Prudential Code & Treasury Management Code of Practice

In a nutshell

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The Chartered Institute of
Public Finance & Accountancy

CIPFA

The Updated Codes

Who needs an awareness of these codes?

- Chief Financial Officers and Deputies
- Treasury Management Teams
- Capital Accounting Teams
- Financial Planning Teams
- Internal Auditors
- External Auditors
- Business Support Teams
- Elected Members
- Monitoring Officers
- Students

Status of the Codes

- Primary Legislation
  - Local Government Act 2003 s15

15 Guidance

(1) In carrying out its functions under this Chapter, a local authority shall have regard—

(a) to such guidance as the Secretary of State may issue, and

(b) to such other guidance as the Secretary of State may by regulations specify for the purposes of this provision.

(2) The power under subsection (1)(b) is not to be read as limited to the specification of existing guidance.

- Secondary Legislation
  - Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 No. 3146

Code of practice

2. In complying with their duties under section 3(1) and (2) (duty to determine affordable borrowing limit), a local authority and the Mayor of London shall have regard to the code of practice entitled the "Prudential Code for Capital Finance in Local Authorities" published by CIPFA, as amended or reissued from time to time([8]).

Guidance

24. In carrying out its functions under Chapter 1 of Part 1, a local authority shall have regard to the code of practice contained in the document entitled "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes" published by CIPFA, as amended or reissued from time to time([1]).

Objectives of Prudential Code

To ensure, within a clear reporting framework, that:

- a local authority’s capital expenditure plans and investment plans are affordable and proportionate
- all external borrowing and other long-term liabilities are within prudent and sustainable levels
- the risks associated with investments for commercial purposes are proportionate to their financial capacity, and
- treasury management decisions are taken in accordance with good professional practice.

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How is it demonstrated that the objective are achieved?

- Capital Strategy
  - High level overview of how capital expenditure, capital financing, investments and treasury management decisions contribute to the delivery of corporate objectives
    - Capital Expenditure
    - Debt, Borrowings, Investments & Treasury Management
    - Investments for Commercial or Service Purposes
    - Other Long Term Liabilities
    - Knowledge & Skills

How is it demonstrated that the objective are achieved?

Through a series of Prudential Indicators

- Set and revised alongside processes established for setting and revising the budget
- Indicators for prior years should be taken from Statement of Accounts
- Consider local indicators
- Treasury Management Prudential Indicators set out in TM Code
- Establish processes to monitor and report performance against Prudential Indicators on a quarterly basis

The Prudential Indicators - Prudence

Considerations for Prudence

- Borrowing to invest primarily for financial return is not considered prudent
- Therefore rules out financing investments from prudential borrowing unless relevant to functions and financial returns are incidental to main purpose
- Whilst not required to sell existing commercial investments, prior to borrowing new loans, LAs should review options for exiting financial investments
- Any LAs with statutory ring fenced accounts (e.g. HRA or Police Fund) should report indicators for Prudence separately for those Accounts

The Prudential Indicators - Prudence

Capital Expenditure

- Estimates of capital expenditure
- Estimates of capital financing requirement

External Debt

- Authorised Limit (Loans & Other Long Term Liabilities)
- Operational Boundary
- Gross debt does not exceed capital financing requirement

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The Prudential Indicators - Affordability

Considerations for Affordability

- Ensure that level of investment in capital assets being proposed means that the total capital investment of the LA remains within sustainable limits
- Consider the financial position, including all of the resources currently available and estimated for the future together with totality of its capital, borrowing and investment plans, income and expenditure forecasts and risks
- Considered against any ringfenced resources available to fund borrowing
- Ensure that the revenue implications of capital finance re properly taken into account in the option appraisal process, capital programme and MTFS

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The Prudential Indicators - Affordability

- Estimates of Financing Costs to Net Revenue Stream

- Estimates of net income from commercial and service investments to Net Revenue Stream

Treasury Management in the Public Services

"The management of the organisation's borrowings, investments and cashflows, including 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."

