

# Prudential Indicators 2008-09 to 2010-11

## Capital Expenditure Prudential Indicators

### a) Estimate of capital expenditure

This indicator requires reasonable estimates of the total of capital expenditure to be incurred during the forthcoming financial year and at least the following two financial years.

The draft capital programme for 2008-09 to 2012-13 is included elsewhere on this agenda and the 2008-09 to 2010-11 figures below are taken from that report. The 2008-09 estimates include £1.082m capital contingency on the General Fund.

The 2007-08 figures, which are included for completeness, are taken from the latest proposed budget in the Capital Monitoring – Position as at 31 December 2007 report, which was agreed by Cabinet on 11 February.

Estimates for 2009-10 and 2010-11 include continuation schemes from previous years and outline proposals for new bids. The programme will be adjusted as necessary in line with the actual bids submitted and the resources available when the annual programmes for the two years are agreed.

Capital Expenditure				
	2007-08	2008-09	2009-10	2010-11
	Latest Estimate £000	Estimate £000	Estimate £000	Estimate £000
General Fund	10,363	5,595	26,843	3,447
HRA	9,075	14,616	14,616	14,316
<b>Total</b>	<b>19,438</b>	<b>20,211</b>	<b>41,459</b>	<b>17,763</b>

Risk – There is a real risk of cost variations to planned expenditure against the capital programme, arising for a variety of reasons, including tenders coming in over budget, changes to specifications, and slippage or acceleration of project phasing. There is also the possibility of needing to provide for urgent and unplanned capital works. The risks are managed by officers on an ongoing basis, by means of active financial monitoring, with monthly reports to Cabinet.

The availability of financing from capital receipts, grants and external contributions also carries significant risk. This is particularly true of capital receipts, as projects in the programme are dependant on forecast receipts, which may or may not materialise in year. Where capital receipts are not received in year the funding gap has to be plugged by prudential borrowing, which has a knock on impact of the Council's debt financing position, and on the other prudential indicators. The

financing position of the capital programme is also closely monitored by officers on an ongoing basis and reported to Cabinet.

## **b) Estimate of capital financing requirement (CFR)**

External borrowing arises as a consequence of all the financial transactions of the authority and not simply those arising from capital spending. The CFR can be understood as the Council's underlying need to borrow money long term for a capital purpose – that is, after allowing for capital funding from capital receipts, grants, third party contributions and revenue.

The council is required to make reasonable estimates of the total CFR at the end of forthcoming financial year and the following two years thereafter. A local authority that has an HRA must identify separately estimates of the HRA and General Fund CFR.

The CFR has been calculated in line with the methodology required by the relevant statutory instrument and the guidance to the Prudential Code. It incorporates the borrowing impacts of the Council's proposed capital programme. The current years estimated closing CFR is also shown for completeness.

Capital Financing Requirement (Closing CFR)				
	2007-08	2008-09	2009-10	2010-11
	31 March 2008 Estimate £000	31 March 2009 Estimate £000	31 March 2010 Estimate £000	31 March 2011 Estimate £000
Non-HRA	21,771	24,335	23,696	23,082
HRA	(8,175)	(8,175)	(8,175)	(8,175)
<b>Total</b>	13,596	16,160	15,521	14,907

## **Prudential Indicators of Affordability**

### **c) Estimates of ratio of financing costs to net revenue stream**

The indicator has been calculated as estimated debt interest costs for the year divided by the net budget requirement for the non-HRA element and total HRA income for the HRA element. The objective is to enable trends to be identified.

The Code requires separate indicators for the HRA and non-HRA element.

The 2007-08 figure is shown for completeness; Members should note that it has been adjusted from the previously reported figure to take into account latest forecasts on the debt-financing budget and to include HRA depreciation as required by the guidance. The negative GF figure for 2007-08 is as a result of the levels of cash balances available for investment and prevailing interest rates both being in excess of budget.

