

# **APPENDIX E**

## **WAVERLEY BOROUGH COUNCIL**

**EXECUTIVE – 3 FEBRUARY 2009**

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**Title:**

**PRUDENTIAL CODE FOR CAPITAL FINANCE**

**[Portfolio Holder for Finance: Cllr M H W Band]**

**[Wards Affected: N/A]**

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**Summary and Purpose**

The purpose of this report is to seek the Executive's approval for the capital finance prudential indicators, as required by the Chartered Institute of Public Finance and Accountancy's (CIPFA's) Prudential Code. This report must be considered in conjunction with the budget setting report and the Treasury Management Policy report also on this agenda.

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**How this report relates to the Council's Corporate Priorities:**

Effective treasury operation is a key element in the management of Waverley's financial resources. This supports the Value for Money Priority and ensures that sufficient cash is available to deliver services.

**Equality and Diversity Implications:**

There are no implications arising from this report.

**Resource/Value for Money implications:**

There are no direct resource implications associated with this report. However, the Prudential Code is referred to in Waverley's Financial Strategy as an opportunity for providing funding for the capital programme in the longer-term.

**Legal Implications:**

There are no legal implications arising from this report.

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**Prudential Indicators**

1. To fulfill the requirements of the Code, the Council must produce and maintain the following set of specified 'Prudential Indicators'. In setting and revising these indicators, and more importantly in any decision on borrowing, the Council must take into account affordability, e.g. implications for Council Tax and housing rents and prudence and sustainability, e.g. implications for external borrowing. An explanation of the indicators is included at Annexe 1. Additional indicators are included in the treasury management policy report.

2. The prudential indicators are there to support decision making and are not designed to be comparative performance indicators with other councils. The indicators which require future forecasts are rolling scenarios, not fixed for the 3 year period. They can be reviewed at any time by the S151 Officer, subject to Council approval. The S151 Officer must monitor performance against each indicator during the year.
  
3. Waverley's capital improvement schemes at the Council's leisure facilities will potentially require the Council to borrow up to £5million. Where appropriate, the impact of this decision on the prudential indicators is shown in this report. The Council may also give further consideration to options for providing affordable housing in the Borough in future years and this may result in a request to consider borrowing for capital investment. However, a comprehensive business model will be required before this can be considered. Other financial options to be considered first would include sales of land and S106 contributions. The prudential indicators and the Medium Term Financial Strategy will reviewed as this work develops.

Indicator 1 - Estimates of capital expenditure

	<b>2007-08 £000 Actual</b>	<b>2008-09 £000 Estimate</b>	<b>2009-10 £000 Estimate</b>	<b>2010-11 £000 Estimate</b>	<b>2011-12 £000 Estimate</b>
General Fund	3,534	4,082	5,525	7,407	1,617
HRA	8,123	8,759	6,011	4,541	4,050
<b>Total</b>	<b>11,657</b>	<b>12,841</b>	<b>11,536</b>	<b>11,948</b>	<b>5,667</b>

Indicator 2 - Estimates of the ratio of financing costs to net revenue stream

	<b>2007-08 £000 Actual</b>	<b>2008-09 £000 Estimate</b>	<b>2009-10 £000 Estimate</b>	<b>2010-11 £000 Estimate</b>	<b>2011-12 £000 Estimate</b>
General Fund	-8.1%	-6.4%	-3.2%	0.3%	0.3%
HRA	0.6%	0.6%	0.7%	0.7%	0.7%

4. The estimates of financing costs include current commitments and the proposals in the budget report. At 1 April 2008, investments totaling £31million were held, some of which represent balances and reserves, with the balance being held for cash flow purposes. The projected reduction in the General Fund ratio reflects estimates of the overall draw on capital receipts to fund the capital programme. However, the ratios show a prudent position with Waverley's net investment position contributing towards the General Fund revenue budget. The HRA figures are determined by Regulations.

Indicator 3 -Capital financing requirement

	<b>2007-08 £000 Actual</b>	<b>2008-09 £000 Estimate</b>	<b>2009-10 £000 Estimate</b>	<b>2010-11 £000 Estimate</b>	<b>2011-12 £000 Estimate</b>
General Fund	-4,423	-4,423	-4,423	577	577
HRA	3,374	3,374	3,374	3,374	3,374
<b>Total</b>	<b>-1,049</b>	<b>-1,049</b>	<b>-1,049</b>	<b>3,951</b>	<b>3,951</b>

5. This indicator is a measure of the underlying need to borrow for capital purpose, it is not the level of actual borrowing held or required. Waverley is currently debt-free and intends to finance most of its routine capital programme from existing resources in the medium term, so this indicator is showing a prudent position. Other than the potential to borrow to deliver the leisure strategy, it is the intention to review the programme as part of each year's General Fund budget setting process to match planned expenditure to the level of resources available.

**Indicator 4 - Authorised limit for external debt**

	<b>2008-09 Estimate</b>	<b>2009-10 Estimate</b>	<b>2010-11 Estimate</b>	<b>2011-12 Estimate</b>
General Fund	£5million	£5million	£10million	£5million
HRA	nil	nil	nil	nil
<b>Total</b>	£5million	£5million	£10million	£5million

6. Whilst cash flows are currently managed using the investment portfolio, it is possible that short-term borrowing may be necessary. As the indicators in this report show, other than potential borrowing for leisure improvements, a significant amount of borrowing for capital purposes is not currently expected to be necessary in the short term. However, it is sensible to have in place an authorised borrowing limit at the current prudent level to enable treasury activity if necessary. Actual external debt at the 31<sup>st</sup> March 2008 was zero. In approving this limit, the Council is approving the limit as required under section 3(1) of the Local Government Act 2003.

