SECTION 12

12. SETTING PRUDENTIAL INDICATORS FOR 2010/11

Introduction

12.1 The introduction of a new prudential system of borrowing in the 2003 Local Government Act gave new opportunities for councils to assess their requirements for capital spending, and not have them artificially restricted by nationally set credit approvals, as they were under the previous system. But it also brought new responsibilities on councils to ensure that:

a. capital expenditure plans are affordable;

b. all external borrowing and other long term liabilities are within prudent and sustainable levels; and

c. treasury management decisions are taken in accordance with good professional practice.

12.2 Under regulations issued under the 2003 LGA, councils are required to follow the Prudential Code issued by CIPFA which sets out how councils ensure they use their new freedom responsibly. The code sets out indicators which councils are required to set before the beginning of each year, to monitor during the year, and to report on at the end of each year.

12.3 In setting their prudential limits, Members must have regard to:

a. Affordability e.g. implications for council tax and council housing rents.

b. Prudence and sustainability, e.g. implications for external borrowing.

c. Value for money, e.g. options appraisal.

d. Stewardship of assets, e.g. asset management planning.

e. Service objectives, e.g. strategic planning for the authority.

f. Practicality, e.g. achievability of the forward plan.

12.4 This section sets out proposed prudential limits for Brent for 2010/11 and subsequent years, which Members are asked to agree. It also sets out the arrangements for monitoring the prudential indicators.

Affordability

12.5 The Code requires Members to consider the affordability of decisions on investment in council assets.

12.6 Affordability of capital expenditure cannot be isolated from the affordability of the council's overall revenue expenditure. Section 10 of this report set out proposed changes to the capital programme which ensure total forecast capital commitments are maintained at previously agreed levels. General Fund revenue spending in 2010/11 to fund the unsupported borrowing proposed in that year is estimated at £451k (see section 10). Members should note however that proposed unsupported borrowing in the capital programme for 2010/11 onwards will have a cumulative impact on the council's budget and the costs of funding it are growing from £451k in 2010/11 to £1.442m in 2011/12, £1.907m in 2012/13 and 2.382m in 2013/14.

12.7 The CIPFA code requires that the council estimates:

a. capital financing charges as a proportion of net revenue stream for both the General Fund and Housing Revenue Account; and

b. the incremental impact of changes to the capital programme on council tax and rents.

12.8 The required calculations for 2010/11, and the three subsequent years are set out in Table 12.1 below. The ratio of capital financing charges to spending in the General Fund is 9.27% in 2010/11, increasing to 10.00% by 2013/14. Capital financing charges within the HRA also rise as a proportion of the budget over the same period, increasing from 36.40% in 2010/11 to 37.30% by 2013/14. The impact on Council Tax at Band D of unsupported borrowing was set out in Section 10. These figures should be treated with some caution because the operation of the revenue grant regime – and in particular absence of funding for so-called 'supported' borrowing for councils on the grant floor – means that the impact of 'supported' borrowing and 'unsupported' borrowing on the council's future financial plans is broadly similar. Members should also note that this calculation does not take account of the provision made for self-supported borrowing detailed in Section 10.

Table 12.1 Prudential Indicators of Affordability

	2010/11	2011/12	2012/13	2013/14
Capital financing charges as a proportion of net revenue stream:				
- General Fund	9.27%	9.59%	9.78%	10.00%
- HRA	36.40%	36.86%	37.09%	37.30%
Impact of unsupported borrowing on:				
- Council tax at Band D	£4.68	£14.95	£19.77	£24.69
- Weekly rent	-	-	-	-

12.9 Future years' projections of the overall General Fund revenue budget indicate that the council needs to do more to bring overall expenditure plans within acceptable limits, but this is within its historic capability. Section 10 of this report has set out measures the council plans to take in the short term to maintain capital expenditure. The measures proposed take account of the need not to build up commitments in future years. However, ultimately affordability remains a political judgement and Members need to assure themselves that the plans set out in the report are affordable in terms of council tax and rent increases.

Prudence and Sustainability

12.10 The issues of prudence and sustainability are closely related to that of affordability. Are borrowing levels sensible and prudent and sustainable over the longer period? In particular is borrowing set at a level to finance capital investment in total and not for other purposes?

12.11 The indicators for prudence and sustainability cover capital spending, external debt, and treasury management.

12.12 For *capital spending*, the prudential indicators are as follows:

- Planned capital spending on the General Fund and HRA (see chapter 10);
- The estimated capital financing requirement for General Fund and HRA, reflecting the council's underlying need to borrow. This covers borrowing to fund past capital spending and in-year capital spending.

