MEETING	**COUNCIL BOARD**
DATE	**16 FEBRUARY 2010**
TITLE	**TREASURY MANAGEMENT STRATEGY STATEMENT, MINIMUM REVENUE PROVISION STRATEGY AND ANNUAL INVESTMENT STRATEGY FOR 2010/11**
RECOMMENDATION	**TO REFER THE STRATEGIES FOR 2010/11 AND THE CHANGES TO THE TREASURY MANAGEMENT SCHEDULES TO THE FULL COUNCIL FOR ADOPTION**
AUTHOR	**DAFYDD L EDWARDS - HEAD OF FINANCE**
PORTFOLIO LEADER	**COUNCILLOR DYLAN EDWARDS**

Introduction and Background

1. The Code of Practice for managing Treasury Management in the Public Services published by CIPFA, requires the Council to prepare a Policy Statement and practice papers together with detailed schedules setting out the Council's approach to all treasury operations. The primary requirement of the Code is the approval by the Full Council of the Policy Statement, the practice papers and the schedules. These were approved by the Council at its meeting of 4th March 2004.

2. The Welsh Assembly Government's Statutory Guidance on Local Government Investments ("The Guidance"), requires the Council, as part of its treasury management function to prepare an Annual Investment Strategy. The Guidance states that authorities can combine the Treasury Management Strategy Statement and the Annual Investment Strategy into one report. The Council has adopted that suggestion and the Annual Investment Strategy is therefore included as section 6 of **Appendix A.**

3. The Council is required by the Code and the Guidance to approve an annual Treasury Management Strategy Statement, MRP Strategy and an Annual Investment Strategy prior to the commencement of each financial year. The proposed strategy for 2010/11 is detailed herewith as **Appendix A.**

4. In addition the Local Government Act 2003 introduced a new prudential framework for local authority's capital investment. The new arrangements, which were applicable from 1st April 2004 introduced a new system of governance for local authority capital expenditure, based largely on self regulation. The Prudential Code for Capital Finance in Local Authorities has been developed by CIPFA as a professional code of practice, with statutory backing, to support local authorities in taking these decisions. Key objectives are to ensure that the capital investment plans of local authorities are affordable, prudent and sustainable. Local authorities, before the beginning of each financial year, are required to set certain prudential indicators for the forthcoming and following years. The indicators which are based on the capital and revenue budget proposals contained elsewhere on the agenda are shown in **Appendix B**.

5. Currently the Council only invests with the 8 institutions who are part of the Credit Guarantee Scheme. As conditions in the financial sector have begun to show improvement, in order to diversify our counterparty list **(Appendix C)**, we now need to extend our list to include some 19 overseas banks. As a result changes need to be made to the Council's current Treasury Management Schedules relating to the list of Authorised Counterparties. These changes are noted in bold print in **Appendix C** with the previous limits shown in brackets.

6. With effect from 31st March 2008, the Welsh Assembly Government introduced the Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2008 [the "Amendment Regulations"]. These Regulations introduce certain amendments to those introduced in 2003 [the "Original Regulations"] as part of the implementation of the Prudential Borrowing regime. Amongst the changes introduced is the requirement for an Annual Minimum Revenue Provision (MRP) Policy Statement.

7. The Original Regulations set out a statutory basis and a complex formula for the calculation of MRP. The Amendment Regulations only require a charge that is 'prudent', and authorities are permitted more discretion in terms of the charge levied, albeit within certain parameters. The attached strategy in Section 8 of **Appendix A** therefore also incorporates the Annual MRP Statement for 2010/11.

8. The members of the Principal Scrutiny Committee have asked me to confirm if the Council have "any investments pertaining to arms". Excluding the Pension Fund's investments, which are much more varied and are subject to the appropriate attention from the Pensions Committee and the Principal Scrutiny Committee apart from this report, all the Council's "investments" (i.e. the general fund's investments) are held as cash deposits in banks (or similar). Details of such institutions are shown in Section 6 of Appendix A on pages 8-9 of this paper, and Appendix C on page 15 provides details of all the specific banks. Of course, it is highly likely that a number of these banks will be lending money to companies that have something to do with arms, but that is unavoidable, because even if we did select a list of "clean" banks there's nothing to stop these companies from changing to one of the banks on our "clean" list. The Council definitely does not invest directly in any company which is involved in arms manufacturing or the arms trade.

