CABINET

18 DECEMBER 2012

TREASURY MANAGEMENT STRATEGY MID-YEAR REVIEW REPORT 2012/13

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Summary

On the 23 February 2012, Full Council approved the 2012/13 Treasury Management Strategy. As part of that strategy and in line with the Chartered Institute of Public Finance Accountancy's (CIPFA) code of Practice for Treasury Management, there should be a review of that strategy at least half yearly. This report is the mid year review of the Treasury Management Strategy 2012/13.

1. Budget and Policy Framework

1.1 Business Support Overview and Scrutiny is responsible for the scrutiny of the Council's Treasury Management, Investment Strategy and Minimum Revenue Provision Policy Statement along with Treasury Management Practices and associated Schedules.

1.2 There needs to be, at a minimum, a mid year review of treasury management strategy and performance. This is intended to highlight any areas of concern that have arisen since the original strategy was approved.

1.3 The Mid Year report should be considered by Business Support Overview and Scrutiny Committee, Cabinet and Full Council.

2. Background

2.1 The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensures this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering maximising investment return.

2.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer-term cash may involve arranging long or short-term loans, or using long-term cash flow surpluses, and on occasion, debt previously incurred may be restructured to meet Council risk or cost objectives.

2.3 As a consequence treasury management is defined as:

"The management of the local authority'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. "

2.4 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2011 needs to be formally adopted by this Council (Appendix 1). This replaces the CIPFA Code of Practice on Treasury Management revised November 2009 which was adopted by this Council on 25 February 2010.

2.5 The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
3. Receipt by full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a **Mid-year Review Report** and an Annual Report (stewardship report) covering activities during the previous year.
4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is: Business Support Overview and Scrutiny Committee.

2.6 This mid year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first six months of 2012/13;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- A review of the Council's investment portfolio for 2012/13;
- A review of the Council's borrowing strategy for 2012/13;
- A review of any debt rescheduling undertaken during 2012/13; and
- A review of compliance with Treasury and Prudential Limits for 2012/13.

2.7 Recommendations

Recommend approval of the adoption of the CIPFA Code of Practice on Treasury Management 2011.

3. Economic update

3.1 <u>Economic performance to date</u>

3.1.1 The economic view on the prospect of the UK economy recovering swiftly from recession suffered a significant set back in August when the Bank of England lowered its expectations for the speed of recovery and rate of growth over the coming months and materially amended its forecast for 2012 and 2013. The UK economy is heavily influenced by worldwide economic developments, particularly in the Eurozone, and on-going negative sentiment in that area would impact on the UK's economic performance. Investor confidence remains weak for the Eurozone and the continuing Eurozone debt crisis is having a major effect in undermining business and consumer confidence in, America, the Far East/China, Europe and the UK.

3.1.2 UK consumer confidence remains low with unemployment concerns, indebtedness and pressure on real incomes from high inflation and low pay rises. Inflation has fallen considerably, however, this is the slowest recovery from a recession of any of the five UK recessions since 1930. The weak recovery has resulted in social security payments remaining at a high level and tax receipts low. The Monetary Policy Committee has kept the bank rate at 0.5% and quantitative easing was increased by £50 billion to £375 billion in July. In June the Bank of England and the Government also announced schemes to free up banking funds for business and consumers.

3.1.3 However, on a positive note the UK's sovereign debt remains one of the first ports of call for surplus cash to be invested in.

3.2 <u>Outlook for the next six months of 2012/13</u>

3.2.1 The risks in economic forecasts are ongoing from the previous treasury strategy. Concern has been escalating that the Chinese economy is heading for a sharp slow down rather than a gentle slowdown. America's presidential election in November prevented a positive approach to countering weak growth. Urgent action will be required early in 2013 to address the US debt position. On 13 September the Federal Reserve System (US central banking system) announced an aggressive stimulus programme for the economy with a third round of quantitative easing to boost growth in job creation and announced that interest rates were unlikely to increase until at least mid 2015.

3.2.2 Eurozone growth will remain weak due to austerity programmes in various countries. Greece has failed again to achieve deficit reduction targets and may require a third bail out. There is also a possibility that some of the northern European countries could push for the ejection of Greece from the Eurozone unless its financial prospects improve. A financial crisis was rapidly escalating over the situation in Spain however, in early September the European Central Bank announced that it would purchase unlimited amounts of shorter term bonds of Eurozone countries which have formally agreed the terms for a bailout. This support would be subject to conditions and include supervision from the International Monetary Fund. This has resulted in a surge in confidence in the Eurozone however it is not known whether Spain and Italy will accept the terms for a bailout.

3.2.3 The Bank of England Quarterly Inflation Report in August lowered inflation expectations and forecast a weaker and delayed robust recovery. Weak export markets will remain a drag on the economy and consumer expenditure will continue to be downcast due to a focus on paying off debt, negative economic sentiment and job fears.

The overall balance of risks is weighted to the downside:

- Sector expect low growth in the UK to continue, bank rate unlikely to rise in the next 24 months linked with a possible further extension of quantitative easing. This will keep investment returns low.

- Sector expect the longer run trend for Public Works Loan Board (PWLB) borrowing rates to eventually rise, primarily due to the need for a high volume of gilt issuance in the UK and the high volume of debt issuance in other major western countries. However, the current safe haven status of the UK may continue for some time, tempering any increases in yield.

- Sectors interest rate forecast is based on an assumption that growth starts to recover in the next three years to a near trend rate (2.5%). However, if the Eurozone debt crisis worsens as a result of one or more countries having to leave the Euro, or low growth in the UK continues longer, then Bank Rate is likely to be depressed for even longer than in this forecast.

3.3 Sector's interest rate forecast

	17.9.12 actual	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15
BANK RATE	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75	1.00
3m LIBID	0.55	0.60	0.60	0.60	0.60	0.60	0.60	0.70	0.90	1.10	1.40
6m LIBID	0.85	0.85	0.85	0.85	0.85	0.85	1.00	1.10	1.30	1.50	1.80
12m LIBID	1.30	1.30	1.30	1.30	1.40	1.50	1.70	1.90	2.10	2.30	2.60
5yr PWLB	1.89	1.50	1.50	1.50	1.60	1.70	1.80	1.90	2.00	2.10	2.30
10yr PWLB	2.91	2.50	2.50	2.50	2.60	2.70	2.80	2.90	3.00	3.20	3.30
25yr PWLB	4.15	3.70	3.70	3.70	3.80	3.80	3.90	4.00	4.10	4.20	4.30
50yr PWLB	4.32	3.90	3.90	3.90	4.00	4.00	4.10	4.20	4.30	4.40	4.50

The above Sector forecasts for PWLB rates incorporate the introduction of the **PWLB certainty rate** in November 2012, which will reduce PWLB borrowing rates by 0.20% for most local authorities. The actual PWLB rates on 17 September 2012 are prior to the reduction of 20 basis points (bps).

4 Treasury Management Strategy Statement and Annual Investment Strategy update

4.1 The Treasury Management Strategy Statement (TMSS) for 2012/13 was approved by Council on 23rd February 2012. There are no policy changes to the TMSS.

4.2 Limits to Borrowing Activity

4.2.1 The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowing less investments) will only be for a capital purpose. Net external borrowing should not, except in the short term, exceed the total of Capital Financing Requirement (CFR) in the preceding year plus the estimates of any additional CFR for 2012/13 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

	2012/13 Original Estimate £m	Current Position 30 Sept 2012 £m	2012/13 Revised Estimate £m
Gross borrowing	172.410	182.450	172.325
Plus other long term liabilities*		3.123	3.123
Less investments	(52.817)	(72.940)	(51.547)
Net borrowing	119.593	135.573	123.901
CFR (year end position)	257.489	253.991	253.991

4.2.2 On the 21 November 2012, £10 million PWLB loan was repaid, bringing the debt portfolio in line with the original estimate, and invested cash is likely to be in line with the original estimate producing a net borrowing figure of some £124 million – well within the CFR.

4.2.3 The Chief Finance Officer reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator for maintaining net borrowing to CFR.

4.2.4 A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in longer-term scenario. It is a forecast of maximum borrowing requirement with some capacity for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The council’s authorised borrowing limit for 2012/13 is £440.545 million and it will not exceed this limit.

5 Investment Portfolio 2012/13

5.1 In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As set out in Section 3, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the 0.5% Bank Rate. The continuing Euro zone sovereign debt crisis, and its potential impact on banks, prompts a low risk and short-term strategy. Given this risk adverse environment, investment returns are likely to remain low.

5.2 The investment portfolio yield for the first six months of the year for the in-house team is 1.71% (on an annual basis) and Investec is currently 0.61% (on an annual basis) however the outturn position for Investec is estimated to be between 0.8% and 1%.

5.3 The rates payable on investments have started to fall and there is a high risk that this trend will continue. The interest which was being paid on Svenska Handelsbanken 35 day notice account dropped from 0.875% to 0.475% on the 2 November 2012. NatWest have advised that they will be dropping the rate payable on their instant access account from 1.05% to 0.80% (base rate + 30 bps) on the 1 February 2013, and a further drop to 0.60% (base rate + 10 bps) from the 1 May 2013.

