REDDITCH BOROUGH COUNCIL

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Executive
Committee

No Direct Ward Relevance

10th March 2010

PRUDENTIAL INDICATORS and MINIMUM REVENUE PROVISION POLICY

(Report of the Head of Resources)

1. Summary of Proposals

To set the limits under the new Prudential Code for borrowing which the Council is required to agree before the start of the 2010/11 financial year and to review the Prudential Indicators for the current financial year.

To seek members approval to the Minimum Revenue Provision (MRP) Policy for 2010/11.

2. Recommendations

The Committee is asked to RECOMMEND that

1) the Prudential Indicators as set out in the report be approved; and

2) the Minimum Revenue Provision Policy for 2010/11 as defined in option 3, be approved.

3. Financial, Legal, Policy, Risk and Climate Change / Carbon Management Implications

Financial

3.1 The financial implications are contained throughout the report.

Legal

3.2 The Prudential Code for Capital Finance in Local Authorities (Prudential Code) was developed by the Chartered Institute of Public Finance and Accountancy to provide a code of practice to underpin the new system of capital finance embodied in Part 1 of the Local Government Act 2003. Local Authorities are no longer subject to government controlled borrowing approvals and are free to determine their own level of capital investment controlled by self-regulation.

3.3 The setting and revising of prudential indicators should be undertaken by the body that that sets the budget, namely, full Council.

Policy

3.4 The Council's policy regarding borrowing and investments is contained in its Treasury Management Strategy.

3.5. This report will determine the Council's policy on making a MRP for 2010/11.

Risk

3.6. The Council would be failing in its legal obligations under the Local Government Act 2003 if it failed to agree a set of Prudential Indicators for the forthcoming financial year and in its legal obligations under the Local Authorities (Capital Finance and Accounting) (Amendment) Regulations 2008 if it failed to prepare an annual statement of policy on making a MRP.

Climate Change / Carbon Management

3.7 None have been identified.

Report

4. Background

Prudential Indicators

4.1 The key objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable; also, that treasury management decisions are taken in accordance with good professional practice and in a manner that supports prudence, affordability and sustainability.

4.2 To demonstrate that local authorities have fulfilled these objectives, the Prudential Code sets out the indicators that must be used, and the factors that must be taken into account. The Code does not include indicative limits or ratios, these are for the local authority to set for itself subject to the controls under [clause 4] of the Local Government Act 2003.

Minimum Revenue Provision

4.3. The requirement to make a MRP is contained within the Local Authorities (Capital Finance and Accounting) (Amendment) Regulations 2008.

4.4. Following the publication of the Local Authorities (Capital Finance and Accounting) Regulations issued on the 26th February 2008 local authorities are required to prepare an annual statement of policy for making a MRP. The annual statement should be submitted to Council before the start of the financial year.

4.5 MRP is the amount of revenue which an authority sets aside for the repayment of the principal element of any borrowing undertaken to finance capital expenditure. The interest cost of borrowing continues to be a direct charge to revenue. The new regulations that came into force on the 31st March 2008 impose a duty on the Council to make an amount of MRP which it considers to be a "prudent provision".

4.6 The broad aim of "prudent provision" is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of the grant. This authority does not have any borrowing supported by Revenue Support Grant.

4.7 MRP is calculated in the financial year after the capital expenditure has been incurred and so the capital spend in 2009/10 informs the MRP set aside in the revenue account for 2010/11. The new regulations have added an exception to this in that if expenditure has been incurred on an asset which has not become operational then MRP does not need to be set aside until the financial year after the asset becomes operational. In effect authorities are entitled to a "MRP holiday" until the new asset becomes operational.

5. Key Issues

Prudential Indicators

5.1 The Council is required to publish the following indicators introduced by the Code for the next and following two financial years:

a) Actual and estimated capital expenditure,
b) Ratio of financing costs to net revenue stream,
c) Capital financing requirement,
d) Actual limit for external debt,

e) Operational boundary for external debt,
f) Council tax implications of the incremental effect of capital decisions,
g) Treasury Management indicators.

