Committee:	**Finance & Administration**	**Agenda Item**
Date:	**25 June 2009**	**8**
Title:	**Treasury Management & Landsbanki update**	
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Summary

1 This report summarises treasury management activity for the period 13 March to 8 June. The report includes details of loans placed during this period and a schedule of balances as at 8 June.

2 The Council no longer has any funds placed in Irish financial institutions or UK building societies. Apart from the Landsbanki deposit, all other funds are with the Government Deposit Account and UK banks that have access to the UK government credit guarantee scheme, in accordance with current policy.

3 The Council complies with the recommendations and guidance issued in March by the Audit Commission and CIPFA respectively in wake of the Icelandic banks issue. Detailed self assessments are attached to this report.

4 There is still no reliable information about the prospects of recovering the Landsbanki deposit or the timetable for determining this. Encouraging advice has been received from CIPFA about how to measure the value of the deposit. The latest information available is summarised in the report.

Recommendations

The Committee is recommended to:

a) note this report

b) approve the self assessments at Appendix A and Appendix B

c) agree the proposal in paragraph 24.

Background Papers

Audit Commission report March 2009

CIPFA Treasury Management Panel Bulletin March 2009

CLG Select Committee Report June 2009

Impact

Communication/Consultation	No specific implications
Community Safety	No specific implications
Equalities	No specific implications
Finance	Detailed in the report
Human Rights	No specific implications
Legal implications	No specific implications
Sustainability	No specific implications
Ward-specific impacts	No specific implications
Workforce/Workplace	No specific implications

Treasury Management Activity 13 March 2009 to 8 June 2009

5 The following are the deposits made during the above period.

Date of deal	Amount	Institution	Interest rate	Return date
31.3.09	£1,500,000	Government DMO	0.30%	1.4.09
1.4.09	£1,000,000	Clydesdale Bank	1.44%	1.7.09
1.4.09	£2,000,000	Nationwide BS	1.59%	1.7.09
1.4.09	£1,300,000	Government DMO	0.30%	22.4.09
3.4.09	£1,300,000	Government DMO	0.35%	17.4.09
15.4.09	£2,200,000	Government DMO	0.30%	17.4.09
1.5.09	£1,000,000	Government DMO	0.30%	18.5.09
1.5.09	£1,300,000	Government DMO	0.32%	26.5.09
15.5.09	£3,500,000	Government DMO	0.30%	21.5.09
18.5.09	£2,000,000	Government DMO	0.30%	19.5.09
26.5.09	£1,000,000	Royal Bank of Scotland	1.10%	26.8.09
28.5.09	£1,000,000	Government DMO	0.30%	18.6.09
1.6.09	£1,200,000	Government DMO	0.30%	3.6.09
1.6.09	£1,000,000	Government DMO	0.30%	19.6.09
1.6.09	£1,000,000	Clydesdale Bank	0.90%	1.9.09
3.6.09	£1,000,000	Royal Bank of Scotland	1.09%	3.9.09
5.6.09	£1,500,000	Government DMO	0.30%	19.6.09

6 All deposits complied with the Council's approved counterparty policy operating at the time the deal was made.

7 The above table shows a combination of rolling 3 month deposits with UK institutions and use of the Government Debt Management Office for short term cash flow management. There is increasing reliance on DMO, a consequence of the current policy to restrict use of banking counterparties to those UK banks that have access to the UK Government Credit Guarantee Scheme (currently Abbey, Barclays, Clydesdale, HBOS/Bank of Scotland, HSBC, Lloyds TSB, Nationwide BS and Royal Bank of Scotland). In practice, it is not always the case that every such bank is accepting deposits of the size UDC has available, so options are usually fairly restricted – hence use of DMO.

8 Investment income on the above deposits totals £20,686 for an approximate 3 month period. This is about 60% of the level of income assumed in the budget.