5.4 A full list of in house investments held as at 30 September 2012 is shown below:

Investments	**Principal 30 Sept 2012 £**	**Interest %**
Core Investments		
Svenska Handelsbanken	10,000,000	0.875%
Lloyds TSB	20,000,000	2.4%
Lloyds TSB	5,000,000	3.0%
Total In house Core Investments	35,000,000	
Liquid Investments		
Natwest Special Interest Account	15,000,000	1.05%
Total In house Liquid Investments	15,000,000	

5.5 The average balances, interest rate earned to 30 September 2012 and forecast average interest rate for 2012/13 comparing the performance of the externally managed fund to the In house team is shown below.

	Average Balance 30 Sept 2012 £	Average Interest Rate 30 Sept 2012 %	Forecast Average Interest Rate 2012/13 %
Externally Managed			
Investec (excluding fees)	22,959,474	0.61%	0.8% - 1%
Managed In-House			
In-house Core Investments	29,010,989	2.28%	2.21%
In-house Liquid Investments	23,532,088	1.01%	0.93%
Total In-House		1.71%	1.70%

5.6 The Chief Financial Officer confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2012/13.

5.7 The Council's budgeted investment return for 2012/13 is £1.175 million and performance for the year to date is in line with the budget.

5.8 Investment Counterparty Criteria

The current investment counterparty criteria selection approved in the Treasury Strategy is meeting the requirement of the treasury management function.

6 Borrowing

6.1 The Council's capital financing requirement (CFR) for 2012/13 is £253.991 million. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. The table in section 4.21 shows the Council has external borrowings of £182.45 million against a CFR of £253.991 million.

6.2 The current borrowing strategy is to repay debt rather than enter into new borrowing as a consequence of the relationship between investment and borrowing interest rates. Using invested funds to repay debt also has the benefit of mitigating counterparty risk. This policy has been adhered to for the first six months of this financial year. However, as specified within the strategy, in the event that it was deemed advantageous to borrow then we will evaluate the economic and market factors to form a view on future interest rates so as to determine the manner and timing of decisions to borrow.

6.3 The general trend has been a reduction in interest rates during April to October, across all maturity bands.

6.4 It is anticipated that no external borrowing will be undertaken during this financial year, unless it is found to be advantageous as mentioned in paragraph 6.2.

7 Debt Rescheduling

7.1 Debt rescheduling opportunities have been limited in the current economic climate and consequent structure of interest rates. During the first six months of the year, no debt rescheduling was undertaken and it is not envisaged that any will occur before the end of the financial year. However, officers and the council's financial advisers 'Sector' will continue to monitor the situation and opportunities will be carefully considered.

8 Compliance with Treasury and Prudential Limits

8.1 It is a statutory duty for the Council to determine and keep under review the "Affordable Borrowing Limits". Council's approved Treasury and Prudential Indicators (affordability limits) are outlined in the approved TMSS.

8.2 During the financial year to date the Council has operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices.

9 Business Support Overview and Scrutiny Committee

9.1 The committee considered this report at its meeting held on 6 December 2012. Members discussed the performance of the in-house and externally managed funds and asked if officers had considered managing the whole fund in-house, as it had out-performed the external fund manager in the current financial year. Officers advised that the two forms of fund management adopted different tactics in order to spread the risk. The internal funds were placed in 'safe' bank deposits with variability in earnings dependant on market opportunities and availability of funds at a point in time, whereas the external fund manager was also able to trade in gilts and bonds, and take opportunities presented by the markets in these areas to make gains (or suffer losses) as global markets react. The return on internal funds was easier to predict and less volatile but equally less able to respond to volatility in the market place and take a risk premium.

9.2 Members asked about the fees paid to the external fund manager, counter-party protection with regard to creditworthiness, how Investec was chosen as the council's external fund manager and the cash flow of the council. Following the committee's concern at the breakdown of the Nat West banking system earlier in the year, Members also discussed the council's contract with Nat West to act as its main bank. Members were informed that the contract with Nat West was due to end in September 2013 and invitations to tender for this business would be issued soon. Part of the tender would include qualitative issues, including the processes the applicant had set in place to overcome technical difficulties.

9.3 The committee noted the report and recommended to Council the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2011.

10 Risk management

10.1 Risk and the management thereof is a feature throughout the strategy and in detail within the treasury management Practices 1 within the Treasury strategy.

11 Financial and legal implications

11.1 The Finance and Legal implications are highlighted throughout this report.

12 Recommendations

12.1 Cabinet is requested to consider the contents of this report (including the views of the Business Support Overview and Scrutiny Committee) and recommend the report to Council.

12.2 Cabinet is also requested to recommend to Council the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2011, as set out in Appendix 1 to the report.

13. Suggested reasons for decision

13.1 The Treasury Management Strategy requires that Cabinet and Council receives and considers a mid year review of treasury management strategy and performance.

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Background papers

Treasury Strategy 2012/13:
http://democracy.medway.gov.uk/ieIssueDetails.aspx?IId=7574&Opt=3

Investec report – September 2012

CIPFA The Chartered Institute of Public Finance & Accountancy

Appendix 1

treasury management

in the Public Services

Code of Practice and Cross-Sectoral Guidance Notes

2011 Edition

CIPFA, the Chartered Institute of Public Finance and Accountancy, is the professional body for people in public finance. Our 14,000 members work throughout the public services, in national audit agencies, in major accountancy firms, and in other bodies where public money needs to be effectively and efficiently managed. As the world's only professional accountancy body to specialise in public services, CIPFA's qualifications are the foundation for a career in public finance. We also champion high performance in public services, translating our experience and insight into clear advice and practical services. Globally, CIPFA shows the way in public finance by standing up for sound public financial management and good governance.

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in the Public Services

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SECTION 1

Introduction

This *Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes* (the Code) represents a revision of the 2009 Code.

This Code has been reviewed and updated following recent developments in the market place and the introduction of the Localism Act for English local authorities.

There is no universally agreed or formal definition of the public services. For the purposes of this Code and its accompanying guidance notes, public services have been taken to include those organisations which are, in terms of government expenditure classification, the public sector, together with certain other organisations which are materially reliant on government funding or subsidy, and/or have significant social, democratic or political influences on their activities.

Specifically, the Code and guidance notes have been designed to be primarily for the use of local, police and fire authorities, registered social landlords or registered providers of social housing under the Tenant Services Authority regulatory framework, higher and further education institutions, and the National Health Service.

Within these organisations, CIPFA recognises that there is a wide range of interpretations of what activities comprise treasury management. For the purposes of this Code and accompanying guidance notes, CIPFA has adopted the following as its definition of treasury management activities:

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.

This definition is intended to apply to all public service organisations in their use of capital and project financings, borrowings and investments.

There are substantial variations between different parts of the public services in the nature of and extent to which they employ treasury management activities and techniques in pursuit of their business and service objectives. These variations are primarily a function of the respective statutory and regulatory regimes under which they operate, the powers they possess in respect of treasury management, and the services and businesses they pursue. Nothing in this Code overrides or should be taken as overriding statutory provision. Nor does the Code make intra vires anything that is otherwise ultra vires.

The essentially more commercial nature of some public service organisations creates pressures and perhaps conflicts in their treasury management activities which do not impact so heavily on those organisations that are largely service orientated. These differences are explained more fully in the sector-specific guidance notes.

CIPFA recognises that many organisations will find that certain parts of this publication are not relevant to the scope and nature of their treasury management activities. It believes, however, that the recommendations made in the Code provide a basis for all public service organisations to create clear treasury management objectives and to structure and maintain sound treasury management policies and practices.

The guidance notes serve three functions:

- First, they provide general background and explanatory information on the issues raised and recommendations made in the Code.
- Second, they give suggestions for schedules to accompany the Code's recommended treasury management practices.
- Third, they draw attention to features of treasury management that are particular to those individual parts of the public services covered by the Code.

CIPFA gratefully acknowledges the contributions made by the many organisations and individuals who assisted during the preparation of the Code and guidance notes. Responsibility for their contents rests solely with CIPFA, **and they should not be relied on by any third party in their treasury management dealings with public service organisations, nor as an authoritative interpretation of law.**

Whilst the Code has wide-ranging support of various bodies, the **application and maintenance of these recommendations is the responsibility of the organisations themselves.**

SECTION 2
Purposes

CIPFA has produced this Code and the accompanying guidance notes to help satisfy nine main purposes:

1. To assist public service organisations in the development and maintenance of firm foundations and clear objectives for their treasury management activities, and thereby to add to their credibility in the public eye.
2. To emphasise the overriding importance of effective risk management as the foundation for treasury management in all public service bodies.
3. To provide transparency for treasury management decisions including the use of counterparties and financial instruments that individual public service organisations intend to use for the prudent management of their financial affairs.
4. To encourage the pursuit of value for money in treasury management, and to promote the reasoned use, development and appreciation of appropriate and practical measures of performance.
5. To enable CIPFA members to fulfil their professional and contractual responsibilities to the organisations they serve and, in accordance with the members' charter, '*to maintain and develop the professional competence of both themselves and those they supervise*'.
6. To help facilitate a standardisation and codification of treasury management policies and practices in the public services.
7. To assist those involved in the regulation and review of treasury management in the public services, particularly those charged with the audit of the same.
8. To foster a continuing debate on the relevance and currency of the statutory and regulatory regimes under which treasury management in the various parts of the public services operates.
9. To further the understanding and confidence of, and to act as a reference work for, financial and other institutions whose businesses bring them into contact with the treasury management activities of public service organisations.

