

**CIPFA Prudential Code for Capital Finance in Local Authorities
Prudential Indicators for 2006/07**

Capital expenditure

1. Mutual and Estimated Capital Expenditure

	2004/5 Actual £000	2005/6 Forecast £000	2006/7 Estimate £000	2007/8 Estimate £000	2008/9 Estimate £000
Gross*	16,426	21,189	20,598	19,234	13,614
Net	11,269	18,251	14,675	17,992	13,067

* excludes investments

2. The proportion of the budget financed from government grants and council tax that is spent on interest

The negative figures reflect that the Authority is a net investor and so the interest earned is used to help fund the budget.

2004/5 Actual £000	2005/6 Forecast £000	2006/7 Estimate £000	2007/8 Estimate £000	2008/9 Estimate £000
-28%	-23%	-17%	-11%	-7%

3. The impact of schemes with capital expenditure on the level of council tax

This calculation highlights the hypothetical impact on the level of Council Tax from capital schemes that the Council is making a decision on in this report (i.e. it ignores changes already approved, slippage, inflation and savings). The actual change in Council Tax is different because of the impact of other schemes and the use of revenue reserves.

	2006/7 Estimate	2007/8 Estimate	2008/9 Estimate
Increase	£1.19	£0.16	£5.93
Cumulative	£1.19	£1.35	£7.28

4. The capital financing requirement.

This represents the need for the Authority to borrow to finance capital expenditure. Whilst the Authority has capital reserves it will not need to borrow for capital purposes:

31/3/05 Actual £000	2005/6 Forecast £000	2006/7 Estimate £000	2007/8 Estimate £000	2008/9 Estimate £000
0	0	0	0	1,124

5. Net borrowing and the capital financing requirement.

Net external borrowing must not be used to finance revenue spending except in the short term. In the short term there are legitimate uses of borrowing to cover cash flow e.g. funding salaries pending receipt of council tax income or return of investments.

The forecast shows that capital reserves are forecast to run out in 2008/09 and the Authority will then need to fund most of its capital expenditure from long-term borrowing. However it is permitted to borrow in advance of the need to fund expenditure by borrowing, (see paragraph 7 below).

External debt

6. The actual external borrowing at 31 March 2005

There was £2.5m of short-term borrowing for cash-flow purposes.

7. The authorised limit for external debt

This is the maximum limit for borrowing and is based on a worst-case scenario. It reflects the Treasury Management Strategy which allows for the Authority to borrow up to £10m as long term debt in order to finance future capital expenditure if it appears that long term rates are lower than they will be in later years.

2005/6 Limit £000	2006/7 Limit £000	2007/8 Estimate £000	2008/9 Estimate £000
22,000	30,000	30,000	30,000

8. The operational boundary for external debt

This reflects a less extreme position. Although the figure can be exceeded without further approval it represents an early warning monitoring device to ensure that the authorised limit (above) is not exceeded. It allows the management of the Council's day to day cashflow and, in accordance with the Treasury Management Strategy, temporary borrowing to delay the return of funds from the Fund Managers if this is in the Council's interests. The operational boundary does not include the allowance for the £10m long-term borrowing referred to above.

2006/7 Limit £000	2007/8 Estimate £000	2008/9 Estimate £000
15,000	15,000	15,000

Treasury management

9. Adoption of the CIPFA Code

The Prudential Code requires the Authority to have adopted the CIPFA Code of Practice for Treasury Management in the Public Services. This has been adopted.

10. Exposure to investments with fixed interest and variable interest.

These limits are given as a percentage of total investments.

The parameters currently set for our Fund Managers could theoretically result in a significant amount of the funds being at variable rates as gilts and corporate bonds are also deemed to be variable rate investments for the purpose of this indicator. In practice the exposure to variable rates is likely to be less.

	2006/7 Limit £000	2007/8 Estimate £000	2008/9 Estimate £000
Upper limit on fixed rate exposure	100%	100%	100%
Upper limit on variable rate exposure	84%	50%	50%

11. Borrowing Repayment Profile

The proportion of 2006/7 borrowing that will mature in successive periods.

The table refers to temporary borrowing for cash flow purposes; 100% will mature in less than 12 months. If long-term borrowing takes place in 2006/07 it will all be for maturities in excess of ten years.

	Upper limit	Lower limit
Under 12 months	100%	100%
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	0%	0%

12. Investment Repayment Profile

Limit on the value of investments that cannot be redeemed within 364 days. The only investments that meet this criterion are time deposits that are invested to a fixed maturity date for a year or longer.

2006/7 Limit £000	2007/8 Estimate £000	2008/9 Estimate £000
20,000	15,000	10,000

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SENSITIVITY

The proposed strategy as outlined in paragraph 6.9 and detailed in Annex C has been modelled to identify the impact that variations in investment rates, borrowing rates and increases in pay will have. The table below shows the items considered and resulting change in the level of savings required.

	Impact on Council spending in year:		
	2006/07 £M	2010/11 £M	2016/17 £M
0.5% extra pay award every year	+0.1	+0.6	+1.6
0.5% higher investment returns each year	-0.3	0	0
0.5% higher borrowing costs each year	0	0	+0.1

Inflation, other than pay, is fairly neutral as long as fees and charges are increased in line with it.

Continual extra pay awards become costly due to the compound effect. An increase from 2.5% per year to 3% per year has been included in the report. Pay negotiations are not based on what has been included in the budget.

The impact of investment rates disappears quite quickly as reserves are used.

The impact of higher borrowing rates is not significant.

It has been assumed that the combination of turnover and performance pay will become increasingly neutral over the plan period. This will be reviewed annually.

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RESERVES AND THE ROBUSTNESS OF THE 2006/07 BUDGET

The Local Government Act 2003 requires me, as the Council's Chief Financial Officer, to report on the robustness of the 2006/07 budget and the adequacy of reserves when you consider it and the consequent Council Tax.

Robustness

The Council has tended in recent years to underspend its budget. This demonstrates that it has budgeted prudently and that managers have taken a mature approach to budgetary control rather than spend any spare sums on low priority items. Thus there is consistent, effective application of financial controls and a sound base for setting future budgets. The latest round of efficiency savings/budget reductions will result in tighter budgets but managers were asked to propose only reductions that could be achieved without affecting service levels.

The 2006/07 budget has been prepared using the budget for 2005/06 as a base, and amending it for known changes, particularly -

- ◆ Inflation, including pension contributions and electricity which are in excess of general inflation.
- ◆ Potential pay rises.
- ◆ The impact of MTP schemes.
- ◆ Forecast interest rates, which have a significant impact on our investment income.

There will always be some items that emerge after the budget has been prepared. These are normally met by compensating savings elsewhere in the budget, the use of the contingency (£132k) or, if necessary, the use of revenue reserves.

The most significant predictable risks to the budget are –

- ◆ higher inflation than anticipated;
- ◆ lower interest rates.

A ½% increase in general and pay inflation, **assuming no compensating increase in fees and charges was possible**, would result in a net cost of approximately £190k.

A ½% reduction in interest rates would result in lost income of approximately £260k.

Certain types of eventuality are mitigated in other ways. Many significant risks are insured against, so losses are limited to the excesses payable. The Government's Bellwin Scheme meets a large proportion, over a threshold, of the costs of any significant peacetime emergencies (e.g. severe flooding).

Considering all these factors, I believe that the 2006/07 budget is adequately robust.

Revenue Reserves

These are estimated to be £16.9m at April 2006 and £15.3m at March 2007. This is significantly above what would be considered a safe minimum level, which would be in the region of £2m.

Steve Couper
Head of Financial Services