9 All deposits due to return to the Council during this period were repaid on schedule and without difficulty.

10 The following are the deposited balances as at 8 June 2009.

Date of deal	Amount	Institution	Interest rate	Return date
17.10.07	£2,200,000	Landsbanki	6.15%	15.10.08
1.4.09	£1,000,000	Clydesdale Bank	1.44%	1.7.09
1.4.09	£2,000,000	Nationwide BS	1.59%	1.7.09
26.5.09	£1,000,000	Royal Bank of Scotland	1.10%	26.8.09
28.5.09	£1,000,000	Government DMO	0.30%	18.6.09
1.6.09	£1,000,000	Government DMO	0.30%	19.6.09
1.6.09	£1,000,000	Clydesdale Bank	0.90%	1.9.09
3.6.09	£1,000,000	Royal Bank of Scotland	1.09%	3.9.09
5.6.09	£1,500,000	Government DMO	0.30%	19.6.09

11 In addition, the following balances were held with on call deposit accounts as at 8 June:

Balance	Institution	Interest rate
£1,995,084	Abbey National Business Reserve	0.60%
£1,996,782	Bank of Scotland Corporate Base Plus Account	0.51%
£1,393,511	Barclays Bank	1.50%

Landsbanki update

12 As at 11 June there is still no definitive information about the prospects of recovering the deposit, or the timescale for determining this.

Landsbanki administration and claims registration

13 In early November 2008, officers registered UDC's claim with Landsbanki, in accordance with instructions issued at that time.

14 On 8 May, the Landsbanki announced that creditors should re-register their claims by 30 October 2009. Registered claims are to be discussed by the Landsbanki creditors committee in November. It is not until after this meeting that we expect to receive news about recovery prospects.

15 The LGA's appointed legal advisers, Bevan Brittan, have been representing all affected councils in discussions with Icelandic authorities. Landsbanki's administrators have requested that one composite claim be submitted on behalf of all local authority creditors. Bevan Brittan are to prepare the composite claim.

16 The key issue remains whether local authorities will be treated as preferential creditors. It is anticipated that the claims registration process referred to above will provide clarity on this point.

Accounting for the impairment

17 Accounting rules require the 2008/09 Statement of Accounts to show that the value of the Landsbanki deposit has reduced, to reflect the risk that some money may not be returned. This is known as "impairment".

18 CIPFA have issued guidance to local authorities on how to measure the impairment. Based upon CIPFA's interpretation of the LGA's legal advice on Icelandic law, unaudited financial information published by Landsbanki, and the general progress in relation to all Icelandic banks, CIPFA's advice is to assume that 95% of the sum deposited (plus interest) will be repaid to the Council in four equal instalments between March 2010 and December 2012. In the absence of any more definitive information the Chief Finance Officer has decided to follow the CIPFA guidance and the 2008/09 accounts have been prepared on this basis.

19 The amount deposited plus interest is £2.335m. 95% of this is £2.218m. However, there is a requirement for the accounts to discount this sum to reflect the fact that money in the future is worth less than money now. After making the required discounting calculations, the value of the investment is deemed, purely for the purpose of including an impairment in the 2008/09 Statement of Accounts, to be £1.931m, an impairment of £0.404m. This is charged to the Income & Expenditure Account.

20 The impairment does not affect the Council's bottom line in 2008/09 (or 2009/10), because of special Government regulations that defer any bottom line impact until 2010/11. The charge to the Income & Expenditure Account in 2008/09 is therefore reversed out. Although there is no bottom line impact, the reader of the Statement of Accounts can see that there is a risk to the amount deposited.

21 The CIPFA advice (95% recovery by end of 2012) is not definitive and should not be relied upon for financial planning purposes. Nevertheless, the advice is encouraging and is the most positive news since Landsbanki became insolvent. It does however remain the case that a substantial write off to revenue balances may be required in 2010/11. It will remain prudent until definitive information becomes available to build up a Landsbanki contingency fund in accordance with the Medium Term Financial Strategy. As mentioned information above, it will be late 2009 before anything definitive is known.

Audit Commission report

22 On 26 March, the Audit Commission published a report on Local Authority Icelandic deposits. The report alleged that seven councils had acted negligently in placing funds with Icelandic banks after warnings about their solvency had been made. UDC was not one of the seven and therefore there is no suggestion that UDC acted negligently.

23 UDC is one of 18 authorities named in the report as having a level of exposure to Icelandic banks greater than the level of unearmarked reserves. This is a consequence of all monies being pooled for deposit purposes including council tax and NNDR receipts, capital receipts, Section 106 funds and general cash flow buoyancy. Nevertheless, this underlines the risk to the Council in the event of any permanent loss, and emphasises that the Council should maintain its prudent approach to ensuring that unspent funds are diverted to a contingency reserve pending resolution of this matter.

