SECTION 11

11. SETTING PRUDENTIAL INDICATORS FOR 2011/12

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 2011/12 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 2011/12 and subsequent years. General Fund revenue spending in 2011/12 to fund the unsupported borrowing proposed in that year is estimated at £182k (see section 9). Members should note however that proposed unsupported borrowing in the capital programme for 2011/12 onwards will have a cumulative impact on the council's budget and the costs of funding it are growing from £182k in 2011/12 to £825k in 2012/13, £1.450m in 2013/14 and £1.978m in 2014/15.

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 2011/12, 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 8.77% in 2011/12, increasing to 9.93% by 2014/15. Capital financing charges within the HRA reduce slightly as a proportion of the budget over the same period, decreasing from 36.50% in 2011/11 to 36.32% by 2014/15. 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

	2011/12	**2012/13**	**2013/14**	**2014/15**
Capital financing charges as a proportion of net revenue stream:				
- General Fund	8.77%	9.14%	9.45%	9.93%
- HRA	36.50%	36.47%	36.41%	36.32%
Impact of unsupported borrowing on:				
- Council tax at Band D	£1.87	£8.48	£14.91	£20.34
- Weekly rent	0	0	0	0

11.9 At a time when revenue budgets are being reduced 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 2011/12 and subsequent years in the light of the new 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 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 11.2 Prudential Indicators for Capital Spending

	2010/11 £m	2011/12 £m	2012/13 £m	2013/14 £m	2014/15 £m
Planned capital spending:					
- General Fund	133.383	128.045	83.085	62.096	34.291
- HRA	20.127	9.284	9.284	9.284	9.284
- Total	153.510	137.329	92.369	71.380	43.575
Estimated capital financing requirement for[1]:					
- General Fund	371.526	421.176	447.197	453.680	440.296
- HRA	337.724	338.324	338.924	339.524	340.124
- Total	709.250	759.500	786.121	793.204	780.420

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 £45m above the capital financing requirement from 2011/12 onwards to allow for the proposed second tranche loan to the BHP for continuation of the Settled Home Initiative as reported to the February meeting of the Executive.

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 £45m above the capital financing requirement from 2011/12 onwards to allow for the proposed

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

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

	2010/11 £m	**2011/12 £m**	**2012/13 £m**	**2013/14 £m**	**2014/15 £m**
Authorised limit for external debt	929	980	1,006	1,013	1,000
Operational boundary for external debt	829	880	906	913	900
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 2011/12, 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.
- 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).