CIPFA Treasury Management in the Public Services Code of Practice & Cross-sectorial Guidance Notes 2021

Treasury Management in the Public Services

	Expenditure	Income	Net
Revenue	Service expenditure Interest paid Grants given MRP T/F to reserves Increases in provisions Revenue financing of capital	Council tax Business rates Grants received Fees & charges T/F from reserves Interest received	Balanced Budget
Capital	Expenditure on assets Loans for service purposes Assets primarily for yield Certain financial instruments	Capital receipts Grants & contributions Use of reserves Financing from revenue Prudential Borrowing	Fully financed capital programme

Treasury Management in the Public Services

	Payments	Receipts	Net
Revenue	Service expenditure Interest paid Grants given **MRP** **T/F to reserves** **Increases in provisions** **Revenue financing of capital**	Council tax Business rates Grants received Fees & charges **T/F from reserves** Interest received	Net Cash inflows / outflows
Capital	Expenditure on assets Loans for service purposes Assets primarily for yield Certain financial instruments	Capital receipts Grants & contributions **Use of reserves** **Financing from revenue** **Prudential Borrowing**	Net cash inflows / outflows

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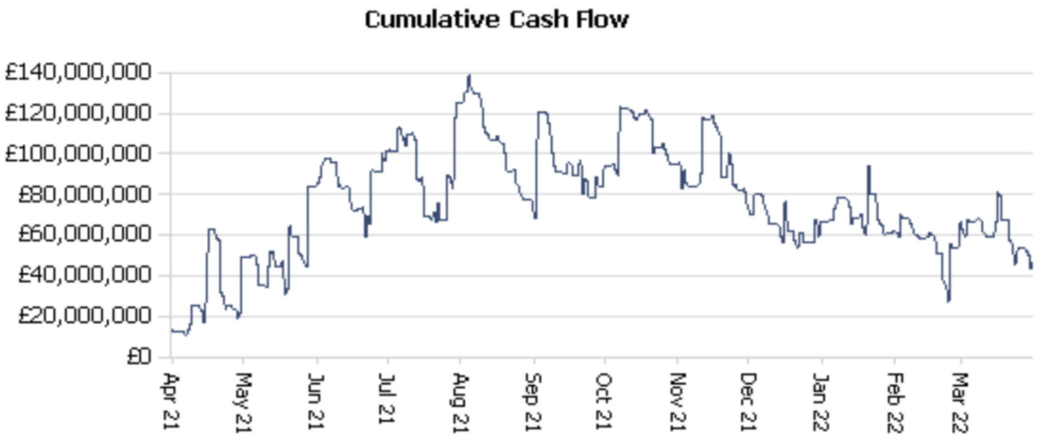
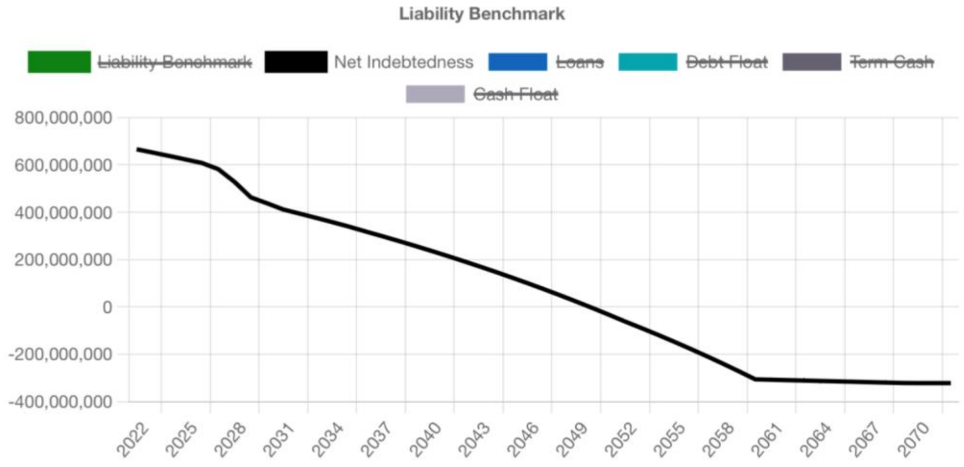
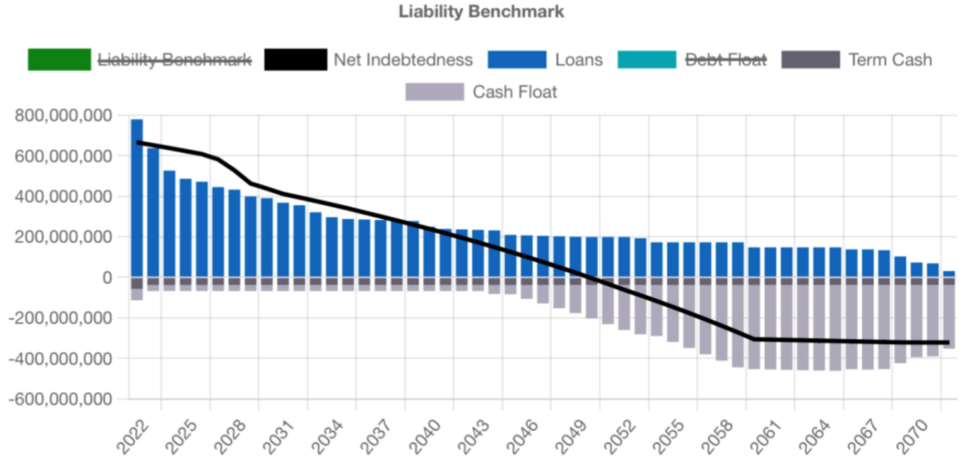
Treasury Management in the Public Services