24 The report included recommendations for councils to consider. A self-assessment against the Audit Commission recommendations has been completed and is attached at Appendix A. The Council already complies with the recommendations, subject to the need to ensure that members have received sufficient training to enable them to scrutinise effectively and be accountable for the treasury management function. It is proposed that a short bespoke session be organised, to be delivered by Arlingclose.

CIPFA guidance

25 In March CIPFA issued interim guidance to local authorities in wake of the Icelandic banks issue. A self-assessment against the CIPFA guidance has been completed and is attached at Appendix B. The Council already complies with the guidance, subject to keeping under review whether the Scrutiny Committee and/or Performance Select Committee could play a role in the oversight of treasury management activity.

26 CIFPA intend to publish a revised and updated Code of Practice in Summer 2009. It will be necessary to purchase and adopt the revised Code.

Communities & Local Government Select Committee

27 On 11 June the CLG Select Committee published its report into local authority investments. UDC is not mentioned in the report.

28 The Committee's view is that warning signs about Icelandic banks were evident from 2006 and therefore local authorities in general are criticised. However, certain treasury management advisers and the Audit Commission come in for particular criticism. The Council's new advisers, Arlingclose, emerge with considerable credit.

29 The Committee supports the approach of CLG i.e. there are no recommendations for more direct support by Government such as underwriting the risk of loss.

30 The key conclusions and recommendations were:

a) The primary consideration of local authority investment should remain security and liquidity; but yield should not be neglected.

b) Local authorities should be aware of the level of expertise which is necessary to run a successful treasury management operation, and have all the checks and balances in place to ensure adequate monitoring.

c) The Government, CIPFA and the LGA should study ways in which local authorities, particularly smaller ones, could join together to share expertise and pool treasury management resources.

d) All local authorities should have an Audit Committee with specific responsibility for the scrutiny of the treasury management function.

e) Specific training in treasury management should be undertaken by those councillors with responsibility for overseeing treasury management arrangements.

f) Credit ratings should not be used in isolation as a justification for the soundness of an investment.

g) Treasury management advisers must decide, define and communicate what services they are providing clients, particularly in relation to the provision of “information” and/or “advice”.

h) CIPFA should warn local authorities about over-reliance on treasury management advisers, whose services have been shown to be variable and, in some cases, inadequate.

i) The Audit Commission failed to realise that treasury management was becoming an increasingly risky area and, in that respect, it must share some of the blame for the potential loss of funds in the Icelandic banks

j) The Government’s approach to assisting those local authorities that have funds at risk in the failed Icelandic banks is an appropriate way of protecting the council tax payer whilst avoiding the “moral hazard” inherent in an unconditional, open-ended guarantee of local authorities’ investments.

31 The report will be studied and issues arising for UDC will be summarised in the next treasury management report to this Committee in September.

Risk Analysis

Risk	Likelihood	Impact	Mitigating actions
Volatility in the financial sector creates risk that funds deposited by the Council may be unsafe	1	4	Funds are placed with UK Government-backed banks and the Government deposit account facility. Proactive advice from independent Treasury Management consultants.
Investment income may fall below budgeted levels	3	2	The situation will be closely monitored but security of funds will be the prime consideration.
There is a risk that some or all of the Landsbanki deposit may not be recoverable	4	4	Claim has been lodged with the relevant authorities. LGA is lobbying on behalf of all affected councils. Establishment of a Landsbanki contingency fund.

Appendix A

Audit Commission recommendations for local authorities

Source: "Risk and Return – English Local Authorities and the Icelandic Banks"

