REPORT TO THE OVERVIEW & SCRUTINY COMMITTEE

Report No. 11

Date of Meeting	**25th January 2007**
Title of Report	**Annual Prudential Indicators Statement**
Portfolio	**Leader's Responsibilities**
Link to Corporate Priorities	All
Key Decision	Yes
Executive Workplan Ref	A17
Public Report	Yes

Summary of Report

To propose the Council's prudential indicators for 2007/08, 2008/09 & 2009/10 as part of the 2007/08 Budget Setting process. This report will need to be submitted for the approval of the Council.

Officer Recommendations

That the Executive,

1. Note the report and that four indicators (3,4,5 & 7) are subject to further information that will be provided at the meeting;
2. Agree to recommend to Council the prudential indicators;
3. Agree to delegate to the S151 Officer and the Leader the updating of the PI's to be reported to Council.

Other than those implications agreed with the relevant Officers and referred to below, there are no other implications associated with this report.

Financial Implications	Legal Implications	Community & Environmental Implications	Human Resources Implications	Equality & Diversity Implications
Yes	Yes	None	None	None

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1. Background

1.1 The Prudential Code for Capital Finance in Local Authorities, hereafter referred to as the Code, is a statutory requirement laid down in the Local Authorities (Capital Finance & Accounting) (England) Regulations 2003 & enacted in Part 1 of the Local Government Act 2003.

1.2 The Code requires all Councils to consider and set “prudential indicators”, hereafter referred to as the indicators, as part of their budget process.

1.3 The indicators link to the approval of the Council’s capital and revenue budget for 2007/08 and the Medium Term Financial Plan. The indicators also set an integrated framework for the Council’s treasury management activities and guide the Treasury Management Strategy.

1.4 The Code is designed to ensure budgetary plans are affordable, prudent, sustainable & practical. They aim to improve value for money, ensure stewardship of assets & demonstrate service delivery of Council priorities.

1.5 The Prudential Indicators are a key element in the corporate goal of ensuring the Council is a well-managed local authority.

1.6 There is a timing problem in reaching a decision to recommend to Council, which is why the recommendations seek some flexibility and the ability to update the PI’s. Briefly, the shape of the budget will not become clear until late January, after this meeting, but before the matter is considered by Council on January 30th. Even then, the budget will not be finally decided until February 22nd, which might require the PI’s to be reconsidered by Council, for the authority may revise the indicators at any time (Audit Commission advice).

2. The Indicators

1	The Estimate of Capital Expenditure	This shows the planned level of capital expenditure over the planning period. I.e. 2007-2010
2	Not used at present	
3	Ratio of Financing Costs to Net Revenue Stream	This helps to evaluate the impact of funding the capital programme on revenue by stating the debt as a percentage of the Council’s income.
4	Capital Financing Requirement (CFR)	This is calculated from the Council’s actual and forecast balance sheet. It is a measure of the Authority’s underlying need to borrow.
5	Authorised Limit for External Debt	The limit is currently set at £4 million and cannot be exceeded without Council approval.
6	Operational Boundary for External Debt	The limit is currently set at £2 million and represents the expected maximum borrowing to cover short-term cash flow requirements.

7	Incremental Impact of Capital Expenditure Plans	This indicator shows the opportunity cost of the capital programme in terms of lost interest.
8	Upper Limit for Fixed Interest Exposure	This is the maximum percentage of the total borrowing that can be at fixed rate.
9, 10	Upper Limit for Variable Rate Exposure	This is the maximum percentage of the total borrowing that can be at variable rate.
11	Upper Limit for Total Principal Sums invested for over 364 (per maturity date)	This indicator sets the maximum percentage of Council investment funds that can be lent for 1 year or more.
12	Maturity structure of new fixed rate borrowing during 2007-08	This indicator shows the borrowing profile upper and lower limits (%) by time period e.g. < 12 months, 12 – 24 months, 24 months – 5 years, 5 – 10 years & 10+ years.