Balance Sheet as at 31/03/2021	General Fund
Capital Financing Requirement	£1,046.52m
Other Balance Sheet Items	(£332.13)m
Net Loans Requirement/(Net Surplus)	**£714.39m**
Represented by:	
Loans	£812.70m
Investments	(£98.31)m
Net Loans Requirement/(Net Surplus)	**£714.39m**







Treasury Management Code

KEY PRINCIPLE 1

Public service organisations should put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities.

KEY PRINCIPLE 2

Their policies and practices should make clear that the effective management and control of risk are prime objectives of their treasury management activities and that responsibility for these lies clearly within their organisations. Their appetite for risk should form part of their annual strategy, including any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and portfolio liquidity when investing treasury management funds.

KEY PRINCIPLE 3

They should acknowledge that the pursuit of value for money in treasury management, and the use of suitable performance measures, are valid and important tools for responsible organisations to employ in support of their business and service objectives; and that within the context of effective risk management, their treasury management policies and practices should reflect this.

CIPFA recommends that all public service organisations adopt, as part of their standing orders, financial regulations or other formal policy documents appropriate to their circumstances, the following four clauses.

1. This organisation will create and maintain, as the cornerstones for effective treasury and investment 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
   - investment management practices (IMPs) for investments that are not for treasury management purposes.

   The content of the policy statement, TMPs and IMPs will follow the recommendations contained in Sections 6, 7 and 8 of the TM Code, subject only to amendment where necessary to reflect the particular circumstances of this organisation. Such amendments will not result in the organisation materially deviating from the TM Code's key principles.
2. This organisation (ie full board/council) will receive reports on its treasury and investment management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close in the form prescribed in its TMPs and IMPs.
3. This organisation delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to [note 1], and for the execution and administration of treasury management decisions to [note 2], who will act in accordance with the organisation's policy statement, TMPs and IMPs, and if they are a CIPFA member, CIPFA's Standard of Professional Practice on treasury management.
4. This organisation nominates [note 3] to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

Treasury Management Policy & Practices

CIPFA recommends that an organisation's treasury management policy statement adopts the following forms of words to define the policies and objectives of its treasury management activities:

1 This organisation defines its treasury management activities as the management of the organisation's borrowing, investments and cash flows, including 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.

2 This organisation 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 into to manage these risks.

3 This organisation 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.

CIPFA recommends that an organisation's treasury management practices (TMPs) include those of the following that are relevant to its treasury management powers and the scope of its treasury management activities:

TMP1	Risk management
TMP2	Performance measurement
TMP3	Decision making and analysis
TMP4	Approved instruments, methods and techniques
TMP5	Organisation, clarity and segregation of responsibilities and dealing arrangements
TMP6	Reporting requirements and management information arrangements
TMP7	Budgeting, accounting and audit arrangements
TMP8	Cash and cash flow management
TMP9	Money laundering
TMP10	Training and qualifications
TMP11	Use of external service providers
TMP12	Corporate governance

Treasury Management Practice 1 – Risk Management

- Credit & Counterparty Risk Management
- Liquidity Risk Management
- Interest Rate Risk Management
- Exchange Rate Risk Management
- Inflation Risk Management
- Refinancing Risk Management
- Legal & Regulatory Risk Management
- Operational Risk, including fraud, error and corruption
- Price Risk Management

Categorisation of Investments

- Investments for Treasury Management Purposes
  - Arising from management of cashflows
  - Include liquidity and any Investments arising from borrowing in advance
- Investments for Commercial Purposes
  - Primarily for financial return (excl treasury management)
  - Capital Expenditure
- Investments for Service Purposes
  - May not involve commercial terms (soft loans?)
  - Likely met from Capital Expenditure