Website link: Audit Commission report March 2009

Audit Commission Recommendation	UDC position	Compliant?	Further action needed
Set the treasury management framework so that the organisation is explicit about the level of risk it accepts and the balance between security and liquidity and the yield to be achieved. At the highest level, the organisation should decide whether it has: • appetite and capability to be able to manage risk by placing funds with financial institutions; or • no appetite and/or insufficient capability to manage the risk of placing funds in the market, and should instead place funds with the UK Government's Debt Management Office.	The Council's Treasury Management Strategy states that "the primary principle governing the Council's investment criteria is the security of its investments. After this principle the Council will ensure it has sufficient liquidity". Yield is not specified as a criterion when deciding where to place funds: security and liquidity are the only considerations. The Strategy only permits the Council to use UK banks that have access to the UK Government guarantee scheme, the UK Government deposit account facility and Money Market Funds. For longer term deposits, use of Bonds and Gilts may be made. The treasury management framework is therefore explicit about the level of risk and the nature of investments that can be made. The Strategy is subject to annual review and will take account of latest market information and advice from Arlingclose; interim reviews will be carried out if market conditions require prompt adjustment.	Yes	None
Ensure that treasury management policies: • follow the revised CIPFA code of practice; • are scrutinised in detail by a specialist committee, usually the audit committee, before being accepted by the authority; and • are monitored regularly.	CIPFA have not yet issued a revised Code of Practice, but have issued interim guidance. An assessment of UDC's compliance with this guidance is set out below (Appendix B). Treasury management policy is scrutinised by the Finance & Administration Committee prior to adoption by the Council. The Committee carries out regular monitoring.	Yes	None

Audit Commission Recommendation	UDC position	Compliant?	Further action needed
Ensure elected members receive regular updates on the full range of risks being run.	A report detailing all treasury management activity, risks and issues is received by each meeting of the Finance & Administration Committee.	Yes	None
Ensure that the treasury management function is appropriately resourced, commensurate with the risks involved. Staff should have the right skills and have access to information and external advice.	The treasury management function is performed on a day to day basis by the Technical Accountant who is suitably skilled and experienced according to the nature of the activity undertaken and the risks involved. In the absence of the Technical Accountant, the Principal Accountant (Technical) and Service Accountant (Projects) are able to carry out treasury management duties. All deposits receive prior authorisation of the Chief Finance Officer having ascertained that the proposed deal is in accordance with the approved treasury management strategy, that the proposed counterparty is securely rated on the day of the transaction and/or has access to the UK Government guarantee scheme, and that the cash flow forecast ensures liquidity after allowing for the investment to be placed. Appropriate arrangements are in place for deal authorisation if required in the absence of the Chief Finance Officer. The Council has engaged Arlingclose to provide independent specialist advice on all treasury management issues.	Yes	None
Train those elected members of authorities who have accountability for the stewardship of public money so that they are able to scrutinise effectively and be accountable for the treasury management function.	Members have not recently received training on Treasury Management. A tailored training session could be provided by the Council's external treasury management advisers, Arlingclose, at an approximate cost of £1,500.	No	Organise training session for Members e.g. 1 hour session immediately before a meeting of the F&A Committee
Ensure that the full range of options for managing funds is considered, and note that early repayment of loans, or not borrowing money ahead of need,	This is not directly applicable to UDC at present because the Council has no unpaid loans.	Yes	None

Audit Commission Recommendation	UDC position	Compliant?	Further action needed
may reduce risks.			
Use the fullest range of information before deciding where to deposit funds.	To inform decisions on where to deposit funds, the following sources of information are consulted: • UDC treasury management policy • Latest Arlingclose advice • Credit ratings websites • Finance/business media • Brokerage services Risk is minimised by only dealing with UK banks that have access to the UK government guarantee scheme and the UK Government deposit account facility.	Yes	None
Be clear about the role of external advisers, and recognise that local authorities remain accountable for decisions made.	The contract that UDC has with Arlingclose makes clear that responsibility and accountability for decisions rests with UDC. The role of Arlingclose is set out in the contract: in summary, the provision of advice and assistance to support the decision making of the Council. In practice the Chief Finance Officer assumes personal responsibility for all decisions made and reports these in full to each meeting of the Finance & Administration Committee.	Yes	None
Look for economies of scale by sharing resources between authorities or with pension funds, while maintaining separation of those funds.	The Audit Commission report cites examples of county councils looking after funds for police and fire authorities as a potentially good way of reducing costs. The scale and complexity of treasury management in such large organisations provides scope to do this. Treasury management activity in UDC is relatively straightforward and amounts to c. 0.35 FTE so there is no significant scope for realising economies of scale. Sharing resources with other authorities is not considered to be desirable due to possible reduction in direct oversight and control. For these reasons, there is not a strong case to pursue opportunities	Yes	None

Audit Commission Recommendation	UDC position	Compliant?	Further action needed
	for sharing resources although the situation will be kept under review.		