**Indicator 5 - Operational boundary for external debt**

	<b>2008-09 Estimate</b>	<b>2009-10 Estimate</b>	<b>2010-11 Estimate</b>	<b>2011-12 Estimate</b>
General Fund	£5million	£5million	£10million	£5million
HRA	nil	nil	nil	nil
<b>Total</b>	£5million	£5million	£10million	£5million

7. As the authorised limit for external debt is currently intended to cover mainly cash flow movements and only a limited amount of capital expenditure, it is not necessary to set the operational boundary at a lower level. If a greater degree of borrowing for capital purposes is required in the future, both indicators will be reviewed.

**Indicator 6 - Incremental impact of current capital investment decisions**

	<b>2009-10 Estimate</b>	<b>2010-11 Estimate</b>	<b>2011-12 Estimate</b>
For Band D Council Tax	Nil	£2.10	£2.10
For average weekly housing rents	Nil	Nil	Nil

8. It is assumed at this stage that the borrowing of up to £5million to finance leisure improvements will fall in 2010/11. The full repayment cost of this borrowing is partly offset by savings in the management fees that the Council pays to run its leisure facilities. It is the net cost that is used to calculate the

above indicators. The precise timing of the capital expenditure and revenue savings will be known as the contract develops during 2009, particularly around the Godalming leisure scheme. **It is important for Members to note that this calculation is purely an indicator based on a mathematical calculation of the estimated impact of the borrowing decision on Waverley's council taxpayer. In reality, it would not be the intention to increase council tax to pay for the net costs of the leisure capital spend and this cost would be met from savings in other budgets.**

### **Risks**

9. In terms of the capital programme, there is a risk of increased capital costs or capital receipts falling short of estimate. The Financial Regulations and regular budget monitoring should reduce the risk of unknown variations and enable early action to be taken if necessary. A separate risk assessment process is in place for the leisure capital investment programme.

### **Conclusion**

10. The forward-looking prudential indicators shown above are best estimates taking into account the Financial Strategy, current budget projections and the current level of reserves, balances and capital receipts.
11. There are other major decisions for the Council in the next few years that may have a significant impact on capital financing decisions, such as the East Street development and further appraisal of options for affordable housing in the borough. As these details become available, the indicators will be reviewed and, if necessary, reconsidered by Members.

### **Recommendation**

It is recommended that the Executive approves the above Prudential Indicators 1 to 6, as amended if necessary following the decisions taken in approving a draft General Fund budget.

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### **EXPLANATION OF PRUDENTIAL INDICATORS**

#### Indicator 1 - Estimates of capital expenditure

These estimates are as included in the capital programme report and, in the case of the previous year's actuals, as shown in the Statement of Accounts. The risks section of this report is relevant when considering this indicator.

#### Indicator 2 - Estimates of the ratio of financing costs to net revenue stream

The net revenue stream is the net amount to be met from Government grant and local taxpayers or, in the case of the HRA, the net amount to be met from housing subsidy and rent income.

Financing costs are the net of any interest on borrowing, interest earned on investments and any amounts made as revenue provision to repay debt.

#### Indicator 3 -Capital financing requirement

The capital financing requirement measures the underlying need to borrow for a capital purpose. The requirement increases as capital expenditure is incurred or planned, and reduces when financing from capital receipts, grants or revenue is applied.

The code requires councils to ensure that, to demonstrate prudence, in the medium term net borrowing must not exceed the total of capital financing requirement in the preceding year plus the estimates of any additional requirement for the current and next two financial years. Net borrowing is defined in the code as total external borrowing less investments less/plus cash held/overdrawn.

For debt-free councils, the capital financing requirement is likely to be zero or negative. If capital programmes are fully funded from sources other than borrowing, the capital financing requirement will not increase significantly over time.

#### Indicator 4 - Authorised limit for external debt

In accordance with best professional practice, Waverley does not associate its treasury management activities with particular items or types of expenditure. At any point in time, the Council has a number of cash flows both positive and negative and it manages its treasury position in accordance with its approved treasury management strategy. The authorised external debt limit replaces the old statutory borrowing limit that Waverley has been required to set in the past, despite being debt-free.

#### Indicator 5 - Operational boundary for external debt

The operational boundary for external debt is the most likely, prudent but not worst-case scenario, without the additional headroom allowed for in the authorised limit to allow for unusual cash movements.

## Indicator 6 - Incremental impact of capital investment decisions

This shows the impact of the capital investment decisions on the Council Tax and rent levels. It allows the totality of the Council's plans to be considered at budget setting time. Whilst this is an indicator that Members must consider when taking decisions on borrowing, it doesn't necessarily follow that council tax has actually been increased by the amount shown in the indicator. In reality, due to the pressures on Waverley's budget, any net cost of borrowing will have to be offset by savings in other budgets, therefore the impact on the council taxpayer in cash terms would be zero. This is the intention with the net borrowing costs of the leisure improvement capital works currently being considered by Members.