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Shropshire and Wrekin Fire and Rescue Authority
Strategy and Resources Committee
22 January 2010

Capital Programmes 2010/11 to 2014/15 and Prudential Guidelines

Report of the Treasurer

For further information about this report please contact Keith Dixon, Treasurer, on 01743 260202.

1 Purpose of Report

This report presents the capital programmes for 2010/11 to 2014/15, for consideration by the Committee in the context of Prudential Guidelines.

2 Recommendations

The Committee is asked to recommend that the Fire Authority:

a) Consider the 2010/11 onward programmes, as set out in the Appendix, as part of its final precept deliberations;

b) Approve the Prudential Indicators and the Treasury Strategy for 2010/11; and

c) Approve the Minimum Revenue Provision 2010/11.

3 Background

Consideration of the future capital programmes must be in the context of producing a balanced budget. This means that the increases in capital expenditure must be limited by increases in debt charges caused by increased borrowing and increases in running costs from new capital projects.

The Fire Authority must also have regard to the Prudential Code and must set Prudential Indicators for the next three years to ensure that its capital investment plans are affordable, prudent and sustainable.

4 Amendments to the Capital Programme

The capital programme approved for consultation purposes in December produced the following summary.

Total Cost of Schemes	Revenue Consequences				
	2009/10	2010/11	2011/12	2012/13	2013/14
£'000	£'000	£'000	£'000	£'000	£'000
5,960	86	153	342	516	679

Since the December 2009 meeting, no changes have been made to the programme.

The capital programme now proposed to the Fire Authority for its 2010/11 budget is attached as an appendix to this report.

Detailed project appraisals are available electronically for further consideration by the Committee.

5 Treasury Management Strategy Statement

The Local Government Act 2003 requires the Authority to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance issued subsequent to the Act); this sets out the Authority's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The Fire Authority employs Shropshire Council to manage its Treasury Functions, who in turn have appointed Sector Treasury Services as their advisor.

6 Prudential Guidelines

The Act requires the Authority to 'have regard to' the Prudential Code for Capital Finance in Local Authorities and to set Prudential Indicators for the next three years to ensure that the Authority's capital investment plans are affordable, prudent and sustainable.

The key issue is to ensure that the revenue consequences of the proposed investment will not lead to unacceptable financial pressures in later years.

The position is as follows:

a) Ratio of Financing Costs to Net Revenue Stream

	2009/10 Revised	2010/11 Budget	2011/12 Budget	2012/13 Budget
	£ 000	£ 000	£ 000	£ 000
2009/10 and Earlier Programmes	813	927	1,025	1,025
2010/11 Programmes		51	112	112
2011/12 Programmes			42	187
2012/13 Programmes				44
Investment Income	-40	-20	-20	-20
	773	958	1,159	1,348
Net Revenue Stream (Budget)	20,846	21,367	22,434	23,229
Ratio	3.71%	4.48%	5.16%	5.80%

b) The impact of Capital Investment on the level of Band D Council Tax is:

2010/11	£185,000	divided by 158,543.24	117p
2011/12	£201,000	divided by 158,543.24	127p
2012/13	£189,000	divided by 158,543.24	119p

c) The capital programme that gives rise to these increases is:

	2010/11	2011/12	2012/13
	£ 000	£ 000	£ 000
Payments (see appendix) financed by:			
Loan – supported by grant	250	497	497
– prudential borrowing	0	573	623
Capital Reserve	550	100	100
Capital Grant	45	0	0
	845	**1,170**	**1,220**

d) The Capital Financing Requirement

The Prudential Code requires the calculation of the Capital Financing Requirement for 31 March in current and future years. The Capital Financing Requirement is simply the amount of capital spending not funded by grant, receipts or revenue, i.e. that which is financed from borrowing.

The position is estimated to be:

	In Year Requirement	At 31 March
	£ 000	£ 000
31 March 2009 (Preceding Year)		6,331
31 March 2010 (Current Year)	292	6,623
31 March 2011	542	7,165
31 March 2012	1,540	8,705
31 March 2013	512	9,217

The importance of the Capital Financing Requirement is that net external borrowing must not (except in the short term) exceed the total of capital financing requirements in the preceding year plus the estimates of any additional capital financing requirements for the current and next two years, i.e. £8,705,000. At present, gross external borrowing is around £5.8 million.

e) Authorised Limit for External Debt

The limit is established, beyond which borrowing is not permitted. The limit must not only accommodate the capital financing requirement, but must be adequate to meet temporary borrowing, e.g. if income is delayed.

The following limits are recommended:

	£ 000
2008/09	9,217
2009/10	9,623
2010/11	10,165
2011/12	11,705
2012/13	12,217

f) Operational Boundary for External Debt

This is set as a likely and prudent boundary that can be exceeded, but, if so, would prompt investigation and, if necessary, corrective action. The following boundaries are recommended, based solely on budgeted capital expenditure:

	£ 000
2010/11	7,205
2011/12	8,753
2012/13	9,273

7 Treasury Strategy 2010/11

Economic Background

The credit crunch of August 2007 and the near collapse of the world banking system in September 2008 pushed most of the major economies of the world into a sharp recession during 2009. Many governments were forced to recapitalise and rescue their major banks, and central banks cut bank rates to 0.10 – 1.00% in order to counter the recession.

