

PRUDENTIAL INDICATORS FOR THE 2006/07 BUDGET

Prudential Indicators related to Affordability

1. Estimates of financing costs to net revenue stream.

This is a ratio (expressed as a percentage) of estimated financing costs compared to an estimate of the "net revenue stream". This ratio must be prepared for the General Fund and HRA, and also a combined ratio.

For Runnymede, financing costs comprise mainly investment income, offset by a small amount of borrowing costs.

The "net revenue stream" is a term used to describe the amount in the General Fund to be met from government grant and local taxpayers. For the HRA it is the total HRA income shown in the accounts i.e. rent, other income and (if positive) HRA Subsidy.

The ratios are set down in Table 1:

Table 1 - Ratio of financing costs to net revenue stream			
	General Fund	HRA	Overall
	Ratio	Ratio	Ratio
2004/05 Actual	-15.59%	16.03%	0.44%
2005/06 Estimate	-12.09%	16.78%	4.69%
2006/07 Estimate	-11.75%	15.99%	4.24%
2007/08 Estimate	-12.72%	15.88%	3.16%
2008/09 Estimate	-12.31%	16.01%	3.70%

The General Fund ratio is a negative percentage because investment income significantly exceeds any marginal borrowing costs. The HRA ratio is a positive figure because the depreciation charge (equivalent to the Major Repairs Allowance) is treated as a financing cost.

2. Actual financing costs to net revenue stream

This figure is calculated in the same way as for the estimates. The actual for 2004/05 is shown in Table 1 for illustrative purposes.

3. Estimates of the incremental impact of capital investment decision on the Council Tax & Rents

This is a measure of affordability i.e. the impact of changes to the capital programme on Council Tax and housing rents. This indicator looks at CHANGES to the capital programme and is in the nature of a "before and after" exercise. It looks at the revenue costs (including capital financing charges) and any savings or incomes arising from the proposed changes.

Of all the performance indicators, this is the most difficult to interpret. The indicator does not distinguish between capital schemes that have an element of choice, or those that are critical (or

statutory). This indicator will undoubtedly be refined as experience of the new capital system is gained and guidance from CIPFA and the government reflects feedback from authorities.

The calculation is required separately for General Fund and HRA capital investment decisions. Table 2 sets out these indicators.

Table 2 - Impact on Council Tax and Rents of Capital Spending Decisions		
	Council Tax (At Band D)	Average Weekly HRA Rents
	£	£
2005/06 Estimate	0.48	0.00
2006/07 Estimate	3.97	0.00
2007/08 Estimate	-4.90	0.00

Impact on Council Tax

The starting point in calculating this indicator is establishing a base position. For this purpose the capital programme used in the 2005/06 Budget Book has been used. New schemes that are in the programme for 2005/06 are included in the indicator. Capital budgets that form an established part of the capital programme (e.g. grant aid, computer hardware replacement programme) are not taken into the calculation as these do not represent incremental changes to the programme. Schemes that follow on from 2005/06, either as a result of slippage or planned completion are also not taken into the calculation.

So that Members can further understand the way the indicator for General Fund schemes calculation has been calculated, a copy of the working paper used is produced at the end of this Appendix.

The impact of the capital programme has always formed part of the financial planning process in Runnymede. The costs and savings form part of the Financial Strategy approved by the Council. At a detailed level, the Council's capital project appraisal rules require the estimated costs and benefits of individual schemes to be considered by the relevant Committees before any approvals are granted.

Impact on Housing Rents

The capital programme for the HRA comprises the ongoing planned major repair and improvement programmes, and a modest provision of £40,000 for the assisted private purchase schemes. The Council's forward HRA capital programme is based on no changes other than those included in the HRA Business Plan (based on need to spend and the profile of that spending), hence the impact of incremental changes on rents is nil.