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Service & Commercial Investments

- All investments that are not for treasury management purposes need to be categorised into:
    - Commercial purposes
    - Service purposes
- Risks should be proportionate to financial capacity
- Must not borrow to invest for the primary purpose of commercial return
- Prudential borrowing must not be used for investments unless service led and returns incidental

Treasury Management Prudential Indicators

- Maturity Structure of Borrowing

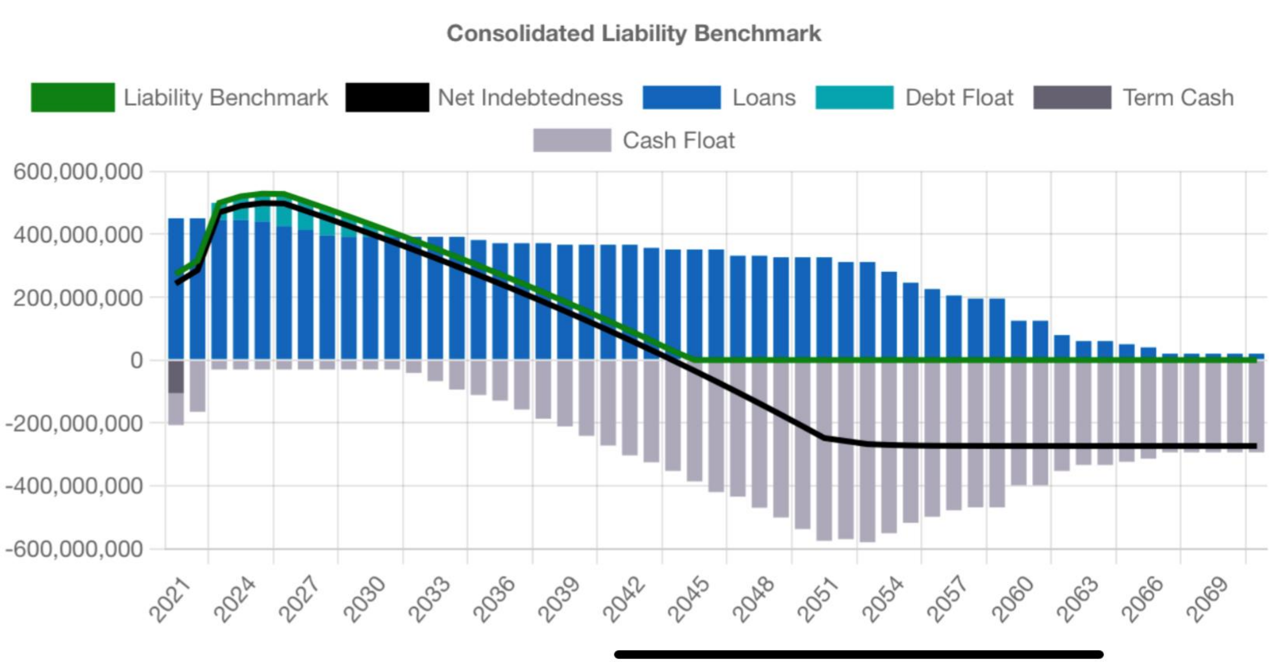
	Lower Limit %	Upper Limit %
Under 12 months		
1 – 2 years		
2 – 5 years		
5 – 10 years		
Over 12 years		

