

## **SECTION 11**

### **11. SETTING PRUDENTIAL INDICATORS FOR 2012/13**

#### **Introduction**

- 11.1 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.
- 11.2 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.
- 11.3 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.
- 11.4 This section sets out proposed prudential limits for Brent for 2012/13 and subsequent years, which Members are asked to agree. It also sets out the arrangements for monitoring the prudential indicators.

#### **Affordability**

- 11.5 The Code requires Members to consider the affordability of decisions on investment in council assets.
- 11.6 Affordability of capital expenditure cannot be isolated from the affordability of the council's overall revenue expenditure. Section 9 of this report sets out the proposed capital programme for 2012/13 and subsequent years. General Fund revenue spending in 2012/13 to fund the unsupported borrowing proposed in that year is estimated at £68k (see section 9). Members should

note however that proposed unsupported borrowing in the capital programme for 2012/13 onwards will have a cumulative impact on the council's budget and the costs of funding it are growing from £68k in 2012/13 to £426k in 2013/14, £1.007m in 2014/15 and £1.599m in 2015/16.

- 11.7 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.
- 11.8 The required calculations for 2012/13, and the three subsequent years are set out in Table 11.1 below. The ratio of capital financing charges to spending in the General Fund is 9.82% in 2012/13, increasing to 11.43% by 2015/16. Capital financing charges within the HRA reduce as a proportion of the budget over the same period, decreasing from 22.28% in 2012/13 to 13.66% by 2015/16. The impact on Council Tax at Band D of unsupported borrowing was set out in Section 9 members should note that this calculation does not take account of the provision made for self-supported borrowing.

**Table 11.1 Prudential Indicators of Affordability**

	2012/13	2013/14	2014/15	2015/16
Capital financing charges as a proportion of net revenue stream:				
Capital Financing Charges (£m)	25.563	26.603	28.104	29.668
Budget Requirement (£m)	260.392	258.816	254.581	259.450
- General Fund	9.82%	10.28%	11.04%	11.43%
HRA Financing Charges (£m)	11.204	10.249	8.187	7.379
HRA Net Revenue Stream (£m)	50.518	51.773	53.060	54.378
- HRA	22.18%	19.80%	15.43%	13.57%
Impact of unsupported borrowing on:				
- Council tax at Band D	£0.69	£4.33	£10.23	£16.25
- Weekly rent	0	0	0	0

- 11.9 At a time when revenue budgets are under severe pressure the Council's ability to meet the costs associated with borrowing is significantly limited. Section 9 of this report has set out the Council's proposed Capital Programme for 2012/13 and subsequent years in the light of the Local Government Settlement announcement. 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

11.10 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?

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

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

- Planned capital spending on the General Fund and HRA (see chapter 9);
- 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.
- HRA Limit on indebtedness reflecting the limit imposed at the time of implementation of self-financing by the Department of Communities and Local Government. This is monitored against the HRA Capital Financing Requirement which should remain below the limit set.

**Table 11.2 Prudential Indicators for Capital Spending**

	2011/12 £m	2012/13 £m	2013/14 £m	2014/15 £m	2015/16 £m
Planned capital spending:					
- General Fund	141.806	182.090	78.647	57.718	54.793
- HRA	14.668	13.846	9.284	9.284	9.284
- Total	156.474	195.936	87.931	67.002	64.077
Estimated capital financing requirement for <sup>1</sup> :					
- General Fund	413.547	482.722	477.421	470.436	463.641
- HRA	338.527	140.527	140.527	140.527	140.527
- Total	752.074	623.249	617.948	610.963	604.168
HRA Limit on Indebtedness:					
- HRA	n/a	199.291	199.291	199.291	199.291

<sup>1</sup> The Capital Financing Requirement estimates in this table are at 31<sup>st</sup> March of each year.

11.13 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 to provide this flexibility. In addition the limit is set a further £25m above the capital financing requirement for 2011/12 onwards to allow for the second tranche loan to the BHP for continuation of the Settled Home Initiative.
- 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 to allow for early borrowing either for restructuring or where interest rates may rise. The boundary is also set a further £25m above the capital financing requirement for 2011/12 onwards to allow for the loan to the BHP, as detailed above. 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 11.3 Prudential Indicators for External Debt**

	2011/12 £m	2012/13 £m	2013/14 £m	2014/15 £m	2015/16 £m
Authorised limit for external debt	754	823	818	811	804
Operational boundary for external debt	654	723	718	711	704
Net borrowing	Below CFR	Below CFR	Below CFR	Below CFR	Below CFR

## **Achieving Value for Money**

- 11.14 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 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**

- 11.15 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.
- 11.16 The capital programme as a whole is linked to the Borough Plan and other plans and objectives of the council. This is a key criterion 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**

- 11.17 This is the last of the issues Members have to consider in setting prudential indicators. Is the capital programme set out in Section 9 of this report capable of delivery? Is it practical?
- 11.18 In 2012/13, monthly monitoring of the implementation of the delivery of the programme will continue and required action taken where there is delay. Section 9 has also set out the main risks associated with the capital programme and how these will be managed.

## **Monitoring and Reporting on Prudential Indicators**

11.19 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.

11.20 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 General Purposes Committee on audited accounts.
- Prudential indicators on affordability and capital spending are also reported in Performance and Finance Review reports to the Executive as appropriate.
- Prudential indicators on external debt and treasury management are monitored daily within Finance and Corporate Services. The Director of Finance and Corporate Services and Deputy Director of Finance and Corporate Services 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).