

Report of:	Director of Finance (S151 Officer)
Relevant Executive Member:	Executive Member for Finance and Governance
Submitted to:	Executive
Date:	28 February 2024
Title:	Prudential Indicators and Treasury Management Strategy 2024/25
Report for:	Decision
Status:	Public
Strategic priority:	All
Key decision:	Yes
Why:	Decision(s) will incur expenditure or savings above £250,000
Subject to call in?	No
Why:	Part of the statutory budget setting process

Proposed decision(s)

For Executive to review and endorse the following and refer for consideration and approval by Council at the budget meeting on 8 March 2024:

- The Prudential Indicators (PI) and limits for 2024/25 to 2026/27 relating to capital expenditure and treasury management activity.
- The Treasury Management Strategy (TMS) for 2024/25, which includes the Annual Investment Strategy for 2024/25.
- The Minimum Revenue Provision (MRP) Policy 2024/25.
- An Authorised Limit for External Debt of £372m for the financial year.

Executive summary

The Council is required to approve annually a Treasury Management Strategy and a set of Prudential Indicators, which self-regulate the level of capital financing activities of the Council and the affordability of the capital programme. These need to be set on an annual basis to comply with the Local Government Act 2003 and the Chartered Institute of Public Finance and Accountancy (CIPFA) Codes of Practice on Capital Finance and Treasury Management.

The Treasury Management Strategy is important from both a financial and governance perspective as it sets the framework within which the Council manages its borrowing and investments, how it delivers these services, and how it controls the risks attached to financial decisions made. It also sets out the parameters and criteria that govern the day-to-day cashflow management activity and how these impact on medium to long term financial planning. These include achieving value for money from any borrowing undertaken, managing risk, and protecting any resources that have been invested.

The Prudential Indicators are an integral part of the CIPFA Capital Finance Code and demonstrate whether the capital programme is affordable, sustainable, and prudent. They include the level of capital expenditure over the next three years, how this has been financed, the maximum level of external debt and the cost to the revenue budget.

The MRP policy governs how the Council plans to account for the repayment of loan principal in relation to its borrowing activities and has a fundamental impact upon the annual revenue cost of borrowing and over the long term. The Council adopted its current MRP policy in 2021/22 which is based on a 2% annuity model in line Government permitted prudent methodologies available to and used by all local authorities. The effect of this methodology compared to others available, is to improve annual affordability over the medium term which are offset by higher revenue charges in 25 – 50 years' time.

The Council's underlying need to borrow is measured by the Capital Financing Requirement (CFR) which is forecast to be £331.863m at the end of 2024/25 rising to £352.332m by 2026/27. This results in the annual cost of revenue cost of borrowing of £11.154m (7.8% of Net Revenue Budget) in 2024/25 rising to £14.496m (9.8% of Net Revenue Budget) as shown below. This level of borrowing is provided to include the contingency sums repayable if the Council is required to utilise the full amount of Exceptional Financial Support (EFS) of £13.4m as explained further below. The actual level of borrowing will be less provided that revenue savings are delivered to plan and capital receipts from planned asset sales realised to fund transformation as set out in the 2024/25 Budget and MTFP report.

	2022/23 actual	2023/24 forecast	2024/25 forecast	2025/26 forecast	2026/27 forecast
Financing costs (£m)	8.058	9.376	11.154	12.814	14.496
Net Revenue Budget (£m)	118.329	126.354	143.190	148.601	148.127
Proportion of net revenue budget (%)	6.8%	7.4%	7.8%	8.6%	9.8%

Whilst the Council is not an outlier compared to other authorities in terms of its level of total debt (see the graph below), it is approaching the CIPFA advisory limit of 10% for revenue affordability on borrowing to fund its future capital investment. The Council will therefore need to strictly prioritise its capital investment decisions over the medium and longer term and secure its financing through third party funds such as contributions and grants or further capital receipts from the sale of assets in order to maintain borrowing at affordable levels over the longer term.

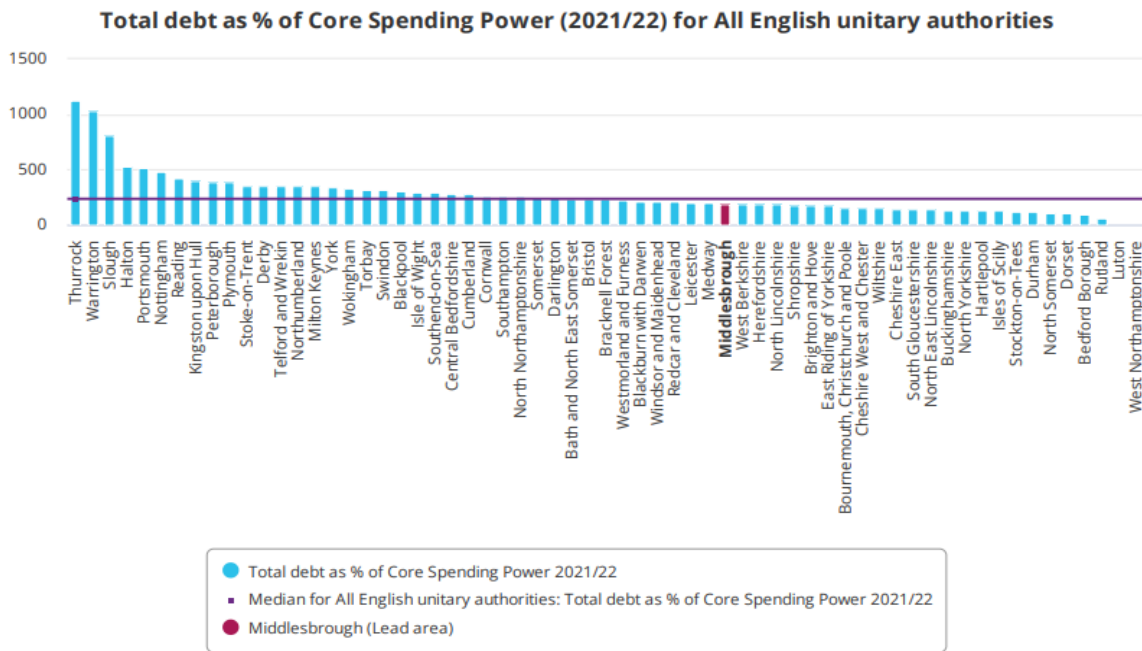
Total debt as percentage of core spending power

'Total debt' is Capital Financing Requirement, a measure of capital indebtedness that the council has built up over many years of capital financing decisions, but based on a methodology. (It is perhaps more accurate to describe this as the amount of capital expenditure that has not yet been funded by capital receipts, capital grants or revenue contributions and which therefore will need to be funded in future years. As such is some kind of measure of capital indebtedness, but arguably not a perfect one.

