Finance & Audit Scrutiny Panel

Grand Jury Room, Town Hall

29 July 2008 at 6:00pm

The Finance and Audit Scrutiny Panel deals with the review of service areas and associated budgets, and monitors the financial performance of the Council, and the operational performance of the Council. The panel scrutinises the Council's audit arrangements, including the annual audit letter and audit plans, and Portfolio Holder 'Service' decisions reviewed under the Call in procedure.

Information for Members of the Public

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There is wheelchair access to the Town Hall from West Stockwell Street. There is an induction loop in all the meeting rooms. If you need help with reading or understanding this document please take it to Angel Court Council offices, High Street, Colchester or telephone (01206) 282222 or textphone 18001 followed by the full number that you wish to call, and we will try to provide a reading service, translation or other formats you may need.

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Terms of Reference

Finance and Audit Scrutiny Panel

- To review all existing service plans and associated budget provisions against options for alternative levels of service provision and the corporate policies of the Council, and make recommendations to the Cabinet

- To have an overview of the Council's internal and external audit arrangements and in particular with regard to the annual audit plan, the audit work programme and progress reports, and to make recommendations to the Cabinet

- To monitor the operational and financial performance of the Council, and to make recommendations to the Cabinet in relation to operational performance, financial outturns, revenue and capital expenditure monitors

- To scrutinise the Audit Commission's annual audit letter

- To scrutinise progress made on best value action plans

- To scrutinise executive 'service' decisions made by Portfolio Holders and officers taking key decisions which have been made but not implemented referred to the Panel through the call-in procedure

    The panel may a) confirm the decision, which may then be implemented immediately, b) refer the decision back to the decision taker for further consideration setting out in writing the nature of its concerns, or c) refer the matter to full Council in the event that the Panel considers the decision to be contrary to the Policy Framework of the Council or contrary to, or not wholly in accordance with the Budget.

COLCHESTER BOROUGH COUNCIL
FINANCE & AUDIT SCRUTINY PANEL
29 July 2008 at 6:00pm

Members

Chairman	:	Councillor Lissimore.
Deputy Chairman	:	Councillor Willetts.
		Councillors Bentley, Bouckley, Goss, Harris, Maclean, Manning, Offen, Oxford and Sykes.
Substitute Members	:	All members of the Council who are not Cabinet members or members of this Panel.

Agenda - Part A
(open to the public including the media)

Members of the public may wish to note that Agenda items 1 to 5 are normally brief and items 6 to 9 are standard items for which there may be no business to consider.

Pages

1. Welcome and Announcements

(a) The Chairman to welcome members of the public and Councillors and to remind all speakers of the requirement for microphones to be used at all times.

(b) At the Chairman's discretion, to announce information on:

- action in the event of an emergency;
- mobile phones switched to off or to silent;
- location of toilets;
- introduction of members of the meeting.

2. Substitutions

Members may arrange for a substitute councillor to attend a meeting on their behalf, subject to prior notice being given. The attendance of substitute councillors must be recorded.

3. Urgent Items

To announce any items not on the agenda which the Chairman has agreed to consider because they are urgent and to give reasons for the urgency.

4. Declarations of Interest

The Chairman to invite Councillors to declare individually any personal interests they may have in the items on the agenda.

If the personal interest arises because of a Councillor's membership of or position of control or management on:

- any body to which the Councillor has been appointed or nominated by the Council; or
- another public body

then the interest need only be declared if the Councillor intends to speak on that item.

If a Councillor declares a personal interest they must also consider whether they have a prejudicial interest. If they have a prejudicial interest they must leave the room for that item.

If a Councillor wishes to make representations on an item on which they have a prejudicial interest they may do so if members of the public are allowed to make representations. In such circumstances a Councillor must leave the room immediately once they have finished speaking.

An interest is considered to be prejudicial if a member of the public with knowledge of the relevant facts would reasonably regard it as so significant that it is likely to prejudice the Councillor's judgement of the public interest.

Councillors should consult paragraph 7 of the Meetings General Procedure Rules for further guidance.

5. Minutes **1 - 5**

To confirm as a correct record the minutes of the meeting held on 30 June 2008.

6. Have Your Say!

(a) The Chairman to invite members of the public to indicate if they wish to speak or present a petition at this meeting – either on an item on the agenda or on a general matter not on this agenda. You should indicate your wish to speak at this point if your name has not been noted by Council staff.

(b) The Chairman to invite contributions from members of the public who wish to Have Your Say! on a general matter not on this agenda.

7. **Items requested by members of the Panel and other Members**

(a) To evaluate requests by members of the Panel for an item relevant to the Panel's functions to be considered.

(b) To evaluate requests by other members of the Council for an item relevant to the Panel's functions to be considered.

8. **Referred items under the Call in Procedure**

To consider any Portfolio Holder decisions, taken under the Call in Procedure.
The panel may a) confirm the decision, which may then be implemented immediately, b) confirm the decision back to the decision taker for further consideration setting out in writing the nature of its concerns, or c) refer the matter to full Council in the event that the panel considers the decision to be contrary to the Policy Framework of the Council or contrary to, or not wholly in accordance with the Budget.

9. **Decisions taken under special urgency provisions**

To consider any Portfolio Holder decisions taken under the special urgency provisions.

10. **Work Programme 2008-09**

See report from the Scrutiny Officer

11. **2007-08 Risk Management Summary** **6 - 22**

See report from the Head of Resource Management

12. **Annual Report on Treasury Management** **23 - 50**

See report from the Head of Resource Management

13. **Exclusion of the public**

In accordance with Section 100A(4) of the Local Government Act 1972 and in accordance with The Local Authorities (Executive Arrangements) (Access to Information) (England) Regulations 2000 (as amended) to exclude the public, including the press, from the meeting so that any items containing exempt information (for example confidential personal, financial or legal advice), in Part B of this agenda (printed on yellow paper) can be decided. (Exempt information is defined in Section 100I and Schedule 12A of the Local Government Act 1972).

FINANCE & AUDIT SCRUTINY PANEL
30 JUNE 2008

Present :-	Councillor Sue Lissimore (Chairman) Councillors Kevin Bentley, John Bouckley, Martin Goss, Jackie Maclean, Jon Manning, Nigel Offen, Gerard Oxford, Laura Sykes and Dennis Willetts
Also in Attendance :-	Paul Smith
Substitute Member :-	Councillor Dave Naish for Councillor Dave Harris

3. Minutes

The minutes of the meetings on 18 March 2008 and 14 May 2008 were confirmed as a correct record.

Councillor Sue Lissimore (in respect of being a former member of the Board of Colchester Borough Homes) declared a personal interest in the following item pursuant to the provisions of Meetings General Procedure Rule 7(3)

4. Items requested by members of the Panel

Councillor Oxford requested a report giving an update on the Decent Homes Programme, to include information on the number of homes that have received an upgrade and those, by ward or district, that were still to be upgraded, the proposed number of bathroom, windows and doors upgrades and the estimated costs, with assurances that the monitoring procedures in place would avoid duplication of effort.

RESOLVED that the panel agreed to the request for the Head of Strategic Policy and Regeneration to present to the panel at the earliest convenient meeting an update report on the Decent Homes Programme, with an invitation to attend going to the Chairman of Colchester Borough Homes and the Chief Executive of Colchester Borough Homes.

Councillor Sue Lissimore (in respect of being a former member of the Board of Colchester Borough Homes) declared a personal interest in the following item pursuant to the provisions of Meetings General Procedure Rule 7(3)

5. 2008-09 Audit and Inspection Plan

Mr. Paul King, District Auditor and Ms. Christine Connelly, Audit Commission, attended the meeting for this item.

Mr. King introduced the 2008-09 Audit and Inspection Plan, the Audit Commissions proposed work plan for 2008-09 as described in pages 9-10 of the Audit and Inspection Plan. Mr. King confirmed that the three major projects in Colchester, the Community Stadium, Firstsite Newsite and the Housing Repairs contract including the Decent Homes Programme would all remain under constant review.

Mr. King summarised the fees to be charged by the Commission, saying this represented a small increase, and with Colchester's scale fee at -16%, this was the lowest point for any Council in Essex.

In response to Councillor Goss, Mr. King said the detailed audit and inspection fee on page 21 of the plan illustrated and ensured the overall audit and inspection work would be co-ordinated and kept to a minimum.

In response to Councillor Bentley, Mr. King said the Audit Commission was responsible for appointing the auditors for public bodies and could appoint private companies or Audit Commission staff to carry out audits on their behalf. The fee scales were determined by the Audit Commission and apply irrespective of the auditor appointed.

Mr. King acknowledged the concerns raised by Councillor Oxford in respect of the previous arrangements for Decent Homes Programme Contract and the potential problems associated with transactions that may not be properly reflected in the financial statements, and the ongoing risks for any future works.

In response to Councillor Willetts, Mr. King confirmed that the Value for Money exercise on the early cessation of the Decent Homes Contract would include what the decision making process was, the financial outcomes and what legal advice the Council received, plus the risks and benefits of alternative outcomes.

RESOLVED that the panel noted the Audit and Inspection Plan 2008/09.

Councillor Sue Lissimore (in respect of being a former member of the Board of Colchester Borough Homes) declared a personal interest in the following item pursuant to the provisions of Meetings General Procedure Rule 7(3)

6. Work Programme

Councillor Offen proposed a future item, a value for money review of waste recycling, including what we recycle, the way we recycle and the waste stream revenue.

Councillor Manning requested further information on visiting numbers to Leisure World, illustrating peaks and troughs in usage.

In response to Councillor Manning's request, the panel suggested that Councillor Manning should speak to the Portfolio Holder for Culture, Tourism and Diversity.

RESOLVED that:-

i) The panel noted the work programme for 2008/09.

ii) The panel agreed to invite the Head of Street Services to report to the panel on a review of recycling, at the next convenient meeting.

Councillor Sue Lissimore (in respect of being a former member of the Board of Colchester Borough Homes) declared a personal interest in the following item pursuant to the provisions of Meetings General Procedure Rule 7(3)

7. 2007-08 Revenue Expenditure pre-audit outturn

Mr. Steve Heath, Finance Manager, attended the meeting for this item and introduced the report, giving an overview of the year end results for the Pre-Audit Revenue Outturn 2007/08.

In response to Councillor Willetts, Mr. Charles Warboys, Head of Resource Management said that whilst there had not been any litigation or award against the Council in respect of the cessation of the Decent Homes and Housing Repairs Programme Contract, the agreed negotiated settlement of the repairs contract was reflected in the pre-audit revenue outturn for the Housing Revenue Account. Mr. Warboys, Head of Resource Management said the agreed settlement figure was paid for all completed works.

Councillor Smith, Portfolio Holder for Resources and Business addressed the panel to explain that due to the confidentiality clause within the negotiated settlement of the contract, he was happy to answer questions on the detail of the settlement in closed session.

Councillor Bentley, Willetts and Lissimore expressed deep concern about what had happened in regards to the contract and felt it was a step backwards to discuss in private session, registering their disappointment that this would be discussed in closed session after the exclusion of the general public.

Councillor Manning felt it would be prudent to add in additional contributions over the following years of the five year Buildings Maintenance Programme.

In response to Councillor Bouckley, Mr. Heath said the £100,000 allocated for funding economic development initiatives did include £15,000 towards the refit of the SOS bus.

Councillor Offen said the variance of £138,000 on advertising income was due to the over ambitious targets set at the beginning of the year. Ms. Ann Wain , Executive Director said the income from advertising will improve in 2008-09 as a result of ‘Roundabout Advertising’.