Appendix B

CIPFA interim guidance for local authorities

Source: Treasury Management in Local Authorities – Post Icelandic Banks Collapse

Website Link: [CIPFA Treasury Management Panel Bulletin March 2009]

CIPFA Guidance	UDC position	Compliant?	Further action needed
Treasury management policies adequately reflect risk and in particular security, liquidity and yield risk in that order of importance	The Council's Treasury Management Strategy states that "the primary principle governing the Council's investment criteria is the security of its investments. After this principle the Council will ensure it has sufficient liquidity". Yield is not specified as a criterion to take into account when deciding where to place funds: security and liquidity are the only considerations.	Yes	None
Diversification between counterparties, countries, sectors and instruments should be a key consideration	The Strategy only permits the Council to use UK banks that have access to the UK Government guarantee scheme, the UK Government deposit account facility and Money Market Funds. Operational limits on individual counterparties apply. For longer term deposits, use of Bonds and Gilts may be made.	Yes	None
Regular review by councillors in both executive and scrutiny functions	A report detailing all treasury management activity, risks and issues is received by each meeting of the Finance & Administration Committee. The Chairmen of Performance Select and Scrutiny Committees are members of the Finance & Administration	Partly	Consider role of Performance Select and/or Scrutiny Committee (see below)

CIPFA Guidance	UDC position	Compliant?	Further action needed
	Committee.		
Consider whether Audit Committees should be given an explicit responsibility to keep treasury management arrangements under review	In UDC the Performance Select Committee carries out the functions of an Audit Committee. The Chairman of Performance Select is a member of the Finance & Administration Committee.	No	Consider role of Performance Select Committee (see above)
The role of internal audit should be reviewed on a regular basis	Internal Audit plans are reviewed by the Performance Select Committee. Treasury management is reviewed every year. The Chief Finance Officer is consulted on the terms of reference for the annual audit.	Yes	None
Authorities should formally report on treasury management at least twice a year and preferably quarterly. Reports should be publicly available to all councillors.	A report detailing all treasury management activity, risks and issues is received by each meeting of the Finance & Administration Committee.	Yes	None
Gross and net debt levels should be reviewed and risks and benefits considered by councillors	Not applicable as UDC does not have any debt.	Yes	None
Borrowing for the explicit purpose of re-investment is ultra vires	UDC does not engage in this practice. Borrowing would only be taken out to finance capital spending or to ensure cash flow liquidity.	Yes	None
Local authorities should recognise the importance of their treasury management function and ensure they are adequately resourced including adequately trained staff.	The treasury management function is carried out by appropriately trained and experienced staff under the direct supervision of the Chief Finance Officer and with access to independent advice from Arlingclose.	Yes	None

CIPFA Guidance	UDC position	Compliant?	Further action needed
Authorities should have regard to the ratings issued by all three main agencies, Fitch, Moodys and Standard & Poor, and to make decisions on the basis of the lowest rating. Ratings should be kept under regular review and 'ratings watch' notices acted upon.	This is a feature of the Treasury Management Strategy and credit ratings checks are carried out prior to placing any funds. From April 2009, the Council is operating a variation from its usual policy on ratings by permitting the use of UK banks that have access to the UK Government Credit Guarantee Scheme, even if credit ratings fall below the usual acceptable standards.	Yes	None
Authorities should set limits on the amount invested and duration of deposits, and apply sector and country limits.	A limit of £2,000,000 per bank is operated, with a maximum length of deposit of 3 months to allow regular review and updating of the portfolio. No limits are operated in relation to DMO deposits.	Yes	None
Authorities should be clear on the status of the service they are receiving from their treasury management advisers and satisfy themselves of their appropriateness.	Arlingclose were appointed from January 2009 following a competitive tendering process in which Arlingclose demonstrated that their approach to providing services and advice met the Council's needs and was distinct from their competitors. The contract that UDC has with Arlingclose makes clear that responsibility and accountability for decisions rests with UDC. The role of Arlingclose is set out in the contract: in summary, the provision of advice and assistance to support the decision making of the Council.	Yes	None
Authorities should regularly review their decisions on the use of external investment managers	Not applicable as UDC does not use external investment managers.	Yes	None
Benchmarking should include information on security, liquidity and yield.	The Council subscribes to the CIPFA Statistical Information Service which enables comparison of UDC's investment portfolio with other councils. The usefulness of such comparisons is reduced while security remains the prime consideration.	Yes	None