Core Spending Power is a measure of the funding the government makes available to councils for service delivery but it excludes several important elements that may be contributing to the servicing of debt including schools grants, investment income, service income and housing rents.

In 2021/22, the total debt as a percentage of Core Spending Power for Middlesbrough was 190.1%, which was below the All English unitary authorities median percentage of 229.4%.

Note the metric on total debt as a percentage of core spending power used by Oflog uses different financial years for the denominator and numerator, whereas LG Inform uses the same financial year so the numbers will differ slightly.



Source:

Calculated by LG Inform, N/A, [Total debt as % of Core Spending Power](#), Data updated: 22 Nov 2023

The Council is reliant upon the capitalisation of £4.7m of revenue expenditure to balance its 2024/25 revenue budget. In the absence of available capital receipts this will be funded by borrowing via Exceptional Financial Support (EFS) over a period of up to 20 years. The period and rate of borrowing will be determined at an appropriate point during 2024/25, taking account the Council's financial performance, prevailing interest rates and the impact and affordability of revenue repayments over the period. This will be a professional judgement of the s151 Officer, based upon the expert advice of the Head of Finance and Investments and the Council's external Treasury Management advisers. A contingency amount of £0.6m is provided in relation to setting the revenue budget.

EFS of up to a further £3.5m is required to provide capital financing to cover the risk of any shortfall in the delivery of savings and up to £4.6m for any shortfall on the timing of realising planned capital receipts required to fund transformation expenditure under Flexible Capital Receipts regulations. Provided that savings are delivered to plan, and

flexible receipts are realised in accordance with expected profiles, it will not be necessary to draw down this borrowing.

However, this does emphasise that the successful delivery of all savings to plan during 2024/25 is critical to the Council's financial recovery and its medium term financial sustainability. Further, that investment in transformation must deliver substantial revenue savings in excess of the projected budget gap of £7.965m in the 2024/25 Budget and MTFP report presented elsewhere on this agenda, given that further financial challenges are likely to occur within the financial planning period that are not yet known.

The revenue costs of borrowing under EFS of up to £13.4m for a period of up to 20 years (£1.150m maximum per annum) is factored into the TM Strategy and is within the Prudential Indicators and authorised limits. This reflects the borrowing required to support the proposed budget and MTFP as set out elsewhere in this agenda.

1. Purpose

This report outlines the Council's prudential indicators for the financial years 2024/25 – 2026/27 and sets the framework and approves the limits within which the treasury management operations for this period. It fulfils key legislative and guidance requirements:

- (a) The setting of the prudential indicators in relation to the expected capital activities and treasury management prudential indicators (included as treasury indicators) in line with the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management Code of Practice.
- (b) The treasury management strategy statement which sets out how the Council's treasury function will support capital decisions taken above, day to day treasury management activities on service delivery and any limitations on these, via the treasury prudential indicators.
- (c) The approval of the Council's Minimum Revenue Provision (MRP) Policy, which sets out how the Council will pay for borrowing to fund capital investment through the revenue budget each year.
- (d) The key indicator is the Authorised Limit, the maximum amount of debt the Council could enter into during the financial year. This amount acts as the legal limit for debt activity.
- (e) The investment strategy which sets out the Council's criteria for choosing the investment counterparties and limiting exposures to the risk of loss.

The information contained in the report regarding the Council's capital expenditure plans, Treasury Management and Prudential Borrowing activities indicate that they are:

- Within the statutory framework and consistent with the relevant codes of practice.
- Prudent, affordable, and sustainable.
- An integral part of the Council's Revenue and Capital Medium Term Financial Plans.

2. **Recommendations**

That the Executive review and endorse and recommend for approval and adoption at the Council meeting on the budget on 8 March 2024:

- To approve the Prudential Indicators and limits for 2024/25 to 2026/27 relating to capital expenditure and treasury management activity set out in tables 1 to 10 of Appendix 1.
- To approve the Treasury Management Strategy for 2024/25, which includes the Annual Investment Strategy for 2024/25 at Appendix 1
- To approve the Minimum Revenue Provision (MRP) Policy for 2024/25 at Appendix 1.
- To approve an Authorised Limit for External Debt of £372m for the 2024/25 financial year.

3. **Rationale for the recommended decision(s)**

The recommendations above will fulfil the following for the local authority:

- a) To comply with the Prudential Code for Capital Finance in Local Authorities and the Department for Levelling Up, Housing & Communities (DLUHC) guidance on investments.
- b) To comply with the Treasury Management Code of Practice for Local Authorities.
- c) To comply with the requirements of the Local Government Act 2003 Part 1.
- d) To approve a financial governance framework within which officers will operate when making both borrowing and investment decisions and entering financial transactions.

4. Background and relevant information

4.1. The PI & TMS for 2024/25 covers the following areas:

- How the capital programme is financed including the impact of Exceptional Financial Support required to set a lawfully balanced revenue budget.
- The relevant prudential Indicators to monitor the performance, revenue budget affordability and sustainability of the capital expenditure being proposed in line with the requirements of the prudential code.
- Treasury Management arrangements in place for investing surplus funds and borrowing to fund capital expenditure.
- The types of investments the Council makes as part of managing its cash balances – the Annual Investment Strategy.
- Knowledge and skills of staff involved in the Treasury Management process.
- Minimum Revenue Provision policy – including outlining how much the Council accounts for the revenue costs of re-paying borrowing incurred in relation to historical and future capital investment to support the operational delivery of services.

