

Treasury Management Practice Credit and Counterparty Risk Management

1 Introduction

- 1.1 The Office of the Deputy Prime Minister (now DCLG) issued investment guidance on 12th March 2004. In common with the relaxation of borrowing controls in the prudential system, the more flexible guidance replaces the current regulatory approach. These guidelines do not apply to either trust funds or pension funds which are regulated by different regulatory regimes.
- 1.2 The key intention of the guidance is to maintain the current requirement for councils to invest prudently, and to ensure that priority is given to security and liquidity before yield. In order to facilitate the achievement of this objective the guidance requires this Council to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. This Council adopted the Code on 27 March 2003 and will apply its principles to all investment activity. In accordance with the Code the Head of Corporate Finance has produced its treasury management practices and this part, in respect of investment, requires amendment.

2 . Annual Investment Strategy

- 2.1 The key requirements of both the Code and the investment guidance are for the Council to set an annual investment strategy, as part of its annual treasury strategy for the following year, covering the identification and approval of following:
- the strategy guidelines for decision making on investments, particularly non-specified investments,
 - the principles to be used to determine the maximum periods for which funds can be committed,
 - the specified investments that the Council will use. These are high security (i.e. high credit rating, although this is as defined by the Council since no guidelines are given), and high liquidity investments in sterling and with a maturity of no more than 364 days. This defines the broad categories of investment to be used and the regularity of monitoring, and
 - the non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and setting a limit to the overall amount of the various categories that can be held at any time.
- 2.2 This strategy is to be approved by full Council.

3 Investment Policy

3.1 The investment policy proposed for the Council is:

- **Strategy Guidelines** – The main strategy guidelines are contained in the body of the treasury management strategy report.
- **Specified Investments** – These investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the council has the right to be repaid within 12 months if it wishes. These are low risk assets where the possibility of loss of principal or investment income is negligible. Such investments include:
 1. The United Kingdom Government (such as the Debt Management Office, United Kingdom Treasury Bills or gilts with less than one year to maturity).
 2. A local authority.
 3. An investment scheme that has been awarded a high credit rating by a credit rating agency.
 4. A body that has been awarded a high credit rating by a credit rating agency, such as a bank or building society.

Category 3 covers any money market fund rated AAA by Standard and Poor's, Moody's or Fitch rating agencies.

Category 4 covers bodies with a minimum rating of F1 (or the equivalent) as rated by Standard and Poor's, Moody's or Fitch rating agencies. Within these bodies, and in accordance with the Code, the Council has set additional criteria to set the time and amount of monies which may be invested in these bodies. This criterion is

- No more than £2,000,000 or 25% of funds available (whichever is the greater) will be invested with one counterparty at any time.
- **Non-Specified Investments** – Non-specified investments are any other type of investment (i.e. not defined as specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Non specified investments would include any sterling investments with:

	Non Specified Investment Category	Limit (£ or %)
a.	Building societies not meeting the basic security requirements as specified investments. The operation of some building societies does not require a credit rating, although in every other respect the security of the society would match similarly sized societies with ratings. The council may use such building societies which are ranked in the top 20 building societies as classified by Butlers (The Council's Treasury Management advisors).	£2,000,000 or 25%
b.	Building societies not meeting the basic security requirements as specified investments. The operation of some building societies does not require a credit rating, although in every other respect the security of the society would match similarly sized societies with ratings. The council may use such building societies which have assets in excess of £500m, but are not ranked in the top 20 building societies as classified by Butlers (The Council's Treasury Management advisors).	£1,500,000

Within categories 3 and 4, and in accordance with the Code, the Council has developed additional criteria to set the time and amount of monies which will be invested in these bodies. These criteria are:

- No more than £2,000,000 shall be invested for longer than 364 days.
 - No more than £2,000,000 or 25% of funds available (whichever is the greater) will be invested with one counterparty at any time.
- **The Monitoring of Investment Counterparties** - The credit rating of counterparties will be monitored regularly. The Council receives credit rating advice from its advisers, Butlers, on a daily basis as and when ratings change, and counterparties are checked promptly. On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria, or those on the minimum criteria or placed on negative Creditwatch, will be removed from the list immediately by the Head of Corporate Finance, and if required new counterparties which meet the criteria will be added to the list.

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