SECTION 3
Status

The Code has the support of a wide range of organisations.

In the case of local authorities in England and Wales, the Code has a particular significance under the provisions of the Local Government Act 2003. This requires local authorities *'to 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'*. The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 in paragraph 24 require local authorities to have regard to this guidance. In Scotland, Finance Circular 5/2010[1] requires local authorities to *have regard* to the Code.

The Local Government Association has expressed strong support for the Treasury Management Code. It is encouraging the good practice set out in the Code.

The Chartered Institute of Housing is happy to support the Treasury Management Code, recognising that it is suitable for adoption by local authorities as housing owners and managers, their arm's-length management organisations and housing associations.

The recommendations in the Code are similarly relevant to cash handled in respect of an organisation's pension fund, trust or endowment fund cash.

Nothing in this Code overrides or should be taken as overriding statutory provision. Nor does the Code make intra vires anything that is otherwise ultra vires.

The Code applies to all organisations that have adopted it as part of their standing orders, financial regulations or other formal policy documents appropriate to their circumstances.

CIPFA recognises that some organisations may not find the Code's recommended or proposed forms of wording to be precisely suitable to their circumstances. An organisation may, where they can justify doing so, make alterations to the recommended or proposed wording without adversely affecting its stated adoption of the Code, so long as, when taken as a whole, those alterations do not result in an organisation materially deviating from the Code's key principles as described in Section 4.

The accompanying guidance notes include explanations of the Code's recommendations and contain supporting suggestions. They are not prescriptive.

The Bank of England introduced a revised Non-Investment Products Code (NIPs Code) that has been drawn up by a wide cross-section of market practitioners in April 2009. The NIPs Code, which is market guidance, has no statutory underpinning; and there are no arrangements for supervision or enforcement. CIPFA commends the NIPs Code to its members as good practice to

1. Finance Circular 5/2010 *The Investment of Money by Scottish Local Authorities* (The Scottish Government, 2010).

which they should adhere. Copies of the NIPs Code can be obtained from www.bankofengland.co.uk.

SECTION 4

Key principles

This Code identifies three key principles.

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 liquidity when investing 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.

In framing these recommendations, CIPFA acknowledges the difficulties of striving for effective risk management and control, whilst at the same time pursuing value for money. This Code does not seek to be prescriptive about how this issue should be handled, particularly since it covers such a wide variety of organisations. However, where appropriate, the sector-specific guidance notes give suitable advice. CIPFA recognises that no two organisations in the public services are likely to tackle this issue in precisely the same manner; but success in this area of treasury management is likely to be viewed, especially in value for money terms, as an indicator of a strongly performing treasury management function.

Even though it dates back to 1991, CIPFA considers that the report by the Treasury and Civil Service Committee of the House of Commons on the BCCI closure is still pertinent, wherein it was stated that:

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

Paragraph 58, Second Report, December 1991

Indeed this view was supported by the Communities and Local Government Select Committee report into local authority investments in 2009.

It is CIPFA's view that throughout the public services the priority is to protect capital rather than to maximise return. The avoidance of all risk is neither appropriate nor possible. However, a balance must be struck with a keen responsibility for public money.

Clauses to be formally adopted

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 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.

   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 particular circumstances of this organisation. Such amendments will not result in the organisation materially deviating from the Code's key principles.
2. This organisation (ie full board/council) will receive reports on its treasury 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.
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 and TMPs and, if he/she is 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.

Note 1: name of responsible body (for example, committee, board or council) or nominated group of individuals or relevant committee such as cabinet or executive.

Note 2: title of responsible officer (for the purposes of this Code, the term 'responsible officer' has been used, although it is recognised that, in practice, many different terms exist). For example in higher education, the vice-chancellor/principal or equivalent is the 'designated officer' who will ensure that the governing body complies with all terms and conditions of funding provided by the funding body, However it is usual for day-to-day financial management to be delegated to a director of finance who will take professional responsibility for such areas of an institution's work and this is the officer who is referred to here.

Note 3: name of responsible body (for example, committee, board or council) or nominated group of individuals or relevant committee such as audit committee or relevant scrutiny committee.

SECTION 6

The treasury management policy statement

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 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.
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.

The policy statement should include the organisation's high level policies for borrowing and investments.

SECTION 7

Treasury management practices

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

It is expected that the following forms of words will be suitably amended to reflect an organisation's particular circumstances in defining its TMPs. Specific details of the systems and routines to be employed and the records to be maintained should take the form of schedules to their TMPs. Suggestions on the detail of what might be included in these schedules are given in the accompanying guidance notes.

General background information about each of the above practices, and the particular circumstances of each part of the public services covered by this Code, are also given in the guidance notes.

The nature and extent of the involvement of an organisation's responsible body in approving and monitoring its TMPs and accompanying schedules is a matter for local decision. CIPFA recognises that in some organisations this may be delegated to the responsible officer. In all cases it should be subjected to scrutiny by the responsible body following recommendations by the responsible officer.

TMP1 RISK MANAGEMENT

General statement

The responsible officer will design, implement and monitor all arrangements for the identification, management and control of treasury management risk, will report 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 organisation's objectives in this respect, all in accordance with the procedures set out in TMP6 *Reporting requirements and management information arrangements*.

In respect of each of the following risks, the arrangements which seek to ensure compliance with these objectives are set out in the schedule to this document.

[1] credit and counterparty risk management

This organisation regards a key objective of its treasury management activities to be the security of the principal sums it invests. Accordingly, it will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with whom funds may be deposited, and will limit its investment activities to the instruments, methods and techniques referred to in TMP4 *Approved instruments,* methods and techniques and listed in the schedule to this document. It also recognises the need to have, and will therefore maintain, a formal counterparty policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing or derivative arrangements.

[2] liquidity risk management

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

This organisation will only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.

[3] interest rate risk management

This organisation 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 management information arrangements.

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

It will ensure that any hedging tools such as derivatives are only used for the management of risk and the prudent management of financial affairs and that the policy for the use of derivatives is clearly detailed in the annual strategy.

[4] exchange rate risk management

It will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income/expenditure levels.

[5] refinancing risk management

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

It will actively manage its relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid overreliance on any one source of funding if this might jeopardise achievement of the above.

[6] legal and regulatory risk management

This organisation 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 counterparty policy under TMP1[1] *credit and counterparty risk management*, it will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the organisation, particularly with regard to duty of care and fees charged.

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

[7] fraud, error and corruption, and contingency management

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

[8] market risk management

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

TMP2 PERFORMANCE MEASUREMENT

This organisation is committed to the pursuit of value for money in its treasury management activities, and to the use of performance methodology in support of that aim, within the framework set out in its treasury management policy statement.

Accordingly, the treasury management function will be the subject of ongoing analysis of the value it adds in support of the organisation's stated business or service objectives. It will be the subject of regular examination of alternative methods of service delivery, of the availability of fiscal or other grant or subsidy incentives, and of the scope for other potential improvements. The performance of the treasury management function will be measured using the criteria set out in the schedule to this document.

TMP3 DECISION-MAKING AND ANALYSIS

This organisation will maintain full records of its treasury management decisions, and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time. The issues to be addressed and processes and practices to be pursued in reaching decisions are detailed in the schedule to this document.

TMP4 APPROVED INSTRUMENTS, METHODS AND TECHNIQUES

This organisation will undertake its treasury management activities by employing only those instruments, methods and techniques detailed in the schedule to this document, and within the limits and parameters defined in TMP1 *Risk management*.

Where this organisation intends to use derivative instruments for the management of risks, these will be limited to those set out in its annual treasury strategy. The organisation will seek proper advice and will consider that advice when entering into arrangements to use such products to ensure that it fully understands those products.

TMP5 ORGANISATION, CLARITY AND SEGREGATION OF RESPONSIBILITIES, AND DEALING ARRANGEMENTS

This organisation considers it essential, for the purposes of the effective control and monitoring of its treasury management activities, for the reduction of the risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that there is at all times a clarity of treasury management responsibilities.

The principle on which this will be based is a clear distinction between those charged with setting treasury management policies and those charged with implementing and controlling these policies, particularly with regard to the execution and transmission of funds, the recording and administering of treasury management decisions, and the audit and review of the treasury management function.

If and when this organisation intends, as a result of lack of resources or other circumstances, to depart from these principles, the responsible officer will ensure that the reasons are properly reported in accordance with TMP6 Reporting requirements and management information arrangements, and the implications properly considered and evaluated.

