authority has responsibility for the implementation and regular monitoring of its treasury management policies and practices and for the execution and administration of treasury management decisions to the Finance officer, who will act in accordance with the organisation's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

4. The Authority nominates the Governance Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.