The long awaited start of growth eventually came for some economies in quarter 3 of 2009, although not for the UK.

Inflation has plunged in most major economies and is not seen as a current problem by many, with widespread pay freezes seen in some countries in 2009.

Most major economies have introduced huge financial stimulus packages in order to encourage a fast exit from recession. This, together with expenditure on direct support to ailing banks, has led to a drastic expansion of government debt levels, which will take many years to eliminate.

Borrowing Strategy

It is anticipated that borrowing will continue to be made through the Public Works Loan Board (PWLB).

Rates are expected to start the financial year at around 4.55% - 4.6%, and gradually increase during the year. It would be advantageous to time new long-term borrowing for the start of the year, when 25 year PWLB rates fall back to, or below, the central forecast rate of 4.65%. Rates are expected to end the year at around 4.9%.

There is expected to be little difference between 25 year and 50 year rates, so loans in the 25-50 year periods could be deemed more attractive than 50 year borrowing.

External versus Internal Borrowing

The next financial year is expected to be one of historically low bank rates, and again offers the opportunity for the Fire Authority to review its strategy of undertaking new external borrowing.

As long as borrowing rates are expected to be higher than rates to be earned on investing our cash balances, and look likely to be for the next couple of years, external borrowing could be avoided in order to maximise short-term savings.

The running down of investments also has benefits of reducing exposure to interest rates and credit risk.

However, short-term savings should also be weighed against the potential for incurring long-term extra costs by delaying unavoidable new external borrowing until later years, when PWLB long term rates are forecast to be significantly higher.

Borrowing strategy will, therefore, be based on the balance of advantage. Borrowing will be avoided initially, but the situation will be monitored, and, should the prospect of borrowing rates rising significantly in future years, and/or investment rates recovering, increase, some PWLB loans will be taken. It is not, however, intended that money will be borrowed in advance of spending needs.

Investment Strategy

The Fire Authority will have regard to Communities and Local Government's (CLG) Guidance on Local Government Investments ("the Guidance") issued in March 2004, any revisions to that guidance, the Audit Commission's report on Icelandic Investments and the 2009 revised Chartered Institute of Public Finance and Accountancy's (CIPFA's) Treasury Management in Public Services Code of Practice and Cross Sectorial Guidance Notes ("the CIPFA TM Code"). The Fire Authority's investment priorities are:

a) Firstly, the security of capital; and
b) Secondly, the liquidity of its investments.

The Fire Authority will also aim to achieve the optimum return on its investments within the primary objectives of security and liquidity.

The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Authority will not engage in such activity.

This is the initial strategy for 2010/11, and will only be revised by the approval of the Fire Authority, should there be significant improvement in the position of current lending uncertainties.

The Fire Authority will only lend to bodies of high credit quality, that is, the UK Government, local authorities or counter parties with a credit rating acceptable to Shropshire Council and endorsed by your Treasurer, or which effectively take on the creditworthiness of the UK Government itself.

The Fire Authority employs Shropshire Council to manage its investments, and they:

- Use three credit rating agencies;
- Are advised by investment consultants;
- Monitor and review creditworthiness regularly; and
- Provide appropriate training to Treasury Management staff.

The CLG are currently consulting on “Guidance to Local Government Investments”, and any significant new issues will be reviewed at the April meeting of the Fire Authority.

The Treasurer is updated regularly on all changes to acceptable borrowers and may be more restrictive to ensure that security of capital is prioritised. It has been agreed that investments with any one borrower will be limited to £2.0m, except the UK Government through the Debt Management Office (DMO). In the current period of uncertainty, and to ensure liquidity, no loans will be made for a period of more than 12 months.

Investments will be sterling denominated. Funds available for investment are cash flow derived, but there is a core balance available through the Fire Authority’s reserves. This explains much of the difference between gross and net borrowing, which should reduce, particularly as the Unearmarked Capital Reserve is used to fund the St Michael’s Street project.

At the end of the financial year, the Fire Authority will report on its investment activity as part of its Annual Treasury Report, and will also provide quarterly updates throughout the year.

Prudential Indicators for Borrowing and Lending

Consistent with Treasury and Investment Strategies, the Fire Authority is recommended to adopt the following Prudential Guidelines for the period to 31 March 2013:

1. Borrowing

a) Upper limit for net principal fixed interest rate exposure - 100%
b) Upper limit for net principal variable interest rate exposure - 20%

2. Investment

a) Upper limit for net principal fixed interest rate exposure -100%
b) Upper limit for net principal variable interest rate exposure - 100%

3. Maturing Structure of Fixed Rate Borrowing

	Upper Limit (%)	**Lower Limit (%)**
Under 12 months	30	0
12 months to 24 months	30	0
24 months and within 5 years	30	0
5 years and within 10 years	30	0
10 years and above	100	70

4. Investments for more than 364 days – nil

8 Minimum Revenue Provision 2010/11

The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 came into force on 31 March 2008. These regulations introduced several changes to the capital finance regime for local authorities (including fire authorities) in England. The most significant of these was the new provision for dealing with the calculation of Minimum Revenue Provision (MRP), which is the amount that an authority charges to its revenue account in respect of the financing of capital expenditure.

