AGENDA ITEM NO. 7

TAUNTON DEANE BOROUGH COUNCIL

EXECUTIVE 28TH MAY 2003

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

THE PRUDENTIAL CODE

1. Purpose of Report

1.1 Local government finance is going through a period of exceptional change – as outlined in the Local Government Bill of 2002 and the Accounts and Audit Regulations 2003.

1.2 In particular the introduction of the prudential regime for capital will have a significant impact on all local authorities, and is the main subject for discussion in this paper.

2. Background

2.1 Part 1 of the Local Government Bill 2002 concentrates on the capital finance regime. The existing system of credit approvals (Basic Credit Approval (BCA) and Supplementary Credit Approval (SCA)) is to be abolished at the end of the current financial year 2003/04 and replaced by a new system, referred to as the "Prudential Regime" for financial years 2004/05 onwards.

2.2 The basic principle of the prudential regime is that local authorities will be free to invest as long as their capital spending plans are affordable, prudent and sustainable.

2.3 The new system will be regulated by the Prudential Code (a document drafted by CIPFA), which sets out indicators that local authorities must use and the factors they must take into account to demonstrate that they have fulfilled the objectives outlined in 2.2 above. The Code will apply to both the General Fund and the HRA.

2.4 CIPFA have published the draft Prudential Code for comment, and the remainder of this section deals with the content therein.

3. **Objectives and Principles of The Code**

3.1 The key objective of The Code is to provide authorities with a more **flexible framework** within which to undertake capital planning. In the existing system, local authorities effectively require centralised consent to make capital investment to support the provision of services. This consent will no longer be needed in the new system. Instead, local authorities will have a statutory duty to keep the scale of their capital investment under review – by **self regulation** (by having regard to the Prudential Code).

3.2 The draft Code places great weight on the importance of **affordability** as the ultimate constraint on the amount that an authority can spend or borrow. This will include consideration of the resources likely to be available, the revenue consequences of capital projects, interest costs arising from borrowing and investments, reserves, balances and risks and uncertainties associated with all these areas.

3.3 The draft Code promotes an **integrated framework for capital and revenue planning over a minimum 3-year timeframe**. In order to achieve this it anticipates that authorities will integrate the decisions required for The Code into the local strategic planning and asset management frameworks and anticipates that capital spending decisions will be made through proper options appraisals.

3.4 The draft Code emphasises how borrowing should be **prudent** and **sustainable**, based on affordability calculations and medium term financial plans and strategies.

3.5 The draft Code promotes the use of **prudential indicators** to assist in the management of these objectives.

3.6 And finally the draft Code requires adherence to the CIPFA Code of Practice for Treasury Management in the Public Services.

4. Potential Implications of the Code

4.1 All the financial planning documents currently produced by the Council will be required to reflect the principles of the Code.

4.2 The draft Code has some significant procedural implications, the most obvious being the requirement to undertake 3year forecasting of all the resources available to the Council. This should result in a budget report that not only sets the budget and Council Tax for the year ahead, but also looks forward and provides estimates of the budget and Council Tax levels for the subsequent two years (these are estimates only and not prescriptive). The output should be a rolling financial planning process.

4.3 The draft Code identifies a number of key prudential indicators – each contributing to one or two of the key principles of affordability, prudence and sustainability, as well as issues of good professional practice. The Code does not specify what the indicators should be set at, as this will be different for each authority, depending on their local circumstances. These should be considered and approved through the same process as the budget. The indicators, like the financial forecasts, must cover the forthcoming year plus the subsequent 2 years.

4.4 The draft code requires the Chief Finance Officer (Head of Finance at TDBC) to establish measurement and monitoring procedures for all forward looking indicators to ensure that proper account and action is taken in the event of a deviation from the forecasts.

5. Taunton Deane's Perspective

5.1 The Head of Finance has responded to this technical consultation on behalf of the Council. The main issues drawn out in the response include:-

- Comment that the Code should be finalised as soon as possible to allow authorities proper time to consider its' implications for the 2004/05 budget setting round.
- Comment on the issue of "monitoring the prudential indicators". Whilst it is right that the full Council (the budget setting body) set the initial indicators, it is felt more appropriate for the monitoring of those indicators to be done by the body responsible for budget monitoring (ie not full Council).
- A request to the Government to explain how they intend to provide revenue support for borrowing under the new regime (the draft Code is silent on this issue). The Office of the Deputy Prime Minister have stated that the Single Capital Pot will continue, but have not yet offered any indication on how it will work. It is hoped that a further consultation document will be published on this area in the next few months.
- A request to the Government to consider an early announcement on the floors and ceilings to be applied to the 2004/05 Local Government Finance Settlement.
- A request to the Government to consider moving towards a 3 year funding plan for the Local Government. Again this would allow authorities to plan ahead with greater certainty, and make the (now published) 3 year financial plans more robust.

6. Impact on Corporate Priorities

6.1 The Prudential Code will underpin all aspects of local authority capital spending, and consequently will affect all corporate priorities.

7. Recommendations

7.1 The Executive is requested to note the introduction of the Prudential Regime for capital and to consider the implications on Taunton Deane Borough Council set out in this report.

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<u>Background Papers</u>

CIPFA Prudential Code – Preliminary Guidance March 2003
CIPFA Prudential Code for Capital Finance – Second Exposure Draft March 2003