The indicator is a misnomer for the HRA in any case. Rents are set according to the government rent restructuring formula. Expenditure on housing stock (capital and revenue) is based on allowances made in the HRA Subsidy system, plus any locally generated incomes (e.g. garage rents) and savings. The link between rent and expenditure is therefore very tenuous.

Prudential Indicators related to Prudence

4. Net borrowing & the capital financing requirement

By law local authorities can only borrow to finance capital expenditure. Other than for short-term cash flow requirements, an authority cannot plan to borrow to finance revenue deficits. This indicator is intended to be the key indicator for prudence, i.e. to illustrate that any borrowing is only for capital purposes.

Runnymede does not have net external borrowing, but net investments. This is because all debt has been repaid and the accumulation of revenue and capital reserves has generated equivalent cash balances.

The "Capital Financing Requirement" is the term used in the new system to show underlying need to borrow for a capital purpose. The underlying need is different from the actual need because of the presence of revenue balances and associated cash flows that enable treasury activities to be undertaken in a holistic manner.

The Capital Financing Requirement will increase where existing resources (e.g. capital receipts, or government grant or other contributions) are not sufficient to finance capital expenditure. In this instance the authority's underlying need to borrow will increase (irrespective of immediate cash requirements).

The Capital Financing Requirement for Runnymede is nil. This is because the Council has fully financed past capital expenditure.

	Net external borrowing (investments) at the year end	Capital Financing Requirement	Headroom
	£000	£000	£000
2005/06 Estimate	(22,737)	0	(22,737)
2006/07 Estimate	(18,192)	0	(18,192)
2007/08 Estimate	(21,749)	0	(21,749)
2008/09 Estimate	(20,004)	0	(20,004)

For Runnymede this is a particularly difficult indicator to interpret. The key point is that the Council does not currently plan to use debt to finance its capital programme, i.e. the current programme will be financed by capital receipts, and grants and contributions.

It is possible that the Council may need to borrow for capital purposes in the future, particularly for large schemes and/or where capital receipts are delayed or otherwise expected in future years. For instance, the Civic Offices project is large and may consume all available capital resources if capital receipts are delayed. If this were the case the capital financing requirement would become a positive figure and depending on the overall cash position, borrowing may be required. In this instance the purpose behind this prudential indicator is that relevant borrowing should not exceed the capital financing requirement.

Prudential Indicators related to Capital Expenditure

5. Estimates of Capital Expenditure

This indicator is simply an extract from the Council's capital programmes. Table 4 summarises the estimates by service area:

Table 4 - Estimates of capital expenditure by service area					
	2004/05 Actual	2005/06 Estimate	2006/07 Estimate	2007/08 Estimate	2008/09 Estimate
	£000	£000	£000	£000	£000
Housing First	114	263	1,200	950	500
Housing Renewal	420	814	864	878	894
Community Services	0	0	70	50	50
Leisure Services	700	1,864	1,817	83	0
Environmental Services	264	149	139	139	139
Economic Development	2,675	953	1,038	285	285
Civic Offices Re-provision	119	1,000	8,000	7,255	0
IT	609	383	438	461	281
Other	4,138	1,666	53	53	53
Total – General Fund	9,040	7,092	13,619	10,154	2,202
HRA	3,169	3,790	3,529	4,658	3,889
Grand Total	12,209	10,882	17,148	14,812	6,091

The Prudential Code requires the capital programme to be approved when the indicators are produced. The capital programme forms part of the overall Budget approval process accordingly. Capital expenditure is a significant source of risk and uncertainty since cost variations, slippage or acceleration of major projects and changing specifications are often a feature of capital schemes. Capital expenditure also carries risk in relation to the availability of capital finance from capital receipts, grants and external contributions. For Runnymede, planned capital spending is often heavily dependant on achieving capital receipt targets. Examples of this uncertainty are the dependency of the affordable housing provision (Homes First) on sale of housing assets, and the assumption that the sale of the Civic Offices site will significantly finance the re-provision project.

