

**OFFICE OF THE POLICE AND CRIME COMMISSIONER  
FOR HUMBERSIDE  
DECISION RECORD**

Decision Record Number: **40/2013**

Title: **Annual Treasury Management Report 2012/13**

**Executive Summary:**

The Annual Treasury Management Report provides comprehensive information on treasury management activity undertaken during the period 1 April 2012 – 31 March 2013 and provides a commentary on events affecting the money markets during the financial year. You are required to consider the report by regulation and in line with your approved treasury management strategy statement (TMSS). It indicates that you and the Police Authority operated in compliance with agreed treasury management practices and within the approved prudential and treasury indicators.

**Decision:**

That the Annual Treasury Management Report 2012/13 be approved.

**Background Report:** Open

**Police and Crime Commissioner for Humberside**

I confirm I have considered whether or not I have any personal or prejudicial interest in this matter and take the proposed decision in compliance with my code of conduct.

Any such interests are recorded below.

The above decision has my approval.

**Signature**

*Matthew Crowe*

**Date 29.10.13**

**POLICE AND CRIME COMMISSIONER  
FOR HUMBERSIDE**

**SUBMISSION FOR DECISION - OPEN**

**Title: Annual Treasury Management Report 2012/13**

**Date: 4 October 2013**

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**1. Executive Summary**

The Annual Treasury Management Report provides comprehensive information on treasury management activity undertaken during the period 1 April 2012 – 31 March 2013 and provides a commentary on events affecting the money markets during the financial year. You are required to consider the report by regulation and in line with your approved treasury management strategy statement (TMSS). It indicates that you and the Police Authority operated in compliance with agreed treasury management practices and within the approved prudential and treasury indicators.

**2. Recommendations**

That you note and approve the Annual Treasury Management Report for 2012/13.

**3. Background**

The Prudential Code for Capital Finance in Local Authorities (the Prudential Code) underpins the system of capital finance. Local authorities, including police and crime commissioners (and police authorities previously), can determine their own programmes for capital investment and the Prudential Code has been developed as a professional code of practice to support them, when making decisions on strategic planning, asset management and capital investment.

The Code seeks to ensure that there is a clear framework within which to operate so that authorities and PCCs can satisfy themselves that investment plans are considered affordable, prudent and sustainable and that treasury management decisions are taken in accordance with good professional practice. The process is designed to support and record local decision making in a manner that is publicly accountable.

By Regulation, there is a requirement to have regard to the Prudential Code when carrying out duties in accordance with the Local Government Act 2003.

A primary requirement of the Code is the formulation and agreement by the full Police Authority originally and now the Police and Crime Commissioner of a Treasury Management Strategy Statement (TMSS) and details of Treasury Management Practices (TMPS). These set out the responsibilities, delegation and reporting arrangements with regard to treasury management.

The original TMSS for 2012/13 was approved in March 2012 by the Police Authority. You approved your own TMSS and updated TMPS immediately on taking up office on 22 November 2012. The prudential and treasury indicators were based upon the information set out in the Medium Term Financial Strategy (MTFS) approved by the Police Authority after the budget was set for the year in February 2012. These indicators were maintained when you approved the TMSS in November.

The TMSS requires owners of the policy to receive a minimum of a mid-year review and an annual report on treasury management activities. The mid-year review was considered by the Police Authority at its final meeting on 30 October 2012 (minute 58 refers). This report ensures that the requirements of the strategy, and therefore the Code are met.

Treasury Management in this context is defined as: "the management of the organisation'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 Annual Report has been prepared in conjunction with treasury management advisers Sector, who have now been rebranded as Capita Asset Services.

## **INFORMATION**

The Annual Treasury Management Report for 2012/13 is attached at Annex A.

