

Date: 27 March 2007

**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 2007/08 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 2007/08 financial year is attached as an annex to this report.

RECOMMENDATION

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

**Irene Brannon
Senior Finance Officer**

7 March 2007

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

YORKSHIRE DALES NATIONAL PARK AUTHORITY

27 March 2007

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 three year period up to 2009/10 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 for 2006/07 covering the period up to 2008/09 were approved by the Authority on 28 March 2006.

- 2.3 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 28 March 2006.

- 2.4 As part of the 2007/08 Budget process a fresh set of Indicators for the period up to 2008/09 now needs to be considered and approved.

- 2.5 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 2007/08 to 2009/10

- 3.1 The proposed Prudential Indicators for the Authority for the 2007/08 financial year are as follows. It should be noted that although many of the indicators are relatively small in size 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 2005/06 are as follows:-

Year	Basis	%
2005/06	actual	0
2006/07	estimate	0
2007/08	estimate	0
2008/09	estimate	0
2009/10	estimate	0

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

The actual capital expenditure that was incurred by the Authority in 2005/06 and the estimates of capital expenditure to be incurred for the current and future years are outlined in the table below.

It is important to note that this table reflects the 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	£
2005/06	actual	2,222.0
2006/07	estimate	70.0
2007/08	estimate	70.0
2008/09	estimate	70.0
2009/10	estimate	70.0

(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	£
31 March 2006	estimate	0
31 March 2007	estimate	0
31 March 2008	estimate	0
31 March 2009	estimate	0
31 March 2010	estimate	0

The above figures relate to the borrowing plans of the Authority for 2006/07, 2007/08, 2008/09 and 2009/10, which currently stand at £nil. However the level of debt outstanding (were there to be any) needs to be 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 the year following the financial year in which borrowing is undertaken (where the repayment period extends over more than one year) 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 £	Other Long Term Liabilities £	Total £
2006/07	250,000	0	250,000
2007/08	250,000	0	250,000
2008/09	250,000	0	250,000
2009/10	250,000	0	250,000

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 **£250,000** will act as this limit for 2007/08.

(v) **Operational Boundary for external debt**

This indicator is based on the probable external debt position during the course of the year and has been set at £nil. 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 £250,000 which provides headroom for unusual cash movements.

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

Year	Borrowing Limit	Other Long Term Liabilities	Total
	£	£	£
2006/07	0	0	0
2007/08	0	0	0
2008/09	0	0	0
2009/10	0	0	0

(vi) **Actual external debt**

This Authority had no external debt at 31 March 2006 and does not plan to have any at 31 March 2007.

(vii) **CIPFA Code compliance**

This Authority already complies with the CIPFA Code of Practice for Treasury Management 2001 as reported to the Authority meeting as part of the Annual report (also on the agenda of this meeting).

(viii) **Interest Rate exposures**

If the Authority were to borrow in 2007/08, it would follow the annual Borrowing Strategy within the Treasury Management Report elsewhere on the agenda. An application would be made to the Public Works Loan Board (PWLB), the Government's lending agency to Local Authorities.

A decision required by officers would be whether to take the borrowing in the form of a fixed interest rate or a variable interest rate loan. This decision would be made based on the prevailing interest rate environment at the time. A fixed rate loan is usually considered less risky than a variable loan due to the difficulty in predicting future interest rate changes. Fixed rate borrowing is generally considered the most appropriate form of borrowing and also gives certainty for budget purposes. However if interest rates were predicted to decrease in the short term gains could be accrued through variable rate borrowing.

It is therefore recommended that the Authority sets an upper limit on its fixed interest rate exposures for 2006/07, 2007/08 and 2008/09 of **100%** of its net outstanding principal sums. In essence all borrowings could be taken at fixed rates if required.

It is also recommended that the Authority sets an upper limit on its variable interest rate exposure for the same period at **30%** of its net outstanding principal sums. This is based on advice from the Treasurer and reflects the riskier nature of these types of loan.

If the Authority does decide to borrow the Treasurer will manage fixed interest rate exposures within the range 70% to 100% and variable interest rate exposures

within the range 0% to 30%. This is a continuation of the Authority's current treasury management practice.

(ix) **Maturity structure of borrowing**

A further decision to be made when borrowing is in respect of the length of loan taken from the PWLB. The Board offers loans of one to fifty years for fixed rate loans and one to ten years for variable rate loans.

The Authority's treasury management advisers recommend that the length of loan taken is linked to PWLB interest rates at the time.

It is recommended that the Authority sets upper and lower limits for the maturity structure of its borrowings as follows to allow maximum flexibility-

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.

However 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 Treasurer's advice in this area, a prudential indicator of **20%** of the Authority's core cash balances is recommended for investments longer than 364 days. It should be noted that to date no investments of this nature have been made.

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 **£250,000** for 2007/08 under Section 3(1) of the Local Government Act 2003 as set out in **Paragraph 3(iv)** of this report
- (iii) 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

23 February 2007

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