Note

The figures for the "Housing First" service area (provision of affordable housing) are those elements of the Council's overall housing capital programme that is financed from Runnymede capital resources. Therefore, the figures exclude new affordable housing schemes financed directly from government and the Housing Corporation.

6. Actual Capital Expenditure

This figure is calculated as for the estimates. The actual for 2004/05 is shown in Table 4 for illustrative purposes.

7. Estimates of Capital Financing Requirement

Note: The Capital Financing Requirement is also used in the preparation of prudential indicator 4.

The Capital Financing Requirement is designed to show the underlying need to borrow for a capital purpose. The underlying need is different from the actual need because of the presence of revenue balances and associated cash flows that enable treasury activities to be undertaken in a holistic manner.

The Capital Financing Requirement will not increase where capital expenditure is financed from capital receipts, or government grant or other contributions. Where existing resources are not sufficient to finance capital expenditure, this will increase the authority's underlying need to borrow (irrespective of immediate cash requirements).

In the medium term net borrowing can only be for a capital purpose. This is because local authorities cannot borrow for revenue purposes (except for short-term cash flow needs). Therefore, net external borrowing must not exceed the total of the capital financing requirement for the preceding year plus the estimates for the following three years. Runnymede has no difficulty in meeting this requirement.

This indicator requires separate estimates for the HRA capital financing requirement (as determined under legislation), and for the General Fund. These estimates are set out in Table 5.

	General Fund	HRA	Total
	£000	£000	£000
2003/04 Actual	0	0	0
2004/05 Estimate	0	0	0
2005/06 Estimate	0	0	0
2006/07 Estimate	0	0	0
2007/08 Estimate	0	0	0

There is no change in the capital financing requirement for the foreseeable future. This is because the Council's capital programme will be fully met from capital receipts, and grants and contributions. No borrowing is planned.

These estimates do not commit the Council to particular methods of financing. The Council will continue to determine the actual financing of capital expenditure incurred after the end of the particular financial year.

8. Actual Capital Financing Requirement

This figure is calculated as for the estimates except that it is an extract from the Council's Statement of Accounts. The actual for 2004/05 is shown in Table 5 for illustrative purposes.

Prudential Indicators related to External Debt

9. Authorised Limit

The "Authorised Limit" is simply a limit on the maximum amount the authority expects to borrow at any one point in time. It is the same as the overall borrowing limit in the old regime. The limit includes short-term borrowing. The Council now has no external long term debt and is unlikely to borrow long term in the foreseeable future. However, there may be cause to borrow short term.

Council's fund manager – Alliance Capital – invests those funds that are not required in the short term. The remainder of cash balances are held in house and are invested as required to meet cash flow requirements. The Council generally has strong cash flows in the first 10 months of the financial year as Council Tax and Business Rates instalments are collected.

In the last two months of the year the need to make payments of Precepts, contributions to the Business Rates pool and general revenue and capital obligations significantly reduces cash balances. In early April the cash balances are replenished as Council Tax and Business Rate instalments become receivable again.

Cash flow projections for 2005/06 indicate that no temporary borrowing will be necessary.

In 2006/07 the Council's forecasts assume further net reductions in the amount invested. These cash forecasts are heavily dependent on capital receipts being realised in accordance with the expected programme. There are also large sums in the capital programme for the affordable housing programme, and the Civic Offices re-provision project. The timing of these spending commitments will also significantly impact on the level of cash reserves.

Should the timing of cash flows from capital receipts or expenditure be different from the forecast, then it may be necessary to borrow temporarily to cover the shortfall. Short-term borrowing may also arise from two specific areas:

- Day to day cash management of the authority's bank account which will on occasion be in overdraft; and
- The need to meet unexpected payments prior to the availability of monies previously invested.

Given this range of variables, it is suggested that the Council's authorised limit for 2006/07 be set at £5,000,000 which will be sufficient to accommodate any short term borrowing undertaken. This limit should also be sufficient for the following three years.