The responsible officer will ensure that there are clear written statements of the responsibilities for each post engaged in treasury management, and the arrangements for absence cover. The responsible officer will also ensure that at all times those engaged in treasury management will follow the policies and procedures set out. The present arrangements are detailed in the schedule to this document.

The responsible officer will ensure there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds. The present arrangements are detailed in the schedule to this document.

The delegations to the responsible officer in respect of treasury management are set out in the schedule to this document. The responsible officer will fulfil all such responsibilities in accordance with the organisation's policy statement and TMPs and, if a CIPFA member, the *Standard of Professional Practice on Treasury Management*.

TMP6 REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS

This organisation will ensure that regular reports are prepared and considered on the implementation of its treasury management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; on the implications of changes, particularly budgetary, resulting from regulatory, economic, market or other factors affecting its treasury management activities; and on the performance of the treasury management function.

As a minimum:

The organisation (ie full board/council) will receive:

- an annual report on the strategy and plan to be pursued in the coming year
- a mid-year review
- an annual report on the performance of the treasury management function, on the effects of the decisions taken and the transactions executed in the past year, and on any circumstances of non-compliance with the organisation's treasury management policy statement and TMPs.

The committee/board/council will receive regular monitoring reports on treasury management activities and risks.

The body responsible for scrutiny, such an audit or scrutiny committee, will have responsibility for the scrutiny of treasury management policies and practices.

Local authorities should report the treasury management indicators as detailed in their sector-specific guidance notes.

The present arrangements and the form of these reports are detailed in the schedule to this document.

TMP7 BUDGETING, ACCOUNTING AND AUDIT ARRANGEMENTS

The responsible officer will prepare, and this organisation will approve and, if necessary, from time to time will amend, an annual budget for treasury management, which will bring together all of the costs involved in running the treasury management function, together with associated income. The matters to be included in the budget will at minimum be those required by statute or regulation, together with such information as will demonstrate compliance with TMP1 *Risk management*, TMP2 *Performance measurement*, and TMP4 *Approved instruments, methods and techniques*. The responsible officer will exercise effective controls over this budget, and will report upon and recommend any changes required in accordance with TMP6 *Reporting requirements and management information arrangements*.

This organisation will account for its treasury management activities, for decisions made and transactions executed, in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

TMP8 CASH AND CASH FLOW MANAGEMENT

Unless statutory or regulatory requirements demand otherwise, all monies in the hands of this organisation will be under the control of the responsible officer, and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis, and the responsible officer will ensure that these are adequate for the purposes of monitoring compliance with TMP1[1] *liquidity risk management*. The present arrangements for preparing cash flow projections, and their form, are set out in the schedule to this document.

TMP9 MONEY LAUNDERING

This organisation is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. Accordingly, it will maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that staff involved in this are properly trained. The present arrangements, including the name of the officer to whom reports should be made, are detailed in the schedule to this document.

TMP10 TRAINING AND QUALIFICATIONS

This organisation recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The responsible officer will recommend and implement the necessary arrangements.

The responsible officer will ensure that board/council members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.

Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.

The present arrangements are detailed in the schedule to this document.

TMP11 USE OF EXTERNAL SERVICE PROVIDERS

This organisation recognises that responsibility for treasury management decisions remains with the organisation at all times. It recognises that there may be potential value in employing external providers of treasury management services, in order to acquire access to specialist skills and resources. When it employs such service providers, it will ensure it does so for reasons which have been submitted to a full evaluation of the costs and benefits. It will also ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review. And it will ensure, where feasible and necessary, that a spread of service providers is used, to avoid overreliance on one or a small number of companies. Where services are subject to formal tender or re-tender arrangements, legislative requirements will always be observed. The monitoring of such arrangements rests with the responsible officer, and details of the current arrangements are set out in the schedule to this document.

TMP12 CORPORATE GOVERNANCE

This organisation is committed to the pursuit of proper corporate governance throughout its businesses and services, and to establishing the principles and practices by which this can be achieved. Accordingly, the treasury management function and its activities will be undertaken with openness and transparency, honesty, integrity and accountability.

This organisation has adopted and has implemented the key principles of the Code. This, together with the other arrangements detailed in the schedule to this document, are considered vital to the achievement of proper corporate governance in treasury management, and the responsible officer will monitor and, if and when necessary, report upon the effectiveness of these arrangements.

Cross-Sectoral Guidance Notes

Introduction

These guidance notes accompany CIPFA's *Treasury Management in the Public Services: Code of Practice* (the Code), and should be read in conjunction with it. They are divided into two sections and serve the following purposes:

1. Section 1 provides background and explanatory notes on the main issues raised and the key principles stated in the Code.
2. Section 2 proposes the contents of schedules to accompany the statement of an organisation's treasury management practices (TMPs), which the Code recommends every public service organisation should have.

Sections 1 and 2 are common to all organisations, whilst Section 3 covers guidance which is sector-specific. Section 3 for local authorities is due for publication in 2009.

The guidance notes are structured in this way to enable users of the Code and other interested parties to create separately a source of reference on CIPFA's guidance for each distinct part of the public services covered by the Code.

Responsibility for the guidance in this document and the views expressed in it rests solely with CIPFA. It should not be relied upon by any third party in dealings with public service organisations, nor should it be relied upon as an authoritative interpretation of the law.

CIPFA wishes to thank the members of its Treasury Management Panel, who have overseen the updating of these guidance notes:

Ken Barnes (Chair)
Mandy Bretherton, CIPFA
Martin Easton, Birmingham City Council
Innes Edwards, Edinburgh City Council
Mark Frankel, PWLB
Jonathan Hunt, Westminster City Council
Kevin Jaquest, Society of District Council Treasurers
Gill Kilpatrick, Society of County Treasurers
Paul Mayers, Audit Commission
Joy Robson, Monmouthshire County Council
Janet Senior, London Borough of Lewisham
Will Spinney, Association of Corporate Treasurers
Martin Upton, Open University

SECTION 1

Background and explanatory notes

The Code recommends that:

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.

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 liquidity when investing funds.

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.

Source: The Code – Key Principles

The Code further recommends the adoption of four key clauses and the preparation of a treasury management policy statement and treasury management practices in order to achieve the above.

This section of the guidance notes explains the reasons for CIPFA's recommendations, and expands on the specific proposals concerning an organisation's approved treasury management practices.

1.1 RISK MANAGEMENT

The Code acknowledges the substantial variations that exist between different parts of the public services in the nature of and extent to which they employ treasury management activities and techniques in pursuit of their business and service objectives. These variations are primarily a function of the respective statutory and regulatory regimes under which organisations operate, the powers they possess in respect of treasury management, and the services and businesses they pursue.

The Code states, however, that in CIPFA's view, the common and overriding aim of such organisations should be the effective identification, monitoring and control of risk. The Code recommends strongly that organisations' treasury management policies and practices reflect this belief, and this message is further reinforced in this section of the guidance notes. Some public service organisations may use derivatives for the management of risk; where this is the case public service organisations should satisfy themselves that they understand fully how underlying risks are affected and any additional risks that may result.

The Code identifies eight main treasury management risks. These guidance notes define these risks as follows:

Credit and counterparty risk

The risk of failure by a counterparty to meet its contractual obligations to the organisation under an investment, borrowing, capital, project or partnership financing, particularly as a result of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources.

Liquidity risk

The risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, and that the organisation's business/service objectives will be thereby compromised.

Interest rate risk

The risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.

Exchange rate risk

The risk that fluctuations in foreign exchange rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.

Refinancing risk

The risk that maturing borrowings, capital, project or partnership financings cannot be refinanced on terms that reflect the provisions made by the organisation for those refinancings, both capital and current (revenue), and/or that the terms are inconsistent with prevailing market conditions at the time.

Legal and regulatory risk

The risk that the organisation itself, or an organisation with which it is dealing in its treasury management activities, fails to act in accordance with its legal powers or regulatory requirements, and that the organisation suffers losses accordingly.

Fraud, error and corruption, and contingency management

The risk that an organisation fails to identify the circumstances in which it may be exposed to the risk of loss through fraud, error, corruption or other eventualities in its treasury management dealings, and fails to employ suitable systems and procedures and maintain effective contingency management arrangements to these ends. It includes the area of risk commonly referred to as operational risk.

Market risk

The risk that, through adverse market fluctuations in the value of the principal sums an organisation borrows and invests, its stated treasury management policies and objectives are compromised, against which effects it has failed to protect itself adequately.

Managing treasury management risks

CIPFA believes that the substantial majority of public service organisations embody within their business or service planning processes the means by which they can identify treasury management risks. It also believes that many are familiar with and have implemented methods by which those risks can be successfully managed and contained. If an organisation is not so doing, it is unlikely to be treating the subject of risk management with sufficient priority.

For an organisation to manage and contain its risks successfully, it must first identify what they might be, and consider to what extent it is able and prepared to suffer the consequences of those risks impacting adversely on its finances. To the extent that it is unable or unprepared to bear those consequences, it should be seeking to protect itself against that eventuality.

