TAUNTON DEANE BOROUGH COUNCIL

AGENDA ITEM NO. 4

EXECUTIVE 10 DECEMBER 2003

REPORT OF THE HEAD OF FINANCE
This Matter Is The Responsibility of Executive Cllr Williams (Leader of the Council)

THE PRUDENTIAL CODE – AN INTRODUCTION

1 **Executive Summary**

1.1 This report sets out the main changes to the capital finance regime that is contained within the new Prudential Code (The Code).

1.2 The Code has been developed by CIPFA after a lengthy consultation process including a "Dry Run" where a number of local authorities have tested the implications of the code.

1.3 The Code has been established to ensure that local authority capital investment plans are affordable, prudent and sustainable and that all decisions on capital spending are linked to option appraisal, asset management planning, strategic planning and the achievability of any forward plan.

1.4 The Prudential Code will become effective on the 1 April 2004, the indicators prescribed by the code will therefore have to be considered as part of the 2004/05 budget setting process. Further information will be presented at the January Executive meeting where our treasury management advisors, Sector, will be making a presentation on the new Code.

2 Background

2.1 In response to the requirements of the Local Government Bill 2003 and in particular the Prudential Regime for Capital Finance the Chartered Institute of Public Finance and Accountancy (CIPFA) have developed a Prudential Code (the Code).

2.2 Under the new regime Local Authorities will be able to determine their own programmes for capital investment in fixed assets that are central to the delivery of quality local public services. The Code has been developed as a Professional Code of Practice to support Local Authorities in making these decisions. Prudential borrowing will therefore replace credit approvals, which were government issued borrowing entitlements for local authorities.

3 Objectives of the Code

3.1 The key objectives of the code are to ensure that within a clear framework the capital investment plans of a Local Authority are Affordable, Prudent and Sustainable. A further key objective is to ensure that Treasury Management decisions are taken in accordance with good professional practice and in a manner that supports Prudence, Affordability and Sustainability.

3.2 To demonstrate that Local Authorities have fulfilled these objectives, the Code sets out indicators that must be used and the factors that must be taken into account. The code does not include suggested indicative limits or ratios, these are for Local Authorities to set themselves. The Prudential Indicators required by the Code have been designed to support and record local decision making, they are not designed to be comparative Performance Indicators. A schedule of the indicators, providing details as to their use, is shown at Appendix A.

4 Scope and Governance Issues

4.1 The Code will apply to all Local Authorities in England and Wales and sets out a clear governance procedure for the setting and revising of the Prudential Indicators.

4.2 This will be done by the same body that takes the decision for setting the Councils budget ie Full Council. The Chief Financial Officer (Head of Finance) will be responsible for ensuring that all maters required to be taken into account are reported to the decision making body for consideration and for establishing procedures for monitoring performance.

5 Effect on Corporate Priorities

5.1 The Prudential Code will underpin all aspects of local authority capital spending and consequently will have an impact on all corporate priorities.

6 Conclusions and Recommendations

6.1 The code gives greater freedom for borrowing to local authorities but this must be done responsibly. This report details the range of indicators included within the Code. The Code will require the following matters to be taken into account when making capital investment decisions

a) Value for Money - Option appraisal for all projects
b) Stewardship of assets - Asset management planning
c) Service objectives - Strategic planning for the authority
d) Practicality - Achievability of the forward plan
e) Prudence - Implications for external borrowing
f) Affordability - Implications for Council tax

6.2 The indicators contained in Appendix A to this report will assist the Council in ensuring that the above principles are complied with. The Executive should also recognise that the Prudential Code will place a duty on local authorities to ensure that when making any decisions on capital investment explicit regard must be made to:

- Option appraisal
- Asset management planning
- Strategic planning
- Achievability of the forward plan

6.3 It could be viewed that the indicators as set out above are merely making statutory the safeguards which many authorities already have in place, however the freedom to borrow brings with it responsibilities and the code is designed to make sure that local authorities understand those responsibilities. In order to provide further information to members the Council's Treasury management advisors, Sector, are due to attend the January Executive meeting with their expert view on what the Code means for this Council.

6.4 The Executive is RECOMMENDED to note the introduction of the Prudential Code and the work being done on the Prudential indicators as detailed in Appendix A.

Background Papers: Executive, 28 May 2003, The Prudential Code.

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APPENDIX A

Indicator	Information	Measure
Indicator 1 – Capital Expenditure	The local authority will make reasonable estimates of the total of capital expenditure that it intends to incur during the forthcoming financial year and the following two financial years	Affordability – Highlights the capital spending plans for the next three years
Indicator 2 – Capital Financing Requirement	The local authority will make reasonable estimates of the total financing requirement at the end of the forthcoming financial year and the forthcoming financial years.	Affordability – a measurement of the Councils underlying need to borrow.
Indicator 3 – Authorised Limit for external debt	The local authority will set for the forthcoming financial year and the following two financial years a prudential limit for its external debt, gross of investments.	Affordability - This limit represents the maximum amount the Council may borrow at any point in time in the year and has to be set at a level the Council considers to be "prudent".
Indicator 4 – Operational boundary for external debt	The local authority will also set for the forthcoming financial year, and the following two years an operational boundary for its total external debt.	Affordability - The operational boundary is a measure of the most money the Council would borrow at any time during the year.
Indicator 5 – Actual Gross Borrowing outstanding	After the year end the closing balance for actual gross borrowing plus Other long term liabilities will be obtained directly from the authority' s balance sheet.	Affordability – highlights the amount of debt outstanding at the end of each financial year
Indicator 6 – Adoption of CIPFA Code of Practice for Treasury Management	This indicator is linked to the concept of Prudence and ensures the council's investment decisions are being made in line with the CIPFA code of practice	Prudence – ensures investment decisions are being made in accordance with best practice

Indicator	Information	Measure
Indicator 7 – Limits on Variable Interest Rate Exposure	The local authority will set for the forthcoming year and the Following Two years, both upper and lower limits for its variable	Prudence – Interest Rate Risk Management
Indicator 8 – Limits on Fixed Interest Rate Exposure	The local authority will set for the forthcoming year and the following Two years, both upper and lower limits for its Fixed interest rate exposure.	Prudence – Interest Rate Risk Management
Indicator 9 – Maturity Structure of Borrowing	The local authority will set for the forthcoming year both upper and lower limits with respect to the maturity structure of its borrowing	Prudence – Highlights when a local authorities debt will be maturing
Indicator 10 – Investments held over 364 days	The amount of investment held for periods in excess of 364 days.	Prudence - Interest Rate Risk Management
Indicator 11 – Financing Costs Ratio	The local authority will estimate for the forthcoming financial year and the following two financial years the ratio of financing costs to net revenue stream	Affordability – The cost of financing costs as a percentage of revenue
Indicator 12 – Impact on Council Tax	The local authority will estimate for the forthcoming year the impact of financing costs on the Council Tax	Affordability – The impact of capital expenditure on the Council Tax payer