

Date: 25 March 2008

**Report: CAPITAL FINANCE AND THE PRUDENTIAL CODE – REPORT OF THE
TREASURER**

Purpose of the Report

1. To seek approval of the Capital Finance and the Prudential Code Report for 2008/09 as prepared by the Treasurer and attached as an annex to this report.

Strategic Planning Framework

2. The information and recommendations contained in this report are consistent with the Authority's statutory purposes and its approved strategic planning framework, and in particular its objective 'to manage all aspects of the Authority's business so as to make the most effective use of our resources' (Best Value Performance Plan).

Capital Finance and the Prudential Code

3. Prior to the commencement of the financial year the Treasurer to the Authority prepares an Annual report on Capital Finance and the Prudential Code in compliance with the CIPFA Prudential Code for Capital Finance in Local Authorities. A copy of the report for the 2008/09 financial year is attached as an annex to this report.

RECOMMENDATIONS

4. That members approve the recommendations contained in the Report of the Treasurer.

**Irene Brannon
Senior Finance Officer**

7 March 2008

Background documents: CIPFA Prudential Code for Capital Finance in Local Authorities

YORKSHIRE DALES NATIONAL PARK AUTHORITY

25 March 2008

CAPITAL FINANCE AND THE PRUDENTIAL CODE

Report of the Treasurer

1.0 PURPOSE OF REPORT

- 1.1 To recommend to the Authority an updated set of Prudential Indicators for the period 2008/09 to 2010/11 as required by the Prudential Code.

2.0 BACKGROUND

- 2.1 The new Capital Finance system introduced on 1 April 2004 is underpinned by the CIPFA Prudential Code for Capital Finance in Local Authorities. This Code requires every local authority to set a range of Prudential Indicators
- (i) as part of the Budget process and;
 - (ii) before the start of the financial year;
- to ensure that capital spending plans are affordable, prudent and sustainable.

- 2.2 The Prudential Indicators focus on the Capital expenditure of an authority and the requirement to finance that expenditure by borrowing. The Prudential Indicators are a way of monitoring the borrowing that is undertaken. In the case of the authority it is unlikely that borrowing will be undertaken as the forecast is that revenue contributions will finance any capital expenditure. However, in accordance with statute - Local Government Act 2003 – and if unforeseen circumstances arose, it may be necessary to borrow and therefore Prudential Indicators are set at the beginning of each financial year.

- 2.3 The Prudential Indicators for 2007/08 covering the period up to 2009/10 were approved by the Authority on 27 March 2007.

- 2.4 The Prudential Code also requires appropriate arrangements to be in place for the monitoring, reporting and revision of Prudential Indicators previously set. These arrangements were also agreed by the Authority on 27 March 2007.

- 2.5 As part of the 2008/09 Budget process a fresh set of Indicators for the period up to 2010/11 now needs to be considered and approved.

- 2.6 This report should be read in conjunction with the separate report on the agenda regarding Treasury Management as some of the indicators, particularly those relating to borrowing, have implications for Treasury Management.

3.0 Updated Prudential Indicators proposed for 2008/09 to 2010/11

- 3.1 The proposed Prudential Indicators for the Authority for the 2008/09 financial year are as follows. It should be noted that although many of the indicators are relatively small in size (recognising only a small borrowing need in future years) it is the underlying framework and monitoring process that is important.

(i) **Estimated Ratio of Capital Financing Costs to the Net Revenue Budget (Affordability)**

This indicator identifies the trend in the cost of borrowing (principal and interest) against total revenue income (National Park Grant and Contributions from Other Authorities).

The estimated ratios for the current and future years and the actual figures for 2006/07 are as follows:-

Year	Basis	%
2006/07	Actual	0.00
2007/08	estimate	0.00
2008/09	estimate	0.03
2009/10	estimate	0.40
2010/11	estimate	1.37

(ii) **Capital Expenditure Plans (Actual and Estimated)**

The actual capital expenditure that was incurred by the Authority in 2006/07 and the estimates of capital expenditure to be incurred for 2007/08 and future years are outlined in the table below.

In the years 09/10 and 10/11 the capital expenditure figures are seen to rise. This is on the basis that Members give approval going forwards to the development of the Dales Countryside Museum. This project is at an early stage but it is included in the prudential indicators to highlight the potential need to borrow.

It is important to note that this table reflects the **potential** total capital spending plans for the Authority funded by both external borrowing and National Park Grant. All the prudential indicators that follow are based upon the borrowing element of these spending plans only.

Year	Basis	£k
2006/07	actual	70
2007/08	estimate	70
2008/09	estimate	150
2009/10	estimate	650
2010/11	estimate	570

(iii) **Capital Financing Requirement and Forecast**

The capital financing requirement relates to the underlying need of the Authority to borrow to finance capital purposes. Estimates of the capital financing requirement at the future financial year end dates are as follows:-

Date	Basis	£k
31 March 2007	actual	0
31 March 2008	estimate	0
31 March 2009	estimate	80
31 March 2010	estimate	727
31 March 2011	estimate	1,268

The above figures relate to the borrowing plans of the authority and the level of debt outstanding has been adjusted for the statutory 4% Minimum Revenue Provision (MRP). This applies to debt outstanding at the end of each financial year and therefore the MRP charge will be applicable from 2009/10 onwards and the capital financing requirement will be reduced accordingly.

(iv) **Authorised Limit for External Debt**

This indicator represents the limit beyond which borrowing by the Authority is prohibited and is based upon the best estimate of increases in debt arising from the capital financing requirement plus a margin to allow some flexibility for unforeseen cash movements. This has been included at £250,000.