4.2 Capital Expenditure relates to how the Council plans to invest in long-term assets and infrastructure (such as property, equipment, vehicles, roads etc.). The Council must consider how this expenditure is paid for and what the long-term financial implications are of undertaking this investment. The Council is also permitted to borrow funds to finance the capital programme under the Local Government Act 2003. It needs to consider the impact on the revenue budget of the level of borrowing being proposed, how it funds the repayment of this debt and the period over which this debt is repaid.

4.3 The Council must ensure the capital programme and its plans to borrow to finance it are prudent and affordable. Where elements of this are funded by borrowing (either externally or internally), the Council must set aside budgetary allocations in the general fund revenue budget to meet the cost of this debt. These budgets include the interest payable to lenders on external borrowing and the setting aside of funds to re-pay the principal element of debt (known as the Minimum Revenue Provision).

Prudential Indicators and Capital Investment Plans

4.4 The Council demonstrates the concepts of affordability, sustainability, and prudence on its investment plans by setting a range of Prudential and Treasury Management indicators. These are set out in **Appendix 1** and are key metrics to the Director of Finance and Council when setting the budget plans each year.

4.5 Any variance from these indicators during a year indicates either a higher level of indebtedness or a lower level of prudence on the capital activities of the Council than when the budget was set. The following paragraphs give a brief commentary on these key indicators as we approach the start of the 2024/25 financial year.

4.6 There is total outstanding debt of **£233.491m** on 31 December 2023, with a further **c£25m** of borrowing expected to be required before 31 March 2024.

- 4.7 The forecast overall total long term external debt at the end of 2023/24 of **£259.498m** should be compared with the estimated *Capital Financing Requirement* (the underlying value which the Council needs to borrow to fund capital activities) of **£299.928m**. The Council therefore has an expected under-borrowed position of **£40.430m**, which provides some savings in interest payments as other revenue and capital cash has been used in lieu of external borrowing. This is a key strategic decision each year as to whether the under-borrowing position is increased or reduced and is influenced by the expectation of interest rates available to generate income on investments vs interest rates incurred on borrowing.
- 4.8 **Table 6 in Appendix 1** shows the profile of outstanding external debt over the whole of the medium-term financial planning period, and this will rise to a maximum of **£333.294m** by 31st March 2026 before starting to reduce in the following financial year. This increase in debt is a direct result of the amount required to fund the capital programme in each year, the EFS borrowing required, and any additional cash flow demands in each financial year.
- 4.9 The Council holds revenue budgets for repaying debt and interest (known as Capital Financing Costs). The repayment of debt costs for 2024/25 are **£11.154m** (7.8% of the net revenue budget for 2024/25). For comparison purposes the forecast capital financing costs in 2023/24 are expected to be £9.376m (which represented 7.4% of the planned net revenue budget for 2023/24).

Table 1: Prudential Indicators

<u>Prudential Indicator</u>	2023/24 (£m)	2024/25 (£m)	2025/26 (£m)	2026/27 (£m)
Capital Financing Requirement (underlying need to borrow)	299.928	331.863	355.426	352.332
External Borrowing	259.498	310.535	333.294	329.910
Internal Borrowing	40.430	21.328	22.132	22.422
Authorised limit for External Debt	328.000	372.000	396.000	393.000
Annual Capital Financing Cost	9.376	11.154	12.814	14.496
% of Net Revenue Budget on debt costs	7.4%	7.8%	8.6%	9.8%

- 4.10 The table above illustrates the key figures from paragraphs 4.6 to 4.9 and how these change over the period to 2026/27. It also shows that the proportion of capital financing costs is increasing over the period due to the level of external debt required to fund the capital programme and to provide for EFS of up to £13.4m in order to set a balanced and robust revenue budget.
- 4.11 Although the Council does not have relatively high debt levels than its comparator authorities, the strain on the revenue budget is increasing. When CIPFA introduced the Capital Finance Code of Practice in 2007, an amount of 10% of the net revenue

budget was advised as being a threshold for sustainability and financial prudence. Whilst some councils have exceeded this limit, the S151 Officer advises Members to constrain capital investment funded by borrowing going forward as a key criteria for achieving its financial sustainability plans.

- 4.12 It is a statutory requirement for the Council to set an authorised limit for external debt at the start of each financial year. This is an amount beyond which it would be ultra-vires (or outside of its powers) to exceed in a particular financial year. The authorised limit for 2023/24 is £328m, with this increasing to **£372m** for 2024/25 due to an increase in the level of borrowing required.
- 4.13 It should be noted that the authorised limit for the Council is currently higher than either the expected level of external debt or the capital financing requirement. This is common practice to enable local authorities to build in contingency for unexpected urgent capital expenditure, potential unexpected debt re-financing opportunities and the remote possibility of needing to borrow for any further exceptional revenue purposes. The Council's authorised legal limit is recommended to be set at £40m above its capital financing requirement. It is not recommended to go beyond the specified capital financing requirement other than for temporary and specifically defined borrowing purposes.

Treasury Management

- 4.14 Treasury Management is defined as *'the management of the Council's cash flows, borrowing and investments, and the associated risk'*. The main risks that affect a local authority include credit risk, interest rate risk, liquidity risk and refinancing risk.
- 4.15 The Council is generally cash rich in the short term as many grants and contributions are paid in advance of need. Because of this, any excess cash is invested with an appropriate counterparty until the funds are required. When making an investment, the Council follows the advice set out in the Local Government Act 2003 and within the Treasury Management Code with paramount consideration given to the security of the sum invested, followed by the liquidity position of the Council and finally the interest rate achievable on the investment.
- 4.16 Given that credit criteria are the most important factor when making an investment decision, the Council receives regular updates from its professional expert external treasury management adviser, Arlingclose, on changes in credit ratings for individual financial institutions. They also advise on maximum amounts to be invested with each counterparty and maximum durations for any fixed term deposits made. This framework helps to protect against the loss of any sums invested (credit risk), ensures liquidity is not compromised and earns interest to support the revenue budget (not a major factor at present).
- 4.17 On 31 December 2023, the Council had cash balances of **£21.847m** invested either on fixed term deposit with central government or in liquidity accounts with appropriate banks. The strategic level of cash holdings is a minimum of £15m, below which the Council will look to borrow to maintain liquidity.