3 Prudential Indicators for 2007/08 – 2009/10

PI 1 Estimate of Capital Expenditure

Description	2005/06 Actual £000's	2006/07 Projected £000's	2007/08 Budget £000's	2008/09 Budget £000's	2009/10 Budget £000's
Capital Programme & Bids	6,727	6,616	6,271	2,902	3,042
Equipment Fund	552	661	500	500	500
Total	7,279	7,277	6,771	3,402	3,542

These figures are based on the Council's medium term financial plan (MTFP) and include capital spending financed from the Equipment fund. For 2007/08 the amount shown is the total of the base programme and bids and is an upper limit to the projected capital spend. Capital programmes for future years are liable to change as new bids are received in future.

PI 2 N/A

PI 3 Ratio of Financing Costs to Net Revenue Stream

Description	2005/06 Actual £000's	2006/07 Projected £000's	2007/08 Budget £000's	2008/09 Budget £000's	2009/10 Budget £000's
Financing Costs	-1,039	-714			
Net Revenue Stream	12,662	14,096	14,671	14,860	15,361
Ratio	-8.2%	-5.1%			

This indicator reflects the costs of all borrowing, less the interest gained on investments as a percentage of the net revenue stream. The net revenue stream is defined as the finance arising from Government Grants & local taxpayers. (RSG, Council Tax, NNDR)

Whilst the Council is debt-free & has negative financing costs i.e. investment interest exceeds other financing costs, the ratio is negative. When the Council enters into borrowing and the financing costs begin to exceed the investment returns the ratio becomes positive.

If a decision on financing options is effected, this indicator will change.

PI 4 Capital Financing Requirement (CFR)

Description	2005/06 Actual £000's	2006/07 Projected £000's	2007/08 Budget £000's	2008/09 Budget £000's	2009/10 Budget £000's
Capital Financing Requirement (CFR)	-185				

This indicator calculates the Council's underlying need to borrow for capital purposes. The Council is 'debt free' & at the 31st March 2006 has a negative capital financing requirement (CFR).

If a decision on financing options is effected, this indicator will change.

PI 5 Authorised Limit for External Debt

Description	2005/06 Actual £000's	2006/07 Projected £000's	2007/08 Budget £000's	2008/09 Budget £000's	2009/10 Budget £000's
Borrowing	4,000	4,000			
Other Long Term Liabilities	9,310	9,296	9,076	8,842	8,593
Total	13,310	13,296			

The "Other Long Term Liabilities" figure is the creditor arising from the PFI scheme for Monkton Park Offices

If a decision on financing options is effected, this indicator will change.

PI 6 Operational Boundary for External Debt

Description	2005/06 Actual £000's	2006/07 Projected £000's	2007/08 Budget £000's	2008/09 Budget £000's	2009/10 Budget £000's
Borrowing (Short Term)	2,000	2,000	2,000	2,000	2,000
Other Long Term Liabilities	9,310	9,296	9,076	8,842	8,593
Total	11,310	11,296	11,076	10,842	10,593

In 2006/07 to date, no borrowing has taken place reflecting the Council's positive cash flow.

The total authorised limit is made up of external borrowing and 'long term liabilities' for the Monkton Park PFI offices. The operational boundary is based on officers' expectations of the maximum level for external debt, allowing for expected borrowing to cover short term cash flow variations.

The borrowing elements of the authorised limit and operational boundary for external debt will cover the Council's need to borrow for cash flow purposes. Both indicators reflect the Section 151 Officer's estimate of the most likely, prudent but not worst case scenario, with the authorised limit including a factor of additional headroom to allow for unusual cash movements.

PI 7 Incremental Impact of Capital Expenditure Plans

Description	2005/06 Actual £000's	2006/07 Projected £000's	2007/08 Budget £000's	2008/09 Budget £000's	2009/10 Budget £000's
Increase in Council Tax (per band D property)					
Incremental effect					
Cumulative effect					

Whilst the capital programme anticipates no borrowing in the medium term, there is a cost from the loss of interest on capital receipts that would otherwise be invested and this impacts on future Council Tax levels.

If a decision on financing options is effected, this indicator will change.

Treasury Indicators

The Council is also required to set indicators in relation to its treasury activities for the coming year. Together with the treasury management strategy, these will determine the framework for the treasury function.