The limit is analysed between borrowing and other long term liabilities (such as finance leases or credit arrangements) to show the actual debt owed by the Authority and any other financing instruments that have been used.

It is recommended that Members agree to delegate authority to the Treasurer to effect any changes between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal, value for money and any other relevant factors.

The recommended Authorised limits for external debt are as follows:

Year	Borrowing Limit £k	Other Long Term Liabilities £k	Total £k
2007/08	250	0	250
2008/09	330	0	330
2009/10	977	0	977
2010/11	1,518	0	1,518

The Treasurer can confirm that the Authorised Limit is consistent with the Authority's current commitments and budget process.

A final point to note is that under **Section 3(1) of the Local Government Act 2003** the Authority must determine a Statutory Limit in terms of how much money it can afford to borrow. This affordable borrowing limit is to be set on a rolling basis for the forthcoming financial year and two successive years. The Authorised limit of **£330k** will act as this limit for 2008/09.

(v) **Operational Boundary for External Debt**

This indicator is based on the probable external debt position during the course of the year. It is not a limit and actual borrowing could vary around this boundary during the year. The difference between this indicator and the Authorised Limit is the £250k which provides headroom for unusual cash movements.

In line with the Authorised limit the operational boundary, is analysed between borrowing and other long term liabilities separately. In a similar vein the Authority is recommended to delegate any in year changes to the operational boundary and its subcategories to the Treasurer.

Year	Borrowing Limit £k	Other Long Term Liabilities £k	Total £k
2007/08	0	0	0
2008/09	80	0	80
2009/10	727	0	727
2010/11	1,268	0	1,268

(vi) **Actual External Debt**

This Authority had no external debt at 31 March 2007 and does not plan to have any at 31 March 2008. At 31 March 2009 and in future years, if capital expenditure plans are funded by revenue contributions then no borrowing will be required.

(vii) **CIPFA Code Compliance**

This Authority already complies with the CIPFA Code of Practice for Treasury Management 2001 which the Authority agreed to adopt at its meeting on 25 March 2005.

(viii) **Interest Rate Exposure**

The authority needs to set for the forthcoming financial year and the following two financial years, upper limits to its exposures to the effects of changes in interest rates. This indicator is for both fixed and variable interest rate exposures and relates to the authority's net principal sum outstanding on its borrowing and investments.

The effect of setting these upper limits is to provide ranges within which the authority will manage its exposure to fixed and variable rates of interest.

The variable and fixed limits together look at the whole portfolio and will therefore together always show 100% exposure. Interest rate limits can be positive or negative as investments are credit balances. Borrowing and investment principals are offset against each other to give the net interest rate exposure position. Investments and borrowing, for periods up to 364 days are classed as being at a variable rate. As YDNPA currently has no borrowing and has investments under 364 days, the variable interest rate exposure at the current time is 100%.

The table below shows how this might change if borrowing was undertaken.

Year	Upper Limit on fixed interest rate exposure	Upper Limit on variable interest rate exposure	Net position
2008/09	-2%	102%	100%
2009/10	-26%	126%	100%
2010/11	-57%	157%	100%

It should be noted in this instance that the variable interest rate exposure is positive. This is because for the upper limit, investments under 364 days are greater than borrowing that will occur. Therefore the overall net position will be negative leading to a positive upper limit for variable interest rate exposure.

In addition to the above upper limit on fixed and variable interest rate prudential indicator which is required by statute, a local indicator has also been set for the limits of borrowing and investments separately. This is detailed below:

Borrowing	%age of outstanding principal sums
Limits on fixed interest rate exposures	70 to 100
Limits on variable interest rate exposures	0 to 30
Investing	
Limits on fixed interest rate exposures	0 to 20
Limits on variable interest rate exposures	80 to 100

(ix) **Maturity Structure of Borrowing**

A further decision to be made when borrowing is in respect of the length of the loan taken. Loans can be taken with the PWLB up to 50 years and on the money market to 70 years.

The Authority's treasury management advisers recommend that the length of loan taken is linked to the interest rates at the time. However in general, loans will be taken in varying periods in order to spread the risk.

At present there is no borrowing, but for borrowing to be undertaken it is recommended that the authority sets flexible upper and lower limits for the maturity structure of its borrowings as follows:

Period	Upper Limit	Lower Limit
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

(x) **Total Principal Sums Invested for Periods longer than 364 days**

So far all the prudential indicators have considered the borrowing needs of the Authority. If borrowing is undertaken then the funds received could relate to

commitments and expenditure for several years in the future. It may therefore be prudent to invest these sums to match the expenditure profile of future capital schemes.

Prior to the Local Government Act 2003 and the introduction of the Prudential Code, local authorities could only invest to a maximum of 364 days due to the risk associated with future interest rate movements. These regulations now allow investment in these types of instruments as long as specialist advice is taken beforehand and a maximum limit is set.

In line with the County Council's policy and advice in this area, a prudential indicator of **20%** of the Authority's core cash balances is recommended for investments longer than 364 days.

4.0 **RECOMMENDATIONS**

4.1 That the Authority approves:

- (i) the Prudential Indicators as set out in **Paragraph 3** of this report
- (ii) an affordable borrowing limit of £330k for 2008/09 under Section 3(1) of the Local Government Act 2003 as set out in **Paragraph 3(iv)** of this report
- (ii) the specific delegations to the Treasurer proposed in **Paragraph 3** of this report in relation to day to day management of Prudential Indicators (iv) and (v).

JOHN MOORE
Treasurer to the Yorkshire Dales National Park Authority

11 February 2008