This formal report supplements the monthly investment reports that were provided to Members via the Authority's website and that are available to you, together with briefings and information provided by Sector and from other sources of market data. It also draws on discussions at Investment Review Meetings chaired by the Deputy Chief Executive and Treasurer and attended by key members of the Force's Treasury Management team. The meetings were held monthly throughout the year to agree short term actions in light of the latest information on market conditions, creditworthiness of potential counterparties and actual and forecast rates of interest along with details of the current and projected cash flows.

Details of performance and information on the agreed Prudential and Treasury Management Indicators are set out in Appendix 1 to Annex A.

#### **4. Options**

The reporting requirements are intended to ensure that treasury management activity has been conducted in accordance with the policy and strategy agreed by you and by the Police Authority previously and demonstrates that operations have been performed within agreed limits. There is no option but to consider this report which is a requirement in terms of demonstrating compliance with the Prudential Code

#### **5. Risks**

The strategy statement sets out detailed information in relation to risks associated with treasury management activity and proposed mitigating actions whilst acknowledging that the risk cannot be entirely eliminated. The TMSS and the TMPs and the procedures detailed within them are intended to limit the exposure to unforeseen and unbudgeted financial consequences of treasury management activity.

#### **6. Financial Implications**

The Annual Treasury Management Report sets out details of the treasury management activity undertaken in the period 1 April 2012 to 31 March 2013. The financial implications of this activity have been factored into the budget, budget monitoring reports and medium term financial plans. They reflect in year investment and borrowing assumptions and information on current and predicted cash flows together with actual interest rates and interest rate forecasts.

#### **7. Legal Implications**

The Authority is required to comply with the requirements of the Local Government Act 2003 and to have regard to guidance from the Department for Communities and Local Government and the CIPFA Code when determining its treasury management policy and strategies together with detailed practices.

There is a minimum requirement for a mid-term review of treasury management activity to be considered together with an annual report. The former was considered by the Police Authority in October 2012, prior to its abolition. Consideration of this report ensures that the requirements of the strategy, and therefore the Code are met.

#### **8. Equalities Implications**

There are no equalities implications in the context of the submission.

#### **9. Consultation**

Sector has been consulted on treasury management issues and have provided officers of the Authority, the Force and the Office of the Police and Crime Commissioner with additional information in relation to the activities undertaken during the year. However, it must be recognised that the

responsibility for all decisions with regard to policies, strategy and transactions remained with the Police Authority and have remained with you since its abolition.

**10. Media information**

There are not considered to be any particular media issues in relation to this report which is largely technical in nature.

**11. Background documents**

JB File Ref: JB/TM/Annual Report/2012/13

**12. Publication**

The report is open.



**Police and Crime Commissioner for  
Humberside**

**Annual Treasury Management Report  
2012/13**

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# Annual Treasury Management Report 2012/13

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## 1. Introduction

This PCC is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management report on the activities undertaken during the year and to provide details of the actual prudential and treasury indicators. This report for 2012/13 meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

During 2012/13 the minimum reporting requirements were that the following reports should be provided:-

- an annual treasury strategy
- a mid-year treasury update report
- an annual report following the end of the year describing the activity compared to the strategy

2012/13 saw the responsibility for treasury management moved from the Police Authority to the Police and Crime Commissioner. In November 2012 the Police Authority was abolished. The annual treasury strategy for 2012/13 was approved by the Police Authority on 27 March 2012. The Authority received a mid-term review report on 30 October 2012. The Police and Crime Commissioner approved the treasury strategy for the balance of the financial year immediately upon taking up his appointment on 22 November 2012.

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

This PCC confirms that the requirements under the Code have been met.