9. The members of the Principal Scrutiny Committee have asked me to note "what is happening with our investment in Iceland". I attach details on the relevant events, developments and expectations in Appendix D on page 16.

10. For the second year running, the Working Group for Specialist Financial Matters have already received a detailed presentation of this paper and have carefully scrutinised the sections that have changed. Councillor John Gwilym Jones, Councillor Dewi Llewelyn and the relevant Corporate Director (Dilwyn O Williams) met with the Portfolio Leader for Finance (Councillor Dylan Edwards) and relevant officers from the Finance Department on 28 January. Explanations were received on numerous matters and changes were made to some parts of the draft version presented to the Working Group. The full Council will have to adopt the Strategy, but certainly, members of the Principal Scrutiny Committee, the Board and the full Council will be relying on the members of the Working Group for Specialist Financial Matters who have had relevant "training" and who have had a chance to question and to challenge in an informal environment.

Recommendation

11. The Board is asked to recommend to the Full Council on 25 February that the Treasury Management Strategy Statement, MRP Strategy and the Annual Investment Strategy for 2010/11 (Appendix A), the Prudential Indicators (Appendix B) and changes to the Treasury Management Schedules (Appendix C) are adopted.

APPENDIX A

TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2010/11 TO 2012/13

1. Introduction

CIPFA has defined Treasury Management 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 Council is responsible for its treasury decisions and activity. No treasury management activity is without risk. The successful identification, monitoring and control of risk is an important and integral element of its treasury management activities. The main risks to the Council's treasury activities are:

- Liquidity Risk (Inadequate cash resources);
- Market or Interest Rate Risk (Fluctuations in interest rate levels);
- Inflation Risk (Exposure to inflation);
- Credit and Counterparty Risk (Security of Investments);
- Refinancing Risk (Impact of debt maturing in future years);
- Legal & Regulatory Risk;
- The risk of failing to receive the best possible rate of interest available.

The strategy also takes into account the impact of the Council's Revenue Budget and Capital Programme on the Balance Sheet position, the current and projected Treasury position, the Prudential Indicators and the outlook for interest rates.

The purpose of this Treasury Management Strategy Statement is to approve the:

- Treasury Management Strategy for 2010-11;
- Prudential Indicators;
- MRP Statement; and
- Use of Specified and Non-Specified Investments.

2. Balance Sheet and Treasury Position

The underlying need to borrow for capital purposes as measured by the Capital Financing Requirement (CFR) together with Balances and Reserves are the core drivers of Treasury Management Activity. The estimates are set out below:

	31 Mar 10 Estimate £m	**31 Mar 11 Estimate £m**	**31 Mar 12 Estimate £m**	**31 Mar 13 Estimate £m**
CFR	147.3	149.7	156.5	157.7
Balances & Reserves	(46.0)	(39.4)	(36.3)	(33.3)
Net Balance Sheet Position	**101.3**	**110.3**	**120.20**	**124.4**

Market conditions, interest rate expectations and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position.

As the CFR represents the level of borrowing for capital purposes, and revenue expenditure cannot be financed from borrowing, net physical external borrowing should not exceed the CFR other than for short term cash flow requirements.