Councillor Bentley considered the sums set aside in the allocation of the 2007-08 underspend / additional income budget for front line services was meagre and that more attention should be given to services such as Street Wardens and Waste Services, though he applauded the £100,000 contribution to the capital expenditure reserve for opportunity purchases.

Councillor Smith believed the sums made for a prudent budget, and in response to Councillor Lissimore said the £100,000 allocated to the Concessionary Fares Scheme was the best estimate at this time for meeting the costs for the extended hours of the scheme, though there was no guarantee this would be sufficient funding.

RESOLVED that the panel noted the Pre-Audit Revenue Outturn 2007/08.

Councillor Sue Lissimore (in respect of being a former member of the Board of Colchester Borough Homes) declared a personal interest in the following item pursuant to the provisions of Meetings General Procedure Rule 7(3)

8. 2007-08 Capital pre-audit outturn

Mr. Andy Wilks, Finance Manager, attended the meeting for this item and introduced the report on the Pre-Audit Capital Outturn 2007/08.

In response to Councillor Offen, Mr. Wilks explained that the total value of the Capital Programme was £64,566,500, with £60,566,500 approved to proceed and £4,000,000 where approval was still needed.

Councillor Smith said the future Capital programme was reliant on the sale of assets, and he and officers would need to look at the programme with a view to reducing risk and funding in the current financial climate.

Councillor Bouckley expressed his thanks to officers for the speedy and efficient completion to the Mersea Pontoon project.

RESOLVED that the panel noted the Pre-Audit Capital Outturn 2007/08.

The Committee/Panel resolved under Section 100A(4) of the Local Government Act 1972 to exclude the public from the meeting for the following item as it involved the likely disclosure of exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act 1972.

Councillor Sue Lissimore (in respect of being a former member of the Board of Colchester Borough Homes) declared a personal interest in the following item pursuant to the provisions of Meetings General Procedure Rule 7(3)

9. Early Cessation of Decent Homes and Housing Repairs Contract

Councillor Willetts, in respect of his diappointment that the following item would be discussed in closed session, left the meeting.

Councillor Smith, Portfolio Holder for Resources and Business addressed the panel explaining that a confidentiality clause within the mediation settlement agreement prevented him and officers from discussing details of the settlement in public. Councillor Smith explained to panel members the consequences to the Council should the settlement agreement be breached.

Councillor Smith said the Council considered the legal costs to terminate the contract versus the option of going to mediation, choosing mediation, in which negotiations took place over two days. The final settlement figure was agreed by the Executive Director, Mr. Ian Vipond, the Head of Financial Services, Mr. Charles Warboys and the Head of Housing and Environmental Policy, Mr. Matthew Young under delegated powers by the Chief Executive, Mr Adrian Pritchard.

Councillor Bentley, as previously mentioned on the item ‘Year End Internal Assurance Audit Report’ considered one internal auditor working on behalf of, but under the individual protocol of Colchester Borough Council and Colchester Borough Homes did not sit comfortably with him, especially in light of this information and the realisation that the appropriate financial controls were not in place. Councillor Bentley asked what the Cabinet are going to do, and what action will be taken, to correct this situation. Councillor Bentley concluded by requesting a review of the Decent Homes and Housing Repairs Contract, including an investigation into how it went wrong and why there were limited financial controls in place, and the outstanding works.

Councillor Smith said the Council would continue the Decent Homes Programme, but with a completion date of 2010, still within Government guidelines. An assessment will be made of outstanding works and how best to service an affordable but fair programme for the remaining properties to be brought up to standard.

In response to Councillors Manning and Offen, Councillor Smith said interim arrangements for the new contract were being managed by Colchester Borough Homes with works being undertaken by the company Ridge. Councillor Smith said that as a member of Colchester Borough Homes Board, he would be closely scrutinising the financial reports for the contract, and confirmed that negotiations between the partners was being vetted by lawyers representing all partners.

RESOLVED that the panel agreed to request the Head of Strategic Policy and Regeneration to present to an agreed forthcoming meeting of the Finance and Audit Scrutiny Panel or a non public meeting in private session, the meeting and meeting date to be agreed by the panel, a report to review the Decent Homes and Housing Repairs Contract, including an investigation into how it went wrong and why there were limited financial controls in place, and the outstanding works, with an invitation to attend going to the Chairman of Colchester Borough Homes and current and previous Chief Executive’s of Colchester Borough Homes.

COLCHESTER

Finance & Audit Scrutiny Panel

Item **11**

29 July 2008

Report of	**Head of Resource Management**	**Author**	**Hayley McGrath 282461**
Title	**Year End Review of Risk Management**		
Wards affected	Not applicable		

This report reviews the Risk Management work undertaken in 2007/08

1. Decisions Required

1.1 Consider and comment on the proposed risk management strategy for 2008/09.
1.2 Consider and note the review of risk management work undertaken during 2007/08.
1.3 Consider and note the intended work plan for 2008/09.
1.4 Endorse the submission of this report to Cabinet.

2. Reasons for Decision(s)

2.1 In January 2007 Cabinet, and subsequently full Council, agreed a revised risk management process that assigned responsibility to this panel for monitoring the Council's risk management activity on behalf of Cabinet. A formal reporting process was also agreed and this included the submission of an annual review of the strategy and a report to both this panel and Cabinet reviewing the work undertaken in the previous year.

3. Background

3.1 The management process of formally managing risk was first introduced in the Council in 2003 when the original risk management strategy was adopted and included within the policy framework.

3.2 In broad terms risks are split into three categories:

- Strategic – those risks relating to the long term goals of the Council
- Operational – risks related to the day-to-day operation of each individual service
- Project – consideration of the risks occurring as a result of the Council's involvement in specific initiatives

With each area having their own risk registers.

3.3 Since 2003 the external assessments of risk management have always endorsed our approach to managing risk but have highlighted areas for improvement. The Audit Commission's Use of Resources assessment of 2006/07 showed that the Council was adequately managing its business risks. The internal audit assessments have highlighted areas for improvement which include ensuring that the reporting process is fully implemented and development of training programmes.

4. Risk Management Strategy for 2008/09

4.1 The Council's approach to managing risk was fundamentally reviewed in 2006/07 and a revised strategy was produced. A requirement within the strategy, and also under the Use of Resources assessment, is an annual review of the strategy to ensure that it is still appropriate to the Council' needs. Therefore a review has been undertaken and the strategy has been updated for 2008/09. The revised strategy is attached at appendix A. There are no fundamental changes to the risk process with only the external review comments and work plans being updated.

5. Summary of 2007/08

5.1 The primary focus for 2007/08 was to continue to embed risk management throughout the Council by developing the registers and providing further training.

5.2 There were no major changes to the risk management function during 2007/08 and the key achievements were:

- The development of the renaissance project risk registers to ensure that they fully captured the Council's risks from all of the projects. The ownership of these has been passed to the renaissance team and they are updated and reviewed on a monthly basis and communicated to all parties concerned.

- Reviewing the internal audit plan to ensure that it is more risk focused. Consideration of risk areas was made in the 2008/09 plan and it is planned to develop this further for the 2009/10 plan, where more audit days will be dedicated to high risk areas.

5.3 Due to the extended absence of the Audit & Risk Manager during the year it was not possible to achieve all of the actions that had been anticipated during the year. However an assessment of the outstanding items has been carried out and the action plan detailed below highlights the areas where improvements will be made during 2008/09.

5.4 During 2007/08 internal and external assessments of the risk process where carried out including the Use of Resources assessment, External Audit letter, an Internal Audit review and the Annual Governance Statement. Whilst the assessments all concluded that the basic process for managing risk was sound there was a need to further develop the process and to fully implement the actions outlined in the strategy.

6. Work Plan for 2008/09

6.1 With regard to the comments made in the above assessment reports and the direction contained within the risk management strategy the following areas will be the primary focus for developing risk management during 2008/09:

- Revised operational registers – ensuring that the new service areas have robust registers of their own service specific issues.

- Training – Developing training courses for both members and officers to ensure that understanding of risk is embedded. Also looking at other practical alternatives to traditional training sessions (it is not always practical to send every member and officer on a training course) such as newsletters, quizzes and an information area on the hub.

- Ensuring that the reporting process set out in the revised strategy is embedded.

- Developing a risk register specifically relating to Members.

6.2 Detailed progress against these areas will be provided quarterly to this panel during the year.

7. Proposals

7.1 That the panel consider and note the review of risk management work undertaken during 2007/08 and the work plan for 2008/09 and endorse the submission of this report to Cabinet.

8. Other Standard References

8.1 There are no direct Strategic Plan, Financial, Consultation, Human Rights, Risk Management, Community Safety or Health and Safety implications as a result of this report

RISK MANAGEMENT STRATEGY

This document outlines the Council's commitment to managing risk in an effective and appropriate manner. It is intended to be used as the framework for delivery of the Risk Management function and provides guidance on developing risk management as a routine process for all services.

INTRODUCTION

The Council undertakes that this strategy will promote and ensure that:

1. The management of risk is linked to performance improvement and the achievement of the Council's strategic objectives.

2. Members and the Senior Management Team own, lead and support on risk management.

3. Ownership and accountability are clearly assigned for the management of risks throughout the Council.

4. There is a commitment to embedding risk management into the Council's culture and organisational processes at all levels including strategic, programme, project and operational

5. All members and officers acknowledge and embrace the importance of risk management as a process, by which key risks and opportunities are identified, evaluated, managed and contribute towards good corporate governance.

6. Effective monitoring and reporting mechanisms are in place to continuously review the Council's exposure to, and management of, risks and opportunities.

7. Best practice systems for managing risk are used throughout the Council, including mechanisms for monitoring and reviewing effectiveness against agreed standards and targets.

8. Accountability to stakeholders is fully demonstrated through periodic progress reports and an annual statement on the effectiveness of and the added value (benefits) from the Council's risk management strategy, framework and processes.

9. The Council's approach is regularly assessed by an external, independent body against other public sector organisations, national standards and Best Practice.

10. The Risk Management Strategy is reviewed and updated annually in line with the Council's developing needs and requirements.

Endorsement by Adrian Pritchard, Chief Executive

"*Colchester Borough Council is committed to ensuring that risks to the effective delivery of its services and achievement of its overall objectives are properly and adequately controlled. It is recognised that effective management of risk will enable the Council to maximise its opportunities and enhance the value of services it provides to the community. Colchester Borough Council expects all officers and members to have due regard for risk when carrying out their duties*."

A. R. Pritchard.

WHAT IS RISK MANAGEMENT

Risk Management is the control of business risks in a manner consistent with the principles of economy, efficiency and effectiveness. It is an essential performance management process to ensure that both the long and short term objectives of the Council are achieved and that opportunities are fully maximised.

Risk Management is not about eliminating risk, as this would limit the ability of the organisation to develop and deliver its ambitions. Its purpose is to recognise the issues that could effect the achievement of our objectives and develop actions to control or reduce those risks. Acknowledgement of potential problems and preparing for them is an essential element to successfully delivering any service or project. Good management of risk will enable the Council to rapidly respond to change and develop innovative responses to challenges and opportunities.

'The Good Governance Standard for Public Services' issued by The Independent Commission on Good Governance in Public Services states that there are six core principles of good governance including 'Taking informed, transparent decisions and managing risk'. The document goes on to state 'Risk management is important to the successful delivery of public services. An effective risk management system identifies and assesses risks, decides on appropriate responses and then provides assurance that the chosen responses are effective'.

BACKGROUND

Current Position

The first Risk Management Strategy was adopted by the Council in September 2003 and incorporated in the Council's policy framework. This introduced the concept of risk and identified the process to be followed.