## 2. The Economy and Interest Rates

The financial year 2012/13 continued the challenging investment environment of previous years, namely low investment returns and continuing heightened levels of counterparty risk. The original expectation for 2012/13 was that Bank Rate would start gently rising from quarter 4 2014. However, economic growth in the UK was disappointing during the year due to the UK austerity programme, weak consumer confidence and spending, a lack of rebalancing of the UK economy to exporting and weak growth in our biggest export market - the European Union (EU). The UK coalition Government maintained its tight fiscal policy stance against a background of warnings from two credit rating agencies that the UK could lose its AAA credit rating. Key to retaining this rating will be a return to strong economic growth in order to reduce the national debt burden to a sustainable level, within the austerity plan timeframe. Weak UK growth resulted in the Monetary Policy Committee increasing quantitative easing by £50bn in July to a total of £375bn. Bank Rate therefore ended the year unchanged at 0.5% while CPI inflation fell from 3% at the start of the year to end at 2.8% in March, with a fall back to below 2% pushed back to quarter 1 2016. The EU sovereign debt crisis was an ongoing saga during the year with first Greece and then Cyprus experiencing crises which were met with bailouts after difficult and fraught negotiations.



**Gilt yields** oscillated during the year as events in the ongoing Eurozone debt crisis ebbed and flowed, causing corresponding fluctuations in safe haven flows into / out of UK gilts. This, together with a further £50bn of QE in July and widely expected further QE still to come, combined to keep PWLB rates depressed for much of the year at historically very low levels.

**Deposit rates.** The Funding for Lending Scheme, announced in July, resulted in a flood of cheap credit being made available to banks and this has resulted in money market investment rates falling sharply in the second half of the year. However, perceptions of counterparty risk have improved after the ECB statement in July that it would do “whatever it takes” to support struggling Eurozone countries. This has resulted in some return of confidence to move away from only very short term investing.

### 3. Overall Treasury Position as at 31 March 2013

At the beginning and the end of 2012/13 the treasury position was as follows:

TABLE 1	31 March 2012 Principal	Rate/ Return	Average Life yrs	31 March 2013 Principal		Rate/ Return	Average Life yrs
Total debt	£17.293m	4.46%	8.48	£23.612m		3.85%	8.22
CFR	£42.149m			£52.804m			
Over / (under) borrowing	(£24.856m)			(£29.192m)			
Total investments	£13.650m	0.79%		£4.050m		0.75%	
Net debt	£3.643m	3.67%		£19.562m		3.10%	

### 4. The Strategy for 2012/13

The expectation for interest rates within the strategy for 2012/13 anticipated low but rising Bank Rate (starting in quarter 4 of 2014) with similar gradual rises in medium and longer term fixed borrowing rates over 2012/13. Variable or short-term rates were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

In this scenario, the treasury strategy was to balance borrowing need with the cost of carry and holding higher levels of investments given counterparty risks.

The actual movement in gilt yields meant that PWLB rates fell during the first quarter of the year to historically low levels. This was caused by a flight to quality into UK gilts from EU sovereign debt, and from shares, as investors became concerned about the potential for a Lehman’s type crisis of financial markets if the Greek debt crisis were to develop into a precipitous default and exit from the Euro. During the second and third quarters, rates rose

gradually and agreement of a second bail out for Greece in December saw the flight to quality into gilts reverse somewhat, as confidence rose that the Eurozone crisis was finally subsiding. However, gilt yields then fell back again during February and March as Eurozone concerns returned, with the focus now shifting to Cyprus, and flight to quality flows into gilts resumed. This was a volatile year for PWLB rates, driven by events in the Eurozone which oscillated between crises and remedies.