The authorised limit for 2006/07 is also the statutory limit determined under Section 3(1) of the Local Government Act 2003

Financial Year	£'000
2005/06	5,000
2006/07	5,000
2007/08	5,000
2008/09	5,000

10. Operational Boundary

The operational boundary is the term used to describe the most likely scenario of cash flow movements and equates to the maximum level of external debt projected by the authorities

estimates. The Authorised Limit differs in that it provides over and above the operational boundary for unusual cash movements (hence, one is a **limit**, the other a **boundary**).

For Runnymede, an operational limit of £2m is appropriate and will act as a warning signal that cash flows are not as robust as expected.

Financial Year	£'000
2005/06	2,000
2006/07	2,000
2007/08	2,000
2008/09	2,000

11. Actual External Debt

This is a simple year-end figure taken from the Statement of Accounts. In comparison with the Authorised Limit and Operational Boundary this is just the debt at a point in time (i.e. 31 March).

	Borrowing	Overdraft	Long Term Liabilities	Total
	£'000	£'000	£'000	£'000
Short Term Borrowing	47	637	0	684

This statistic comprises of the bank overdraft – a result of cheques outstanding and not yet cashed against the Council's account rather than a real cash shortage - and a small sum borrowed from the Cabrera Trust (which gives the Trust certainty of income and quick access if needed).

Prudential Indicators related to Treasury Management

12. Code of Practice for Treasury Management

The first prudential indicator in respect of treasury management is that the Council has adopted the CIPFA *Code of Practice for Treasury Management in the Public Services*.

The Council adopted the Code in October 2002.

13. Interest Rate Exposures

This indicator includes both borrowing and investment interest rate exposures. The intention of this indicator is to limit the potential risk of an authority becoming too dependant on fixed or variable rate borrowings. For instance, if an authority has too high a proportion of variable rate debt it will be very vulnerable to increases in short term interest rates.

Runnymede is an investor of funds. For investments the key treasury risk is determined by the length of time money is invested, rather than whether fixed or variable rates are used. For example a fixed rate investment can be for a week, a month or for a number of years. In this case, the investment that has a maturity date furthest into the future carries the greatest risk.

The Council's policies for investment exposures are contained in detail in the Treasury Management Strategy. There is currently no benefit to arbitrarily limiting exposure to either fixed or variable rates. Therefore 100% limits are prudent in these circumstances.

Given no long-term borrowings is planned, interest payable on any short-term borrowings will equal the total interest paid. Short term borrowing either by way of overdraft or from money markets is often made at variable interest rates. Therefore, it is recommended that a limit of 100% of the Council's total interest payable to be at variable rates would be an appropriate level to enable efficient operation of the Council's borrowing requirements.

	Fixed	Variable
	%	%
2006/07 Estimate	100	100
2007/08 Estimate	100	100
2008/09 Estimate	100	100

For investments, similar rules apply. Most of the Council's investment portfolio is held by Fund Managers. They principally use the investment instruments of government stock (gilts) and certificates of deposit. Both these investment instruments are at fixed rates of interest, although the periods they are held for are often short term. Again there is no benefit from distinguishing between fixed and variable rates.

	Fixed	Variable
	%	%
2006/07 Estimate	100	100
2007/08 Estimate	100	100
2008/09 Estimate	100	100

It should be noted that there are other important controls on the interest rate and other market risks that the Fund Managers can expose the Council to. These are set down in the agreements with the Fund Managers.

14. Maturity Structure of Borrowing

This is an indicator that has relevance to authorities with significant debt portfolios. Runnymede has need for only short-term borrowing. The proposed structure is therefore:

	Upper	Lower
	%	%
Under 12 months	100	0
12 -24 months	0	0
24 months to 5 years	0	0
5 to 10 years	0	0
Over 10 years	0	0

15. Total sums invested for periods longer than 364 days

Where the Council invests, or plans to invest, for periods longer than 364 days, an upper limit for the amount of investments maturing in future years must be set.