In broad terms risks are split into three categories:
- Strategic – those risks relating to the long term goals of the Council
- Operational – risks related to the day-to-day operation of each individual service
- Project – consideration of the risks occurring as a result of the Council's involvement in specific initiatives

A significant amount of progress has been made in managing the risks to the Council. The following are some of the achievements since the adoption of the strategy:
- Creation of an overall strategic register.
- Creation of operational risk registers for all service areas.
- Consideration of risk in Committee reports.
- Development of a comprehensive risk register for the renaissance projects and consideration of risk as a project management tool.
- Successful internal and external assessment.
- Provision of advice to other authorities regarding our management of risk.

The CPA score was an endorsement that we have devised a practical and workable approach to managing risk. This has resulted in the Council becoming more risk aware and actually taking more risks, as demonstrated by the comprehensive risk register for the renaissance projects. Colchester is also highly regarded for managing risk by both our insurers and other authorities.

The Audit Commission, in the 2006/07 Audit and Inspection Letter, stated that "*Risk Management arrangements continue to be embedded. A risk strategy is in place and approved by Members. A corporate risk register is regularly updated, and contains specific and generic risk in respect of partnerships*".

The annual Use of Resources assessment highlighted areas of Risk Management that were performing well but by the same token highlighted areas where further development is required, including:
- Staff and Member training
- Development of the operational risk registers
- More frequent reporting to members

This has been reflected in the 2007/08 Internal Audit assessment of the risk management system which has highlighted these as areas to be improved.

The Council's 2007/08 Annual Governance Statement also acknowledges that further actions are required to ensure that the risk management process is fully embedded.

OWNERSHIP

The responsibility to manage risk rests with every member and officer of the Council however it is essential that there is a clearly defined structure for the co-ordination and review of risk information and ownership of the process.

Appendix D is from the CIPFA/SOLACE risk management guide, Chance or Choice. It is a generic map of responsibility for each part of the risk management process.

The following defines the responsibility for the risk management process at Colchester:

Cabinet – Overall ownership of the risk management process and endorsement of the strategic direction of risk management.

Portfolio Holder for Resources & Business – Lead member for the risk management process

Finance & Audit Scrutiny Panel (FASP) – Responsible for reviewing the effectiveness of the risk management process and reporting critical items to cabinet as necessary.

Performance Management Board (PMB) – Ownership of the strategic risks and overview of the operational risks. Actively support the Risk Management Strategy and framework.

Executive Director – Lead officer for the risk management process, demonstrating commitment to manage risk

Head Of Finance – Responsible for co-ordination of the risk management process, co-ordinating and preparing reports and providing advice and support.

Heads of Service – Ownership, control and reporting of their service's operational risks. Contribute to the development of a risk management culture in their teams.

All Employees – To understand and to take ownership of the need to identify, assess, and help manage risk in their individual areas of responsibility. Bringing to the management's attention at the earliest opportunity details of any emerging risks that may adversely impact on service delivery.

Internal Audit, External Audit and other Review Bodies – Annual review and report on the Council's arrangements for managing risk throughout the Council, having regard to statutory requirements and best practice. Assurance on the effectiveness of risk management and the controls environment.

THE WAY FORWARD

Aims & Objectives

The aim of the Council is to adopt best practices in the identification, evaluation, cost-effective control and monitoring of risks across all processes to ensure that risks are properly considered and reduced as far as practicable.

The risk management objectives of Colchester Borough Council are to:

- Integrate risk management into the culture of the Council
- Ensure that there are strong and identifiable links between managing risk and all other management and performance processes.
- Manage risk in accordance with best practice
- Anticipate and respond to changing social, environmental and legislative requirements
- Prevent injury, damage and losses and reduce the cost of risk
- Raise awareness of the need for risk management by all those connected with the Council's delivery of services.
- Ensure that opportunities are properly maximised through the control of risk.
- Reduce duplication between services in managing overlapping risks and promote 'best practise'.

Risk Management forms an important part of the Council's system of Internal Control and is therefore one of the Use of Resources Key Lines of Enquiry. The Risk Management function is currently assessed as performing at level 2 however it is the aim to be at level 3 at the time of the 2008 assessment. The objectives outlined above complement this aim. Appendix C outlines the 2007 Use of Resources criteria for Risk Management.

Strategic Risk Management

Strategic risks are essentially those that threaten the long term goals of the Council and therefore are mainly based around meeting the objectives of the Strategic Plan. They may also represent developing issues that have the potential to fundamentally effect service provision, such as proposals to dramatically change the corporate assessment process.

Strategic risks will be controlled using a register that will detail the risks and associated controls. The register will be owned by the Senior Management Team, with ownership for risks being assigned to individual officers, and will be reviewed every quarter. The strategic risks will be reported to F.A.S.P. every quarter.

Operational Risk Management

Operational risks are those that threaten the routine service delivery of the Council. Each service area will have their own operational risk register that details the risks associated with providing the service. These registers will be reported, in summary format, to the Senior Management Team and committee on an annual basis. High risks and the success in controlling them will be reported to Senior Management Team on a quarterly basis, as these will help in the formulation of the strategic risk register.

Links

It is essential that risk management does not operate in isolation to other management processes. To fully embed a risk management culture it has to be demonstrated that risk is considered and influences all decisions that the Council makes. It is essential that there is a defined link between the results of managing risk and the following:

- The Strategic Plan
- Service Plans
- Revenue and Capital Budgets
- Annual Internal Audit Plan

Action Required

The following actions will be implemented to achieve the objectives set out above:

- Considering risk management as part of the Council’s strategic planning and corporate governance arrangements.
- Ensuring that the responsibility for risk management is clearly and appropriately allocated
- Maintaining documented procedures for managing risk
- Maintaining a corporate approach to identify and prioritise key services and key risks across the Council and assess risks on key projects.
- Maintain a corporate mechanism to evaluate these key risks and determine if they are being adequately managed and financed.
- Establish a procedure for ensuring that there is a cohesive approach to linking the risks to other management processes
- Including risk management considerations in all committee reports
- Providing risk management awareness training to both members and officers.
- Developing risk management performance indicators.
- Establishing a reporting system which will provide assurance on how well the Council is managing its key risks and ensures that the appropriate Members and officers are fully briefed on risk issues.
- Preparing contingency plans in areas where there is a potential for an occurrence to have a significant effect on the Council and its business capability.
- Regularly reviewing the risk process to ensure that it complies with current national Governance Standards and Best Practice.
- Creation of an annual ‘Action Plan’ that details particular areas of development for the coming year, including details of the value added and how they will be embedded.

REVIEW

To ensure that the risk management process is effective it will need to be measured and reported to P.M.B., F.A.S.P. & Cabinet. As well as a structured reporting process of risks and controls during the year there will need to be an annual review demonstrating the success of the following:

- The inclusion of risk management principles within Service Plans and budgets.
- The development of the Internal Audit plan based on the risk issues.
- Achievement against identified performance indicators.
- Members consistently ensuring managing risk is considered as part of the decision making processes within the Council.
- Service managers making recommendations that regard risk as an opportunity as well as a threat .
- Risk management principles being considered in service reviews, for example in areas such as options for change and service improvements.
- Changes in risk being independently identified and assessed by Service Managers
- Compliance with the use of resources criteria and self assessment requirements.

Suitable opportunities to benchmark the risk management service against other organisations should also be explored to ensure that it is effective and the work carried out by the Council conforms to best practise.

The four appendices attached give greater detail of key issues:

Appendix 1 – Outline of the risk management process
Appendix 2 – Details of how Risk Management will be reported.
Appendix 3 – The 2006 Use of Resources Criteria for Risk Management
Appendix 4 – CIPFA guidance on Risk Management Responsibilities

APPENDIX A

The Risk Management Process

Risk Management is a continual process of identifying risks, evaluating their potential consequences and determining the most effective methods of controlling them and / or responding to them. The risks faced by the Council are constantly changing and the continual process of monitoring risks should ensure that we can respond to the new challenges. This process is referred to as the risk management cycle.

Stage 1 – Risk Identification
Identifying and understanding the hazards and risks facing the council is crucial if informed decisions are to be made about policies or service delivery methods.

Stage 2 – Risk Analysis
Once risks have been identified they need to be systematically and accurately assessed. If a risk is seen to be unacceptable, then steps need to be taken to control or respond to it.

Stage 3 – Risk Control
Risk control is the process of taking action to minimise the likelihood of the risk event occurring and / or reducing the severity of the consequences should it occur.

Stage 4 – Risk Monitoring
The risk management process does not finish with the risk control procedures in place. Their effectiveness in controlling risk must be monitored and reviewed. It is also important to assess whether the nature of the risk has changed over time.

APPENDIX B

Reporting

No matter how good the process to identify and control risks is, it will not be effective unless the information gained from it is reported and used to influence other management issues / processes. Therefore it is essential that there is a defined process and timetable for reporting the results of the risk management process to both members and officers.

Types of Report

- A quarterly report to P.M.B., detailing the *high level* operational risks along with comment from the Services regarding the progress that they have made in controlling the risk.
- The strategic risk register needs to be reviewed on a quarterly basis by P.M.B.
- A quarterly report needs to be provided to Committee (F.A.S.P.) detailing the current strategic and high level operational risks and the progress made in controlling them.
- Six monthly review of the operational risk registers and a summary report of these reviews to P.M.B.
- An annual report reviewing Risk Management activity and an action plan for the coming year - taking into account changes in methodology and results of internal and external reviews. Going to P.M.B., FASP and Cabinet. This needs to cover all of the three areas of risk
- Ad-hoc reports need to be provided to P.M.B. when new, significant risk issues arise.

The reports can be summarised as follows:

	Service's	P.M.B.	F.A.S.P.	Cabinet
Quarterly		Progress of high level operational risks Review of strategic risk register	Progress report of strategic & high level operational risks	
6 Monthly	Review of operational risk register	Summary of operational review from services		
Yearly		Scrutiny of annual progress report to cttee on R.M. & action plan for coming year.	Endorsement of annual progress report on R.M. & action plan for coming year	Summary of past years work on R.M. and agreement of action plan for the coming year.

Appendix C
Use of Resources Criteria

4. **INTERNAL CONTROL**
How well does the council's internal control environment enable it to manage its significant business risks?

Key line of enquiry
4.1 The council manages its significant business risks

Audit Focus

Evidence that:
the council has a risk management process in place
the risk management system covers partnership working

Criteria for Judgement

Level 2	Level 3	Level 4
*** The council has adopted a risk management strategy/policy that has been approved by members.** *** The risk management strategy/policy requires the council to:** • **identify corporate and operational risks** • **assess the risks for likelihood and impact** • **identify mitigating controls** • **allocate responsibility for the mitigating controls.** *** The council maintains and reviews a register of its corporate business risks linking them to strategic business objectives and assigns named individuals to lead on the actions identified to mitigate each risk.** *** Member responsibility for corporate risk management is identified in the terms of reference of one or more committees as appropriate.** *** Reports to support strategic policy decisions, and project initiation documents, include a risk assessment.**	1.1.2 *** The risk management process is reviewed and updated at least annually.** *** The risk management process specifically considers risks in relation to significant partnerships and provides for assurances to be obtained about the management of those risks.** *** All appropriate staff are given relevant training and guidance to enable them to take responsibility for managing risk within their own working environment.** *** The members with specific responsibility for risk management have received risk management awareness training.** *** Members with responsibility for corporate risk management receive reports on a regular basis and take appropriate action to ensure that corporate business risks are being identified and effectively managed, including reporting to full council as appropriate.**	* A senior officer and member jointly champion and take responsibility for embedding risk management throughout the council. * The council can demonstrate that it has embedded risk management in its business processes, including: • strategic planning • financial planning • policy making and review • performance management * All members receive risk management awareness training appropriate to their needs and responsibilities * The council considers the opportunity side of innovative and challenging projects. * Reports to support strategic policy decisions, and initiation documents for all major projects, require a risk assessment including sustainability impact appraisal.