5.2 The prudential indicators for the forthcoming and following years must be set before the beginning of the financial year. They may be revised at any time, and must be reviewed, and revised if appropriate, for the current year when the prudential indicators are set for the following year.

Capital Expenditure

5.3 The estimates of capital expenditure for 2009/10 and future years included in the Council's approved capital programme are:

Approved Programme	2009/10 Estimate £'000	2010/11 Estimate £'000	2011/12 Estimate £'000	2012/13 Estimate £'000
HRA	10,101.4	7,773.0	6,500.4	6,020.0
General Fund	5,653.0	2,169.0	1,670.0	845.0
Total Approved Programme	15,754.4	9,942.0	8,170.4	6,865.0

Ratio of Financing Costs to Net Revenue Stream

5.4 The financing costs include the amount of interest payable and receivable in respect of borrowing and investments. The Net Revenue Stream for the HRA is the amount to be met from housing subsidy and rents and for the General Fund it is the "amount to be met from government grants and local taxation". The estimates of the ratio of financing costs to net revenue stream for the current and future years are:

Ratio of financing costs to net revenue stream				
	2009/10 Estimate	2010/11 Estimate	2011/12 Estimate	2012/13 Estimate
HRA	1.46%	1.37%	1.22%	1.10%
General Fund	(1.08)%	1.85%	2.42%	2.60%

5.5 The figures in the above table are shown as negatives where the interest received from temporary and long term investments is estimated to exceed the cost of temporary borrowing.

Net Revenue Streams for 2009/10 and 2010/11

5.6 The Net Revenue Stream for the HRA is calculated as follows:

	2009/10 Estimate £	2010/11 Initial £
Dwelling rents	19,280,170	19,827,780
Non-dwelling rents	567,410	516,730
Charges for services and facilities	174,090	188,460
Less		
Negative subsidy	6,167,830	6,037,140
Net Revenue Stream	13,853,840	14,495,830

5.7 The Net Revenue Stream for the General Fund is calculated as follows:

	2009/10 Estimate £	2010/11 Estimate £
Revenue Support Grant	1,205,022	818,847
Non-Domestic Rates	5,220,774	5,639,079
Council Tax	5,573,345	5,754,643
Collection Fund	13,782	10,200
Net Revenue Stream	12,012,923	12,222,769

Capital Financing Requirement

5.8 The capital financing requirement is a measure of the extent to which the Council needs to borrow to support capital expenditure. It does not necessarily relate to the actual amount of borrowing at any one point in time. The Council has an integrated treasury management strategy where there is no distinction between revenue and capital cash flows, and the day to day position of external borrowing and investments constantly changes.

Capital Financing Requirement				
	2009/10 Estimate £'000	2010/11 Estimate £'000	2011/12 Estimate £'000	2012/13 Estimate £'000
HRA	13,076	17,576	20,576	22,876
General Fund	15,426	17,125	18,326	18,823
Total	28,502	34,701	38,902	41,699

5.9 Calculation of Capital Financing Requirement from the Council's Balance Sheet

Extracts from Balance Sheet	2008/09 £'000
Fixed Assets	329,945
Less	
Capital Adjustment Account	268,059
Government Grant Deferred Account	967
Revaluation Reserve	42,017
Capital Financing Requirement	**18,902**

5.10 CIPFA's Prudential Code for Capital Finance includes the following key indicator of prudence:

5.11 "In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure 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 Financial Requirement for the current and next two years."

5.12 As at the 31st March 2009 the Council's borrowing exceeded its investments by £9.25 million.

External Debt

5.13 In respect of any external debt, it is recommended that the Council approves the following Authorised Limits for its total external debt gross of investments for the next three financial years. The Authorised Limit for external debt for the forthcoming year is the statutory limit determined under section 3 (1) of the Local Government Act 2003: "A local authority shall determine and keep under review how much money it can afford to borrow."

5.14 The Authorised Limits are consistent with the current capital programme and the proposals for capital expenditure included in the Medium Term Financial Plan and the Council's Capital Strategy. The limits are based on the most likely financial circumstances but with an allowance made for unusual cash movements. It is not anticipated that any borrowing will be undertaken except temporarily until further revenues are received.