- 4.18 In relation to external borrowing, the Council seeks to achieve a low but certain cost of finance, whilst retaining the flexibility to borrow for short-term periods and to respond to demands of the Investment Strategy as needed. The Council therefore looks to create a balance between taking advantage of generally lower rates of interest for short term borrowing (predominantly from other local authorities) versus the need to achieve certainty over rates of borrowing in the longer term from either government or financial institutions (mainly from the PWLB or other banks).
- 4.19 Of the **£233.491m** of external debt on 31 December 2023, 80% is long term from the Public Works Loan Board – the government agency for local authority borrowing and 20% is long term with financial institutions (generally banks). There is £18.3m short-term borrowing in place at present.
- 4.20 Current long term interest rates for borrowing from the PWLB are between 4.5% and 5.25% depending on the length of the loan (local authorities can borrow up to 50 years from central government) with short term rates being between 5.5% and 6.0% for up to one year in duration.
- 4.21 On local authority borrowing, there has been much interest from both regulators and the media in recent years around individual councils taking significant amounts of long-term debt from the PWLB for the sole purposes of commercial activity – generally property investment. Under the Prudential Code, local authorities have lots of freedom to conduct and self-regulate their own borrowing and investment activities.
- 4.22 Both the Government and the Chartered Institute of Public Finance & Accountancy have said that borrowing for the sole purposes of commercial investment is against the spirit of the Code. The PWLB has prevented any local authority applications for this type of activity from 1 April 2021 with Section 151 Officers having to confirm each year that their investment plans do not contain any of these types of activity.
- 4.23 Although the Council has undertaken some capital projects in recent years that have generated a revenue income stream, the primary aim has always been to regenerate the areas involved and to grow the wider economy within the Town. As a result, these activities can continue under the Code and with funding from the PWLB.

Knowledge & Skills

- 4.24 This Strategy provide details of the knowledge and experience in place by Officers and the access to external advice and guidance made available to enhance this. Council officers have a broad range of skills to ensure treasury management decisions are informed and risk-assessed on a consistent basis. The Council uses external consultants (Arlingclose) to provide up to date and specialist advice which is bespoke for local government sector regulations, particularly focusing on risks and opportunities.
- 4.25 The Council also participates in a treasury management benchmarking club run by Arlingclose. This club provides access to data on other local authorities' approaches

to Treasury Management, including strategic information, and the wider performance outputs of the Treasury Management activities.

- 4.26 As part of the Treasury Management Code, it is also a best practice requirement that elected members have the necessary skills & knowledge to scrutinise the Council's plans and processes in this area. This has been achieved in the past by providing training for Members but this training is planned to be delivered during 2024.

Minimum Revenue Provision

- 4.27 The Council is required under the Local Government Act 2003 Part 1 to maintain a policy for the repayment of historic external debt incurred from the annual revenue budget. The policy is split into different elements which are influenced by when the borrowing was originally incurred, the type of assets and the useful economic life of the assets the borrowing is funding. The Council has in previous years amended this policy to reflect the useful economic life of the funded assets more accurately and then in 2021/22 moved to an annuity basis of calculating these revenue costs. **No changes are being proposed to the MRP policy for 2024/25 financial year** and there is no further scope to make annual savings beyond those currently achieved through the current policy on a prudent basis. This policy is set out at the end of **Appendix 1** for information.

5. Other potential alternative(s) and why these have not been recommended

- 5.1 It is a statutory requirement to approve the annual treasury management strategy and set of prudential indicators by the Council. As a result, there are no alternatives available.

6. Impact(s) of the recommended decision(s)

The adoption of this report is an integral part of the annual process for the Council. Ensuring that the capital programme and its financing is within available and affordable revenue resources is a key judgement for the S151 Officer and will inform the Council's view of whether to approve the medium-term financial plans.

6.1 Financial (including procurement and Social Value)

- 6.1.1 All relevant financial implications are outlined within the body of this report and the supporting **Appendix 1**. The capital programme and financing being recommended in the budget report remains affordable within the revenue budget parameters but needs to be strictly managed and prioritised going forward. The treasury indicators and processes remain robust and within prudent limits. The policy on minimum revenue provision also remains in line with the appropriate regulations and government guidance.
- 6.1.2 **Table 1 in Paragraph 4.9** outlines the key debt metrics and the capital financing costs as a % of the net revenue budget over the medium-term financial planning period.

6.2 Legal

- 6.2.1 There are no direct legal implications of this report. All activity on capital financing, investments and borrowing is under current local authority powers under either the local government act or the capital finance and accounting regulations.
- 6.2.2 If for any reason the Council exceeded its authorised limit for external debt in a financial year, the S151 Officer would be required to report this to Council at the earliest opportunity. This would need to set out any implications of this action and would recommend a new authorised limit for the financial year for approval.

6.3 Risk

- 6.3.1 Any risk related issues are set out within the report. Risk management is an integral part of the Council's treasury management strategy, and these are considered as part of business-as-usual activities and are set out in more detail within the Treasury Management Practices document.

6.4 Human Rights, Public Sector Equality Duty and Community Cohesion

- 6.4.1 There are no applicable issues to consider within this report.

6.5 Climate Change / Environmental

- 6.5.1 There are no applicable issues to consider within this report.

6.6 Children and Young People Cared for by the Authority and Care Leavers

- 6.6.1 There are no applicable issues to consider within this report.

6.7 Data Protection / GDPR

- 6.7.1 There are no applicable issues to consider within this report.

Actions to be taken to implement the recommended decision(s)

Action	Responsible Officer	Deadline
To implement and monitor the 2024/25 prudential indicators and treasury management strategy	Head of Finance & Investments	1 April 2024 (and during the 2024/25 financial year)

Appendices

1	Prudential Indicators & Treasury Management Strategy for 2024/25
---	--

Background papers

There are no background papers to this report.

Contact: Justin Weston, Head of Finance & Investments
Email: justin_weston@middlesbrough.gov.uk

PRUDENTIAL INDICATORS &
TREASURY MANAGEMENT STRATEGY - 2024/25

Introduction

The Treasury Management Strategy (TMS) report gives a high-level overview of how capital expenditure, capital financing and treasury management activities contribute to the provision of local public services at the Council. In addition, it also gives an overview of how the associated risks are managed and the implications for future financial sustainability.