Appendix D
Risk Management Responsibilities – CIPFA / SOLACE Guidance

	Framework, Strategy and Process	Identifying risk	Analysing Risk	Profiling risk	Prioritising action based on risk appetite	Determining action on risk	Controlling risk	Monitoring & Reporting	Reporting to external stakeholders.
Members	Agreeing the Framework, Strategy and Process Determined by Officers	Identifying risk	Analysing Risk	Profiling Risk	Determining the risk appetite and prioritising risk. Agreeing the priorities determined by officers			Reviewing the effectiveness of the risk management process.	Reporting to external stakeholders on the framework, strategy, process and effectiveness .
Risk Management Team	Providing advice And support to the executive Management Team and Members	Providing advice and support.	Providing Advice and support	Providing advice and support	Providing advice and support			Co-ordinating the results for reporting to the corporate management team and members	
Senior Management Team	Determining the framework, Strategy and Process	Identifying strategic and cross-cutting issues	Analysing Strategic and cross-cutting issues.	Profiling strategic and cross-cutting issues.	Determining the risk appetite and prioritising strategic and cross-cutting issues	Determining action on strategic and cross-cutting issues. Delegating responsibility for control.		Monitoring progress on managing strategic and cross-cutting risks and reviewing the implementation of the risk management framework, strategy and process. Reporting to members.	Reporting to external stakeholders on the framework, strategy, process and effectiveness.
Head of Finance	Providing Advice and Support	Providing advice and support	Providing advice and support	Providing advice and support	Providing advice and support	Providing advice and support	Providing advice and support	Co-ordinating the results for reporting to the executive management team and members	Preparing draft reports for the corporate management team and members to issue.
Service Managers / G.M.T'ss		Identifying service Risks	Analysing Service risks.	Profiling service risks.	Prioritising action on service risks.	Determining action on service risks. Delegating responsibility for control.		Monitoring progress on managing service risks. Reporting to the group management team	
Employees, contractors And partners		Maintaining awareness of risks and feeding these into the formal process.	Maintaining awareness impact of risks and feeding information into the processes				Controlling risk in their jobs.	Monitoring progress on Managing job related risks Reporting to the service manager.	

COLCHESTER

Finance & Audit Scrutiny Panel

Item 12

29 July 2008

Report of	**Head of Resource Management**	**Author**	**Sean Plummer** **Jacqui Dove** **☎282347**
Title	**Treasury Management – Annual Report 2007/08**		
Wards affected	Not applicable		

This report concerns treasury management and cash fund manager performance in 2007/08

1. Decision(s) Required

1.1 To note the activities relating to treasury management in 2007/08 and consider performance.

1.2 To note the performance of the Council's treasury management advisors.

2. Reasons for Decision(s)

2.1 The CIPFA Code of Practice on Treasury Management and the Council's Treasury Management Policy Statement both require an annual report to be considered.

3. Alternative Options

3.1 During the year alternative approaches to the management of the Council's debt and investments were actively considered.

4. Supporting Information

4.1 Treasury management comprises all borrowing and investment activities of the Council. Details of all treasury management activities during 2007/08 are provided as a background paper which should be read alongside this report. The key areas commented on in this report are:-

- Debt and borrowing
- Investments, including some externally managed funds
- Performance of external advisors

Debt and Borrowing

4.2 The Council's strategy for 2007/08 was to undertake new borrowing of £10.23m in respect of the community stadium. During the year we revised our strategy and a total of £3.5m was borrowed from the Public Works Loan Board (PWLB). Whilst not within the last year, following advice from our external financial advisors (Sector) during February and March 2008, it was agreed that long term rates had reduced and arrangements were made for a further £4m loan to commence in April 2008.

4.3 As the background paper shows our long term debt now stands at almost £58.4million with a reduced average rate of 5.92% compared to 6.22% as at March 2007, a reduction of 0.30%.

4.4 The new borrowing undertaken during the year was close to the lowest point available.

Investments – external cash fund managers

4.5. The Council had previously employed one external cash fund manager, Investec which at the start of the financial year the fund stood at £17.76 million. The decision was taken last year to withdraw all cash from the fund manager and to invest the cash for periods between 1 and 2 years. This strategy does not rule out using an external fund manager in the future and we will continually review our investment performance.

Investments – internally managed

4.6. Following on from the decision to cease using an external fund manager, we have successfully managed all excess surplus funds (since April 2007) alongside other internally managed cash. The outcome of this strategy has been an investment mix of circa £10m invested for periods of 1-2 years and £20m invested predominantly to cover shorter-term cashflow needs. This has proven to be successful in the last financial year and the average rate earned on investments was 5.89%. This is 0.31% higher than the comparative index.

4.7 All investment and borrowing activity in 2007/08 complied with agreed limits and policies.

External advisors

4.9. The Council employ Sector Treasury to provide a consultancy service in respect of treasury management, to include advice on both debt and investments. In 2007/08 Sector provided advice on borrowing and investments throughout the year that assisted the Council in exceeding the benchmark for investment activity and undertaking borrowing at rates below the average. Sector also provide advice on counterparty credit details to help minimise the risk of default on investments and general advice on capital accounting.

5. Proposals

5.1 To note the performance of the treasury management function, including the Council's cash fund managers and treasury advisors, as set out in this report and background paper.

6. Publicity Considerations

6.1 Appendix A to the attached background paper is confidential.

7. Financial implications

7.1 Interest paid and earned on borrowing and investments is shown within the Central Loans and Investment Account (CLIA). Outturn figures for 2007/08 show a budget surplus of £1.041m against budgeted borrowing costs of £3.7m and investment interest costs of £1.3m. The net additional interest is principally due to improved investment returns on in-house investments, increased surplus cash available for investment and delayed long-term borrowing.

8. Risk Management Implications

8.1. Risk Management is essential to effective treasury management. The Council's Treasury Management Statement contains a section on treasury Risk Management (TMP1).

8.2. TMP1 covers the following areas of risk all of which are considered as part of our treasury management activities:

- Liquidity.
- Interest rates.
- Exchange rates.
- Inflation.
- Credit and counterparty.
- Refinancing.
- Legal and regulatory.
- Fraud, error and corruption, and contingency management.
- Markets.

9. Other Standard References

9.1 There are no direct Strategic Plan, Consultation, Human Rights, Community Safety, or Health and Safety implications as a result of this report.

Background Papers

Annual Report on Treasury Management (as attached)
SECTOR Annual Treasury Report 2007/08
Appendix A: Temporary Investments 2007/08 (**confidential**)

Introduction and Background

The Chartered Institute of Public Finance and Accountancy's Code of Practice on Treasury Management 2001 was adopted by Colchester Borough Council on 18 February 2004 and the Council fully complies with its requirements. The primary requirements of the Code are the: -

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities
- Creation and maintenance of Treasury Management Practices that set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the Cabinet / Council of an annual strategy report for the year ahead and an annual review report of the previous year.
- 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.

Treasury management in this context is defined as

> "The management of the local authority's 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 annual treasury report covers:

- The Treasury Management Strategy for 2007/08
- The CLIA budget outturn position
- The economy in 2007/08
- Borrowing
- Investments
- Compliance with treasury limits and Prudential Indicators

Treasury Management Strategy for 2007/08

Cabinet agreed the Council's Treasury Management Strategy for 2007/08 in February 2007 along with the Annual Investment Strategy. The strategy was as follows:

- The strategy assumed that there will be some unsupported borrowing during the year of £10.23m in respect of the funding of the Community Stadium.
- The main investment activity during the year will be managed internally as the decision was made to withdraw the funds from the Council's external fund manager. The council also has a core balance for investment over the longer-term. The council will review its investment limits during the year to take into account the longer-term investments and increased cash balances.
- The council's Treasury advisors forecast interest rates (Bank/"repo" rate) to peak at 5.5% in the first quarter of 2007 before falling back to 5.25% by the end of the calendar year before settling at 5% by the end of the financial year. The 25-30 year PWLB rate is expected to stay in the region of 4.5%.

Budget Outturn

The outturn position for the Central Loans and Investment Account (CLIA) is shown below. This shows a favourable variance of £1042k.

3920 CLIA	2007/08 Budget £	Actual £	Variance £'000
Interest on borrowing	3305000	3380283	75,283
Other interest (incl. S.106)	420000	615734	195,734
Total Interest Paid	**3,725,000**	**3,996,017**	**271,017**
Less: Item 8 debit	(3,208,000)	(3,212,464)	(4,464)
Total less HRA	**517,000**	**783,553**	**266,553**
Total Investments	(1,277,000)	(2,620,786)	(1,343,786)
Less: Item 8 credit	50,000	85,599	35,599
Total less HRA	**(1,227,000)**	**(2,535,187)**	**(1,308,187)**
Total CLIA	**(710,000)**	**(1,751,634)**	**(1,041,634)**

The Central Loans and Investment Account (CLIA) comprise the Council's borrowing costs and investment income and have a net income budget of £710k. The CLIA budget is difficult to predict and can be affected by several factors. The majority of the Council's debt is on fixed rates reflecting the longer-term nature of the borrowing decisions. Investments are generally made for shorter periods and therefore returns can be more variable. This mix is generally more beneficial when interest rates are high or increasing. It is important to add that the exposure to interest rate movements is regularly monitored to minimise risks to changes in returns. There are a number of reasons that have contributed to the variances shown in the table above:-

- Increases in the bank base rates have been higher than was expected when the budget was set. In addition to this, there was a growing expectation during the year that rates would rise to even higher levels, which drove interest rates on offer higher, providing the Council with opportunities to improve investment returns. Furthermore, turmoil in the financial markets caused an increase in investment rates, particularly in the 3-6 month area. This provided further opportunities to improve returns.
- The level of cash balances was higher than was expected. This is due to a number of factors including the Council's borrowing activity, funds added to reserves at the end of 06/07, the variances against 07/08 budgets, capital spending being slower than expected, and total revenue balances being higher than last year.
- The Council's investment strategy was amended from April 2007. This involved withdrawing £18m from the external fund manager, and managing the cash 'in-house'. Some of this has been invested for longer periods to help provide greater certainty of investment returns into the next financial year. The remainder was used to take increased advantage of the economic environment explained earlier.

The Economy

Shorter-term interest rates

Bank Rate started 2007/08 at 5.25% with expectations that there would be further increases in rates. This was reflected in a positive interbank money market curve. A further increase in rates to 5.5% duly occurred on 10th May 2007 but not before the Governor of the Bank of England had written a letter to the Chancellor in April explaining why CPI had risen to 1% or more above the official CPI inflation target of 2%. The Bank of England's Inflation Report issued in May showed inflation would be above target at the two year horizon. Another rise was delivered on 5th July when Bank Rate rose to 5.75% and the markets fully expected Bank Rate to increase again. One year interbank was priced at over

6%, GDP growth was continuing to strengthen and the housing market was still robust. The August Inflation Report showed Bank Rate needed to rise to 6% to keep inflation at target in two years time.