The purpose of this limit is for the Council to be aware of (and contain) its exposure to the possibility of loss that may arise as a result of having to seek early repayment or redemption of sums invested.

This is another limit that forms part of the Council's overall Treasury Strategy and Annual Investment Strategy for 2006/07. To enable effective monitoring of this exposure, the Annual Investment Strategy sets separate limits for in-house investments and the funds managed by Alliance Capital:

In house Limit

The proportion of the in-house portfolio that may be held in short-term and long-term investments will vary at any one time dependant on the cash flow position of the Council. The following table sets out the maximum, minimum and expected range of investments held at various times of the year:

Time of year	Long Term investments		Short term investments	
	Maximum	Minimum	Maximum	Minimum
	%	%	%	%
Start of year	25	0	100	0
June	25	0	100	75
September	25	0	100	75
December	25	0	100	75
End of year	100	0	100	0

Alliance Capital – Long Term investment limit

The limits applying are set out in the Investment Guidelines that are formalised in the agreement with Alliance Capital. These guidelines are attached to the Annual Investment Strategy for 2006/07.

Briefly, the first priority of the Alliance Capital investment fund is the preservation of the capital sum together with an investment objective of optimising returns commensurate with the containment of risk. The fund has limits that are designed to contain the risk of placing too high a proportion of funds in long term investments – the “Maximum weighted portfolio average life” – and an overall maximum term for any one investment. These limits are:

- MAXIMUM WEIGHTED PORTFOLIO AVERAGE LIFE – 18 MONTHS
- MAXIMUM TERM OF ANY ONE INVESTMENT – 5 YEARS

It is mathematically possible for the whole fund to be invested in instruments with a term of over 12 months (but under the 18 month weighted average), although this would be very unlikely. In any case, the fund manager would use liquid investments that could readily be sold in the money markets, and would therefore be quickly able to limit treasury risks as appropriate.

Affordability

Estimates of the Incremental Impact of the New Capital Investment Decisions on the Council Tax

Impact on Council Tax

Requirements for at least the forthcoming year and following 2 years:

- (i) forecast the total non-HRA budgetary requirements for the authority based on no changes to the existing capital programme
- (ii) forecast the total non-HRA budgetary requirements for the authority with the changes to the capital programme included in the calculation
- (iii) take the difference between (i) and (ii) and calculate the addition or reduction to Council Tax that would result

Financing Cost interest rate assumption 5.0%
Council Tax Base 32,500

	Capital Budgets			Financing Costs			Running Costs			Total			
	05/06	06/07	07/08	05/06	06/07	07/08	05/06	06/07	07/08	05/06	06/07	07/08	
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	
Dial-a-ride vehicles	0	70	0	0	4	4	0	0	0	0	4	4	Replacement - No additional running costs
Chertsey Allotment Project	71	0	0	4	4	4	0	0	0	4	4	4	
Abbeyfit Sports Centre	-179	469	0	-9	15	15	0	0	0	-9	15	15	Additional capital outlay - No new revenue
Egham LC - New Equipment	0	200	0	0	10	10	0	0	-58	0	10	-48	Additional income generated
Egham LC - Outside Pitches	0	606	0	0	30	30	0	24	-209	0	54	-179	Additional income generated
New Civic Offices	0	0	54	0	0	3	0	0	0	0	0	3	Additional capital outlay - No new revenue
Hardware Replacement Programme	-104	0	0	-5	-5	-5	0	0	0	-5	-5	-5	
Northgate Planning System	47	0	0	2	2	2	5	9	9	7	11	11	Capital funded by IEG
Single Account for Web Users	0	0	0	0	0	0	11	21	21	11	21	21	Capital funded by IEG
Customer Relationship Management	0	0	0	0	0	0	8	16	16	8	16	16	
Total	-165	1,345	54	-8	59	62	24	70	-221	16	129	-159	

Impact on Council Tax	£0.48	£3.97	-£4.90
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