The Council's estimated treasury management portfolio position is as follows:

	31 Mar 10 Estimate £m	31 Mar 11 Estimate £m	31 Mar 12 Estimate £m	31 Mar 13 Estimate £m
External Borrowing:				
Fixed Rate – PWLB	107.3	103.6	97.8	96.5
Fixed Rate – Market	16.2	16.2	16.2	16.2
IFRS long-term liabilities:				
- **Operating Leases**	0.0	0.2	0.2	0.2
Total External Debt	**123.5**	**119.0**	**114.2**	**112.9**
Total Investments	**(46.0)**	**(39.4)**	**(36.3)**	**(33.3)**
Net Borrowing Position/ (Net Investment position)	**77.5**	**79.6**	**77.9**	**79.6**

* ***PWLB*** *– Public Works Loan Board*

3. Outlook for Interest Rates

The interest rate outlook as at January 2010, is provided by the Council's treasury advisor, Arlingclose Ltd, and is shown below.

	Dec-09	Mar-10	June-10	Sep-10	Dec-10	Mar-11	June-11	Sep-11	Dec-11	Mar-12
Official Base Rate										
Upside Risk				+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50
Central Case	**0.50**	**0.50**	**0.50**	**0.50**	**1.00**	**1.50**	**2.00**	**2.50**	**3.00**	**3.00**
Downside Risk					-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
1 Year LIBID										
Upside Risk				+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central Case	**1.25**	**1.25**	**1.25**	**1.50**	**1.75**	**2.25**	**3.00**	**3.50**	**4.00**	**4.00**
Downside Risk					-0.25	-0.25	-0.50	-0.50	-0.50	-0.50
5 Year Gilt										
Upside Risk		+0.25	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central Case	**2.60**	**2.70**	**2.80**	**2.90**	**3.00**	**3.25**	**3.50**	**3.75**	**4.00**	**4.25**
Downside Risk		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
10 Year Gilt										
Upside Risk			+0.25	+0.25	+0.25	+0.25	+0.25	+0.25	+0.25	+0.25
Central Case	**3.60**	**3.75**	**3.75**	**4.00**	**4.00**	**4.25**	**4.25**	**4.50**	**4.50**	**4.75**
Downside Risk			-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
20 Year Gilt										
Upside Risk		+0.25	+0.50	+0.50	+0.50	+0.25	+0.25	+0.25	+0.25	+0.25
Central Case	**4.10**	**4.25**	**4.50**	**4.75**	**4.75**	**5.00**	**5.00**	**5.00**	**5.00**	**5.00**
Downside Risk		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
50 Year Gilt										
Upside Risk	+0.25	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central Case	**4.00**	**4.25**	**4.50**	**4.50**	**4.50**	**4.75**	**4.75**	**4.75**	**4.75**	**4.75**
Downside Risk			-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

Arlingclose's current interest rate view is that the Bank Rate:-

- will remain at 0.50% until Q4 2010 when it will rise to 1.00% and to 1.5% in Q1 2011.
- it is expected that it will continue it's gentle rise until it reaches 3.0% in Q1 2012.

However, there is a downside risk to these forecasts from downgrades to sovereign ratings and/or political instability.

Their economic forecast is as follows:

- The Bank of England forecasts GDP to grow by 4% in 2011 but concedes growth could be impeded by restrictions in bank credit and consumers' cautious spending behaviour. This is an optimistic forecast in our view; evidence of recovery is scant with weak real economic data and rising unemployment. .
- The employment outlook remains uncertain. Pay freezes and job cuts will continue into 2010.
- Inflation is not an immediate worry. The Bank's forecast is for CPI to rise in the next few months from higher commodity prices and VAT reverting to 17.5%, but is forecast to remain below 2% in the short term, only surpassing the target in 2012.
- The UK fiscal deficit remains acute. Cuts in public spending and tax increases are now inevitable and more likely to be pushed through in 2010 by a new government with a clear majority.
- The net supply of gilts will rise to unprecedented levels in 2010. Failure to articulate and deliver on an urgent and credible plan to lower government borrowing to sustainable levels over the medium term will be negative for gilts.

4. Borrowing Requirement and Strategy

The Council's underlying need to borrow for capital purposes is measured by reference to its Capital Financing Requirement (CFR) – see Appendix B. The CFR represents the cumulative capital expenditure of the local authority that has not been financed. To ensure that this expenditure will ultimately be financed, local authorities are required to make a Minimum Revenue Provision for Debt Redemption (MRP) from within the Revenue budget each year.