August, as it turned out, was the peak of interest rates as what has become known as 'the credit crunch' hit the markets and the global economy. The crunch originated in the US through the sub-prime housing market. Although originating in the US, world wide investors, particularly banks, had invested in packages of sub-prime loans, attracted by the higher yields offered. Fears arose that a large number of these investments would turn out to be worthless and this in turn would lead to bankruptcies amongst the banking sector. As a result of these fears, and the ensuing reluctance of banks to lend to each other, the Federal Reserve Bank injected $38bn of liquidity into the markets on 9th August. The ECB followed suit but the Bank of England only making cash available at a penal rate of 1% above Bank Rate. On 17th August the Federal Reserve cut interest rates by 50 bp to 5.25%. On 20th August Sector revised its interest rate view to reflect a downside risk to its forecast. The dislocation in the markets continued throughout the summer until on 14th September it was announced that the Bank of England had provided billions of pounds of financial support to Northern Rock. Northern Rock had been affected by the drying up of the wholesale money markets which provided 80% of its funding. On 17th September the Chancellor announced a Government guarantee for all deposits held at the stricken bank. A day later the Federal Reserve cut US rates by a further 50bp although oil rose to $80 a barrel and continued to climb reaching a peak, briefly, of $100pb in November. On 24th September Sector revised its interest rate forecast with 5.75% now the peak in rates. At its October meeting the MPC declined to cut Bank Rate, being concerned about the inflation outlook. UK data continued to be robust during the autumn although CPI dropped to 1.8% in September. 3 month LIBID still remained well above Bank Rate. On 31st October the Federal Reserve cut rates yet again to 4.50% and the following day they added $41bn of reserves in an attempt to free up the markets. The MPC eventually cut Bank Rate on 6th December to 5.50% as concerns about the economy and the credit crunch mounted. On 10th December both UBS and Capital Economics revised their interest rate forecasts down sharply. A day later the Federal Reserve cut rates again, this time by 25 bp.

2008 was ushered in with major fears about the global economy. Stock markets fell sharply and government bond yields fell. On 22nd January the Federal Reserve cut rates, this time by a massive 75bp to 3.5%, and once more on 30th January to 3%. The MPC followed suit in February cutting Bank Rate by 25 bp to 5.25%. On 18th February it was announced that the Government would nationalize Northern Rock. In late February and March the markets seized up again, forcing concerted liquidity intervention by the world's central banks, initially to little avail. The UK budget brought increased debt issuance, pushing gilt yields up sharply at the front end and driving PWLB rates up. On 14th March US investment bank Bear Stearns had to be bailed out by the Federal Reserve, culminating in a takeover by JP Morgan. The year ended with the money markets anxious and nervous and 3 month cash 75bp above bank rate.

Longer-term interest rates

The PWLB 45-50 year rate started the year at 4.45 and fell to a low of 4.38% in March 2008. The high point, of which there were several, for 45-50 year was 4.90% before finishing the year at 4.42%. The volatility in yields was a direct reflection of the massive turnaround in interest rate sentiment brought about by the sub-prime crisis in the US. A radical change to the PWLB rate structure was introduced by the DMO on 1st November when they moved to single basis point

moves in their rates and introduced a separate repayment rate at the same time, at a level significantly below the rate at which they would lend new money.

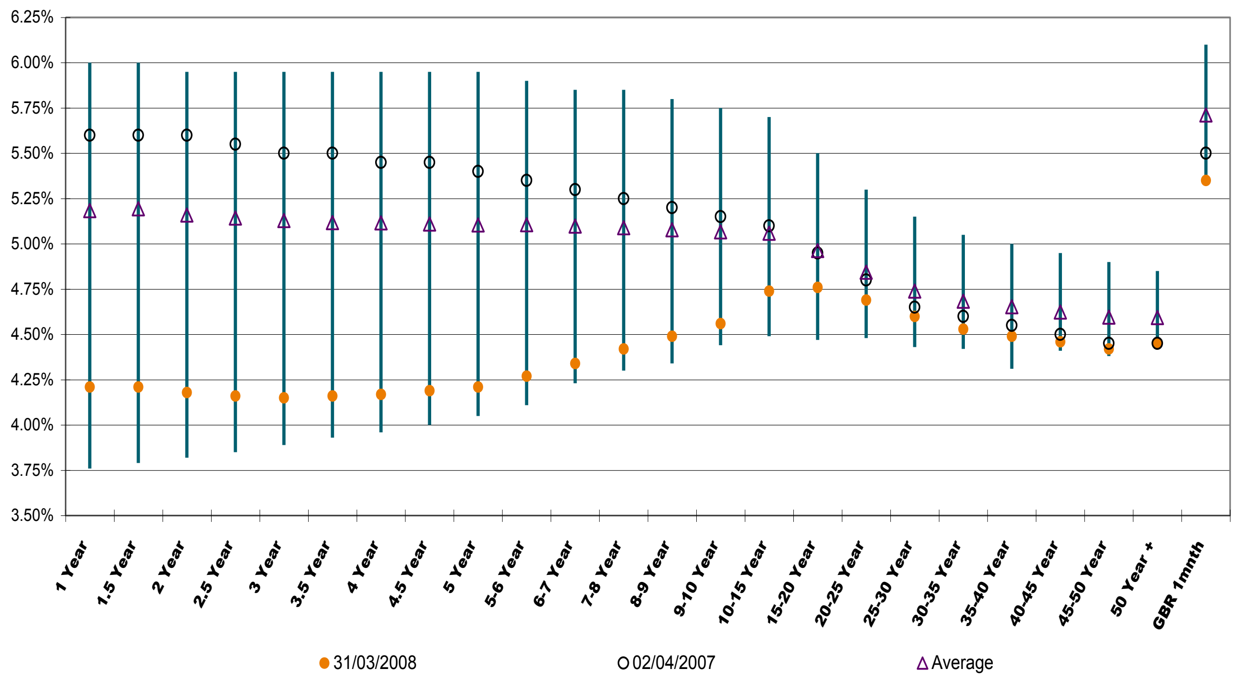
Borrowing

The table below sets out borrowing undertaken this year totalling £3.5million.

Start	Source	Value £	Rate %	Maturity (Years)
Aug-08	PWLB (493762)	3,500,000	4.50	50
	Total	3,500,000		
Note: new loan				
Apr-08	LOBO (B53)	4,000,000	4.01	70

The following graph shows the range (high and low points) in rates for each maturity period during the year, and individual rates at the start and end of the financial year.

PWLB Rates 2007/08



The table below shows the relevant average rate available for loans taken during the year compared to our new borrowing showing that all of our loans were taken at rates at or below the average available.

Source	Value £	Rate %	Average Rate %
PWLB (493762)	3,500,000	4.50	4.60
Total	3,500,000		

The total debt outstanding at 31 March 2008 was £58.4m, which represents an increase on last year of £3.5m. The additional borrowing has led to additional annual interest payments of £158k. It has also resulted in the average rate of the council's debt decreasing by 0.29%, which represents a net decrease of 2.58% over the past three years.

Loans O/S		Maturity	March 08 £	%	March 07 £	%
PWLB	484275	5/2025	700,000	4.88	700,000	4.88
PWLB	482450	11/2038	900,000	4.63	900,000	4.63
PWLB	475958	5/2055	1,300,000	8.88	1,300,000	8.88
PWLB	488963	8/2034	2,000,000	4.80	2,000,000	4.80
PWLB	489406	5/2030	3,000,000	4.55	3,000,000	4.55
PWLB	489978	5/2032	2,500,000	4.45	2,500,000	4.45
PWLB	490717	11/2031	1,000,000	4.25	1,000,000	4.25
PWLB	490718	11/2033	2,000,000	4.25	2,000,000	4.25
PWLB	491155	1/2050	1,000,000	3.70	1,000,000	3.70
PWLB	492019	8/2056	2,500,000	4.25	2,500,000	4.25
PWLB	492218	9/2056	2,500,000	4.05	2,500,000	4.05
PWLB	493046	3/2053	5,000,000	4.25	5,000,000	4.25
PWLB	493762	8/2057	3,500,000	4.50		
Bonds - Stock Issue		5/2020	20,000,000	8.79	20,000,000	8.79
LOBO		1/2046	2,000,000	3.79	2,000,000	3.79
LOBO		1/2066	2,000,000	3.55	2,000,000	3.55
LOBO		1/2056	1,500,000	3.53	1,500,000	3.53
LOBO		7/2076	5,000,000	4.15	5,000,000	4.15
Subtotal			58,400,000	5.93	54,900,000	6.22

Investments – Fund Managers

The main investment activity of the Council had previously been managed externally by Investec Asset Management. At the beginning of the year however the decision was made to withdraw the funds (£17.76m) from their control and manage them internally. In last year's annual report it was reported that we would review the strategy of using external fund managers. It was subsequently reported in the 2007/08 strategy report that we anticipated withdrawing some or all of our funds. Following consideration of our investment options, the poor performance of Investec and our strategy to provide greater certainty on out investment returns we have now closed our external fund. We have invested the cash predominantly in periods between 1 and 2 years to take advantage of longer term rates, and, to reduce the volatility of the Council's investments.

Investments – In-house

The Council manages investments in-house and invests with the institutions listed in the Council's approved lending list. The Council invests for a range of periods from overnight to 3 years, dependent on the Council's cash flows, its interest rate view and the interest rates on offer. In-house managed investments can be analysed as follows:

- Temporary investments
- Overnight investments
- Deposit accounts and small balance accounts

The proportion by value of investments made over the past two years in each of these categories is shown in the table below. This shows that a greater proportion of our investment activity has been carried out in temporary investments rather than using deposit accounts. This reflects the rates on offer from financial institutions resulting from the recent credit crunch.

Analysis	**2007/08 %**	**2006/07 %**
Temporary Investments	89.9	65.1
Overnight Investments	3.9	4.7
Deposit Accounts	5.3	28.1
Small Balance Account	0.9	2.1
Total	**100.0**	**100.0**

Temporary investments are those made for a period of more than one day, and are usually arranged in the money market through brokers (see Appendix A). Investments have been to cover regular cashflow movements and in additional 13 investments of a year or more have been made. The table below shows that on average the Council invested amounts for the same period as last year.

Temporary Investments	**2007/08**	**2006/07**
Total Invested (£'000)	182,891	70,638
Number of Investments	101	31
Average Investment (£'000)	1,811	2,279
Average Length (Days)	95	95
Investments by Counterparty (%)		
Subsidiaries of Clearing Banks	0	0.0
Clearing Banks	15.6%	0.0
Foreign Banks	47.7%	88.0
Building Societies	36.7%	12.0

Twenty one temporary investments totalling £33m were outstanding as at 31 March 2008. In addition, a number of minor long-term trust fund type investments are held.

Overnight Investments are those placed for one night, and are made with the Council's bank (Barclays) and other institutions.

Deposit Accounts are either used as an alternative to overnight deposits or for a longer period in place of temporary investments in the money markets. These accounts offer attractive returns with the additional benefit of flexibility.

High Interest Business Accounts (HIBA) are used for small surplus balances that have not otherwise been invested. These are kept to a minimum through the various other investment options, as interest rates are low.

Investment performance can be assessed through comparison of the Council's average return for the year compared to a suitable benchmark. In this instance this is the 7-Day LIBID Index. The table below shows that the Council has once again exceeded this benchmark at a increased margin to the previous year.

Details	2007/08 %	2006/07 %
Temporary Investments	5.90	4.95
Overnight and Deposit Account	5.88	4.96
HIBA	5.13	3.88
Total	**5.89**	**4.93**
Benchmark (7 Day Rate)	5.58	4.84
Return as a % of the Benchmark	105.5%	101.9%

Compliance with Treasury Limits and Prudential Indicators

The Council's Treasury Management Policy Statement sets out various limits on how much may be invested in various organisations and sources and types of borrowing. The Policy Statement was reviewed in March 2004 in line with recent guidance, and agreed by the Portfolio Holder for Strategy. All the investments and borrowing detailed within this report complied with the policy.