- Long Term Treasury Management Investments

	Principal sums invested beyond the period end £m
2022/23	
2023/24	
2024/25	

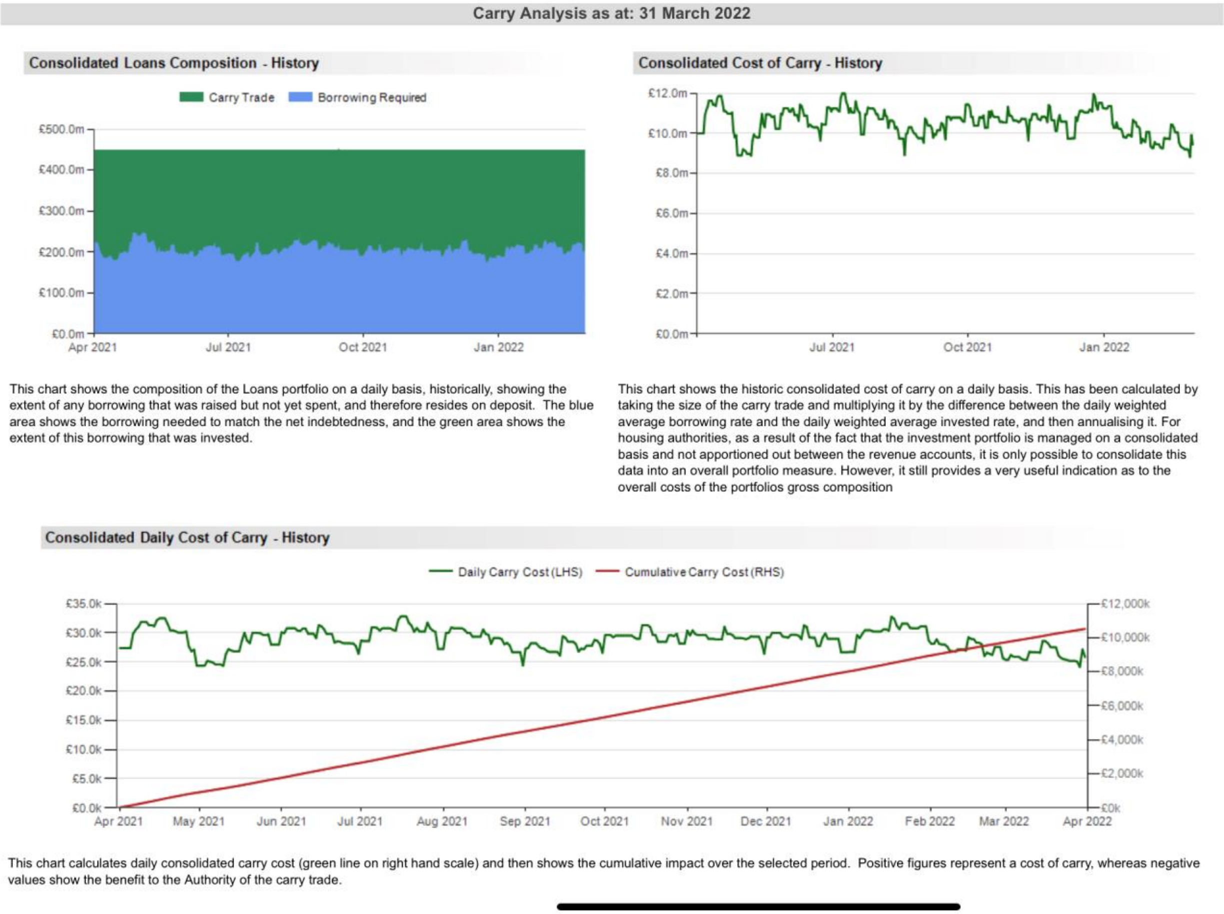
- Interest Rate Exposures
- Credit Risk
- Price Risk
- Liability Benchmark