Authorised Limit for External Debt				
	2009/10 Revised Estimate £'000	2010/11 Estimate £'000	2011/12 Estimate £'000	2012/13 Estimate £'000
Borrowing	38,000	44,500	49,000	52,000
Other long term liabilities	0	0	0	0
Total	38,000	44,500	49,000	52,000

5.15 The Council is asked to approve the following Operational Limit for external debt for the same period. The Operational Limit is based on the same estimates as for the Authorised Limit but differs in that it does not take into account the allowance for unusual cash movements.

Operational Limit for External Debt				
	2009/10 Revised Estimate £'000	2010/11 Estimate £'000	2011/12 Estimate £'000	2012/13 Estimate £'000
Borrowing	35,000	41,500	46,000	49,000
Other long term liabilities	0	0	0	0
Total	35,000	41,500	46,000	49,000

5.16 The Council's actual external debt at the 31st March 2009 was £26,708 million (£21.195 million in short term borrowing, £5.1 million long term borrowing and £0.383 million bank overdraft). It should be noted that the actual external debt is not directly comparable to the authorised limit and the operational boundary, since the actual external debt reflects the position at one point in time.

Treasury Management

5.17 The Council has previously adopted the CIPFA Code of Practice for Treasury Management in the Public Services. Interest rate risk management is a priority and therefore the Code identifies two indicators that will provide the Operational Boundaries to the exposure to interest rate risk.

a) Upper limits for variable rate exposure and
b) Upper limits to fixed rate exposure.

5.18 It is recommended that the Council sets an upper limit on its fixed interest rate exposures for 2010/11, 2011/12 and 2012/13 of 100% and on its variable interest rate exposures on 50%. This limit on variable rates is consistent with the current approved limit.

5.19 The medium term strategy is to undertake borrowing for capital expenditure. The timing of any longer term borrowing will depend on the profile of capital spend.

5.20 The Council's investments are held in a relatively flexible form and therefore fixed interest rate exposure is not considered to be a significant risk.

Maturity Structure of any Fixed Rate Borrowing (as a percentage of total projected borrowing that is fixed rate)		
	Upper Limit	Lower Limit
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

5.21 The Council has recalled its externalised investments of £15 million, which originated in relation to the Council's reserved capital receipts. This sum is now being invested by the in-house team. The Code requires that authorities set out the total principal of sums invested for periods longer than 364 days and set an upper limit for each forward financial year for the maturity of these investments. The purpose of the indicator is to manage the investment portfolio within good treasury management practice guidelines and ensure there is a spread of investment maturities to reduce risks inherent in interest rate volatility. The following limits are recommended.

Total principal sums invested for periods longer than 364 days	
	£ million
31 March 2008	0.0
31 March 2009	0.0
31 March 2010	0.0

Minimum Revenue Provision Policy

5.22 For all unsupported (prudential) borrowing the Minimum Revenue Provision (MRP) will be based on the estimated life of the assets financed by borrowing in accordance with the MRP guidance.

6. Other Implications

Asset Management	-	None identified.
Community Safety	-	None identified.
Health	-	None identified.
Human Resources	-	None identified.
Social Exclusion	-	None identified.
Environment / Sustainability	-	None identified.

7. Lessons Learnt

7.1 In order to comply with the requirement of the Local Government Act 2003 the Council needs to approve a range of prudential indicators as detailed in the body of this report before the start of the forthcoming financial year. At the same time the Council also needs to approve a Minimum Revenue Provision Policy.

8. Background Papers

Working papers held in Financial Services Team.
CIPFA's Prudential Code – Fully revised 2nd edition
Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008

Changes to the Capital Finance System – consultation [DCLG}

Minimum Revenue Provision Guidance – An informal commentary - Department for Communities and Local Government.

9. Consultation

Relevant Council Officers have been consulted in the preparation of this report.

10. Author of Report

The author of this report is Teresa Kristunas (Head of Resources), who can be contacted on extension 3295 (e-mail teresa.kristunas@redditchbc.gov.uk) for more information.

11. Appendices

None.