## 5. The Borrowing Requirement and Debt

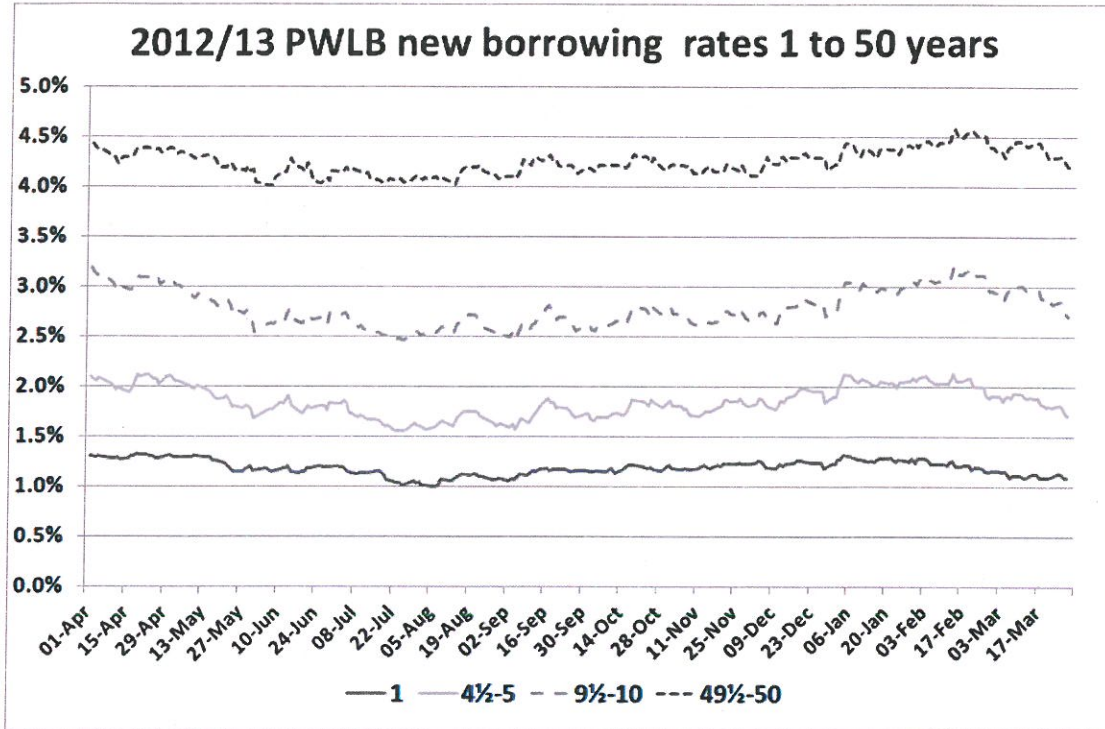
The underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR).

	31 March 2012 Actual	31 March 2013 Budget	31 March 2013 Actual
Total CFR	42.149m	52.892m	52.804m



## 6. Borrowing Rates in 2012/13

PWLB borrowing rates - the graph below shows how PWLB rates remained close to historically very low levels during the year.



## 7. Borrowing Outturn for 2012/13

**Borrowing** – the following loans were taken during the year:

Lender	Principal	Type	Interest Rate	Maturity
PWLB	£7.5m	Fixed interest rate	2.73%	9 years

This compares with a budget assumption of borrowing at an interest rate of 3.50%.