Table 12.2 Prudential Indicators for Capital Spending

	2009/10 £m	2010/11 £m	2011/12 £m	2012/13 £m	2013/14 £m
Planned capital spending: - General Fund	106,221	106,246	137,031	112,434	82,240
- HRA	28,352	15,714	9,284	9,284	9,284
- Total	134,573	121,960	146,315	121,718	91,524
Estimated capital financing requirement for[1]: - General Fund	304,558	338,584	388,762	427,277	446,664
- HRA	330,693	337,723	338,323	338,923	339,523
- Total	635,251	676,307	727,085	766,200	786,187

12.13 For *external debt*, the prudential indicators are as follows:

a. The authorised limit for external debt. This allows flexibility to carry out debt restructuring should opportunities arise. For example, it may be appropriate to borrow in advance of repaying the original debt. It is therefore set at approximately £175m above the capital financing requirement.

b. The operational boundary for external debt. This sets out the expected total of borrowing for each year. This is lower than the authorised limit and is a key management tool for in-year monitoring. It is set at a level that reflects the council's capital financing requirement, the level of the capital programme, and estimated requirements for cash flow. The boundary is set at a level approximately £75m above the capital financing requirement

[1] The Capital Financing Requirement estimates in this table are at 31st March of each year.

(CFR) to allow for early borrowing either for restructuring or where interest rates may rise. The CIPFA code accepts that the operational boundary may on occasions be breached temporarily but that a sustained or regular trend above the operational boundary would be significant and lead to further investigation and action as appropriate.

c. Net *borrowing.* A key indicator of prudence is that net external borrowing – gross borrowing less investment – does not, other than in the short term, exceed the total capital financing requirement. This is to ensure that net borrowing is only used for capital purposes.

Table 12.3 Prudential Indicators for External Debt

	2009/10 £m	2010/11 £m	2011/12 £m	2012/13 £m	2013/14 £m
Authorised limit for external debt	810	850	900	940	960
Operational boundary for external debt	710	750	800	840	860
Net borrowing	Below CFR	Below CFR	Below CFR	Below CFR	Below CFR

Achieving Value for Money

12.15 Members also need to consider achievement of value for money. There are many potential capital projects that are not value for money and the prudential code prohibits borrowing for such purposes. In Brent value for money is addressed in a number of ways including:

a. Projects are initially vetted by the Capital Board for amongst other things value for money before being recommended for inclusion in the Capital Programme.

b. The Capital Strategy requires all projects to be internally assessed for VFM before being submitted.

c. Major projects require approval by the Executive and reports to Executive have to address VFM considerations.

d. Standing orders ensure that letting of contracts is subject to appropriate competitive processes.

e. Internal and external audit assess systems to ensure that appropriate processes are in place in identifying capital projects.

Proper Stewardship of Assets

12.16 The Code also requires consideration of stewardship of assets. The capital programme must deliver properly maintained assets and should not lead to acquisition of assets which put a strain on the council's ability to achieve this objective for all its stock. The council has developed an asset management plan for its general fund assets and a long term business plan for HRA stock which identifies the investment needs to keep assets to an appropriate standard. The long term business plans for the General Fund and HRA demonstrate that sufficient resources are available to maintain this stock at an affordable level.

12.17 The capital programme as a whole is linked to the Corporate Strategy and other plans and objectives of the council. This is a key criterion for the Capital Board before projects can be recommended for inclusion in the capital programme. The service development planning process ensures that spend on revenue and capital is linked to the council's overall objectives. The budget approval process gives Members a final opportunity to check that this objective has been met.

Practicality

12.18 This is the last of the issues Members have to consider in setting prudential indicators. Is the capital programme set out in Section 10 of this report capable of delivery? Is it practical?

12.19 In 2010/11, the Capital Board will continue to meet monthly to monitor implementation of the delivery of the programme and require action to be taken where there is delay. Section 10 has also set out the main risks associated with the capital programme and how these will be managed.

Monitoring and Reporting on Prudential Indicators

12.20 The CIPFA Code requires that prudential indicators are monitored during the year and reported at the end of the year as part of the final accounts.

12.21 The arrangements we have put in place for this are as follows:

- The probable actuals and estimates for all prudential indicators are reported as part of this budget report to the Executive and Full Council;
- The report to the Executive on the capital outturn includes details of the outturn on prudential indicators on affordability, capital spending, and external debt. Any amendments during audit will be included in our report to GPC on audited accounts.
- Prudential indicators on affordability and capital spending are also reported in Performance and Finance Review reports to the Executive.
- Prudential indicators on external debt and treasury management are monitored daily in Finance and Corporate Resources. The Director of Finance and Corporate Resources and Deputy Director of Finance and Corporate Resources review the figures on these indicators on a weekly basis. Any forecast of a breach of the limits or actual breach of the limits will be reported at the first opportunity to General Purposes Committee. The only exception to this is breaches of the operational boundary on borrowing which will be reported in the next budget monitoring report to

the Executive (unless they are sustained in which case they will be reported on an exception basis to General Purposes Committee).

12.22 Members should note that the required implementation of the International Financial Reporting Standards from 1st April 2010 is likely to have an impact on Prudential Indicators particularly regarding the Capital Financing Requirement, Authorised Borrowing Limit and Operational Boundary. This is due to changes in the requirements around the recognition and reporting of leases which could result in certain leases being recognised on the balance sheet where in previous years this has not been required. Any changes will be reported as per the above processes as required in the adoption of the new standards.