The relatively high ratio for the HRA across all years (compared to General Fund) reflects the requirement to include depreciation in the financing costs, as represented by the value of the Major Repairs Allowance (MRA). This is not required in the General Fund figures.

The figures used for the net revenue stream for 2008-09 and onwards are dependent upon the General Fund and HRA revenue budgets to be agreed by Council and are therefore subject to change. If applicable, updated figures will be provided to Cabinet and Council at the earliest opportunity.

Ratio of financing costs to net revenue stream				
	2007-08	2008-09	2009-10	2010-11
	Adjusted %	Estimate %	Estimate %	Estimate %
General Fund	(1.24%)	0.48%	0.98%	0.88%
HRA	16.58%	16.82%	16.91%	17.33%

Risk – Debt financing costs relating to past and current capital programmes have been estimated in accordance with proper practices. Actual costs will be dependant on the phasing of capital expenditure and prevailing interest rates, and will be closely managed and monitored on an ongoing basis.

**d) Estimates of the incremental impact of new capital investment decisions on the Council Tax**

This indicator represents an estimate of the incremental impact of new capital investment decisions on the annual Council Tax (Band D). It is intended to show the effect on the Council Tax of approving more capital expenditure.

It is estimated that new borrowing of £2.5m (net of MRP) in 2008-09 will support the draft General Fund capital expenditure figures, shown at (a) above. No further borrowing is currently planned for 2009-10 or 2010-11. The costs shown below represent the incremental impact on Council Tax of the unsupported borrowing that is being met directly from revenue budgets (i.e. interest and principal repayments)

Estimates of incremental impact of new capital investment decisions on the Council Tax	
	General Fund
	£ p
2008-09	1.96
2009-10	3.15
2010-11	3.07

**e) Estimate of incremental impact of new capital investment decisions on average weekly housing rent**

This represents an estimate of the incremental impact of new capital investment decisions on average weekly housing rents.

Revenue contributions of £2m in each of the years 2008-09, 2009-10 and 2010-11 will support the HRA capital expenditure programme, which is directed at achieving decent homes standards. The impact on average weekly rents is set out in the table below. The annual increase is a result of the fall in stock each year through right to buy sales.

Estimates of incremental impact of new capital investment decisions on the Council Housing Rents	
	HRA
	£ p
2008-09	3.14
2009-10	3.17
2010-11	3.2

## **Prudence**

### **f) Net borrowing and capital financing requirement**

This is the key indicator of prudence. It is intended to show that net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital requirement for the current and new two financial years.

The Council's net external debt figure is a negative figure – ie investments are in excess of debt. The net external debt figure has therefore been presented as zero.

The increases in CFR for future years (2009-10 and 2010-11) are subject to future Council decisions in respect of the capital programme for those years. The Council currently has no plans to undertake further prudential borrowing in 2009-10 and 2010-11, and the forecasts have been prepared on that basis.

Net external debt less than CFR	
	2008-09 £000
Borrowing	31,306
Less investments	58,069
<b>Net external debt</b>	<b>0</b>
2007-08 Closing CFR (Forecast)	13,596
Changes to CFR:	
2008-09	2,563
2009-10	(639)
2010-11	(613)
<b>Adjusted CFR</b>	<b>14,907</b>
Net external debt less than adjusted CFR	Yes

## External Debt Prudential Indicator

### **g) Authorised limit for total external debt**

For the purposes of this indicator the authorised limit for external debt is defined as the authorised limit for borrowing plus the authorised limit for other long term liabilities for years 1, 2 and 3.

This requires the setting for the forthcoming financial year and the following two financial years of an authorised limit for total external debt (including temporary borrowing for cash flow purposes), gross of investments, separately identifying borrowing from other long term liabilities.

The authorised limit represents the maximum amount the Council may borrow at any point in time in the year. It has to be set at a level the Council considers is “prudent” and be consistent with plans for capital expenditure and financing. It contains a provision for forward funding of future years capital programmes, which may be utilised if current interest rates reduce significantly but are predicted to rise in the following year.