### Rescheduling

No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

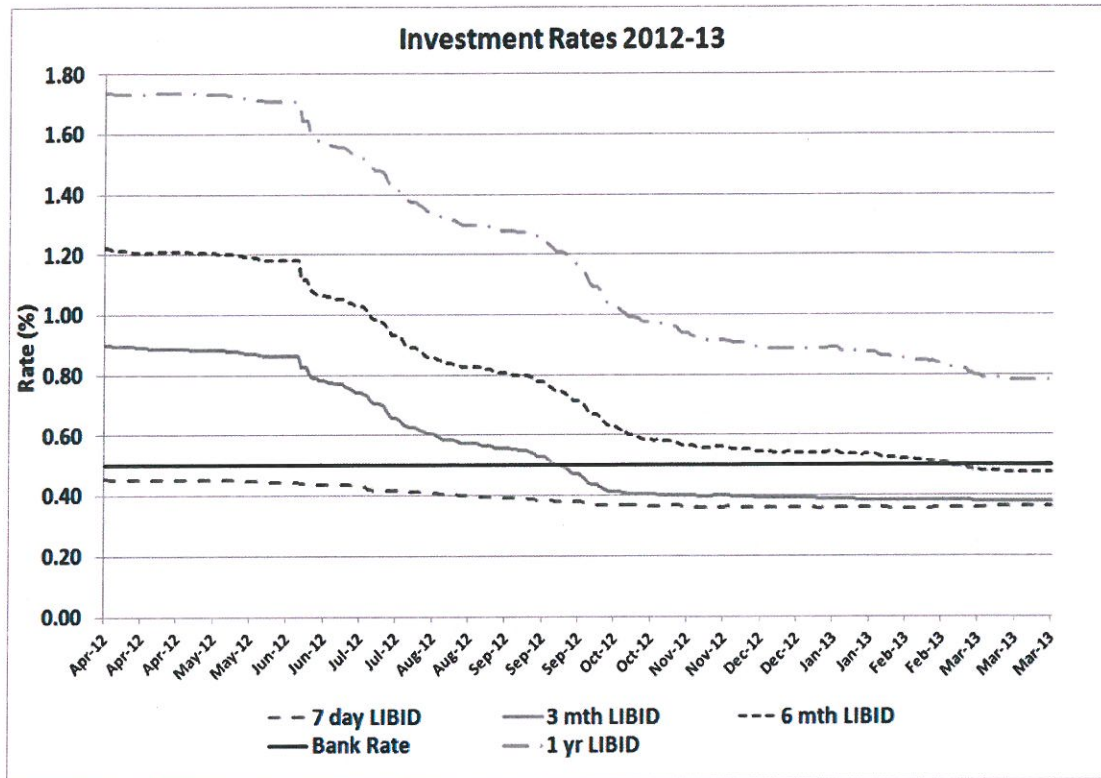
### Repayments

£1.181m was repaid at an average rate of 6.3%.

**Summary of debt transactions** – management of the debt portfolio resulted in a fall in the average interest rate of 0.61%. The ongoing revenue implications will be factored into revised budgets for 2013/14 and updates of the Medium Term Financial Strategy.

## 8. Investment Rates in 2012/13

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for four years. Market expectations of the start of monetary tightening were pushed back during the year to early 2015 at the earliest. The Funding for Lending Scheme resulted in a sharp fall in deposit rates in the second half of the year.



## 9. Investment Outturn for 2012/13

**Investment Policy** – the investment policy is governed by CLG guidance, which was been implemented in the annual investment strategy approved by the Police Authority in March 2012 and in the revision approved by the PCC in November 2012. Both set out the approach for choosing investment counterparties, based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc).

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

**Investments held** - An average balance of £7.692m of internally managed funds was maintained. The internally managed funds earned an average rate of return of 0.75%. The comparable performance indicator is the average 7-day LIBID rate, which was 0.39%. This compares with a budget assumption of £5.000m investment balances earning an average rate of 0.80%.

## 10. Icelandic Bank Defaults

At the time of the collapse of the Icelandic banks in October 2008, the UK subsidiaries Heritable and Kaupthing Singer and Friedlander (KSF) also went into administration. The former Humberside Police Authority had £5.57m deposited across two of these institutions, with varying maturity dates and interest rates as follows:

Institution	Amount (£)	Maturity Date	Interest Rate
KSF	1,000,000	22nd December 2008	6.45%
Heritable	1,000,000	22nd October 2008	5.92%
Heritable	2,000,000	3rd July 2009	6.52%
Heritable	1,570,000	21st September 2009	6.35%

The Icelandic Government has stated its intention to honour all of its commitments as a result of these banks being placed into receivership. The U.K. Government, Administrators and other agencies continue to work with the Icelandic Government to help bring this about with the Local Government Association co-ordinating the efforts of local and police authorities with Icelandic investments.

At the current time, the process of recovering assets is still ongoing with the administrators. In the cases of Heritable Bank plc and KSF, the administrators have made a number of dividend payments to date, with further payments and updates anticipated during 2013/14.

Further information is set out in the annual accounts for 2012/13 and there will be updates on progress in recovering monies outstanding in all future treasury management reports.



