# TREASURY MANAGEMENT PRACTICE NOTES (Extract)

## TMP 1 – RISK MANAGEMENT

### General Statement

The Section 151 Officer will oversee the design, implementation and monitoring of all arrangements for the identification, management and control of treasury management risk. The Section 151 Officer will ensure that reports are presented at least annually, on the adequacy/suitability thereof and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the Council's objectives. In respect of each of the following risks, the arrangements that seek to ensure compliance with these objectives are set out in this document.

### [1] Credit and Counter party risk management

The Office of the Deputy Prime Minister, (now Communities and Local Government), issued Investment Guidance in 2004, and also the Local Authorities (Capital Finance and Accounting) (Amendment) (England) Regulations 2007 (SI 2007/573), which constrain the types of investments that local authorities can use, and so forms the structure of the Council's policy. The CLG issued further guidance effective from 1 April 2010, where the Council had to state its approach to assessing the risk of loss of investments; this has been incorporated into the Council's policy.

The key intention of the Guidance is to maintain the current requirement that councils invest prudently, and that priority is given to security and liquidity before yield. In order to facilitate this objective the guidance requires the Council to have regard to the CIPFA publications Treasury Management in Public Services: Code of Practice and Cross-Sectoral Guidance Notes and the sector specific guidance; Guidance Notes for Local Authorities including Police Authorities and Fire Authorities. The Council first adopted the TM Code in 2003, and adopted the revised 2009 TM Code in March 2010, and adopted the revised 2011 TM Code February 2012. Accordingly, the Council will ensure that its counter party lists and limits reflect a prudent attitude towards organisations with whom fund may be deposited, and will limit its investment activities to the instruments, methods and techniques referred to in TMP4 (Approved instruments, methods and techniques) and listed in the schedule to this document.

It also recognises the need to have, and will therefore maintain, a formal counter party policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing or derivative arrangements.

### Monitoring Investment Counterparties

The assessment of credit worthiness or credit rating of investment counterparties will be monitored regularly. The Council obtains credit rating via its treasury advisers who monitors all 3 credit ratings (FITCH, Moody's and Standard and Poor's), and will notify any changes in ratings as they occur. This includes and takes account of changes, ratings watches and rating outlooks as necessary. In accordance with the revised TM Code the Council will need to have regard to the ratings issued by the three main agencies, and base its decisions on the lowest rating. The Council is already mindful of the other possible sources of information available to assess the credit worthiness of investment counterparties. This includes information direct from brokers, the Financial Times, news agencies and its treasury advisers monitoring the Credit Default Swaps (CDS) market. Officers assess trends of interest rates offered by counterparties.

Officers monitor the credit ratings via the information supplied by its treasury advisers, to ensure compliance to the rating criteria, and where necessary taking into account any other information which may influence the decision as to whether to exclude a counter party or not. Monthly counterparty lists matching the Council's criteria are supplied by its treasury advisers.

On occasions ratings may be downgraded after an investment has been made, however, the criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria or due to adverse information in the public domain, will be removed from the approved list immediately by the Section 151 Officer, and if required new counterparties which meet the criteria will be added to the list.

**[2] Liquidity Risk Management**

The Council will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft facilities to enable it at all times to have a level of funds available to it which are necessary for the achievement of its business/service objectives.

The Council will only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme.

To maintain flexibility a minimum of 65% of investments to remain liquid (specified investments) with a maturity of date of 12 months or less.

**[3] Interest rate risk management**

The Council will manage its exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements as amended in accordance with TMP6 (Reporting requirements and managing information arrangements).

The effects of varying levels of inflation, in so far as they can be identified as impacting directly on its Treasury Management activities, will be controlled by the Council as an integral part of its strategy for managing its overall exposure to inflation.

It will achieve this by the prudent use of its approved financing and investment instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates. This should be subject to the consideration and, if required approval of any policy or budgetary implications.

To minimise the financial risk to which the Council is exposed in both cash deposits and borrowing i.e.

(i) to minimise the interest burden to the Council arising from any borrowing:
(ii) to optimise the interest earned. Unless otherwise directed by the Council whilst protecting capital sums deposited.

In order to achieve this objective the following specific policies should be adopted:

(i) to maintain the Council's debt free position and undertake no new borrowing unless the business case is proven for invest to save projects
(ii) to retain an appropriate minimum level of reserves in order to maintain flexibility in the use of interest earned from deposits
(iii) to lend surplus funds only to approved institutions in accordance with DCLG Investment Guidance. A list of Approved Cash Deposit Instruments is attached at TMP 4 [5].
(iv) To minimise short term borrowing by efficient cash flow management.
(v) To ensure that the use of any hedging tools such as derivatives are only used for the management of risk and prudent management of the financial affairs of the council, and that the policy for the use of derivatives is clearly detailed in the annual strategy.

In balancing risk against return, local authorities should be more concerned to avoid risks than to maximise returns.

**[4] Exchange rate Risk Management**

Whilst the Council does not invest in foreign denominations, it does occasionally make payments to suppliers. In so doing it will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income expenditure levels. Any large contracts let by the Council must be denominated in £Sterling and the Section 151 Officer consulted on any proposed departure from this policy.

**[5] Refinancing risk management**

The Council will ensure that its borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised are managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the Council as can reasonably be achieved in the light of market conditions prevailing at the time.

The Council will actively manage its relationship with counter parties in these transactions in such a manner as to secure this objective, and will avoid over reliance on any one source of funding if this might jeopardise achievement of the above.

**[6] Legal and regulatory risk management**

The Council will ensure that all of its treasury management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance if required to do so, to all parties with whom it deals in such activities. In framing its credit and counter party policy the Council will ensure that there is evidence of counter parties' powers, authority and compliance in transactions they may effect with the Council, particularly with regard to duty of care and fees charged.

The Council recognises that future legislative or regulatory changes may impact on its treasury management activities and, in so far as it is reasonable to do so, will seek to minimise the risk of these impacting adversely on the organisation.

**[7] Fraud error and corruption, and contingency management**

The Council will ensure that it has identified the circumstances that may expose it to the loss through fraud, error, corruption or other eventualities in its treasury management dealings. Accordingly it will employ suitable systems and procedures and will maintain effective contingency management arrangements, to these ends.

**[8] Market Risk Management**

The Council will seek to ensure that its stated treasury management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sums it invests and will accordingly seek to protect itself from the effects of such fluctuations.