Physical external borrowing may be greater or less than the CFR, but in accordance with the Prudential Code, the Council will ensure that net external borrowing does not, except in the short term, exceed the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years.

The cumulative estimate of the long-term borrowing requirement is as follows:

	31 Mar 10 Estimate £m	31 Mar 11 Estimate £m	31 Mar 12 Estimate £m	31 Mar 13 Estimate £m
Capital Financing Requirement	147.3	149.7	156.5	157.7
Less: Existing Profile of Borrowing and Other Long Term Liabilities	**(123.5)**	**(119.0)**	**(114.2)**	**(112.9)**
Maximum External Borrowing Requirement	**23.8**	**30.7**	**42.3**	**44.8**
Balances & Reserves	(46.0)	(39.4)	(36.3)	(33.3)
Net Borrowing Requirement / (Investments)	**(22.2)**	**(8.7)**	**6.0**	**11.5**

The Council's strategy is to maintain maximum control over its borrowing activities as well as flexibility on its loans portfolio. Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimise borrowing costs over the medium to longer term. A prudent and pragmatic approach to borrowing will be maintained to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the Council's Prudential Indicators.

In conjunction with advice from its treasury advisor, Arlingclose, the Council will keep under review the options it has of borrowing up to the available capacity within its CFR and Affordable Borrowing Limit (defined by CIPFA as the Authorised Limit).

The Borrowing Strategy
PWLB variable rates have fallen below 1%. They are expected to remain low as the Bank Rate is maintained at historically low levels to enable the struggling economy emerge from the recession. Against a backdrop of interest rates remaining lower for longer then borrowing long term funds as they are required may remain appropriate.

The PWLB remains the preferred source of borrowing given the transparency and control that its facilities continue to provide.

5. Debt Rescheduling

The Council will continue to maintain a flexible policy for debt rescheduling. Market volatility and the steep yield curve may provide opportunities for rescheduling debt from time to time.

The rationale for rescheduling would be one or more of the following:

- Savings in interest costs with minimal risk;
- Balancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio; and
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

Any rescheduling activity will be undertaken within the Council's treasury management policy and strategy, and will be reported to the Portfolio Leader following its action. If he believes its a matter of substance, it will also be reported to the Board.

6. Investment Policy and Strategy

Guidance from the Welsh Assembly Government on Local Government Investments requires the setting of an Annual Investment Strategy (AIS).

Investment Policy
To comply with this Guidance, the Council's general policy objective is the prudent investment of its treasury balances. The Council's investment priorities are the security of its capital and liquidity of its investments rather than yield. The Council will aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Council will not engage in such activity. Investment instruments identified for use in the financial year are listed below under the 'Specified' and 'Non-Specified' Investments categories.

Specified Investments:
All such investments will be sterling denominated, **with maturities up to a maximum of 1 year,** meeting the minimum 'high' credit criteria where applicable.

	Minimum 'High' Credit Criteria	Use	Maximum Period
Debt Management Account Deposit Facility (DMADF)	High Security although DMADF is not credit rated.	In-house	1 year
Term Deposits with Local Authorities	High Security although Local Authorities are not credit rated.	In-house	1 year
Term Deposits and Certificates of Deposit with banks and building societies including callable deposits with maturities up to 1 year.	Short Term minimum F1 or equivalent. Long Term minimum A+ or equivalent. The Council will also take into account information on corporate developments of and market sentiment toward investment counterparties.	In-house	1 year

Non-Specified Investments:
Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Council's use:

	Minimum Credit Criteria	Use	Maximum Maturity Period	Maximum % of Portfolio
Term Deposits and Certificates of Deposit with banks and building societies	Short Term minimum F1 or equivalent. Long Term minimum AA- or equivalent. The Council will also take into account information on corporate developments of and market sentiment toward investment counterparties.	In-house and Fund Managers	2 years	50% of all the Council's portfolio.
Money Market Funds	AAAm	In-house and Fund Managers	Daily Liquidity	50% of all the Council's portfolio.