As part of its business or service planning processes, an organisation needs to put in place the following:

- **well documented records of the standing of counterparties it does or may deal with, and continuous access to independent sources of advice and information on the same**

All public service organisations need to be alert to the prospect of the counterparties they deal with being unable or unwilling to fulfil their contractual responsibilities, especially as a result of failure to maintain their credit status. This applies not only to contracts relating to capital financing and investment, but also to those concerned with the increasing reliance placed by public service organisations on outsourcing.

Organisations should clearly specify the minimum acceptable credit quality of its counterparties. This should be monitored regularly through the published credit ratings (where available) for both the institution and the country of investment. Organisations should be aware of the differences in how they are rated, what is being measured by each agency and any forward-looking rating warnings.

Know your counterparty is a key principle; organisations should not rely on credit ratings alone for their understanding of counterparties. Credit ratings remain a key source of information but it is important to recognise that they do have limitations. Organisations are advised to have regard to the ratings issued by all three main agencies – Fitch, Moody's and Standard & Poor's – and to make their decisions based on all ratings. Ratings should be kept under regular review and 'ratings watch' notices acted upon.

Credit ratings should only be used as a starting point when considering credit risk. Organisations should make use of generally available market information, such as the quality financial press, market data and information on government support for banks, including the ability and willingness of the relevant government to provide adequate support.

As a general rule, however, organisations need a sound diversification policy with high credit quality counterparties. Such a policy is needed to prevent overreliance on a small number of counterparties and should also consider country, sector and group limits.

- **an effective cash and cash flow forecasting and monitoring system which will identify the extent to which the organisation is exposed to the effects of potential cash flow variations and shortfalls**

For most public service organisations, the prospect of an ongoing liquidity shortage is remote. Such is the nature of their income sources that they are generally more involved with the effective management of surplus liquidity than with concerns over cash flow difficulties. That said, organisations should be mindful of the additional cost implications of unanticipated borrowing for the short term.

It is for each organisation to determine what resources to devote to the forecasting and monitoring of its cash balances and to managing the investment of its surplus liquidity, not only in the light of its own circumstances, but also within the context of the statutory and regulatory regimes applying to its treasury management activities.

The minimum requirement should be that the organisation's liquidity targets are secured, and for this reason alone, every public service organisation should strive for reliability and accuracy in its cash flow forecasting and monitoring. An organisation that decides to devote substantially more resources than necessary to achieve this will need to be in a position to make a reasoned judgement as to whether the cost of those resources is warranted by the beneficial effect it secures on its investment returns.

Section 1.8 of these guidance notes provides further guidance on the management of cash and cash flows.

- **access to financial market commentaries and reviews on the likely future courses of interest rates, exchange rates and inflation, to enable it to assess future treasury risks and scenarios, and to permit the effective management and control and development of suitable risk management strategies**

Public service organisations are subject to exposures to fluctuations in interest rates and exchange rates. A common requirement, however, is for organisations to define their policies and practices in order to deliver the necessary degree of certainty for their plans and budgets. At the same time, however, they need to understand how fluctuations in market conditions impact upon yields and allow sufficient flexibility both to take advantage of potentially advantageous changes in market conditions and to mitigate the effects of potentially disadvantageous changes.

An organisation's treasury management strategy should detail how this risk is being addressed. Should interest rates not follow their likely course this should be reported during the year. The annual treasury strategy should not need updating.

The trade-off between certainty and flexibility is very much a matter of individual choice, within whatever statutory or regulatory framework exists. Public service organisations need to be aware of the potential costs and benefits of those choices. Access to external sources of data and analysis can be an essential ingredient of making informed decisions. The credibility of the sources used is likely to be greater if it can be demonstrated that they are unbiased and not susceptible to conflicts of interest.

Where an organisation seeks to manage its exposures to interest rate or exchange rate fluctuations by the use of specific financial instruments such as derivatives, it should be clear about its policies in its annual strategy. It should only use such instruments for the prudent management of its financial affairs and should fully understand the instruments and the risks it is managing.

- **reliable records and forecasts of the terms and the maturities of its borrowings, capital, project and partnership funding, to allow it to plan the timing of, and successfully negotiate appropriate terms for, its refinancings**

Uncertainty over market conditions at times of renegotiating or replacing borrowings or other market financings is an inevitable consequence of the need for most public service organisations to raise long-term funding. This uncertainty can be reduced, however, if an organisation ensures it has reliable records of its maturities and allows itself time to plan well in advance of its need to negotiate. The effective management and, in particular, the avoidance of a bunching in its maturities can reduce the prospect of having to negotiate at a time that is unfavourable to the organisation.

- **comprehensive documentation of the organisation's own legal powers and regulatory requirements, and of those of its counterparties, to allow it to assess the potential for illegal or irregular dealings in its treasury management activities**

Instances of public service organisations exceeding their legal powers or contravening regulatory controls are rare, since they are almost invariably prescribed very precisely. On the occasions this has occurred, however, the implications have usually been serious, and the problems so created have proved difficult to resolve, especially where they have involved commercial counterparties. It remains essential, therefore, that organisations maintain and make access widely available to up-to-date records of their powers and of the regulatory regime under which they undertake their treasury management activities. They should confirm, if requested to do so by counterparties, the powers and authorities under which they effect transactions with them. Equally importantly, they should question and establish the powers of those with whom they enter into transactions.

- **full analysis and records of the processes pursued in making treasury management decisions, and in executing transactions, to enable an organisation to create a successful audit trail, and to allow it to assess the need for contingency arrangements**

Sections 1.5 and 1.6 of these guidance notes draw attention to the need for clarity of organisation, reporting arrangements and management information systems and controls. As a natural extension of these, the requirement to demonstrate openness and accountability in their treasury management activities demands that public service organisations create and maintain an audit trail of their treasury management decisions and transactions. This is necessary not only to minimise the risk of being challenged over whether they pursued due processes, but also to help meet unforeseen events. These will include back-up measures to cope with staff absences and the destruction of treasury management records, as well as effecting suitable insurance arrangements. All of these need to be kept up to date. Further guidance on the issues to be considered when making treasury management decisions is given in Section 1.3 of these guidance notes.

- **comprehensive records of an organisation's contractual responsibilities and liabilities under treasury management contracts with counterparties, to enable it to fulfil its obligations thereunder**

Maintaining good working relationships with counterparties can be a vital way of ensuring the smooth running of an organisation's treasury management function. This relates not only to ensuring that timely and accurate payments are made under agreements, but also to good housekeeping matters such as the production of information and accounts.

- **reliable information about the potential for fluctuations in the market value of its investments, borrowings, derivatives and other financings, to allow an informed assessment of the potential for capital growth or capital reduction**

The maintenance of the capital value of their funds, and the effective control of any liabilities that may be subject to market fluctuations, should be high priorities for every public service organisation. Taxation issues are frequently difficult to evaluate and quantify, and can have significant consequences for the activities of some public service organisations. Control over these issues demands that organisations have a complete understanding of those treasury management instruments and techniques which are subject to market fluctuations prior to their being used. They should maintain full records of transactions, track actual and potential movements in values, and be familiar with the methods available to limit any potential losses.

When undertaking reviews of risk it is important for an organisation to consider any optionality it may have in relation to its investments or borrowings, ie any instruments which have built-in options for borrowers or lenders. For example, the repayment of a loan arising through the exercise of a Lender's Option, Borrower's Option (LOBO) agreement could alter an organisation's exposure to liquidity, interest rate, refinancing or market risk.

1.2 PERFORMANCE MEASUREMENT IN THE PUBLIC SERVICES

CIPFA advocates the principle that all public service organisations should create appropriate methods by which the performance of their treasury management activities can be measured. They can thereby help to judge whether they are gaining value for money from the resources devoted to these activities, particularly in meeting their wider business and service objectives.

CIPFA recognises the difficulties organisations face in achieving an appropriate balance between risk containment and value for money, but believes that the overriding need for effective risk management should be reflected in their treasury management policy statement and treasury management practices.

Performance measurement is a process designed to calculate the effectiveness of a portfolio's or manager's investment returns or borrowing costs, and the application of the resulting data for the purposes of comparison with the performance of other portfolios or managers, or with recognised industry standards or market indices.

The benefits and applications of performance measurement in the public services include:

1. using past experience beneficially to future treasury management policies and practices
2. by developing an appreciation of the factors influencing performance, improving the future processes of treasury decision-making
3. allowing organisations to assess the potential for adding value through changes to the existing ways in which a portfolio is managed
4. demonstrating an awareness of the need to review regularly the value attached to the treasury management function, and enhancing accountability
5. enhancing the information available to organisations when seeking to review an existing manager's performance or when selecting a new manager

6. permitting an informed judgement and decision about the merits or otherwise of using new treasury management instruments or techniques.

These guidance notes are not intended as a comprehensive guide to the subject of performance measurement in the public services. However, the following general points may serve to assist organisations to avoid some of the most frequently encountered difficulties. CIPFA stresses the need for organisations to be aware of the possibly considerable costs involved in performance measurement and to evaluate the justification for incurring those costs in the context of the potential benefits.