The Council's Prudential Indicators for 2007/08 were agreed by full Council on 21 February 2007. The table below shows the Council's performance against the agreed treasury management prudential indicators. It should be noted that actual external debt is not directly comparable to the authorised limit and operational boundary as it reflects the position at one point in time.

SECTOR

ANNUAL TREASURY REPORT

2007/08

17 Rochester Row, Westminster, London SW1P 1QT
Tel 0871 664 6800 Fax 0871 664 6801
Housing & Specialist Finance: Tel 0871 664 6868 Fax 0871 664 6869
Email treasury@sector-group.com housing@sector-group.com www.sector-group.com
A Trading Division of Sector Treasury Services Ltd

Authorised and regulated by the Financial Services Authority
Registered office as below. Registered in England No. 2652033
Part of The Capita Group Plc, 71 Victoria Street, Westminster, London SW1H 0XA. www.capita.co.uk

ANNUAL TREASURY REPORT 2007/08

1. INTRODUCTION AND BACKGROUND

The Chartered Institute of Public Finance and Accountancy's Code of Practice on Treasury Management 2001 was adopted by this Council on ********* and this Council fully complies with its requirements.

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 the Council of an annual treasury management strategy report (including the annual investment strategy report) for the year ahead and an annual review report of 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.

Treasury management in this context is defined as:

> *"The management of the local authority's 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 ANNUAL TREASURY REPORT COVERS

- the Council's current treasury position;
- performance measurement;
- the strategy for 2007/08;
- the economy in 2007/08;
- borrowing and investment rates in 2007/08;
- the borrowing outturn for 2007/08;
- compliance with treasury limits and Prudential Indicators;
- investment outturn for 2007/08;
- debt rescheduling;
- other issues (*if applicable*).

3. CURRENT TREASURY POSITION (OPTIONAL AREA)

The Council's debt and investment position at the beginning and the end of the year was as follows:

	31st March 2008 Principal		Rate/ Return	Average Life yrs	31st March 2007 Principal	Rate/ Return	Average Life yrs
Fixed Rate Funding:							
- PWLB	£Xxm				£Xxm		
- Market	£Xxm	£Xxm	X%		£Xxm	X%	
Variable Rate Funding:					£Xxm		
- PWLB	£Xxm				£Xxm		
- Market	£Xxm	£Xxm	X%		£Xxm	X%	
Total Debt		***£Xxm***	***X%***		***£Xxm***	***X%***	
Investments:							
- In-House	£Xxm		X%		£Xxm	X%	
- With Managers	£Xxm		X%		£Xxm	X%	
Total Investments		***£Xxm***	***X%***		***£Xxm***	***X%***	

4. PERFORMANCE MEASUREMENT (OPTIONAL AREA)

One of the key changes in the revision of the Code in 1996 was the formal introduction of performance measurement relating to investments, debt and capital financing activities. Whilst investment performance criteria have been well developed and universally accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide *(as incorporated in the table in section 3).*

The use of benchmarks for investments may be inappropriate for those local authorities with small cash balances as they may only be able to place funds for short periods and possibly at lower rates.

5. THE STRATEGY FOR 2007/08

(Clients may wish to check this against their Council strategy submission as Sector's strategy report template was periodically updated to reflect changes in economic conditions and forecasts).

The Sector recommended treasury strategy for 2007/08, (in November 2006), was based on their view of the rate of growth of GDP in the UK economy continuing to be steady at trend during 2007/08. Bank Rate was expected to remain steady at 5% until the final quarter of the year when it would fall to 4.75%. This was predicated on CPI being at target on the two year horizon, that wage growth was below the MPC's threshold of 4.5%, that GDP trend growth would be higher due to inward migration and that the US economy would ease in 2007. Risks to the upside would include house prices continuing to rise, wage pressures rising in response to inflationary pressures and utility prices continuing higher.

The effect on interest rates for the UK was therefore expected to be as follows:

- **Shorter-term interest rates** - The "average" City view anticipated that trend growth in the UK, US and EU would eventually lead to a decrease in U.K. Bank Rate from 5.00% to 4.75% by the end of March 2008.

- **Longer-term interest rates** - The view on longer-term fixed interest rates, 50 years, was that they would remain static around the 4.25% for the whole of the year. The 25 year rate would also remain flat around 4.50%.

Against this view the treasury officers expected... ***(if the Council's view differed from the above view substitute for the above).***

The adopted treasury strategy - The agreed strategy put to the Council based upon the above forecast, was that:

The strategies for each client are particular for their local circumstances - some of the options to choose and edit for your report may be:

1. That the expectation for falling Bank Rate in the future was so strong that the drawing of cheaper, shorter term funding later in the year for << some (or all) select as appropriate>> of the FY 2007/08 borrowing requirement would assist in lowering debt servicing costs. The risk was that leaving longer term borrowing to later years could eventually entail higher longer-term interest costs.
2. That the risks intrinsic to shorter term variable interest rates are such, when compared to historically low long term funding costs, that the Council will maintain a stable, longer term portfolio by drawing longer term fixed rate funding.
3. The Council operated both borrowing and investment portfolios and as a consequence was at lower risk from being impacted by a sharp, unexpected rise in short-term variable interest rates. The strategy for the year was therefore to maintain a balance of funding at short-term rates to match short-term investments thus maintaining balanced treasury risk.

(If you need tailored local options please contact your usual consultant at Sector Treasury Services)

6. THE ECONOMY

(Please use either the concise version…)

Shorter-term interest rates – Bank Rate started 2007/08 at 5.25% with expectations that there would be further increases in rates. This was reflected in a positive interbank money market curve. A further increase in rates to 5.5% duly occurred on 10th May 2007 but not before the Governor of the Bank of England had written a letter to the Chancellor in April explaining why CPI had risen to 1% or more above the official CPI inflation target of 2%. The Bank of England's Inflation Report issued in May showed inflation would be above target at the two year horizon. Another rise was delivered on 5th July when Bank Rate rose to 5.75% and the markets, including Sector, fully expected Bank Rate to increase again. One year interbank was priced at over 6%, GDP growth was continuing to strengthen and the housing market was still robust. The August Inflation Report showed Bank Rate needed to rise to 6% to keep inflation at target in two years time.

August, as it turned out, was the peak of interest rates as what has become known as 'the credit crunch' hit the markets and the global economy. The crunch originated in the US through the sub-prime housing market. Although originating in the US, world wide investors, particularly banks, had invested in packages of sub-prime loans, attracted by the higher yields offered. Fears arose that a large number of these investments would turn out to be worthless and this in turn would lead to bankruptcies amongst the banking sector. As a result of these fears, and the ensuing reluctance of banks to lend to each other, the Federal Reserve Bank injected $38bn of liquidity into the markets on 9th August. The ECB followed suit but the Bank of England stood on the sidelines only making cash available at a penal rate of 1% above Bank Rate. On 17th August the Federal Reserve cut interest rates by 50 bp to 5.25%. On 20th August Sector revised its interest rate view to reflect a downside risk to its forecast. The dislocation in the markets continued throughout the summer until on 14th September it was announced that the Bank of England had provided billions of pounds of financial support to Northern Rock. Northern Rock had been affected by the drying up of the wholesale money markets which provided 80% of its funding. On 17th September the Chancellor announced a Government guarantee for all deposits held at the stricken bank. A day later the Federal Reserve cut US rates by a further 50bp although oil rose to $80 a barrel and continued to climb reaching a peak, briefly, of $100pb in November. On 24th September Sector revised its interest rate forecast with 5.75% now the peak in rates. At its October meeting the MPC declined to cut Bank Rate, being concerned about the inflation outlook. UK data continued to be robust during the autumn although CPI dropped to 1.8% in September. 3 month LIBID still remained well above Bank Rate. On 31st October the Federal Reserve cut rates yet again to 4.50% and the following day they added $41bn of reserves in an attempt to free up the markets. The MPC eventually cut Bank Rate on 6th December to 5.50% as concerns about the economy and the credit crunch mounted. On 10th December both UBS and Capital Economics revised their interest rate forecasts down sharply. A day later the Federal Reserve cut rates again, this time by 25 bp.

2008 was ushered in with major fears about the global economy. Stock markets fell sharply and government bond yields fell. On 22nd January the Federal Reserve cut rates, this time by a massive 0.75bp to 3.5%, and once more on 30th January to 3%. The MPC followed suit in February cutting Bank Rate by 25 bp to 5.25%. On 18th February it was announced that the Government would nationalize Northern Rock. In late February and March the markets seized up again, forcing concerted liquidity intervention by the world's central banks, initially to little avail. The UK budget brought increased debt issuance, but little else, pushing gilt yields up sharply at the front end and driving PWLB rates up. On 14th March US investment bank Bear Stearns had to be bailed out by the Federal Reserve, culminating in a takeover by JP Morgan. The year ended with the money markets anxious and nervous and 3 month cash 75bp above bank rate.

Longer-term interest rates – The PWLB 45-50 year rate started the year at 4.45 and fell to a low of 4.38% in March 2008. The high point, of which there were several, for 45-50 year was 4.90% before finishing the year at 4.42%. The volatility in yields was a direct reflection of the massive turnaround in interest rate sentiment brought about by the sub-prime crisis in the US. A radical change to the PWLB rate structure was introduced by the DMO on 1st November when they moved to single basis point moves in their rates and introduced a separate repayment rate at the same time, at a level significantly below the rate at which they would lend new money.

(….. or the expanded version of shorter term rates)

Shorter-term interest rates – Bank Rate started 2007/08 at 5.25%, having risen to that level in January 2007. The money market yield curve was sharply positive with the one year around the 5.7% level, indicating the market's view that further Bank Rate increases were in the pipeline. 5 year gilt yields were around 5.3% also reflecting the market's views on rates. Sector's interest rate view had already been amended to forecast Bank Rate rising to 5.5%. On 14th April, for the first time, the Governor of the Bank of England had to write a letter to the Chancellor explaining why CPI had risen more than 1% above the official inflation target of 2.0% and what steps the MPC intended to take to get CPI back on track. Indeed a month later the MPC raised Bank Rate to 5.5%. Both one year interbank rates (5.9%) and 5 year gilt yields (5.35%) rose further, presenting some good investment opportunities. Sector upped its interest rate forecast at this time to 5.75%. In June the data continued to show good growth in the UK, the housing market was rising and inflation was still a concern. Sector adjusted its forecast to peak at 6%. The MPC duly delivered another interest rate increase on 5th July and markets again reacted negatively, pushing the one year interbank rate up to 6.23% and five year gilt yield to 5.7%. The August Inflation Report concluded that Bank Rate would need to rise to 6% to keep CPI at 2% in two years time, the MPC's target level.

On 9th August the problems connected to the **US sub-prime housing market** began to impact the global markets. BNP in Paris closed down two funds heavily involved in lending to this sector and both the Federal Reserve in the US and the ECB in Frankfurt injected very substantial amounts of liquidity into the wholesale markets. Fear gripped the markets as lenders were unsure whether the counterparties to which they were lending would default on their loans. This fear caused massive dislocation in the markets and a virtual drying up of activity. Market rates moved far away from the levels set by the central banks for the control of inflation. On 17th August, the Federal Reserve reacted to the paralysis in the markets, by cutting interest rates by 50bp. Sector revised its forecast to reflect that there was now downside risk to their interest rate forecast. The Bank of England made funds available to banks but only at a penal rate, 1% above Bank Rate. Banks in the UK were reluctant to take advantage of this facility as the media would have assumed the borrower was in financial trouble. The money markets seized up and although the one year was nominally quoted at levels above 6.5% no business was being conducted, although gilt yields were edging down due to general concerns about the state of the turmoil in the markets.