The credit crisis has refocused attention on the treasury management priority of security of capital monies invested. The Council uses credit ratings to derive its counterparty list (Appendix C). The Council and its Treasury Advisors, Arlingclose, will continue to maintain a counterparty list and will assess and update the credit standing of the institutions on a regular basis. This assessment will take into account factors such as:

- the individual credit ratings (minimum long term A+);
- credit default swaps;
- a country's net debt as a percentage of its Gross Domestic Product;
- access to government guarantee schemes;
- potential support from a well-resourced parent institution; and
- its share price.

If a downgrade results in a counterparty no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately. If a body is placed on negative rating watch (i.e. there is a reasonable probability of a rating change and the likelihood of that change being negative) and it is currently near the floor of the minimum acceptable rating for placing investments with that body, then no further investments will be made with that body.

Investment Strategy

The Council's in-house managed funds are mainly cash-flow derived and there is a core balance available for investment over a 2-3 year period. Investments will accordingly be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

Given due consideration to the Council's level of cash balances over the next 3 years, the need for liquidity, its spending commitments and provisioning for contingencies, the Council has determined that £40m of its overall cash balances may be held in non-specified investments during the year.

The UK Bank Rate has been maintained at 0.5% since March 2009. Short-term money market rates are likely to remain at very low levels which will have a significant impact on investment income. The Council's strategy must however be geared towards this development whilst adhering to the principal objective of security of invested monies.

Conditions in the financial sector have begun to show signs of improvement, albeit with substantial intervention by government authorities. In order to diversify the counterparty list (Appendix C), the use of comparable non-UK Banks for investments is now considered appropriate. The sovereign states whose banks are to be included are Australia, Canada, Finland, France, Germany, Netherlands, Spain, Switzerland and the US. These countries, and the Banks within them have been selected after careful assessment of the factors noted above. The Council and its Treasury Advisors, Arlingclose, will continue to analyse and monitor these factors and credit developments on a regular basis and respond as necessary to ensure security of the capital sums invested.

7. Balanced Budget Requirement

The Council complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

8. 2010/11 MRP Statement

The Local Authorities (Capital Finance and Accounting)(Wales)(Amendment) Regulations 2008 [SI 2008/588 (W.59)] place a duty on local authorities to make a prudent provision for debt redemption. Guidance on Minimum Revenue Provision has been issued by the Welsh Assembly Government and local authorities are required to "have regard" to such Guidance under section 21(1A) of the Local Government Act 2003.

For capital expenditure incurred before 1st April 2008 or which in the future will be supported capital expenditure, the MRP policy will be based on the Capital Financing Requirement at 4% of the opening balance less an adjustment ('A') (Option 1). "Adjustment A" was intended to achieve neutrality between the CFR and the former Credit Ceiling which was used to calculate MRP prior to the introduction of the Prudential System on 1st April 2004.

From 1st April 2008, for all unsupported borrowing, exercised under the Prudential Code, the MRP policy will be based on the Asset Life Method (Option 3). The minimum revenue provision will be at equal annual instalments over the life of the asset. The first charge will be delayed until the asset is operational.

Estimated asset life periods will be determined under delegated powers. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.

As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

MRP in respect of PFI and leases brought on Balance Sheet under the 2009 SORP and IFRS will match the annual principal repayment for the associated deferred liability.

The Authority will be reviewing this policy annually in light of the Asset Management Plan.

9. Reporting on the Treasury Outturn

The Head of Finance will report to Resources and Corporate Scrutiny Committee on treasury management activity and performance as follows:
(a) Mid year and year end review against the strategy approved for the year.
(b) The Council will produce an outturn report on its treasury activity no later than 30th September after the financial year end.
(c) The Resources and Corporate Scrutiny Committee will be responsible for the scrutiny of treasury management activity and practices.