Under the new regulations, an authority is required to set aside an amount of MRP, which it considers prudent. Interpretation within the guidance states that:
"Provision for the borrowing which financed the acquisition of an asset should be made over a period bearing some relation to that over which the asset continues to provide a service."

Essentially, this means that provision charged to the revenue account in respect of borrowing must reflect the lives of the assets, for which funds have been borrowed.

Authorities are required to produce an annual statement on their policy for MRP for each financial year. This statement is being submitted for the financial year 2010/11, prior to the start of the financial year.

9 Options

The guidance on prudent provision contains four options for calculating MRP. Authorities may choose an alternative method, but must demonstrate that it is prudent.

The following policy is recommended to Members for use by the Fire Authority:

- For all borrowing incurred during or before 2006/07, the MRP applied in 2007/08 will be calculated on the basis of 4% of the Capital Financing Requirement (CFR).

  This method was used for the 2007/08 financial year, and will continue to be used in future years for all capital expenditure incurred before 31 March 2007. In addition, a voluntary revenue provision of 4% has been made on all assets other than land and buildings from schemes starting in 2005/06, to align financing costs to the lives of those assets.

- For all borrowing incurred in 2007/08 and subsequently, the MRP applied has been calculated on the basis of the Asset Life method. This method was selected because it charges the financing costs of assets over the lives of those assets in equal instalments each year, and follows the same principles as the provisions made by the Fire Authority from 2006/07.

- For all borrowing incurred in 2009/10, the MRP applied in 2010/11 will be calculated on the basis of the Asset Life method.

10 Financial Implications

The financial implications are as set out in the report.

11 Legal Comment

The Local Government Act 2003 requires the Fire Authority to "determine and keep under review how much money it can afford to borrow". In doing so, it "shall have regard to the Prudential Code for Capital Finance in Local Authorities".

12 Equality Impact Assessment

Officers have considered the Service's Brigade Order on Equality Impact Assessments (Personnel 5 Part 2) and have decided that there are no discriminatory practices or differential impacts upon specific groups arising from this report. An Initial Equality Impact Assessment has not, therefore, been completed.

13 Appendix

Capital Programme

14 Background Papers

Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Treasury Management in the Public Services

Implications of all of the following have been considered and, where they are significant (i.e. marked with an asterisk), the implications are detailed within the report itself.

Balanced Score Card		Integrated Risk Management Planning	
Business Continuity Planning		Legal	
Capacity		Member Involvement	
Civil Contingencies Act		National Framework	
Comprehensive Performance Assessment		Operational Assurance	
Efficiency Savings		Retained	
Environmental		Risk and Insurance	*
Financial	*	Staff	
Fire Control/Fire Link		Strategic Planning	*
Information Communications and Technology		West Midlands Regional Management Board	
Freedom of Information / Data Protection / Environmental Information		Initial Equality Impact Assessment Form completed	

Capital Programme 2010/11 to 2014/15

Scheme		**Total**	**2010/11**	**2011/12**	**2012/13**	**2013/14**	**2014/15**
		£000	**£000**	**£000**	**£000**	**£000**	**£000**
2010/11							
Training Facilities	Fund	50	7	7	7	7	7
Appliance Replacement	Loan	185	5	24	24	24	24
Building Improvements	Loan	65	3	9	9	9	9
Fire Control Conversions	Grant	45	-	-	-	-	
Fire Kit Replacement	Fund	500	36	72	72	72	72
		845	**51**	**112**	**112**	**112**	**112**
2011/12							
Breathing Apparatus Set Upgrade	Loan	330		8	50	50	50
Training Facilities	Fund	50		7	7	7	7
Information Technology	Fund	50		7	7	7	7
Building Improvements	Loan	65		3	9	9	9
Appliance Replacement	Loan	555		14	98	98	98
Water Carriers	Loan	120		3	16	16	16
		1,170		**42**	**187**	**187**	**187**
2012/13							
Training Facilities	Fund	50			7	7	7
Telford Improvements	Loan	500			13	45	45
Information Technology	Fund	50			7	7	7
Building Improvements	Loan	65			3	9	9
Appliance Replacement	Loan	555			14	98	98
		1,220			**44**	**166**	**166**
2013/14							
Training Facilities	Fund	50				7	7
Wellington Improvements	Loan	1,000				26	90
Information Technology	Fund	50				7	7
Building Improvements	Loan	65				3	9
Appliance Replacement	Loan	370				9	48
		1,535				**52**	**161**
2014/15							
Training Facilities	Fund	50					7
Appliance Replacement	Loan	925					23
Building Improvements	Loan	65					3
Replace 5 Ford Rangers	Fund	100					14
Information Technology	Fund	50					7
		1,190					**54**
			51	**154**	**343**	**517**	**680**