

Devon and Cornwall Police Authority Corporate Governance Committee

17<sup>th</sup> November 2009

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Report of the Treasurer

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## Investment Risk and the Treasury Management Strategy

**Recommended:**

- (i) Members note the Draft Treasury Management Objectives and Governance Arrangements**
- (ii) A sub Committee of the Corporate Governance Committee be formed to review the Annual Treasury Management Strategy in January 2010.**

### Background

1. Following the collapse of Icelandic financial institutions, the House of Commons Select Committee for Communities and Local Government conducted an inquiry into current practice in local authority treasury management and issued a report containing a number of recommendations. The Audit Commission also conducted a review and the recommendations of that review were reported to the Corporate Governance Committee in June 2009. In addition CIPFA has revised its Treasury Management Code of Practice, the revised code is due to be published at the end of November.
2. The Police Authority last substantially revised its Treasury Management policy in April 2002. A Statement of Treasury Management Practices was established at that time and is currently applicable to all treasury management transactions. In addition the Treasury Management Strategy is updated annually and approved by the Police Authority at the same time as the Three-Year Financial Strategy. The Treasurer also reviews and amends our counterparty list frequently in response to market conditions. The Authority has never lost any capital.

### The Police Authority's Treasury Management Arrangements

3. A significant recommendation of the House of Commons Select Committee for Communities and Local Government was that the "Audit Committee" should be given the responsibility for scrutiny of the treasury management function. It is expected that this recommendation will be reflected in the new CIPFA code. Within the Police Authority the role of scrutiny of the treasury management function would fall to the Corporate Governance Committee.
4. When the revised CIPFA code is available the current Treasury Management Practices will be revised to reflect the new best practice. In addition it is proposed that Treasury Management Objectives and Governance Arrangements should be set out in a document that is separate from the Annual Treasury Management Strategy. It is therefore intended that the following documents will be taken to the Police Authority meeting in February 2010 for member's consideration:
  - The Treasury Management Objectives and Governance Arrangements
  - Treasury Management Practices (a detailed set of policies and practices governing individual transactions)
  - The Annual Treasury Management Strategy

5. To provide members of the Corporate Governance Committee with the background required to scrutinise the Annual Treasury Management Strategy a draft of the Treasury Management Objectives and Governance Arrangements that will be recommended to the Police Authority is attached as Annex 1. This draft will be updated when the CIPFA code is published to ensure that it complies with the new code. Members should note the proposed role for the Corporate Governance Committee in overseeing the adequacy of treasury management training for members.
  
6. Annex 2 provides a list of the current Treasury Management Practices in relation to risk management. This gives an overview of the risks inherent in treasury management matters. It is intended that these practices will be updated to reflect the best practice to be set out within the revised CIPFA code and any related guidance.

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Sponsored by: Stephen Barrett, Police Authority Treasurer

**Devon and Cornwall Police Authority  
Draft Treasury Management Objectives and Governance Arrangements**

**Objectives**

1. Effective management and control of risk is the prime objective of the Authority's treasury management activities.
2. The Authority attaches a high priority to revenue cost stability. This aids stable financial planning and avoids a stop-start approach to service delivery. This means it adopts a relatively low-risk attitude to treasury management, and accepts that this may come at a cost.
3. The main risks with regard to treasury management activities are security, liquidity and yield risk. The Authority's treasury management policies will prioritise the risks in that order of importance, that is highest priority will be given to security, followed by liquidity and then yield.
4. The Authority's appetite to manage risk by placing funds with financial institutions (rather than with the UK Government's Debt Management Office) will be set out in the Annual Treasury Management Strategy .
5. The Authority will pursue best value in treasury management within the context of effective risk management.
6. The Authority's debt portfolio will be managed on a long-term basis with a high regard to the effect on future taxpayers and citizens as well as current ones. Fiduciary duty applies to the future as well as the present. Treasury management activity will seek the lowest 'whole life cost' at an appropriate level of risk.
7. The debt management strategy and the investment strategy will be considered together. This will ensure that there is an effective consideration of the risk embodied in the overall position.
8. Diversification will be a key consideration in setting the treasury management strategy. This includes not just diversification between counterparties but also, diversification between countries, sectors and instruments.
9. The Authority will ensure that the instruments used are appropriate when taking account of the skills and understanding of members and officers.
10. All treasury management activity will be undertaken in such a way that it complies with statute, treasury management best practice and accounting requirements.

## Governance Arrangements

1. The Police Authority policies with regard to Treasury management will be contained within the following documents
  - The Treasury Management Objectives and Governance Arrangements
  - Treasury Management Practices (a detailed set of policies and practices governing individual transactions)
  - The Annual Treasury Management Strategy

Decisions in relation to the Treasury Management Objectives, the Statement of Treasury Management Practices and the Annual Treasury Management Strategy are reserved to the Police Authority.

2. The Resources Committee will receive treasury management monitoring information and will have delegated authority to make changes to the Annual Treasury Management Strategy within the constraints of the Treasury Management Objectives
3. The Corporate Governance Committee has responsibility to scrutinise the Annual Treasury Management Strategy. This may be performed through a sub-committee of the Corporate Governance Committee.
4. The counterparty list will be approved annually as part of the Annual Treasury Management Strategy. The Police Authority Treasurer has delegated authority to remove counterparties from the list or reduce the lending limits, any changes will be reported to next Resources Committee. Any addition of counterparties to the list or any increase in the lending limits will be approved by Treasurer after consultation with the Chair of the Resources Committee and the Chair of the Corporate Governance Committee.
5. The Treasurer is responsible for ensuring that specific training in treasury management is made available to all police authority members on an annual basis. The Corporate Governance Committee will have responsibility for monitoring its adequacy.
6. The Authority may use external or internal fund managers to manage all or a portion of its investment portfolio.
7. The Authority may use external advisers to provide advice or information on treasury management activities.
8. Day to day management decision making will be delegated to the Treasurer including such matters as the timing and amount of any new borrowing or lending within the limits as set out in the Annual Treasury Management Strategy.

## **TMP1 Risk Management**

The responsible officer will design, implement and monitor all arrangements for the identification, management and control of treasury management risk, will report at least annually on the adequacy/suitability thereof and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the organisation's objectives in this respect, in accordance with the reporting procedures set out in TMP6 below.

### **(i) Liquidity Risk Management**

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

### **(ii) Interest Rate Risk Management**

The organisation will manage its exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements.

### **(iii) Exchange Rate Risk Management**

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

### **(iv) Inflation Risk Management**

The effects of varying levels of inflation, insofar as they can be identified as impacting directly on its treasury management activities, will be controlled by the organisation as an integral part of its strategy for managing its overall exposure to inflation.

The organisation will achieve the above objectives by the prudent use of its approved financing and investment instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates, exchange rates or inflation. The above are subject at all times to the consideration and, if required, approval of any policy or budgetary implications.

### **(v) Credit and Counter-party Risk Management**

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

(vi) Refinancing Risk Management

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

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

(vii) Legal and Regulatory Risk Management

The organisation will ensure that all of its treasury management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. In framing its credit and counter-party policy, it will ensure that there is evidence of counter-parties' powers, authority and compliance in respect of the transactions they may effect with the organisation, particularly with regard to duty of care and fees charged.

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

(viii) Fraud, Error and Corruption, and Contingency Management

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

(ix) Market Risk Management

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