The selection of appropriate measures and benchmarks is critical to securing value from performance measurement. Their precise nature and construction needs to be fully understood to reduce the likelihood of reaching misleading conclusions and, therefore, making ill-informed decisions. All benchmarking should consider risk as well as return. For example, when selecting appropriate measures by which to judge the investment performance of a cash investment portfolio, there are merits in selecting market indices that closely match the organisation's own cash investment and risk profiles. Alternatively, it may be useful to compare performance with indices that demonstrate the performance the organisation might have expected to achieve had it handled its investment activities differently, especially to judge the relative benefits of passive and active investment management.

Caution should be applied when analysing the performance of other organisations as it is important to establish whether the characteristics of their treasury management activities are truly comparable. It is misleading, for example, to draw conclusions about the respective performances of different organisations without first establishing the positions they take with regard to risk, since this can materially influence investment performance. It is similarly unhelpful to make comparisons between the performance of investment funds that are internally managed and those that are invested by firms of external investment managers. The latter are frequently able to make longer-term investment decisions, whereas the former often deal only with peaks and troughs of the organisation's cash flows.

1.3 DECISION-MAKING AND ANALYSIS IN THE PUBLIC SERVICES

CIPFA considers it vital that the treasury management decisions of organisations in the public services should be subjected to prior scrutiny. The treasury management strategy is approved annually by full board/council, which is a strength. This should be supplemented by the provision of monitoring information and regular review by board members/councillors in both executive and scrutiny functions. It also believes that records should be kept of the processes and the rationale behind those decisions. This is necessary not only for the purpose of allowing a historical assessment of the effectiveness of such decisions, but also as a means of ensuring that appropriate checks and safeguards are in place in the event, for example, of it becoming necessary to demonstrate the legality or probity of transactions. However, in determining the records to be kept, realism is needed to avoid creating a system that may overburden resources and outweigh the potential benefits.

The nature and scope of a particular organisation's treasury management function will determine the precise issues to be considered in reaching treasury management decisions, and the analysis and the methodology to be applied.

However, CIPFA gives the following general guidance on the issues to be considered in connection with various aspects of an organisation's treasury management activities, and which an organisation should demonstrate it has considered.

In respect of every decision made the organisation should:

- above all, be clear about the nature and extent of the risks to which the organisation may become exposed
- be certain about the legality of the decision reached and the nature of the transaction, and that all authorities to proceed have been obtained
- be content that the documentation is adequate both to deliver the organisation's objectives and protect the organisation's interests, and to deliver good housekeeping
- ensure that counterparties are judged satisfactory in the context of the organisation's creditworthiness policies, and that limits have not been exceeded
- be content that the terms of any transactions have been fully checked against the market, and have been found to be competitive.

In respect of borrowing and other funding decisions, the organisation should:

- consider the ongoing revenue liabilities created, and the implications for the organisation's future plans and budgets
- evaluate the economic and market factors that might influence the manner and timing of any decision to fund
- consider the merits and demerits of alternative forms of funding, including funding from revenue, leasing and private partnerships
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use and, if relevant, the opportunities for foreign currency funding.

In respect of investment decisions, the organisation should:

- consider the optimum period, in the light of cash flow availability and prevailing market conditions
- consider the alternative investment products and techniques available, especially the implications of using any which may expose the organisation to changes in the value of its capital.

In respect of decisions regarding derivatives, the organisation should:

- be able to demonstrate that the derivative transaction has reduced the organisation's overall exposure to treasury risks.

1.4 APPROVED INSTRUMENTS, METHODS AND TECHNIQUES

CIPFA's recommended wording of an organisation's treasury management practices makes clear the importance it attaches to defining the boundaries of the treasury management function. This should embrace not only the organisation's treasury management activities, but also the instruments, methods and techniques it may use. There is a wide variety of legal and regulatory frameworks for different public service organisations in this respect.

The matters CIPFA considers it desirable for all organisations to include in the schedules to their treasury management practices are listed in Section 2 of these guidance notes. The following paragraphs explain why CIPFA considers it important that organisations are clear about the treasury management instruments, methods and techniques they may use.

As a general rule, the organisations that comprise the public services are not driven by commercially motivated objectives. That is not to say they are unaware of the need to be efficient in the way they run their services and businesses. It implies that they have influences on their activities which demand that wider issues be taken into account when reaching decisions, notably the need to protect public funds.

The legal and regulatory frameworks governing their activities reflect this in the overriding requirement to control risk. However, many organisations in the public services have the necessary statutory authority to employ treasury management instruments which, if not properly controlled, can expose an organisation to considerable risk.

It is therefore CIPFA's view that organisations need to consider carefully whether they are equipped with the skills and experience to evaluate and control the risks and advantages associated with using the instruments available to them before including them in their approved list, even if they are legally permitted to do so.

In certain parts of the public services, regulation prescribes formal processes to determine whether a particular organisation should be allowed access to the full range of instruments available to them. Whether this is or is not a feature of an organisation's regulatory controls, CIPFA believes that an organisation should regularly make an assessment of its treasury management skills and resources when reviewing its approved list.

This is especially true of organisations which have traditionally placed reliance on brokers and other market practitioners to introduce them to, and to help them evaluate and execute, transactions involving novel techniques, the risks of which may not be immediately or wholly apparent.

1.5 ORGANISATION, CLARITY AND SEGREGATION OF RESPONSIBILITIES, AND DEALING ARRANGEMENTS

CIPFA considers that there are certain organisational features that should be commonly applied to the treasury management activities of all public service organisations, regardless of their size, functions and resources. These relate both to the boards/councils responsible for creating and monitoring policy issues and to the officers responsible for managing and executing decisions.

Officers involved in treasury management must be explicitly required to follow treasury management policies and procedures.

As regards officer responsibilities, CIPFA considers it vital that there should be a clear division of responsibilities, including a written statement of the duties of each post engaged in treasury management. It is especially important that staff responsible for negotiating and closing deals are not responsible for recording them, or for maintaining the cash book. Also, staff who are executing the deals should not be responsible for checking compliance with policies and procedures. This is in order to create a framework for internal check, and reflects both the variety of activities in treasury management and the often very large sums involved.

CIPFA recognises that in smaller organisations and those with limited resources, this is more difficult to achieve. Nevertheless, it is a principle to be acknowledged universally, and applied as far as is reasonably practicable.

CIPFA considers clearly defined responsibilities for the approval and scrutiny of treasury management activities to be an essential element of a public service organisation's treasury management arrangements.

The Code recommends the adoption of the following:

This organisation (ie full board/council) will receive reports on its treasury 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.

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 and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

This organisation nominates [note 3] to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

Note 1: name of responsible body (for example, committee, board or council) or nominated group of individuals or relevant committee such as cabinet or executive.

Note 2: title of responsible officer (for the purposes of this Code, the term 'responsible officer' has been used, although it is recognised that, in practice, many different terms exist). For example in higher education, the vice-chancellor/principal or equivalent is the 'designated officer' who will ensure that the governing body complies with all the terms and conditions of funding provided by the funding body. However it is usual for day-to-day financial management to be delegated to a director of finance who will take professional responsibility for such areas of an institution's work and this is the officer who is referred to here.

Note 3: name of responsible body (for example, committee, board or council) or nominated group of individuals or relevant committee such as audit committee or relevant scrutiny committee.

Source: The Code – Clauses to be Formally Adopted

The following is a list of the main tasks involved in treasury management and a suggested allocation of responsibilities.

(i) Full board/council

- receiving and reviewing reports on treasury management policies, practices and activities
- approval of annual strategy.

(ii) Boards/committees/council/responsible body

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices
- budget consideration and approval
- approval of the division of responsibilities

- receiving and reviewing regular monitoring reports and acting on recommendations
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Body/person(s) with responsibility for scrutiny

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

(iv) The responsible officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers.

(v) Treasury manager

- execution of transactions
- adherence to agreed policies and practices on a day-to-day basis
- maintaining relationships with counterparties and external service providers
- supervising treasury management staff
- monitoring performance on a day-to-day basis
- submitting management information reports to the responsible officer
- identifying and recommending opportunities for improved practices.

The allocation of responsibilities for tasks in (ii) to (iv) above may be influenced by other, wider issues in the way an organisation structures its treasury management function; however, overall responsibility for treasury management cannot be devolved. Each organisation needs to decide on the arrangements most suited to its particular circumstances for the purpose of achieving these aims, although certain organisations in the public services have particular statutory or regulatory responsibilities placed on their officers and board/committee members.

A further principle which is critical to the effectiveness of a treasury management function is the recognition of the benefits to be gained from centralising the resources devoted to the function, and having an integrated system for overall control. Centralisation and system integration can bring several benefits, including:

- economies of scale
- a single point of control
- coherence of treasury activities

- pooling of expertise
- ease of communications.