This limit is based on the estimate of the most likely but not worst case scenario, with in addition sufficient headroom over and above this to allow for operational management, for example unusual cash movements.

The Council is asked to approve these limits and to confirm the existing delegated authority to the S.151 Officer, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal and best value for money for the Council. Any such changes would be reported to the Council at its next meeting following the change.

Authorised limit for external debt				
	2007-08	2008-09	2009-10	2010-11
	Limit £000	Limit £000	Limit £000	Limit £000
Borrowing	47,000	41,000	41,000	41,000
Other long-term liabilities	0	2,000	2,000	2,000
TOTAL	47,000	43,000	43,000	43,000

Other long-term liabilities, shown above, relate to insurance reserves. Any future finance leases entered into would also be included in this category

Risk – Risk analysis and risk management strategies have been taken into account in setting this indicator, as have plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes.

**h) Operational Boundary for total external debt**

The proposed operational boundary is based on the same estimates as the authorised limit. However it excludes the additional headroom included within the authorised limit to allow for unusual cash movements.

The operational boundary represents a key management tool for in year monitoring by the S.151 Officer. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified.

The Council is also asked to confirm the existing delegated authority to the S.151 Officer, within the same operational boundary for any individual year, to effect movement between the separately agreed figures for borrowing and other long-term liabilities, in a similar fashion to the authorised limit. Any such changes will be reported to the Council at the next meeting following the change.

Operational boundary for external debt				
	2007-08	2008-09	2009-10	2010-11
	Boundary £000	Boundary £000	Boundary £000	Boundary £000
Borrowing	40,500	36,000	36,000	36,000
Other long-term liabilities	0	2,000	2,000	2,000
<b>TOTAL</b>	<b>40,500</b>	<b>38,000</b>	<b>38,000</b>	<b>38,000</b>

Risk – Risk analysis and risk management strategies have been taken into account in setting this indicator, as have plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes.

**Treasury Management Prudential Indicators**

**i) Upper limits on fixed interest rate exposures**

This indicator sets the upper limits to which the Council is exposed to the effects of changes in fixed interest rates, and is calculated as borrowing that is at fixed rates less investments that are at fixed rates.

The prudential code guidance states that where in doubt borrowing and investments should be treated as being at variable rates for the purposes of this and the following indicator. With this in mind, borrowing in the form of LOBOs (Lenders Option,

Borrowers Option) has been treated as being at variable rates as the rates are reviewed at agreed intervals of typically 6 months or a year.

The limit can be in terms of principal sums or the associated interest; the Council has chosen the former approach. It can be expressed as a percentage or as an absolute amount. Previously this Council has set a limit based on a percentage of total investments. For 2008-09 onwards a cash limited amount is proposed, since this is more transparent and more straightforward to monitor. The 2007-08 indicator is shown for completeness.

The limit has been set at a level that allows for flexibility. It allows for all new long-term borrowing for 2007-08 and 2008-09 to be at fixed rates (e.g. PWLB loans) and for the option of rescheduling of existing LOBOs to fixed rate loans. All borrowing decisions will be taken in line with best practice and prevailing market conditions and in consultation with the Council’s treasury management advisers.

The limit also allows for a range of possibilities in respect of the value of temporary investments at any one point in time, as this is dependant on the cash position of the authority, and also for all the Council’s temporary investments at the budgeted level of £58m to be in the form of fixed rate investments; typically the figure is around 80% to 90%.

Since the Council has an excess of temporary investments over debt, the calculation should result in a negative figure. The upper limit has therefore been set at zero – i.e. a positive result representing an excess of fixed rate debts over temporary investment would exceed the limit.

Upper limits on fixed interest rate exposures		
	Upper Limit %	Upper Limit £000
2007-08	100%	-
2008-09	-	0
2009-10	-	0
2010-11	-	0

**j) Upper limits on variable interest rate exposures**

This indicator sets the upper limits to which the Council is exposed to the effects of changes in variable interest rates, and is calculated as borrowing that is at variable rates less investments that are at variable rates.