Then on 14th September a bombshell hit the headlines - **Northern Rock**, a UK bank and big mortgage lender, was in financial difficulties as a result of the seizing up of the wholesale lending and borrowing market and was having to borrow from the Bank of England under its 'lender of last resort' facility. (This was not a solvency problem; Northern Rock was still operating at a profit of over £500m per year. However, this was a liquidity problem – a shortage of access to cash.) Although official assurances were given that deposits were safe the public took a more sceptical view and there was a rush to remove cash from the stricken bank, to the extent that long queues formed outside their branches. Northern Rock had to borrow £25bn from the Bank of England. Three days later the Government guaranteed all Northern Rock deposits and the queues disappeared. Interbank yields remained at elevated levels but there was a dramatic downward move in gilt yields as investors fled to the safety of Government backed securities. Five year gilt yields eventually dropped to levels of 4.4% by the end of the calendar year.

On 18th September the Federal Reserve again cut rates by 50bp, to 4.75%, as concerns rose that the credit crunch was having a negative effect on the real economy. The oil price continued to rise and reached $80pb in September, a trend that continued throughout the autumn. Sector adjusted its interest rate forecast indicating rates had peaked at 5.75% and would decline by 50bp during

2008. Although there was no change to the official rate in October, the interbank rate edged down to be only 50bp above Bank Rate. During October UK data releases showed that the economy was still strong with GDP being revised up to 3.3%, well above trend growth. CPI, however, surprised on the downside, coming in at a below target 1.8%. Although mortgage approvals continued at a reasonable level the RICS housing survey price balance fell by 14.6, the greatest drop since September 2005. At the end of October the Federal Reserve cut interest rates yet again to 4.5% and the following day injected $41bn of liquidity into the markets, the largest amount since September 2001. In early November the Halifax announced the second consecutive monthly drop in UK house prices. Finally, on 6th December, the MPC reduced interest rates by 0.25%, citing concerns that the liquidity crisis could plunge the economy into a major downturn. Inflation, though, was still a major concern for the MPC. In addition, and to help alleviate the stresses in the wholesale markets, the Bank of England agreed to accept a wider range of collateral from those counterparties who borrowed from the Bank. These measures helped in reducing the premium over Bank Rate that was being charged in the interbank market. The markets tiptoed nervously into 2008. There was no change in the MPC rate in early January even though stock markets fell sharply in the early part of the New Year.

After one particularly bad day in the equity markets the Federal Reserve cut interest rates by 75bp to 3.5% on January 22nd - outside of the normal six weekly meeting cycle. Two days later **Societe Generale** revealed that (in shades of Nick Leeson at Barings in 1995), a trader had managed to lose £3.6bn in unauthorized dealing. Gilt yields fell a bit further on this news. Again, on 30th January, the Federal Reserve cut rates down to 3.0%.

Markets were recovering their poise when the UK was hit by the announcement that **Northern Rock would be nationalized.** This was, ultimately, the only solution that was acceptable to the Government and it is a solution that will take some considerable time to work through. The MPC cut rates to 5.25% on 6th February. The February Inflation Report indicated that inflation was likely to breach the Government's target again in the near term but that it would achieve the target in two years' time at constant rates. This statement caused the markets to sell-off as there had been an expectation that the MPC would follow a line similar to the Federal Reserve, albeit not of the same magnitude. The MPC, however, expressed concern at the inflation outlook, anticipating having to write another letter to the Chancellor explaining why CPI had breached its target. In the Euro zone the ECB left interest rates unchanged throughout the period of turbulence in the markets, although they did offer liquidity very freely. Continental banks were heavily involved in the sub-prime fiasco, particularly UBS where an $11bn write-off was made. In late February and early March the interbank markets seized up again forcing the central banks to inject massive amounts of liquidity and to relax the quality of collateral that they would lend against. Darling's first budget was a neutral affair, enlivened by a huge increase in debt issuance for 2008/9. This increase temporarily unsettled the gilt market forcing PWLB rates up sharply at the front end.

On 14th March the credit crunch claimed its biggest victim, US investment bank **Bear Stearns**. To avoid systemic issues Bear Stearns was bought by JP Morgan, with help from the Federal Reserve. The year ended with the money markets anxious and nervous and 3 month cash 75bp above bank rate.

7. BORROWING AND INVESTMENT RATES IN 2007/08

12-month bid rates: One year LIBID was on a rising trend until September 2007. Initially the increase was due to the interest rate outlook and the expectation that the MPC would need to increase rates to counter inflation. The sub-prime crisis then took over as lenders became nervous about lending for longer periods. The one year rate reached a level of over 6.5% in September 2007 before easing back down to just over 5.5% by the end of the calendar year. In 2008 interest rate expectations veered towards cuts in rates again and so the one year moved down to 5.1%. Following the February Bank Rate cut and Inflation Report it edged back up again to 5.4% and continued higher to 5.8% in March as interbank markets seized up again.

5 (and 10 year) gilt yields: ***(this paragraph will be relevant to those authorities with externally managed investments).*** These yields followed the pattern of the one year until the end of July. From April to July yields rose as the interest rate outlook was negative. From July onwards however, they benefited from the credit crunch and yields in both areas were driven lower by 'flight to quality' investors. The high point in 10 years was just under 5.6% and in 5 years about 5.7%, both in July. The low point in ten years was in January when the yield dropped to 4.4%.

Longer-term interest rates – The PWLB 45-50 year rate started the year at 4.45% (25 year at 4.65%) and fell to a low of 4.38% in March 2008 (25 year low was 4.45% January). The high point, of which there were several, for 45-50 year was 4.90% (25-30 year had several highs of 5.15% in June/July 2007) before finishing the year at 4.42% (25-30 year 4.60%). The volatility in yields was a direct reflection of the massive turnaround in interest rate sentiment brought about by the sub-prime issue in the US. A radical change to the PWLB rate structure was introduced by the DMO on 1st November when they moved to single basis point moves in their rates and, at the same time, introduced a separate repayment rate at a level significantly below the rate at which they would lend new money.

8. BORROWING OUTTURN FOR 2007/08

Treasury Borrowing** - **Insert actual borrowings and timings.

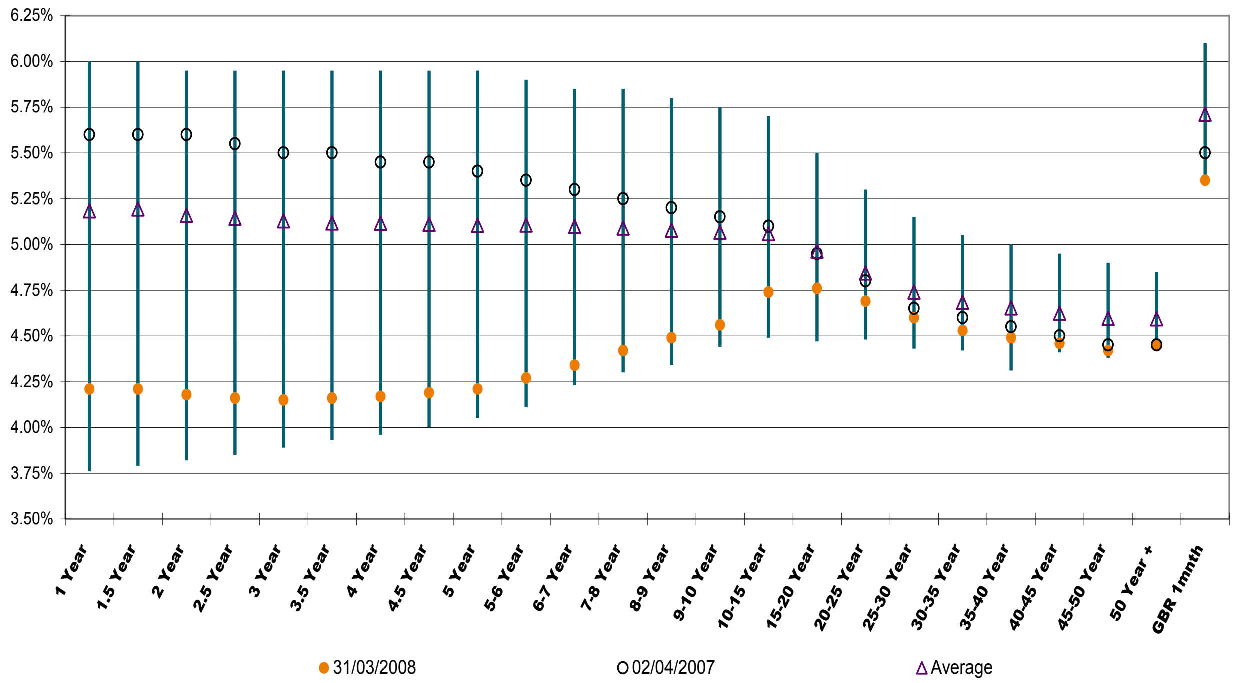
As comparative performance indicators, average PWLB maturity loan interest rates for 2007/08 were:

1 year	5.18%
9.5 - 10 year	5.07%*
25 - 30 year	4.74%*
49.5 - 50 year	4.60%*
1 month GBR variable	5.71%

* due to the change in banding of PWLB rates as from 1.11.07, some interpolation has had to be used to calculate some average figures for 2007/08 and to produce the graph on the next page.

The graph below shows the range (high and low points) in rates for each maturity period during the year, and individual rates at the start and end of the financial year:

PWLB rates 2007/08



Debt Performance - As highlighted in section 1 above the average debt portfolio interest rate has moved over the course of the year from XX*% to XX%.* The approach during the year was:

Select as appropriate:

1. To draw longer term fixed rate debt, to take advantage of low long term rates and reduce exposure to fluctuations in short term interest rates: or
2. To borrow at short term variable rates, as they were generally lower than longer term rates and were not expected to rise significantly within the next year or so; or
3. To maintain borrowing at short term rates to minimise any corresponding risk from maintaining short-term investments; or
4. Fund borrowing from surplus cash.

9. COMPLIANCE WITH TREASURY LIMITS

During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Council's annual Treasury Strategy Statement. The outturn for the Prudential Indicators *is shown in appendix 1.*

10. INVESTMENT OUTTURN FOR 2007/08

Include whichever of the below is applicable.

Internally Managed Investments - The Council manages its investments in-house and invests with the institutions listed in the Council's approved lending list. The Council invests for a range of periods from overnight to XXX days / Y years, dependent on the Council's cash flows, its interest rate view and the interest rates on offer.

New investment instruments – clients may wish to include some comments if there has been diversification during the year into using some new investment instruments or other changes.

(if applicable) **EuroSterling bonds** - In order to build some degree of stability into investment returns over the medium term, the Council invested £x million in bonds issued by ~name the Eurosterling bond issuer(s)~, maturing in ~year~ which will enable the Council to lock into a return of ___% (the gross redemption yield on the bond). These bonds have the highest credit quality and are 'AAA' rated by Moody's/S&P (as applicable).

Externally Managed Investments - The Council has investments managed externally by << name(s) of fund manager(s)>>. The fund management agreement(s) between the Council and the Fund Manager(s) defines the limits for maximum weighting in gilts/bonds and maximum duration of the fund. Counterparty criteria and exposure limits are also pre-defined therein.

Investment Strategy - The expected short-term investment strategy for in-house managed funds was **<u>either:</u>**

1. This Council viewed the market's expectation for Bank Rate as too low, and that short term rates would rise during the year. Investments were, accordingly, kept short, with a view to enabling returns to be compounded more frequently.

OR

2. This Council viewed that the market's expectation for Bank Rate was too high, and investments were accordingly weighted to longer periods, with a view to enabling returns to be maintained in a falling interest rate environment.