The Council adopted the CIPFA Code of Practice for Treasury Management in January 2004.

PI 8 Upper Limit for Fixed Interest Exposure

Description	2005/06 Actual %	2006/07 Projected %	2007/08 Budget %	2008/09 Budget %	2009/10 Budget %
Fixed Interest Exposure Limit	100	100	100	100	100

Fixed rate borrowing contributes to reducing the potential risk from interest rate fluctuations thus, increasing financial certainty. This indicator is the maximum percentage of the total borrowing that can be at fixed interest.

PI 9,10 Upper Limit for Variable Rate Exposure

Description	2005/06 Actual %	2006/07 Projected %	2007/08 Budget %	2008/09 Budget %	2009/10 Budget %
Variable Rate Exposure Limit	0	0	25	25	25

Having a variable rate limit of 25% of total borrowing gives a degree of flexibility in minimising costs at the time finance is arranged. This allows the Section 151 officer to arrange up to 25% of borrowing on a variable rate basis. This is a continuation of existing Treasury Management Policy.

PI 11 Upper Limit for Total Principal Sums invested for over 364 (per maturity date)

Description	2005/06 Actual %	2006/07 Projected %	2007/08 Budget %	2008/09 Budget %	2009/10 Budget %
Upper Limit for Total Principal Sums invested for over 364 (per maturity date)	0	0	20	20	20

It is expected that the majority of lending by both external fund managers and the Council's officers will be for periods of up to 6 months. This indicator allows for a portion of longer-term lending i.e. more than 1 year, which may be needed to achieve optimum treasury performance.

PI 12 Maturity Structure of new fixed rate borrowing during 2007/08

Description	**Upper Limit %**	**Lower Limit %**
Under 12 months	10	0
12 months and within 24 months	0	0
24 months and within 5 years	0	0
5 years and within 10 years	0	0
10 years and above	100	0

During 2007/08 any operational borrowing will be for short periods to meet cash flow changes and will be undertaken at fixed rates.

The Council will be borrowing in 2007-08 to finance its capital programme. Any loan for this purpose will be in excess of 10 years. The best rate the Public Works Loan Board [PWLB] offer at present is a maturity loan at 4.25% for terms over 45 years or more. Lender Option / Borrower Option (LOBO) loans may be an alternative source of funding.

4 Financial Implications

4.1 The Council, post the disposal of its housing stock in 1995, has historically been debt-free. It has been able to finance its capital programme from a combination of its continuing capital receipts, revenue & capital grants coupled with a depletion of it capital balance over a number of years.

4.2 The interest generated from the investment of these capital balances is an essential component to the balancing the Council's Budget. Interest from investments in 2006-07 is forecast to contribute in excess of £1.33 million to the Council. (c. 7% of the net budget)

4.3 A combination of factors arising over the next three year planning period, mean that the Council should consider its debt-free status and its capital programme. These decisions will be recommended to the February 1st Executive and the Council of February 22nd. The largest contributor to this position is the significant reduction in forecast capital receipts over the planning period & beyond.

4.4 A decision needs to be taken about the amount, term, type & source of funding before the financial implications of the Prudential Indicators can be completed.

4.5 Given the relative difficulty in accurately predicting interest rate fluctuations any borrowing would be the subject of regular monitoring. Debt Restructuring may occur from time to time as opportunities arise to repay debt and to re-borrow at a lower interest rate by exploiting differences in the rates for different loan periods.

5 Legal Implications

5.1 The Prudential Code requires that the same Members' decision making group that takes the decision on the authority's budget – the full Council – must set and revise the Prudential Indicators.

5.2 The setting and revision of Prudential Indicators is a continuous process rather than a one-off event. The authority may revise the indicators at any time.

Appendices:	• **Annex 1 – Prudential Indicators Workings**
Background documents Used in the preparation of this Report:	• **The Code of Practice on Treasury Management in the Public Services** • **The Prudential Code for Capital Finance in Local Authorities [CIPFA]**

Previous Decisions Connected with this Report

Report	**Committee & Date**	**Minute Reference**