The prudential code guidance states that where in doubt borrowing and investments should be treated as being at variable rates for the purposes of this and the following indicator. With this in mind, borrowing in the form of LOBOs (Lenders Option,



Borrowers Option) has been treated as being at variable rates as the rates are reviewed at agreed intervals of typically 6 months or a year.

The limit can be in terms of principal sums or the associated interest; the Council has chosen the former approach. It can be expressed as a percentage or as an absolute amount. Previously this Council has set a limit based on a percentage of total investments. For 2008-09 onwards a cash limited amount is proposed, since this is more transparent and more straightforward to monitor. The 2007-08 indicator is shown for completeness.

The limit has been set at a level that allows for flexibility. It allows for all new long-term borrowing for 2007-08 and 2008-09 to be at variable rates or in the form of LOBOs. All borrowing decisions will be taken in line with best practice and prevailing market conditions and in consultation with the Council's treasury management advisers.

The limit also allows for a range of possibilities in respect of the value of temporary investments at any one point in time, as this is dependant on the cash position of the authority, and also for none of the Council's temporary investments at the budgeted level of £58m to be in the form of variable rate investments; typically the figure is around 10% to 20%.

The limit has been set in line with the Council's operational boundary for external borrowing (excluding long term liabilities at (h) above).

Upper limits on variable interest rate exposures		
	Upper Limit %	Upper Limit £000
2007-08	50%	-
2008-09	-	38,000
2009-10	-	38,000
2010-11	-	38,000

#### **k) Principal sums invested for periods longer than 364 days**

Under the Local Government Act 2003 and the DCLG (formerly ODPM Guidance on Local Authority Investments 2004, all Councils are now permitted to invest for periods exceeding 1 year (or 364 days). The Council is required to set a limit to the level of such investments it might wish to make.

Previously this Council has set a limit based on a percentage of total investments. For 2008-09 onwards a cash limited amount is proposed, since this is more transparent and more straightforward to monitor. The limit has been set at a level that

would allow for monies not anticipated to be spent in year e.g. capital receipts, to be invested for longer periods if interest rates are favourable.

Upper limit on investments for periods longer than 364 days		
	Upper Limit %	Upper Limit £000
2007-08	75%	-
2008-09	-	6,000
2009-10	-	6,000
2010-11	-	6,000

The revised limits above were approved by Cabinet on 26<sup>th</sup> June and Council on 21<sup>st</sup> July 2008.

Risk – This upper limit has been set at a prudent level (approx 10% of forecast total external investments) in order not to compromise cash flow liquidity.

#### **l) Prudential limits for the maturity structure of borrowing**

This represents the amount of projected borrowing that is fixed rate maturing in each period expressed as a percentage of total projected borrowing that is fixed rate at the start of the period where the periods in question are:

- 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.

This sets both upper and lower limits for 2008-09 with respect to the maturity structure of the Council's borrowing.

Maturity structure of borrowing		
	Lower Limit %	Upper Limit %
Under 12 months	0%	25%
1-2 years	0%	25%
2-5 years	0%	50%

5-10 years	0%	100%
Over 10 years	0%	100%

Risk – The debt maturity profile is actively managed to ensure that debt maturity is prudently spread across future years. This ensures that the Council can properly plan for the maturity of its borrowings, and is not exposed to unmanageable risks.

#### **m) Adoption of the CIPFA Code of Practice for Treasury Management**

The Prudential Code requires that the local authority has adopted the CIPFA Code of Practice for Treasury Management in Public Services.

The Council adopted the CIPFA Code of Practice for Treasury Management in the Public Services following its publication in 2001. This was formally minuted as a decision at the meeting of 21 January 2008.

Treasury Management Practices (TMPs), setting out the manner in which the Council will seek to achieve its treasury management policies and objectives and how it will manage and control those activities, were approved by Cabinet on 3 July 2006. They should be reviewed on a regular basis, and this will be undertaken during 2008-09 and reported to Cabinet.