1.6 REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS

A key recommendation of the Code is that an organisation's treasury management policy statement should specify formal reporting arrangements by the responsible officer to full board/council, to include at minimum annual reports both before, mid-year and after the year-end. The monitoring reports for local authorities should include the treasury management indicators detailed in the sector-specific guidance notes.

The details of each organisation's reporting arrangements will be a matter for local decision, but in CIPFA's view, there should at least be a mechanism for reviewing the organisation's policies, and for assessing the effectiveness of the last year's treasury management activities and the performance of the treasury management function.

The reporting arrangements should consider the frequency of reporting, the level of detail reported and also the level within the organisation in which reporting takes place. The reporting arrangements should be a minimum, with additional reporting undertaken as deemed necessary to ensure that those responsible for treasury management are kept fully informed.

The following is a suggested process for reporting to the organisation (ie full board/council) and the body responsible for scrutiny. In many cases, additional reporting on a 'by exception' basis may be appropriate.

Annual reporting requirements before the start of the year

- review of the organisation's approved clauses, treasury management policy statement and practices
- strategy report on proposed treasury management activities for the year.

Mid-year review

- activities undertaken
- variations (if any) from agreed policies/practices
- interim performance report
- regular monitoring
- monitoring of treasury management indicators for local authorities.

Annual reporting requirements after the year-end

- transactions executed and their revenue (current) effects
- report on risk implications of decisions taken and transactions executed
- compliance report on agreed policies/practices, and on statutory/regulatory requirements
- performance report
- report on compliance with CIPFA Code recommendations
- monitoring of treasury management indicators for local authorities.

The detail to be included in these reports will vary depending on an organisation's circumstances. Some organisations may report full details, for example, of transactions undertaken, whilst others will report only summarised information.

Whatever form the reports take, they should ensure, as a minimum, that those with ultimate responsibility for the treasury management function appreciate fully the implications of treasury management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

Regular and meaningful management information on day-to-day activities is also an essential characteristic of an effectively organised treasury management function. The form and frequency of management reports will reflect the scope and nature of an organisation's treasury management activities.

1.7 BUDGETING, ACCOUNTING AND AUDIT ARRANGEMENTS

CIPFA recommends that all public service organisations bring together, for budgeting and management control purposes, all of the costs and revenues associated with an organisation's treasury management activities, regardless of how the organisation has actually organised the treasury management function. This enhances accountability, improves awareness of the resource implications of the function, permits the setting of meaningful performance measures, and increases the effectiveness of value for money and comparative reviews.

Budgeting and accounting for treasury management in the public services differ markedly between the various bodies which comprise it, and are often prescribed by statute or regulation, or are the subject of recognised conventions. As a minimum, however, CIPFA recommends that all organisations' treasury management budgets and accounts should clearly identify:

- staffing numbers and related costs
- premises and other administrative costs
- interest and other investment income
- debt and other financing costs (or charges for the use of assets)
- bank and overdraft charges
- brokerages, commissions and other transaction-related costs
- external advisers' and consultants' charges.

It is normal practice for the external auditor to have access to all papers supporting and explaining the operation and activities of the treasury management function. The auditor will be expected to enquire as to whether the Code has been adopted, and whether its principles and recommendations have been implemented and adhered to. Any serious breach of the Code's recommendations should be brought to the external auditor's attention.

1.8 CASH AND CASH FLOW MANAGEMENT

CIPFA believes that the preparation of cash flow projections on a regular and timely basis provides a sound framework for effective cash management in the public services. Procedures for their preparation and review/modification, the periods to be covered, sources of data, etc should be an integral part of the schedules to an organisation's approved treasury management practices.

There are substantial differences between the various sectors within the public services in the nature and profiles of their cash flows and, therefore, in their cash flow management practices and requirements.

CIPFA recommends that every public service organisation should, as a minimum, prepare cash and cash flow management forecasts and actuals so as to be able to determine:

- whether minimum acceptable levels of cash balances plus short-term investments might be (or have been) breached
- the adequacy (or otherwise) of standby/overdraft facilities or other contingency arrangements
- the optimum arrangements to be made for investing and managing surplus cash.

CIPFA also believes that organisations should put in place proper policies and practices concerning the management of their relationships with their debtors and creditors. As a minimum, CIPFA believes these should include:

- payment scheduling to take account of cash flow and agreed terms of trade
- pricing and charging policies
- monitoring the levels of debtors and creditors to enable corrective action for cash flow purposes
- making effective use of clearing bankers' services, particularly concerning clearance of funds and low-cost funds transmission.

1.9 MONEY LAUNDERING

Money laundering has the objective of concealing the origin of money generated through criminal activity. Legislation has given a higher profile to the need to report suspicions of money laundering. The Proceeds of Crime Act (POCA) 2002 established the main offences relating to money laundering. In summary, these are:

- concealing, disguising, converting, transferring or removing criminal property from England and Wales, from Scotland or from Northern Ireland
- being concerned in an arrangement which a person knows or suspects facilitates the acquisition, retention, use or control of criminal property
- acquiring, using or possessing criminal property.

These apply to all persons in the UK in a personal and professional capacity. Any person involved in any known or suspected money-laundering activity in the UK risks a criminal conviction.

Other offences under the POCA include:

- failure to disclose money-laundering offences
- tipping off a suspect, either directly or indirectly

- doing something that might prejudice an investigation – for example, falsifying a document.

The Terrorism Act 2000 made it an offence of money laundering to become concerned in an arrangement relating to the retention or control of property likely to be used for the purposes of terrorism, or resulting from acts of terrorism. All individuals and businesses in the UK have an obligation to report knowledge, reasonable grounds for belief or suspicion about the proceeds from, or finance likely to be used for, terrorism or its laundering, where it relates to information that comes to them in the course of their business or employment.

Organisations pursuing relevant business were required to appoint a nominated officer and implement internal reporting procedures; train relevant staff in the subject; establish internal procedures with respect to money laundering; obtain, verify and maintain evidence and records of the identity of new clients and transactions undertaken and report their suspicions.

In December 2007 the UK Government published the Money Laundering Regulations 2007, which replaced the Money Laundering Regulations 2003.

In order to ensure compliance is appropriately managed, businesses will need to ensure sufficient senior management oversight, appropriate analysis and assessment of the risks of clients and work/product types, systems for monitoring compliance with procedures and methods of communicating procedures and other information to personnel.

Public service organisations and their staff are subject to the full provisions of the Terrorism Act 2000 and may commit most of the principal offences under the POCA, but are not legally obliged to apply the provisions of the Money Laundering Regulations 2007. However, as responsible public bodies, they should employ policies and procedures which reflect the essence of the UK's anti-terrorist financing, and anti-money laundering, regimes and it is for individual organisations to evaluate the prospect of laundered monies being handled by them, and to determine the appropriate safeguards to be put in place. It is the legal responsibility of every person engaged in treasury management to make themselves aware of their personal responsibilities, but CIPFA recommends that organisations bring them to their staff's attention and consider the appointment of a member of staff to whom they can report any suspicions.

For more on the application of the UK anti-money laundering regime to public authorities, see the guidance in 2009 CIPFA publication *Combating Financial Crime*.

1.10 TRAINING AND QUALIFICATIONS

All public service organisations should be aware of the growing complexity of treasury management in general, and its application to the public services in particular. Modern treasury management demands appropriate skills, including a knowledge of money and capital market operations, an awareness of available sources of funds and investment opportunities, an ability to assess and control risk, and an appreciation of the implications of legal and regulatory requirements.

Every public service organisation should secure the necessary training, having assessed the professional competence of both those involved in the treasury management function and those with a policy, management or supervisory role. Arrangements to ensure the availability of suitable skills and resources should recognise the prospect that staff absences may, at times, demand that others step in who do not normally have involvement on a day-to-day basis with the treasury management function.

Public service organisations have a responsibility to ensure that those charged with governance have access to the skills and knowledge they require to carry out this role effectively. The organisation should ensure that this also applies to treasury management.

Those charged with governance also have a personal responsibility to ensure that they have the appropriate skills and training for their role.

1.11 USE OF EXTERNAL SERVICE PROVIDERS

There are substantial numbers of service providers available to support the treasury management activities of public service organisations. The skills of the in-house team should be maintained in order to ensure that the services provided can be challenged and that undue reliance is not placed upon them.

One of the most active and long-standing service providers have been the money-broking companies, whose role it is to act as intermediaries, making introductions between the prospective parties to transactions.

It is not the role of brokers to provide advice on the creditworthiness of those organisations to which public service organisations may lend. They may provide information already in the public domain, but may not interpret it. The use of brokers is a matter for local decision. But it is considered good practice, if their services are used, to ensure that business is spread between a reasonable number of them, and certainly no fewer than two.

Direct dealing with principals is a not uncommon feature of treasury management in the public services which, if nothing else, can provide a useful check on brokers' performance.

An issue that causes some debate is whether it is necessary or desirable for public service organisations to tape conversations with brokers and principals. This is a matter for local discretion, particularly in the context of the costs involved, but is generally to be recommended.