10. Other items

Member Training

CIPFA's revised Code requires the Head of Finance to ensure that members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. The Specialist Finance Matters Working Group met on 28/01/10 and received guidance and support from officers in this respect. More formal training, possibly sourced externally may be provided for relevant members during 2010/11.

PRUDENTIAL INDICATORS 2010/11 - 2012/13

1 Background:

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators. It should be noted that CIPFA undertook a review of the Code in early 2008. The outcome from that review has yet to be published.

The Council is also required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. This was adopted by the full Council on 4 March 2004.

PRUDENTIAL INDICATOR	**2008/09**	**2009/10**	**2010/11**	**2011/12**	**2012/13**
(1). CAPITAL PRUDENTIAL INDICATORS REPORT	**actual**	**estimate**	**estimate**	**estimate**	**estimate**
a) Capital Expenditure	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
General Fund	46,898	39,015	24,548	24,708	21,298
Housing Revenue Account (HRA)	6,885	7,050	0	0	0
TOTAL	**53,783**	**46,065**	**24,548**	**24,708**	**21,298**
b) Ratio of financing costs to net revenue stream					
General Fund	4.28%	5.77%	5.70%	4.96%	4.69%
HRA	8.49%	7.08%	-	-	-
c) Capital Financing Requirement as at 31 March	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
General Fund	144,038	147,278	149,694	156,480	157,698
HRA	14,524	0	0	0	0
TOTAL	**158,562**	**147,278**	**149,694**	**156,480**	**157,698**
d) Incremental impact of capital investment decisions			**£**	**£**	**£**
i) Increase in council tax (band D) per annum (per Code guidance)	-	-	13.54	18.68	38.45
ii) Increase in council tax (band D) per annum (local indicator)	-	-	10.16	0	0

Notes on the Capital Prudential Indicators:

1a) Actual capital expenditure for 2008/09 and estimates for the current and forthcoming years which are based on only reasonably secure sources of finance.

1b) The net cost of financing debt is shown (which includes interest and principal repayments less the interest received from investments) as a percentage of the income receivable from the Government and taxpayers.

1c) The Capital Financing Requirement reflects the authority's basic requirement to borrow for capital purposes.

1d) i) The estimated additional cost of the capital investment decisions on the council tax calculated according to the Code's guidance. The Asset Management Plan, which was adopted by the Council this financial year, has had a major impact on this indicator and the way in which it is calculated. It shows the revenue impact of the Plan assuming that the whole Plan is a 'new capital investment decision'. This official indicator is a purely technical calculation which provides rather misleading estimates. In order to attempt to identify the real impact on revenue of the capital programme, the indicator below has been included.

1d) ii) The estimated additional cost of the capital investment decision on the council tax assuming that the only real impact is the additional corporate revenue contribution of £500,000 that has been included in the 2010/11 base budget.

The following prudential indicators (in table 2 below) are relevant for the purposes of setting an integrated treasury management strategy.

PRUDENTIAL INDICATOR	**2008/09**	**2009/10**	**2010/11**	**2011/12**	**2012/13**
(2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS	**actual**	**estimate**	**estimate**	**estimate**	**estimate**
a) Authorised limit for external debt -	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Borrowing	165,000	160,000	160,000	160,000	160,000
other long term liabilities	0	0	0	0	0
TOTAL	170,000	160,000	160,000	160,000	160,000
b) Operational boundary for external debt -	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Borrowing	150,000	140,000	135,000	130,000	125,000
other long term liabilities	0	0	0	0	0
TOTAL	150,000	140,000	135,000	130,000	125,000
c) Upper limit for fixed interest rate exposure					
Net interest re. fixed rate borrowing	100%	100%	100%	100%	100%
d) Upper limit for variable rate exposure					
Net interest re. variable rate borrowing	50%	50%	50%	50%	50%
e) Upper limit for total principal sums invested for over 1 year	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
(per maturity date)	20,000	40,000	40,000	40,000	40,000

Notes on the Treasury Management Prudential Indicators:

2a) a b) The Authorised Limit and Operational Boundary reflect the authority's expectations which it imposes on itself regarding external borrowing. They are based on the most likely, prudent but not worst case scenario, with additional headroom in the Authorised Limit.

