

## **TREASURY MANAGEMENT PRACTICE NOTES**

### **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 and investment 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 and take into account the risk appetite statement in the Council's Treasury Management Strategy Statement, available via the following link:

<http://www.chichester.gov.uk/article/24169/Treasury-Management-Strategy>

This document is integral to the Council's treasury management practices and all staff involved in treasury management activities should familiarise themselves with its contents.

#### **Overall approach**

The Council has adopted a set of locally tailored risk indicators that it feels provides a balanced picture of the following risk areas

- Security and credit risk
- Liquidity
- Maturity structure of borrowings
- Long term treasury management investments
- Exposure to market and economic risk

Each of these indicators is prescribed in the Council's annual Treasury and Investment Strategy and they will be monitored and reported in line with the procedures described in TMP6

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

This risk is the risk of a third party failing to meet its contractual obligations (for example, to pay any investment money or interest back in full, on time)

Statutory guidance restricts the types of investments that local authorities can use and forms the structure of the Council's policy, which is contained in the Council's treasury management strategy.

The Council's key objective is to invest prudently, giving priority to security, then liquidity before yield.

The Council also has 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 ensures that its counter party lists and limits;

- reflect a prudent attitude towards organisations with whom funds may be deposited, and
- limit its investment activities to the instruments, methods and techniques referred to in [TMP4](#) and in the Council's Treasury Management Strategy, published at the link above.

The Council also maintains 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. This is contained within the Council's Treasury management policy statement and approved each year by the Council.

Once the requirements of security, liquidity and yield are met, as a responsible investor, the Council will prioritise investments with banks or institutions who are able to demonstrate a commitment to sustainability. A comply or explain approach will be used as determined in the annual treasury management strategy.

### **Monitoring Investment Counterparties**

The assessment of credit worthiness or credit rating of investment counterparties will be monitored regularly.

The Council obtains credit rating information from its treasury advisers who monitor leading credit rating agencies and notify the Council of any changes in ratings as they occur. This includes and takes account of changes, ratings watches and rating outlooks as necessary.

The Council has established counterparty limits by sector and credit rating and compliance with these limits is reviewed before any investment decision is made.

In considering credit rating, the lowest rating issued by leading credit rating agencies is used, unless an investment-specific rating is available when this will be used.

The Council considers other possible sources of information available to assess the credit worthiness of counterparties. This includes information direct from brokers, news agencies and its treasury advisers monitoring the Credit Default Swaps (CDS) market.

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**

This risk is the risk that cash will not be available when needed

The Council ensures 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 and statutory authority for doing so and will only do so for the current capital programme.

To maintain flexibility and liquidity the Council determines a maximum amount of principal that can be invested for periods longer than 364 days and closely monitors known future cash demands. To ensure adequate liquidity is maintained, 'worst case' estimates of cash flows are used when considering the Council's medium term investment position.

The Council has also set an operational boundary for external debt that can be used on a short term basis for daily cash management purposes

## **[3] Interest rate risk management**

This risk is the risk of fluctuations in interest rates creating unexpected and unbudgeted burdens on Council finances

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, so far as they can be identified, will be controlled by the Council as an integral part of its strategy for managing its exposure to inflation.

It will achieve this by the prudent use of its approved financing and investment instruments, methods and techniques, to create stability and certainty of costs and revenues, whilst retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates.

To achieve this objective the following specific policies are followed:

- maintaining the Council's debt free position and undertake no new borrowing unless the business case is proven for 'invest to save' projects
- retaining an appropriate minimum level of reserves in order to maintain flexibility in the use of interest earned from deposits
- lending surplus funds only to approved counterparties as specified by the Council's Treasury Management Strategy
- minimising short term borrowing by efficient cash flow management
- ensuring 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, as set out in the Council's Treasury Management Strategy

#### **[4] Exchange rate Risk Management**

The Council does not invest in foreign denominations but does occasionally make payments to foreign suppliers. In so doing we will manage our exposure to fluctuations in exchange rates to minimise any detrimental impact on 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 any borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies are managed, with a view to obtaining offer terms for renewal or refinancing, 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 manages the risk of 'Bail-in' by limiting its exposure to unsecured deposits and also by specifying counterparty investment limits. See TMP4 for further information.

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 ensures 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. It employs suitable systems and procedures and maintains effective contingency management arrangements, to these ends.

The Council's treasury management system is considered sufficiently resilient to contingencies as it is a hosted solution operated by Logotech. Data is backed up to off-site servers operated by the software supplier.

The Council has a business continuity plan and key functions, including cash management and payments are included in that plan

## [8] Fair value risk management

The Council is able to invest in variable Net Asset Value Instruments, or instruments that are revalued to Fair Value each accounting period, subject to the risk management provisions below

For the main classes of such instrument, the risk to security of the principal sum involved are managed as follows

Investment	Risk	Mitigating actions and risk management
Money Market Funds	These funds are likely to be Low Volatility Net Asset value funds	Exposure is limited by restrictions on the total invested in any single Money Market fund
External Pooled funds, including the Local Authority Property Fund	We may incur a loss to the Council's General fund balances if the Fair Value of these investments falls	<p>The Council's investment in external pooled funds (including the Local Authority Property Fund) is limited by the Council's annual Treasury strategy.</p> <p>The Council carefully selects mixed asset and diversified funds to reduce the potential for volatility of capital values.</p> <p>The potential exposure to movements in fair values is considered in determining the adequacy of the Council's revenue reserves and a Treasury indicator has been prepared to monitor this.</p>