Alternative investment strategy - If clients followed Sector's general advice, their investment strategy would have been: (Scottish clients: please note that Sector started a Scottish model investment portfolio in April 2007. The paragraph below is not applicable for use by Scottish clients for the 2007/08 Annual Report).

Version for English and Welsh authorities.
At the start of the year our treasury advisors, Sector, had forecast that interest rates would increase due to concerns around rising inflationary pressures. These concerns grew further and correspondingly caused the forecast for interest rates to rise in order to counter this problem. The Bank of England duly reacted to the inflation threat with two 25bp increases in Bank Rate by August with market expectation that one further increase of 0.25% to 6% would be required.

However, in August the US sub-prime mortgage disaster exploded and stopped any further increase in Bank Rate above 5.75%. This crisis generated even greater volatility and fear that gave rise to a credit squeeze resulting in market rates rising to over 100 basis points above Bank Rate as banks introduced credit spreads. The markets became dislocated from the fundamentals of global economics and became dominated by the vagaries of financial markets in turmoil.

Throughout the year Sector advised to take advantage of the rising rates and invest in the one year period as and when previous investments matured. On occasions the option to place on call, or short dated investment, was taken in order to time investment successfully at better levels and to develop a spread of maturities.

The running return at the year end was 5.69% compared to the benchmark average uncompounded 7 day LIBID rate of 5.30%. The portfolio is now positioned to do well in the coming year.

The return for the year on the portfolio was 5.49%, compared to the average uncompounded 7 day LIBID benchmark of 5.58%, and compares well with the returns generated by Fund Managers. Despite the huge volatility and uncertainty, the portfolio has only marginally under performed the benchmark in 2007/08. Average duration for the portfolio at year end was 262 days with maturities spread from four to fourteen months.

Version for Scottish authorities.

To meet the requirements of Scottish authorities, and authorities restricted to lending to a maximum duration of one year, our treasury advisors, Sector, established a model investment portfolio, specifically to reflect these constraints within the investment strategy.

At the start of the year Sector had forecast that interest rates would increase due to concerns around rising inflationary pressures. These concerns grew further and correspondingly caused the forecast for interest rates to rise in order to counter this problem. The Bank of England duly reacted to the inflation threat with two 25bp increases in Bank Rate by August with market expectation that one further increase of 0.25% to 6% would be required.

However, in August the US sub-prime mortgage disaster exploded and stopped any further increase in Bank Rate above 5.75%. This crisis generated even greater volatility and fear that gave rise to a credit squeeze resulting in market rates rising to over 100 basis points above Bank Rate as banks introduced credit spreads. The markets became dislocated from the fundamentals of global economics and became dominated by the vagaries of financial markets in turmoil.

Throughout the year Sector advised clients to take advantage of the rising rates and invest in the one year period as and when previous investments matured. On occasions the option to place monies on call, or short periods, was taken in order to time investment successfully at better levels and to develop a spread of maturities.

The running return at the year end was 6.09% compared to the benchmark average uncompounded 7 day LIBID rate of 5.30%. The return for the year on the portfolio was 5.96%, compared to the average uncompounded 7 day LIBID benchmark of 5.58%, and compares very well with the returns generated by Fund Managers. The short term nature of the portfolio has enabled advantage to be taken of the volatility that has ensued throughout the year and funds to be locked into the high longer term rates available. The portfolio has significantly out performed the benchmark in 2007/08 in its first year of operation. Average duration for the portfolio at year end was 109 days.

Investment Outturn for 2007/08 - Detailed below is the result of the investment strategy undertaken by the Council.

	Average Investment	Rate of Return (gross of fees)	Rate of Return (net of fees)	Benchmark Return *
Internally Managed			N/A	
Externally Managed				

Please select the benchmark appropriate to your funds. The compounded rates are for externally managed funds. The uncompounded rates are for internally managed funds.

7 day LIBID compounded weekly	5.70%
7 day LIBID uncompounded	5.58%
3 Month LIBID compounded quarterly	6.06%
3 Month LIBID uncompounded	5.92%

***If the benchmark for your externally managed funds was changed to 3 month LIBID during the year; then state*:**

The benchmark for funds managed by XXX was changed from 7-day LIBID compounded weekly to 3 month LIBID compounded quarterly. This was done in consultation with our Treasury advisors, Sector Treasury Services, to reflect a more realistic neutral investment position for core investments with a medium term horizon and a rate which is more stable with fewer fluctuations caused by market liquidity. Historically, this rate has been slightly higher than the 7-day rate and therefore more challenging for the manager, but one which does not necessitate a significantly increased level of risk.

(if applicable) Performance of the Council's Fund Manager(s): Authorities may like to include here the commentary/analysis undertaken by Sector Treasury Services, in particular, the inclusion of the fund manager industry scatter graphs showing how the Council's externally managed investments have performed against their peer group.

No institutions in which investments were made had any difficulty in repaying investments and interest in full during the year.

11. DEBT RESCHEDULING

Our advisers started 2007/8 with the expectation that the 50 year PWLB would reach a level of 4.25% during the financial year, most likely towards the end of the period. Their advice was, therefore, to hold off borrowing longer dated debt until later in the year. By the end of June the forecast had been revised as the 50 year PWLB rose to around 4.85%, generating a revised recommendation to review taking new long term borrowing at levels around 4.50%, although the forecast still allowed for rates to reduce to 4.25% later in 2007/8. With long term PWLB rates at these higher levels, the advice was to borrow (if borrowing was required urgently) at the short end of the interbank market even though Bank Rate was raised to 5.75% in this period. The turmoil that then hit the markets mid year had a marked effect on PWLB rates for the rest of the financial year. Long term rates fell back to, and below, 4.50% (although not as low as 4.25%) while rates at the short end fell below 4% giving an opportunity to lock into yields of 4.25% and lower for periods as long as 6 years. LOBO structures also offered levels of 4.25% and even sub 4% during this period of unprecedented turmoil in the markets.

Rescheduling opportunities presented themselves until 1st November when the PWLB radically changed the structure of their rates. Up to that point there had been various opportunities to improve the terms of the debt holdings by restructuring adjacent periods, whilst being mindful of the requirements of the new SORP. Longer term restructuring could only be done by moving into LOBOs and only if the LOBO offered a rate of 4.25% or lower to fit in with our advisers' forecast.

On 1st November the PWLB imposed two rates for each period, one for new borrowing and a new, significantly lower rate for early repayment of debt. The differential between the two rates ranged from 26bp (basis points) in the shorter dated maturities to over 40bp in the longer ones. They also introduced daily movements of 1bp instead of 5 bp and rates in half year periods throughout the maturity range (previously had been mainly in 5 year bands). These changes effectively prevented the Council from restructuring the portfolio into new PWLB borrowing.

……….(Insert any rescheduling undertaken)

(Clients who have undertaken rescheduling should contact their usual consultant for assistance with this section).

12. OTHER ISSUES

(Please adapt this paragraph if appropriate to your authority.) Authorities may also have needed to take account of extraordinary circumstances arising in 2007/08 e.g. partial or total housing stock transfer (with or without overhanging debt); ALMO funding; borrowing in advance of need; externalisation of internal borrowing etc.

APPENDIX 1: PRUDENTIAL INDICATORS

PRUDENTIAL INDICATOR	2006/07	2007/08	2007/08
(1). EXTRACT FROM BUDGET AND RENT SETTING REPORT	**£'000**	**£'000**	**£'000**
	actual	**original**	**actual outturn**
Capital Expenditure			
Non - HRA	£	£	£
HRA (applies only to housing authorities)	£	£	£
TOTAL	£	£	£
Ratio of financing costs to net revenue stream			
Non - HRA	%	%	%
HRA (applies only to housing authorities)	%	%	%
Net borrowing requirement			
brought forward 1 April	£	£	£
carried forward 31 March	£	£	£
in year borrowing requirement	£	£	£
Capital Financing Requirement as at 31 March			
Non – HRA	£	£	£
HRA (applies only to housing authorities)	£	£	£
TOTAL	£	£	£
Annual change in Cap. Financing Requirement			
Non – HRA	£	£	£
HRA (applies only to housing authorities)	£	£	£
TOTAL	£	£	£
Incremental impact of capital investment decisions	**£ p**	**£ p**	**£ p**
Increase in council tax (band D) per annum *	£xxx.xx	£xxx.xx	£xxx.xx
Increase in average housing rent per week (housing authorities only)	£xx.xx	£xx.xx	£xx.xx
* or increase in precept for police, fire or other precepting authorities			

NOTE. The treasury management Prudential Indicators below would normally be unchanged during the year. This table has been included in case they have changed or if clients wish to include them so as to give a more complete view of Prudential Indicators.

If these indicators have been changed after being originally set in the Treasury Management Strategy Statement, then an explanation should be added as to why they were changed.

PRUDENTIAL INDICATOR	**2006/07**	**2007/08**	**2007/08**
(2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS	**£'000**	**£'000**	**£'000**
	Actual	**Original**	**Final**
Authorised limit for external debt -			
borrowing	£	£	£
other long term liabilities	£	£	£
TOTAL	£	£	£
Operational boundary for external debt -			
borrowing	£	£	£
other long term liabilities	£	£	£
TOTAL	£	£	£
Upper limit for fixed interest rate exposure			
expressed as either:-			
Net principal re fixed rate borrowing / investments OR:-	£ or %	£ or %	£ or %
Net interest re fixed rate borrowing / investments	£ or %	£ or %	£ or %
Upper limit for variable rate exposure			
expressed as either:-			
Net principal re variable rate borrowing / investments OR:-	£ or %	£ or %	£ or %
Net interest re variable rate borrowing / investments	£ or %	£ or %	£ or %
Upper limit for total principal sums invested for over 364 days (per maturity date)	£	£	£

Maturity structure of fixed rate borrowing during 2007/08	**upper limit**	**lower limit**
under 12 months	%	%
12 months and within 24 months	%	%
24 months and within 5 years	%	%
5 years and within 10 years	%	%
10 years and above	%	%

APPENDIX 2: CENTRAL BANK RATE MOVEMENTS

	UK	UK	UK	US	EU	UK	US	ECB
	MPC	MPC Minutes	Inflation Report	FOMC	ECB	Bank Rate	Fed. Rate	Refi Rate
2007								
Jan	10-11	24		30-31	11	5.25%	5.25%	3.50%
Feb	7-8	21	14	21 (mins)	8	5.25%	5.25%	3.50%
Mar	7-8	21		20-21	8	5.25%	5.25%	3.75%
Apr	4-5	18		11 (mins)	12	5.25%	5.25%	3.75%
May	9-10	23	16	9, 30 (mins)	10	5.50%	5.25%	3.75%
Jun	6-7	20		28-29	7	5.50%	5.25%	4.00%
Jul	4-5	18		18 (mins)	5	5.75%	5.25%	4.00%
Aug	1-2	15	8	7, 29 (mins)	2	5.75%	5.25%	4.00%
Sep	5-6	19		18	6	5.75%	4.75%	4.00%
Oct	3-4	17		9 (mins), 30-31	4	5.75%	4.50%	4.00%
Nov	7-8	21	14	21 (mins)	8	5.75%	4.50%	4.00%
Dec	5-6	19		11	6	5.50%	4.25%	4.00%
2008								
Jan	-	-		22		5.50%	3.50%	4.00%
Jan	9-10	23		29-30		5.50%	3.00%	4.00%
Feb	6-7	20	13	21 (mins)		5.25%	3.00%	4.00%
Mar	5-6	19		18		5.25%	2.25%	4.00%

SECTOR

APPENDIX 3: IMPACT OF THE CREDIT CRUNCH