2c) a d) The Upper limit on the authority's exposure to changes in fixed and variable interest rates.

2e) The Upper limit on the authority's exposure to investments for periods longer than 364 days.

Maturity structure of borrowing during 2010/11	Upper Limit	Lower Limit
under 12 months	25%	0%
12 months and within 24 months	25%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and above	100%	0%

APPENDIX C

GWYNEDD COUNCIL'S LIST OF AUTHORISED COUNTERPARTIES

Term Deposits / Call Accounts

Country	**Counterparty**	**Maximum Limit of Investments £m**	**Maximum Length of Loans**
UK	DMADF, DMO	No limit	No limit
UK	UK Local Authorities	£10m (£10m)	1 year
UK	Abbey	**£20m** (£15m)	2 years
UK	Bank of Scotland/Lloyds	**£20m** (£15m)	2 years
UK	Barclays	**£20m** (£15m)	2 years
UK	Clydesdale	**£20m** (£15m)	2 years
UK	HSBC	**£20m** (£15m)	2 years
UK	Nationwide	**£20m** (£15m)	2 years
UK	Royal Bank of Scotland	**£20m** (£15m)	2 years
Australia	**Australia and NZ Banking Group**	**£5m (£0m)**	**1 year**
Australia	**Commonwealth Bank of Australia**	**£5m (£0m)**	**1 year**
Australia	**National Australia Bank Ltd**	**£5m (£0m)**	**1 year**
Australia	**Westpac Banking Corp**	**£5m (£0m)**	**1 year**
Canada	**Bank of Montreal**	**£5m (£0m)**	**1 year**
Canada	**Bank of Nova Scotia**	**£5m (£0m)**	**1 year**
Canada	**Canadian Imperial Bank of Commerce**	**£5m (£0m)**	**1 year**
Canada	**Royal Bank of Canada**	**£5m (£0m)**	**1 year**
Canada	**Toronto-Dominion Bank**	**£5m (£0m)**	**1 year**
Finland	**Nordea Bank Finland**	**£5m (£0m)**	**1 year**
France	**BNP Paribas**	**£5m (£0m)**	**1 year**
France	**Calyon (Credit Agricole Group)**	**£5m (£0m)**	**1 year**
France	**Credit Agricole SA**	**£5m (£0m)**	**1 year**
Germany	**Deutsche Bank A**	**£5m (£0m)**	**1 year**
Netherlands	**Rabobank**	**£5m (£0m)**	**1 year**
Spain	**Banco Bilbao Vizcaya Argentaria**	**£5m (£0m)**	**1 year**
Spain	**Banco Santander SA**	**£5m (£0m)**	**1 year**
Switzerland	**Credit Suisse**	**£5m (£0m)**	**1 year**
US	**JP Morgan**	**£5m (£0m)**	**1 year**

*Investments in Non-UK banks will be restricted to a maximum limit of 40% of the portfolio, with a £10m country limit.

Instrument	**Country**	**Counterparty**	**Maximum Limit of Investments £m**	**Maximum Length of Loans**
Gilts	UK	DMO	No limit	No limit
AAA rated Money Market Funds	UK/Ireland/ Luxembourg	Money Market Funds	£5m per name	Daily Liquidity
Other MMFs and CIS	UK	Collective Investment schemes	£5m per name	Daily Liquidity

APPENDIX D

What is happening with our investment in Iceland?

There have been several misleading articles in the national and regional press during January about the Icelandic President's decision to veto the loan agreement that the Icelandic government had agreed with HM Treasury in relation to the repayment of deposits to UK individual investors in Icesave. This issue has no impact on local authorities. The implications are for the Westminster Government, which would fail to recover what Iceland should pay under pan-European investor compensation agreements.