The following information is a requirement of the 2021 Code of Practice on Treasury Management, issued by the Chartered Institute of Public Finance & Accountancy, and has been produced in an accessible way to enhance members' understanding of these often-technical areas

Capital Expenditure and Financing

Capital Expenditure is where the Council spends money on assets, such as property, IT and vehicles that will be used for more than one financial year. In local government, this also includes spending on assets owned by other bodies, finance leases and loans & grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are generally not capitalised.

In the 2024/25 financial year, the Council is planning a total capital expenditure of £88.549m as summarised below.

Table 1: Prudential Indicator: Estimates of Capital Expenditure

	2023/24	2024/25	2025/26	2026/27
	Estimate £m	Estimate £m	Estimate £m	Estimate £m
Total Capital Expenditure	47.129	88.549	73.218	13.213

All capital expenditure has to be financed, from either external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital

receipts) or debt (borrowing, leasing and private finance initiative). The planned financing of the above expenditure is as follows:

Table 2: Capital financing

	2023/24	2024/25	2025/26	2026/27
FUNDED BY:	£m	£m	£m	£m
Prudential Borrowing	19.300	23.037	28.009	1.913
EFS Borrowing	-	13.400	0.000	-
Capital Receipts	-	6.000	6.000	6.000
Flexible Receipts	3.000	13.700	7.700	5.300
Grants	23.644	29.897	27.931	-
Contributions	1.185	2.515	3.578	-
Total FUNDING	47.129	88.549	73.218	13.213

Any external debt (prudential or EFS) must be repaid over time by other sources of finance. This comes from the revenue budget in the form of Minimum Revenue Provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace/repay debt finance. The Council generally uses capital receipts to finance new capital expenditure rather than to redeem debt. The total cost of MRP included in the Council's revenue budget is as follows:

Table 3: Minimum Revenue Provision

	2022/23 actual £m	2023/24 forecast £m	2024/25 budget £m	2025/26 budget £m	2026/27 budget £
Cost to Revenue Budget	3.383	3.888	4.503	4.946	5.507

- The Council's minimum revenue provision statement for 2024/25 is available towards the end of this report.

The Council's cumulative amount of debt finance still outstanding is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure each year and then reduces with minimum revenue provision and capital receipts used to redeem debt.

The CFR is expected to increase by £31.935m or 10.6% during the 2024/25 financial year. This increase is due to the new capital expenditure funded by external debt of £36.437m less the MRP set aside of £4.503m.

Based on the above plans for expenditure and financing, the Council's estimated CFR for the period of the Medium-Term Financial Plan is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement

	31/3/2023 actual £m	31/3/2024 forecast £m	31/3/2025 budget £m	31/3/2026 budget £m	31/3/2027 budget £m
TOTAL CFR	284.748	299.928	331.863	355.426	352.332

Asset disposals: When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets, or be used to repay debt. Repayments of capital grants, loans and investments also generate capital receipts.

The Council plans to receive c£25m of capital receipts in the coming financial year as follows. These amounts have increased significantly for the next few years due to the asset review being undertaken by the Council.

Table 5: Capital receipts

	2022/23 actual £m	2023/24 forecast £m	2024/25 budget £m	2025/26 budget £m	2026/27 budget £m
TOTAL	0.755	3.037	24.475	13.240	9.709

- The level of capital receipts for each financial year is monitored between Regeneration, Finance and Valuation & Estates teams, and any significant changes are reported to Executive as part of the Quarterly budget updates.
- The Council has adopted and used in the past two financial years, the Flexible Use of Capital Receipts Policy where these proceeds may be used for funding service transformation costs that would otherwise be classed as revenue expenditure. This is mainly to fund the current year’s revenue budget overspend and would be a device to protect reserves.

Treasury Management

Treasury Management is concerned with keeping sufficient but not excessive cash resources, available to meet the Council’s spending needs, while managing the risks involved in these investments. Surplus cash is invested until required, whilst a shortage of cash will be financed by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. Cash balances can be a combination of both revenue and capital cash given that there are timing differences between funds being received from various sources and those being spent on the operational plans of the Council.

The Council is typically cash rich in the short-term as revenue income is received and before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. Revenue cash surpluses are therefore offset against capital cash shortfalls to reduce the overall borrowing amount required, as part of an integrated strategy on Treasury Management. This is in line with best practice.

The Council on 31 December 2023 had £233.5m of borrowing at an average interest rate of 3.3% and £21.8m of treasury investments at an average rate of around 4%.

Both investment and borrowing rates available to the Council are at high levels currently due to the dramatic increase in the level of bank rate over the last 12 months and to curb the high levels of inflation that have been prevalent in the economy in recent months.

Borrowing strategy: The Council's main objectives when borrowing is to achieve a low but certain cost of finance for long-term capital projects whilst retaining flexibility should plans change in future. This is a little easier than in previous years due to long-term borrowing rates being lower than the cost of short-term loans for the first time in a decade. It is anticipated that all borrowing in the 2024/25 financial year will be from the PWLB, unless bank rate reduces rapidly during the financial year.

Projected levels of the Council's total outstanding debt (which comprises borrowing and relevant finance leases) are shown below, compared with its capital financing requirement (need to borrow).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement

	31.3.2023 actual £m	31.3.2024 forecast £m	31.3.2025 budget £m	31.3.2026 Budget £m	31.3.2027 budget £m
External Debt	245.889	259.498	310.535	333.294	329.910
Capital Financing	284.748	299.928	331.863	355.426	352.332

Statutory guidance is that debt should remain below the capital-financing requirement, except in the short-term where the benefits of short-term borrowing may be taken. As can be seen from Table 6, the Council expects to comply with this in the medium term with debt being lower than the capital-financing requirement in all relevant financial years. There may be some opportunity to take more capital funding than is needed whilst interest rates are at low levels. Discussions are ongoing with our treasury advisers on this position and what approach the Council should take.

