

Appendix I - Treasury Management Implications of HRA Reform

As discussed in Section 5 of the report, the reform of the HRA finance system has consequences for the treasury management of the Council. As part of the reform, the HRA's debt portfolio needs to be separately identifiable to that of the General Fund, and the HRA will hold some autonomy over the management of its debt portfolio. However, in order to ensure that the treasury management function of the Council remains effective and provides value for money, and given that the Section 151 officer for both the General Fund and the HRA is the Deputy Chief Executive and City Treasurer, the HRA's treasury portfolio must be run in the context of the overall Council portfolio.

This appendix seeks to explain how the debt portfolio of the Council has been split between the General Fund and the HRA, and how the HRA treasury position will be managed going forward.

The Portfolio Split

One of the principles behind the reform of HRA finance was to provide some level of treasury autonomy for the HRA, separating its debt from the Council's so that its treasury position could be managed separately. To achieve this, the debt portfolio was to be split at the point that the debt settlement was made.

On the 28 March 2012, the Council received c. £294m which was to be used to reduce the debt held by the Council. The table below shows the Council's treasury portfolio before and after the settlement:

| | Pre reform | | Post reform |
|-------------------|----------------|--|----------------|
| | £'000 | | £'000 |
| PWLB | 199,966 | | 0 |
| Market | 549,640 | | 480,215 |
| Stock | 8,159 | | 8,159 |
| Gross Debt | 757,765 | | 488,374 |
| Deposits | -17,954 | | -42,839 |
| Net Debt | 739,811 | | 445,535 |

At this point, the debt was to be split according to the relative capital financing requirements (CFRs) of both the General Fund and the HRA. The cash remainder of the settlement could not be used to redeem further market debt so, to ensure that the HRA CFR fell by the full level of the settlement, a notional transaction took place. An amount of debt equivalent to the cash remainder was transferred from the HRA to the General Fund, alongside the cash. This had a neutral effect on the General Fund's net debt.

The table below shows the CFRs before and after the debt settlement, with the HRA CFR falling by the settlement:

| CFRs | Pre reform | | Post reform | % of total |
|--------------|------------------|--|-----------------------------|----------------|
| | <i>£'000</i> | | <i>£'000</i> | |
| General Fund | 675,454 | | 675,454 | 84.47% |
| HRA | 418,463 | | 124,187 | 15.53% |
| Total | 1,093,917 | | 799,641 | 100.00% |
| | | | <i>Of which financed:</i> | |
| | | | 488,374 | |
| | | | <i>Of which unfinanced:</i> | |
| | | | 311,267 | |

As can be seen from the tables below, the debt was to split in a ratio of 84.47:15.53 between the General Fund and the HRA, including the unfinanced CFR element. This is the level of internal borrowing undertaken in lieu of external borrowing, through the use of cash balances to fund expenditure rather than external borrowing. It was decided, for administrative reasons, that all of the Council's remaining stock debt should be held by the General Fund, which increased the relative level of unfinanced CFR held by the HRA.

The final split of the debt portfolio is shown in the table below:

| | General Fund | HRA | Total |
|----------------------------|----------------|----------------|----------------|
| | <i>£'000</i> | <i>£'000</i> | <i>£'000</i> |
| Market | 405,636 | 74,579 | 480,215 |
| <i>% of total market</i> | <i>84.47%</i> | <i>15.53%</i> | |
| Stock | 8,159 | 0 | 8,159 |
| <i>% of stock</i> | <i>100.00%</i> | <i>0.00%</i> | |
| Total Loans | 413,795 | 74,579 | 488,374 |
| <i>% of total loans</i> | <i>84.73%</i> | <i>15.27%</i> | |
| Unfinanced CFR | 261,659 | 49,608 | 311,267 |
| <i>% of unfinanced CFR</i> | <i>84.06%</i> | <i>15.94%</i> | |
| Total CFR | 675,454 | 124,187 | 799,641 |
| <i>% of total CFR</i> | <i>84.47%</i> | <i>15.53%</i> | |

Future HRA borrowing

Following the split of the portfolio, the HRA can make borrowing decisions according to the needs of their business plan, provided those decisions are aligned with their treasury strategy and are agreed by the Section 151 officer. The amounts and maturity periods of any future loans will be determined by the HRA, in conjunction with the Treasury Management team and the Deputy Chief Executive and City Treasurer. Any future borrowing made by the Council will be for either the General Fund or the HRA and not for the Council in general.

Use of Temporary Cash Balances and Temporary Borrowing

Although the HRA's treasury position is now independent of the General Fund, both are managed in the name of the Council as a whole. As such, the day to day

treasury position of the Council, whilst having regard to the impact on the HRA and the General Fund, will be run on a Council basis – this simplifies the risk management of the treasury position, and should help to ensure that the treasury function is providing value for money.

To achieve this, the General Fund will deposit and temporarily borrow externally, but the HRA will only be able to deposit with the General Fund and, should it be required, will only be able to access temporary borrowing through the General Fund. In order to ensure that this is fair, interest rates will be applied to any such internal transfers, as summarised below:

- If the General Fund has temporary investments, HRA investments with the General Fund will earn – ***average portfolio temporary investment rate***
- If the General Fund does not have temporary investments, HRA investments with the General Fund will earn – ***SONIA***
- If the General Fund has temporary borrowing, HRA temporary borrowing from the General Fund will be charged – ***average portfolio temporary borrowing rate***
- If the General fund does not have temporary borrowing, HRA temporary borrowing from the General Fund will be charged – ***SONIA***

The Bank of England and the Financial Conduct Authority (FCA) are committed to phasing out LIBOR before the end of 2021. Therefore, the market rates used are SONIA which the Council will use for benchmarking investments and temporary borrowing.

Future Reporting

The intention is to continue to report to Members the overall treasury position of the Council, including both the General Fund and the HRA. Separate reports will be provided on the General Fund and the HRA, when required.