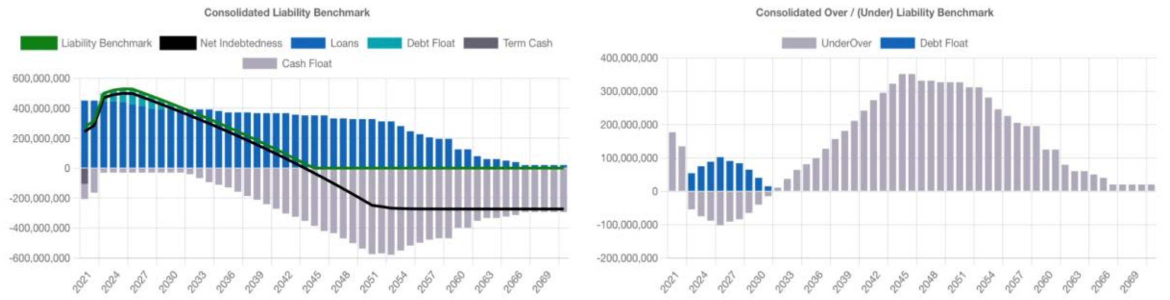
Liability Benchmark

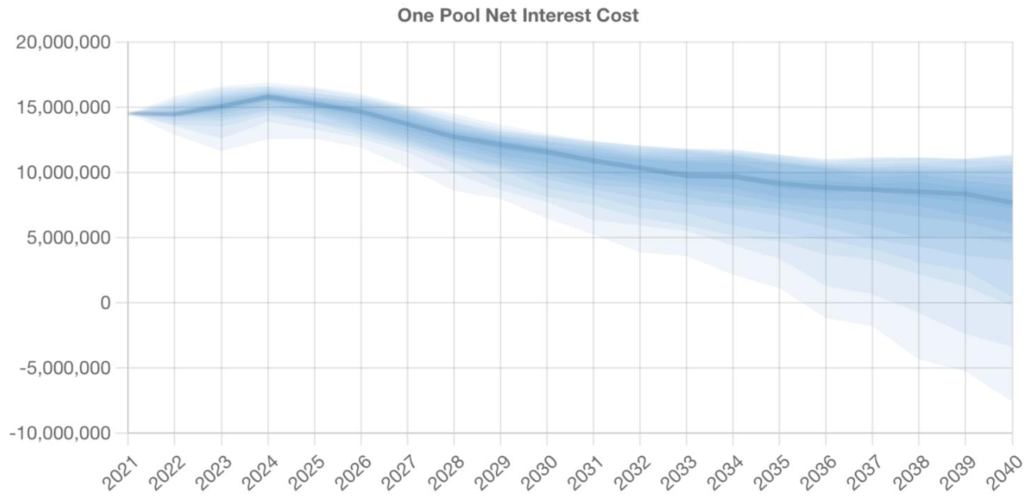


- Framework for establishing optimum external borrowing structure
- Based on corporate spending & financing plans
- Enables projected treasury portfolio balances
- Determines borrowing and investment strategies

Impact of Treasury Management







Source: TreasuryLive – Public Sector Live Ltd

Levelling Up & Regeneration Bill

- Amendments to Local Government Act 2003
- Allows for Secretary of State to make “risk-mitigation directions” if a trigger event has occurred
- A trigger event occurs when:
    - A risk threshold is breached
    - A s114 report has been issued
    - A capitalisation directive has been received
- A direction could be:
    - Limits in relation to borrowing activity
    - Requirement to divest certain assets

Levelling Up & Regeneration Bill

- Risk Thresholds are breached when “capital risk metrics” breach the specified threshold
- Capital Risk Metrics
    - Total debt / financial resources
    - Proportion of assets held wholly or mainly to generate financial return
    - Proportion of debt which is not from central or local government
    - Amount of minimum revenue provision charged in a year
    - Any other metrics specified by the Secretary of State

Summary & Conclusions

- Key governance Codes ensuring prudence and risk management are at the heart of capital strategy and treasury decision making
- Updated emphasis on reducing exposure to commercial investments
    - No longer resource investments in commercial assets from prudential borrowing
    - New considerations on proportionality
- Treasury Management is an integral function with significant impact on finances
- New requirements for a Liability Benchmark indicator
    - Provides structure to borrowing decisions
    - Prevents excess treasury investment risk
- New requirements for quarterly monitoring

CIPFA’s Liability Benchmark Implementation Service

- FREE service to all Local Authorities
- On-boarding done for you
- Tools to update and refine projections
- One-to-one training sessions
- Bespoke step-by-step guide to your position

Register here

https://www.pslive.co.uk/Liability-Benchmark-Registration

Implementing CIPFA Best Practice Treasury Risk Management

TreasuryLive

Transform your Treasury Operations

Exclusively endorsed by CIPFA to deliver best practice and Code compliant tools

- Cloud based treasury risk management system
- One version of the truth
- Real time risk analytics

Deal Recording

Accurately record all treasury transactions

- Every Local Authority transaction type available
- Linked to market data and money market fund feeds
- All round visibility of cash flows

Cash Management

Robust and complete cash flow projections

- Daily cash reconciliations
- Long term forecasting
- Full audit trails

Insightful Reporting

Elegant and insightful visuals

- Back office reconciliations
- Management dashboards
- Cash flow forecasting
- Call account and money market fund reconciliations
- Interactive insights to your evolving treasury portfolios

Liability Benchmarking

Only borrow what you need

- Achieves the requirements of the CIPFA Treasury Code
- Understand your Authority’s long-term projections
- Enhance your decision making
- Develop your treasury management strategy

Risk Analysis

Ensuring risk management at the heart of decision-making

- Quantify revenue risk exposures
- Best in class risk reporting
- Accessible yet powerful suite of tools
- Essential for treasury budget setting and monitoring

Book a demo at https://pslive.co.uk/PSLive-Bookings
Contact us at support@pslive.co.uk for more information

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