Affordable borrowing limit: The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt levels start to approach the legal limit and is a more realistic rather than worst-case view of what will happen during the financial year. Any need to change these during the 2024/25

financial year from the original budget assumptions will be reported by the Director of Finance to the Executive at the earliest opportunity.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt

	2023/24 limit £m	2024/25 limit £m	2025/26 limit £m	2026/27 limit £m
Authorised Limit (OB + £20m)	328.000	372.000	396.000	393.000
Operational Boundary (CFR + £20m)	308.000	352.000	376.000	373.000

Investment strategy: Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

The Council’s policy on treasury investments is to prioritise security and liquidity over yield, which focuses on minimising risk rather than maximising returns. Cash that is likely to be spent in the short term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss.

Table 8: Treasury management investments in £millions

	31/3/2023 actual £m	31/3/2024 forecast £m	31/3/2025 budget £m	31/3/2026 budget £m	31/3/2027 budget £m
Short-term investments	29.107	15.000	15.000	15.000	15.000
Longer-term investments	0.000	0.000	0.000	0.000	0.000
TOTAL	29.107	15.000	15.000	15.000	15.000

Governance: Decisions on treasury management in relation to investment and borrowing are made daily and are therefore delegated by the Director of Finance to the Head of Finance & Investments and staff within the central finance team, who act in line with the treasury management strategy approved by Council. Quarterly updates on treasury management activity are reported to Executive as part of the regular budget monitoring process.

Revenue Budget Implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to the revenue budget, offset by any investment income received. The net annual charge is reported as capital financing costs; this is compared to the net revenue stream i.e., the amount funded from council tax, business

rates and general government grants. This is an important indicator around the affordability of the Council's capital plans going forwards.

Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream

	2022/23 actual £m	2023/24 forecast £m	2024/25 forecast £m	2025/26 forecast £m	2026/27 forecast £m
Financing costs (£m)	8.058	9.376	11.154	12.814	14.496
Net Revenue Budget (£m)	118.329	126.354	143.190	148.601	148.127
Proportion of net revenue stream	6.8%	7.4%	7.8%	8.6%	9.8%

Sustainability: Due to the very long-term nature of capital expenditure and its financing, the revenue budget implications of this expenditure incurred in the next few years could extend for up to some 50 years into the future.

The figures in table have remained relatively stable at a time when debt levels for the Council are still increasing. Members should be aware that this is because of various capital investments in commercial property made by the Council over the last few years for regeneration purposes. This results in around £3.1m of income per year being credited to the capital financing budget by the end of the 2023/24 financial year. It is imperative and a key budget risk that these rental levels are maintained, and the income assumed in the estimates above are generated.

However, the level of revenue budget strain is increasing over the capital programme being proposed as part of the 2024/25 budget process and this may not be sustainable given the revenue budget position and low level of reserves. The Council will need to reduce its reliance on external borrowing to fund the capital programme going forwards and target capital grants and contributions or capital receipts from the asset review.

Taking the figures above in Tables 1 to 9 and the key message of caution to be exercised in the future on capital financing decisions. The Director of Finance is satisfied that the proposed capital programme is prudent, affordable and sustainable because appropriate resources have been allocated from the Council's medium term financial plan, and any borrowing plans have been fully costed and reviewed.

Table 10 – Total Borrowing required for each year of the MTFP

	2023/24	2024/25	2025/26	2026/27
	£m	£m	£m	£m
	Estimate	Estimate	Estimate	Estimate
Capital Programme	19.300	23.037	31.500	1.913
EFS	-	13.400	-	-
Debt Restructuring	10.000	-	-	-
Revenue purposes	10.000	10.000	5.000	-
Total	39.300	46.437	37.000	1.913

This considers any debt needed by the Council to either finance the capital programme, in respect of leasing arrangements, or to finance any debt restructuring required.

The prudential indicators & limits set out in this report are consistent with the Council's current commitments, existing plans, and the proposals in the budget report for capital expenditure and financing, and with its approved treasury management policy statement and practices.

The Director of Finance confirms that these are based on estimates of the most likely and prudent scenarios, with in addition sufficient headroom over and above this to allow for operational management and some scope for flexibility. For example, unusual cash movements or any unbudgeted capital expenditure required. Risk analysis and management strategies have been considered; as have plans for capital expenditure, estimates of the capital financing requirement, and estimates of cash flow requirements for all purposes.

Prudence – Treasury Management Indicators

It is recommended that the Council sets an upper limit on its fixed interest rate exposures for 2024/25, 2025/26 and 2026/27 of 100% of its estimated total borrowing undertaken.

It is further recommended that the Council sets an upper limit on its variable interest rate exposures for 2024/25, 2025/26 and 2026/27 of 25% of its estimated total borrowing undertaken.

This means that the Director of Finance will manage fixed interest rate exposures on total debt within the range 75% to 100% and variable interest rate exposures on total debt within the range 0% to 25%.

It is also recommended that the Council sets upper and lower limits for the maturity structure (when the debt needs to be repaid) of its total borrowing as follows.

Amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate at the start of the period:

	<u>Upper limit</u>	<u>Lower limit</u>
under 12 months	50%	0%
12 months and within 24 months	30%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and above	90%	20%

Currently investments are limited to a maximum of 3 years, with any deals being arranged so that the maturity will be no more than 3 years after the date the deal is arranged.

The maximum % of the total of all investments that have an outstanding period of one year or longer, at the time the investment is made, is 10%.

Knowledge and Skills

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Head of Finance and Investments has more than 25 years' experience in local government treasury management. There is similar experience within the finance teams in relation to budgeting & accounting for capital expenditure and financing. The Council also pays junior staff to study towards relevant professional qualifications including CIPFA, CIMA, ACCA, AAT and other relevant vocational studies.

Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

Treasury Management Practices

Further details of how the treasury management function operates, the procedures used to manage banking, treasury and capital market transactions, how risk is managed by the in-house team and how these fit with the CIPFA Code of Practice is included in the Council's set of Treasury Management Practices.

Minor operational and terminology changes to this are made by the Director of Finance on an ongoing basis to keep the TMP's updated. If any significant changes are required to the document, either because of organisational or regulatory changes, this will be brought to full Council for approval.