There have been articles in the press regarding the decision of the Winding Up Board of Glitnir Bank not to give UK local authorities priority creditor status. As general unsecured creditors, local authorities who have a total £217 million deposited in Glitnir Bank, would be likely to recover 25-30% of their deposits, rather than 100% as priority creditors, and this decision may be challenged in court under Icelandic law. However, Gwynedd Council has no money deposited in Glitnir or in Landsbanki, which is in a similar position (with £414 million of council deposits) but has recognised council deposits as priority claims.

As reported to the Council in October 2008 and in the statutory Financial Statements for 2008/09, Gwynedd Council had £4 million deposited in Heritable Bank which was established in Glasgow and registered as a UK bank, but encountered difficulties because it was a subsidiary of Landsbanki. Since Heritable is a British bank, the winding-up procedures are going ahead under insolvency law in the UK, with Ernst & Young acting as administrators.

The administrators' detailed report to creditors (dated 13 August 2009) was consistent with their previous correspondence reports in referring to a "base case" return of 70-80%. The 70% figure was based on early disposal of Heritable's assets before the end of 2010, while the 80% figure was based on maximising returns during the period to 2012/13. The administrators "base case" included cautious assumptions about the factors affecting recovery, and local authorities have consistently urged the administrators to maximise returns over the long run.

Heritable Bank's administrators have already paid two dividends to creditors:

- 16.13 pence in the pound on 28 July 2009
- 12.66 pence in the pound on 18 December 2009

On each occasion, the dividend payments were slightly higher than the administrator had predicted (in advance of 2008/09 annual accounts closure).

On 28 January 2010, the administrators of Heritable wrote again to creditors to advise that they were increasing their estimates of recoveries. The administrators' current projections suggest revised "base case" estimated return of 79-85% (up from 70-80%).

It is unlikely that the exact final return will be clear until 2012/13, and the value will depend upon the performance of assets held by Heritable, which includes equity, but is thought to be primarily property in the UK. The administrators previous and revised base case are based upon assumptions in respect of key factors which could have a significant impact on returns to creditors, including interest rates, the housing market and the wider economic environment. Ernst & Young state that these factors are impossible to predict over long periods with any significant degree of confidence or accuracy, hence the return to creditors may be significantly higher or lower than predicted, and their estimates remain “provisional”.

However, on the basis of the evidence currently to hand, it is reasonable to conclude that creditors in Heritable Bank should receive returns of 85%. If so, Gwynedd Council would be likely to recover £3.4 million or more of its original deposit of £4 million. If there is a second downturn then less than 85% might be recovered, but if there is further improvement in the condition of Britain’s economy, then it would not be impossible for us to recover the whole £4m.

Since 2008, the Council’s investment policies changed to become more ‘risk-averse’ (see the Treasury Management Strategy for 2009/10 and for 2010/11). However, the potential “real” loss (possibly about £600,000) with Heritable Bank should be considered in the context of significant interest earned during the preceding years. If all the Council’s money had been invested in a securer place, then the interest generated would have been around 2% lower with an annual income of approximately between £1m and £2m lower.

The downfall of Iceland’s banks was the origin of our potential losses, but the money was deposited in a British bank. More recent developments in Iceland will have no effect upon the value of the Council’s investment. The final result of this issue will now be dependent upon the recovery of the UK economy and the success of the administrators in acting effectively on our behalf in order to maximise returns from the assets of Heritable Bank (to date and until 2012/13).

A. Views of the Local Member

B. Views of the Statutory Officers

1. Chief Executive:-

   The events of October 2008 have shown the importance of prudent planning whilst considering our investment policy. I have nothing to add to the report which will, by the time it reaches the Board, have received the attention of the Principal Scrutiny Committee.

2. Monitoring Officer:-

   Nothing to add regarding propriety

3. Chief Finance Officer:-

   Author of the report

C. Background Papers

D. Policy Implications