## Appendix 1: Prudential and Treasury Indicators

During 2012/13, legislative and regulatory requirements were complied with. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Actual prudential and treasury indicators	2011/12 Actual £	2012/13 Original £	2012/13 Actual £
Capital expenditure	15.907m	19.374m	14.356m
Capital Financing Requirement:	42.149m	61.603m	52.804m
Net borrowing	3.643m	30.460m	19.562m
External debt	17.293m	35.460m	23.612m
Investments			
• Longer than 1 year	0	0	0
• Under 1 year	13.650m	5.000m	4.050m
• Total	13.650m	5.000m	4.050m

**Net borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term external borrowing, net of investments, must only be for a capital purpose. This essentially means that borrowing has not been taken to support revenue expenditure. Net borrowing should not therefore, except in the short term, have exceeded the CFR for 2012/13 plus the expected changes to the CFR over 2013/14 and 2014/15 from financing the capital programme. This indicator allows some flexibility to borrow in advance of its immediate capital needs in 2012/13.

It should be noted that this indicator is changing to compare gross borrowing to the CFR with effect from 2013/14; this is expected to provide a more appropriate indicator.

**The authorised limit** - the authorised limit is the “affordable borrowing limit” required by s3 of the Local Government Act 2003. The PCC does not have the power to borrow above this level. The table below demonstrates that during 2012/13 gross borrowing was maintained within its authorised limit.

**The operational boundary** – the operational boundary is the expected borrowing position during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

**Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2012/13
Authorised limit	£86.354m
Maximum gross borrowing position	£23.859m
Operational boundary	£84.354m
Average gross borrowing position	£17.202m
Financing costs as a proportion of net revenue stream	1.50%

Ratio of financing costs to net revenue stream	31 March 2012 actual	2012/13 original limits	31 March 2013 actual
	0.95%	1.50%	1.07%

Incremental impact of capital investment decisions	31 March 2012 actual	2012/13 original limits	31 March 2013 actual
Increase in council tax (band D) per annum	£0.56	£3.63	£2.17

	31 March 2012 Principal	Rate/Return	Average Life yrs	31 March 2013 Principal		Rate/Return	Average Life yrs
Fixed rate funding:							
-PWLB	£17.285m	4.46%	8.48	£23.612m		3.85%	8.22
Variable rate funding:							
-PWLB	£0.008m	0.70%		£0.000m		1.00%	
<b>Total debt</b>	<b>£17.293m</b>	<b>4.46%</b>	<b>8.48</b>		<b>23.612m</b>	<b>3.85%</b>	<b>8.22</b>
<b>CFR</b>	<b>£42.149m</b>				<b>52.804m</b>		
<b>Over/ (under) borrowing</b>	<b>(£24.856m)</b>				<b>(£29.192m)</b>		
<b>Total investments</b>	<b>£13.650m</b>	<b>0.79%</b>			<b>£4.050m</b>	<b>0.75%</b>	
<b>Net debt</b>	<b>£3.643m</b>	<b>3.67%</b>			<b>£19.562m</b>	<b>3.10%</b>	

The maturity structure of the debt portfolio was as follows:

	31 March 2012 actual	2012/13 Lower limits	2012/13 Higher limits	31 March 2013 actual
Under 12 months	7%	0%	50%	5%
12 months and within 24 months	7%	0%	75%	5%
24 months and within 5 years	30%	0%	80%	24%
5 years and within 10 years	44%	0%	80%	53%
10 years and above	12%	0%	100%	13%



The maturity structure of the investment portfolio was as follows:

	2011/12 Actual £	2012/13 Original £	2012/13 Actual £
Investments (all less than one year)	13.650m	5.000m	4.050m

The exposure to fixed and variable rates was as follows:

	31 March 2012 actual £	2012/13 original limits £	31 March 2013 actual £
Fixed rate	3.635m	40.000m	19.562m
Variable rate	0.008m	52.500m	0.000m