ANNUAL INVESTMENT STRATEGY & TREASURY

MANAGEMENT POLICY STATEMENT 2024/25

1. In accordance with revised guidance from the Department for Levelling Up Housing and Communities (DLUHC) {formerly the Ministry of Housing, Communities and Local Government (MHCLG)} a local authority must prepare and publish an Annual Investment Strategy which must be approved by full Council before the start of the financial year to which it relates.
2. The DLUHC guidance offers councils greater freedom in the way in which they invest monies, providing that prior approval is received from Members by approving the Annual Investment Strategy. The guidance also considers the wider implications of investments made for non-financial returns and how these can be evaluated.
3. The Local Government Act 2003, which also introduced the Prudential Code for Capital Finance, requires that a local authority must have regard to such guidance as the Secretary of State issues relating to prudent investment practice.
4. In addition, the Chartered Institute of Public Finance & Accountancy (CIPFA) has published a revised Code of Practice for Treasury Management in the Public Services in December 2021. This replaces the 2017 Code which had been adopted in full by Middlesbrough Council. The revised Code requires the Council to clearly state, in the Annual Investment Strategy document, its policy on effective control, and monitoring of its treasury management function. These controls are set out in Treasury Management Practices (TMP's) which have been approved as part of acceptance of the previous Code.
5. The revised Strategy, showing where the Guidance has determined Council policy, can be set out as:

ANNUAL INVESTMENT STRATEGY 2024/25

6. Middlesbrough Council will create and maintain as the cornerstones for effective treasury management:
 - a treasury management policy statement, stating the policies, objectives, and approach to risk management of its treasury management activities.
 - suitable treasury management practices (TMPs), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.
7. The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the circumstances of this organisation. Such amendments will not result in the organisation materially deviating from the Code's key principles.

8. Middlesbrough Council will receive reports on its treasury management policies, practices, and activities, including, as a minimum, an annual strategy in advance of the year, a mid-year review which will include an annual report on the previous year, in the form prescribed in its TMP's. Revised Strategies can be presented to the Council for approval at any other time during the year if the Director of Finance considers that significant changes to the risk assessment of significant parts of the authority's investments has occurred.
9. Middlesbrough Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Director of Finance. The execution and administration of treasury management decisions is further delegated to *the Head of Finance & Investments*, who will act in accordance with the organisation's policy statement, TMPs and CIPFA's *Standard of Professional Practice on Treasury Management*.
10. Middlesbrough Council nominates the Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.
11. The Council is very circumspect in its use of credit rating agencies with the section on Specified Investments setting out the current policy. Ratings are monitored on a real time basis as and when information is received from either our treasury management consultants or any other recognised source. Decisions regarding inclusion on the Approved List are made based on market intelligence drawn from a number of sources.
12. All staff involved in treasury management will, under the supervision of *the Head of Finance & Investments*, act in accordance with the treasury management practices and procedures, as defined by the Council. Such staff will undertake relevant training, identified during the Council's induction process and, on an on-going basis, the Council's appraisal policy.
13. The general policy objective contained in the guidance is that local authorities should invest prudently the short-term cash surpluses held on behalf of their communities. The guidance emphasises that priority should be given to security and liquidity rather than yield. Within that framework the Council must determine a category of borrowers, who must be of "high credit quality" classified as **Specified Investments**, with whom it can invest surplus cash with minimal procedural formalities and further identify a category of borrowers classified as **Non-Specified Investments**, with whom it can also invest but subject to prescribed limits.
14. Although the guidance definition of Non-Specified Investments is "one not meeting the definition of a Specified Investment", the authority is required to identify which categories of investments are identified as prudent to use and the limits on any such investment either individually or in total. It is because some organisations do not subscribe to credit rating agencies that they have to be included as Non-Specified Investments, rather than any concern over their creditworthiness.

15. The guidance defines investment in such a way as to exclude pension fund and trust fund investments. In practice, Middlesbrough Council, in its role as Administering Authority for the Teesside Pension Fund, follows similar procedures as approved by Members as part of compliance with the CIPFA Code of Practice, albeit with different limits.

LIMITS & DEFINITION OF SPECIFIED INVESTMENTS

16. The following are currently determined as meeting the criteria for Specified Investments:
- The investment is made with the UK Government, or a local authority (as defined in the Local Government Act 2003), or a police authority, or fire, or a UK Nationalised Industry, or UK Bank, or UK Building Society.
 - The investment is made with a Money Market Fund that, at the time the investment is made, has a rating of AAA.
 - The investment is made with one of the bodies listed in section 4 of Schedule 1E of the current version of the Treasury Management Practices document which, at the time the investment is made, has a short-term "investment grade" rating with either Standard & Poors, Moody's Investors Search Ltd or Fitch Ratings Ltd (or in the case of a subsidiary the parent has such a rating). Where ratings awarded differ between the rating agencies any one award below investment grade will prevent the investment being categorised as a Specified Investment. The rating of all listed bodies must be monitored monthly. Where officers become aware of a downward revision of rating, that moves the body out of the "investment grade" category, between such monthly checks, the body should be removed from the list of Specified Investments and, if considered appropriate, the investment should be recalled.
17. All specified investments must be denominated in sterling and must be one where the authority may require it to be repaid or redeemed within 12 months of the date on which the investment is made and must be considered of high credit quality. This is defined as having met the criteria set out above. The investment must not constitute the acquisition of share capital or loan capital in any body corporate.

- | |
|---|
| <ul style="list-style-type: none">• The minimum % of the total of all investments which must be Specified Investments, at the time the investment is made, is 90%• The maximum investment with any one counterparty is £15 million, except for the Debt Management Office which is has no limit.• The maximum investment in any one group (i.e., a bank and its wholly owned subsidiaries) is £15m. |
|---|

LIMITS & DEFINITION OF NON-SPECIFIED INVESTMENTS

18. These categories of investment currently meet the criteria for non-specified investments:

- The investment is made with a UK bank, or UK building society, or a UK subsidiary of an overseas bank.
- The investment is made with one of the bodies listed in section 4 of Schedule 1E of the current version of the Treasury Management Practices document, which is not a Specified Investment.
- The investment is for a period of one year or longer.

19. All non-specified investments must be denominated in sterling. The investment must not constitute the acquisition of share capital or loan capital in any body corporate.