Most public service organisations require the services of clearing bankers, and a growing number make use of the services of a wider group of banks, particularly to meet their need for private finance and partnership funding.

There has also been a growing tendency for public service organisations to employ external advisers and consultants, often for the purposes of a general treasury management advisory service, but also for specific purposes, such as the securing and structuring of funding and for partnership arrangements.

Further, many public service organisations employ the services of external investment managers to help manage their surplus cash and, where relevant, their pension fund, trust fund or endowment fund assets.

Other external providers may include software providers, investment banks and credit rating agencies.

CIPFA advises all organisations using the services of external service providers to document comprehensively the arrangements made with them, to be clear as to the services provided and to ensure that these meet the organisation's needs. Services should be subject to regular competition which would usually be via a competitive tendering process.

Organisations should be mindful of the requirements of the Bribery Act 2010 in their dealings with external providers.

The overall responsibility for treasury management must always remain with the organisation.

1.12 CORPORATE GOVERNANCE

The Code recommends that public service organisations state their commitment to embracing the principles of corporate governance in their treasury management activities, notably openness and transparency.

It is CIPFA's view that:

- adoption of the principles and policies promoted in the Code and in these guidance notes will in itself deliver the framework for demonstrating openness and transparency in an organisation's treasury management function
- publication of and free access to information about an organisation's treasury management transactions and other public documents connected with its treasury management activities will further assist in achieving this end
- establishing clear treasury management policies, the separation of roles in treasury management and the proper management of relationships both within and outside the organisation will establish the integrity of the function
- robust treasury management organisational structures, together with well-defined treasury management responsibilities and job specifications, will enhance accountability
- equality in treasury management dealings, absence of business favouritism and the creation of keen competition in treasury management will lay the groundwork for fairness.

The following paragraphs further emphasise the practices that CIPFA believes an organisation should employ to ensure the principles of corporate governance are successfully implemented.

Procedural responses

The policies and strategies of treasury management should link clearly to the organisation's other key policies and strategies. In the management of risk, in particular, treasury risk management should be an integral part of its overall risk management processes, culminating in a well-defined, organisation-wide strategy for the control of risk and contingency planning.

The management and administration of treasury management should be robust, rigorous and disciplined. Over the years, some of the most significant examples of treasury mismanagement, in both the public services and the private sector, have resulted from procedural indiscipline. This has frequently been as a result of a failure to apply otherwise well-documented management and administration systems, or through failures in transmission, documentation or deal-recording processes.

Reporting arrangements should be applied so as to ensure that those charged with responsibility for the treasury management policy have all the information necessary to enable them to fulfil openly their obligations; and that all stakeholders are fully appraised of and consulted on the organisation's treasury management activities on a regular basis.

The procedures for monitoring treasury management activities through audit, scrutiny and inspection should be sound and rigorously applied, with an openness of access to information and well-defined arrangements for the review and implementation of recommendations for change.

The application and interpretation of performance data should be clear, concise and relevant to the organisation's treasury management activities.

Stewardship responsibilities

The responsible officer should ensure that systems exist to deliver proper financial administration and control, and a framework for overseeing and reviewing the treasury management function.

As regards a control framework, an organisation's formal policy documents should define clearly procedures for monitoring, control and internal check.

With regard to delegation, it is vitally important that those involved in the implementation of treasury management policies and the execution of transactions are unambiguously empowered to undertake their tasks, and that reporting lines are well defined.

An organisation's adoption of and adherence to the Code should be widely broadcast, as should the principles of the Code and the method of its application in the organisation.

The organisation's procedures for reviewing the value of the treasury management function, and the implementation of opportunities for improvement, should be both continuous and open to examination.

The governance of others

In respect of the organisation's dealings with counterparties, external service providers and other interested parties, clear procedures should exist to enable the organisation, as far as is practicable, to monitor their adherence to the legal or regulatory regimes under which they operate.

Where external funds are managed on behalf of a third party or pension fund, these funds should be separately identifiable and income and expenditure attributed in line with an agreed policy.

SECTION 2

Suggested schedules to accompany an organisation's statement of its treasury management practices

The following paragraphs give suggestions to public service organisations on the schedules they might prepare and maintain in support of their approved treasury management practices. CIPFA suggests that these schedules be maintained and updated as necessary, and that they form an integral part of an organisation's treasury management manual.

Additionally, where documentation or contracts exist, for example as evidence of relationships with external service providers, CIPFA suggests that their existence should be referred to in the schedules, and that a full copy, or at minimum a brief summary, of their terms, conditions, maturity dates and renewal arrangements should be appended.

CIPFA recognises that not all these schedules will be relevant or appropriate to every organisation covered by the Code and these guidance notes.

RISK MANAGEMENT

Credit

- criteria to be used for creating/managing approved counterparty lists/limits
- approved methodology for changing limits and adding/removing counterparties
- full individual listings of counterparties and counterparty limits
- country, sector and group listings of counterparties and the overall limits applied to each, where appropriate
- details of credit rating agencies' services and their application
- description of the general approach to collecting and using information other than credit ratings for counterparty risk assessment.

Liquidity

- amounts of approved minimum cash balances and short-term investments
- details of:
  - standby facilities

  - bank overdraft arrangements
  - short-term borrowing facilities
  - insurance/guarantee facilities
  - other contingency arrangements
- policy in terms of borrowing in advance of need.

Interest rate

- details of approved interest rate exposure limits
- trigger points and other guidelines for managing changes to interest rate levels
- minimum/maximum proportions of variable rate debt/interest
- minimum/maximum proportions of fixed rate debt/interest
- policies concerning the use of financial derivatives for interest rate risk management.

Exchange rate

- details of approved exchange rate exposure limits for cash investments/debt
- approved criteria for managing changes in exchange rate levels
- policies concerning the use of financial derivatives for exchange rate risk management.

Refinancing

- debt/other capital financing maturity profiling, policies and practices
- projected capital investment requirements
- policy concerning limits on revenue consequences of capital financings.

Legal and regulatory

- references to relevant statutes and regulations
- procedures for evidencing the organisation's powers/authorities to counterparties
- required information from counterparties concerning their powers/authorities
- statement on the organisation's political risks and management of same.

Fraud, error and corruption, and contingency management

- details of systems and procedures to be followed, including internet services
- emergency and contingency planning arrangements
- insurance cover details.

Market value of investments

- details of approved procedures and limits for controlling exposure to investments whose capital value may fluctuate (gilts, CDs, etc).

PERFORMANCE MEASUREMENT

- methodology to be applied for evaluating the impact of treasury management decisions
- policy concerning methods for testing value for money in treasury management, eg:
  - frequency and processes for tendering
  - banking services
  - money-broking services
  - cash/fund management services
  - consultants'/advisers' services
  - other providers' services
- methods to be employed for measuring the performance of the organisation's treasury management activities
- benchmarks and calculation methodology with regard to risk and return:
  - debt management
  - investment.

DECISION-MAKING AND ANALYSIS

- funding, borrowing, lending, and new instruments/techniques:
  - records to be kept
  - processes to be pursued
  - issues to be addressed.

APPROVED INSTRUMENTS, METHODS AND TECHNIQUES

- listings and individual limits for the use of:
  - approved instruments
  - approved methods
  - approved techniques.

ORGANISATION, CLARITY AND SEGREGATION OF RESPONSIBILITIES, AND DEALING ARRANGEMENTS

- limits to responsibilities/discretion at committee/executive levels
- principles and practices concerning segregation of duties
- treasury management organisation chart
- statement of duties/responsibilities of each treasury post
- absence cover arrangements
- dealing limits
- list of approved brokers
- policy on brokers' services
- policy on taping of conversations

- direct dealing practices
- settlement transmission procedures
- documentation requirements
- arrangements concerning the management of counterparty funds.

REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS

- content and frequency of board/committee reporting requirements
- content and frequency of management information reports.

BUDGETING, ACCOUNTING AND AUDIT ARRANGEMENTS

- statutory/regulatory requirements
- accounting practices and standards
- list of information requirements of external auditors.

CASH AND CASH FLOW MANAGEMENT

- arrangements for preparing/submitting cash flow statements
- content and frequency of cash flow budgets
- listing of sources of information
- bank statements procedures
- payment scheduling and agreed terms of trade with creditors
- arrangements for monitoring debtor/creditor levels
- procedures for banking of funds
- practices concerning prepayments to obtain benefits.

MONEY LAUNDERING

- procedures for establishing identity/authenticity of lenders
- methodology for identifying sources of deposit.

TRAINING AND QUALIFICATIONS

- details of approved training courses
- details of approved qualifications
- details of qualifications of treasury staff
- records of training received by treasury staff
- records of training received by those charged with governance.

USE OF EXTERNAL SERVICE PROVIDERS

- details of contracts with service providers, including bankers, brokers, consultants, advisers and details of the services provided
- regulatory status of services provided
- procedures and frequency for tendering services.

CORPORATE GOVERNANCE

- list of documents to be made available for public inspection
- procedures for consultation with stakeholders
- list of external funds managed on behalf of others and the basis of attributing interest earned and costs to these investments.

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