- The maximum % of the total of all investments which can be non-specified investments, at the time the investment is made, is 10%.
- The maximum investment with any one counterparty is £3 million.
- The maximum investment in any one group (i.e., a bank and its wholly owned subsidiaries) is £3m.
- The maximum % of the total of all investments that have an outstanding period of one year or longer, at the time the investment is made, is 10%.

20. The maximum period for which an investment can be made is 3 years, with the maturity date no more than 3 years and 1 month from the time the deal is agreed.

21. As referred to earlier in the report, borrowing should be kept at, or below, the expected capital financing requirement over the medium term to reduce the risk of exposure to interest rate fluctuations. The balance of 'net borrowing' (loans less investments) should also be monitored to, where prudent, minimise interest rate differences.

22. The Council is empowered by Section 12 of the Local Government Act 2003 for the temporary investment of funds borrowed for the purpose of expenditure in the reasonably near future. While not "borrowing to invest" it is prudent to invest monies raised in advance of expenditure. As required by the Guidance such investment is permitted providing the anticipated expenditure is within this or the next financial year or within a period of eighteen months, whichever is the greater.

TREASURY MANAGEMENT POLICY STATEMENT

23. Middlesbrough Council defines its treasury management activities 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.'
24. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation and any financial instruments entered to manage those risks.
25. The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.
26. The high-level policies and monitoring arrangements adopted by the Council for Borrowing and Investments are as follows:

Borrowing

- Any borrowing decisions will aim to strike an appropriate risk balance between securing low interest rates and achieving cost certainty over the periods for which funds are required. Economic forecasts available from our treasury management advisers and any other available sources will be used to form a view on the target borrowing rates and overall borrowing strategy.
- Any decisions should also look to maintain the stability and flexibility of the longer-term debt portfolio, given the current low interest rate environment where short-term borrowing or borrowing from internal resources offer revenue budget savings.
- The main sources of funding for external borrowing for the Council are the Public Works Loan Board, Other Local Authorities, and private sector financial institutions.

Investments

- The CIPFA and DLUHC guidance require the Council to invest its funds prudently and to have regard to security, liquidity and yield when making these decisions.
- Security being the arrangements in place to protect principal sums invested by a local authority.
- Liquidity being to ensure that enough cash resources are available on a day-to-day basis for transactional needs.
- Yield being the interest rate and total financial return applicable to the investment being made.

- With these strategic issues in mind, the management of credit risk (or security) is key to the Council's investment strategy and any subsequent activity. The Council uses the external advisers' credit worthiness matrix to determine limits with individual counterparties.

MINIMUM REVENUE PROVISION POLICY 2024/25

INTRODUCTION

27. Local authorities are required each year to set aside some of their revenue income as provision for debt repayment. There is a simple duty for an authority each year to make an amount of revenue provision, which it considers “prudent”. (Minimum Revenue Provision) MRP Guidance makes recommendations to authorities on the interpretation of that term.
28. Authorities are legally obliged to “have regard” to any such guidance – which is exactly the same duty as applies to other statutory guidance including, for example, the CIPFA Prudential Code, the CIPFA Treasury Management Code and the DLUHC Guidance on Investments.
29. Authorities are asked to prepare an annual statement of their policy on making MRP and to have this approved by the body before the start of each financial year.

MEANING OF “PRUDENT PROVISION”

30. The main part to the guidance is concerned with the interpretation of the term “prudent provision”. The guidance proposes a number of options. It explains that provision for repayment of the borrowing, which financed the acquisition of an asset, should be made over a period bearing some relation to that over which the asset continues to provide a service or has economic benefit. It should also cover the gap between the Capital Financing Requirement and the various sources of capital income available to the Council to finance its capital programme, such as capital receipts, capital grants, contributions and direct revenue financing.

OPTIONS FOR PRUDENT PROVISION

Option 1: Regulatory Method

31. For debt supported by (Revenue Support Grant) RSG in previous years, authorities will be able to continue to use the formulae in regulations, since the RSG was provided on that basis.

Option 2: CFR Method

32. This is a technically simpler alternative to Option 1 and may also be used in relation to supported debt. While still based on the concept of the Capital Financing Requirement (CFR), which can be derived from the balance sheet, it avoids the complexities of the formulae in the regulations.

Option 3: Asset Life Method

33. For new borrowing under the Prudential system (from 2008) for which no government support is given, there are two main options. Option 3 is to make provision for debt repayment in **equal annual instalments** over the estimated life of the asset for which

the borrowing is undertaken. This is a possibly simpler alternative to the use of depreciation accounting (Option 4), though it has some similarities to that approach.

34. The formula allows an authority to make **voluntary extra provision** in any financial year that this is affordable.
35. In the case of the construction of a new building or infrastructure, MRP would not need to be charged until the new asset comes into service. This “**MRP holiday**” would be perhaps 2 or 3 years in the case of major projects and could make them more affordable. There would be a similar effect in the case of Option 4 under normal depreciation rules.

Option 4: Depreciation Method

36. Alternatively, for new borrowing under the prudential framework for which no Government support is being given, Option 4 may be used. This means making MRP in accordance with the standard rules for depreciation accounting.
37. Councils will normally need to follow the standard procedures for calculating depreciation when making this revenue provision.

Option 5: 2% Annuity Method

38. This method recognises the time value of money and the useful life of the assets funded from borrowing and is seen as a fairer way of charging MRP. It is supported by the Council’s treasury management advisers (Arlingclose) and is being adopted by many local authorities nationally as an equitable and affordable basis for calculating the revenue costs of repaying debt. The adoption of this option for 2024/25 is consistent with the methodology approved in 2023/24.

**2024/2025 MINIMUM REVENUE PROVISION -
STATEMENT FOR MIDDLESBROUGH COUNCIL**

39. The Secretary of State recommends that before the start of each financial year a local authority prepares a statement of its policy on making MRP in respect of that financial year and submits it to the full council as part of its budget setting process. The statement should indicate which of the options listed above are to be followed in the financial year.
40. For supported capital expenditure, Middlesbrough Council intends to use **option 5 - a 2% annuity basis** for the coming financial year.
41. For unsupported capital expenditure, Middlesbrough Council intends to use **option 5 - a 2% annuity basis** for the coming financial year.