RIBLE VALLEY BOROUGH COUNCIL
REPORT TO POLICY AND FINANCE COMMITTEE

meeting date: 20 MARCH 2018

Agenda Item No 20

title: PRUDENTIAL CODE CHANGES

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1 PURPOSE

1.1 To provide members with information on the recent changes to the Prudential Code

1.2 Relevance to the Council’s ambitions and priorities:
   - Community Objectives – none identified
   - Corporate Priorities - to continue to be a well-managed Council providing efficient services based on identified customer need. To meet the objective within this priority, of maintaining critical financial management controls, ensuring the authority provides council tax payers with value for money.
   - Other Considerations – none identified.

2 WHAT IS THE PRUDENTIAL CODE

2.1 Key to the current system of capital finance is CIPFA’s Prudential Code. It is a professional code of practice to support the decisions councils have to make to plan for capital investment at a local level.

2.2 Councils are required by regulation to have regard to the Prudential Code when carrying out their duties under Part I of the Local Government Act 2003.

2.3 The code applies to all local authorities, including police, fire and other authorities defined in the enabling primary legislation.

2.4 The key objectives of the code are:
   - to ensure within a clear framework that capital expenditure plans are affordable, prudent and sustainable
   - that treasury management decisions are taken in accordance with good professional practice
   - that local strategic planning, asset management planning and proper option appraisal are supported; and
   - to provide a clear and transparent framework to ensure accountability.

2.5 In order to demonstrate that we have fulfilled the objectives of the Prudential Code, we are required to prepare, monitor and report on a number of indicators. These have to be set annually on a three year basis as a minimum and are designed to support and record local decision-making, rather than be a means of comparing authorities.

2.6 Prior to review of the Prudential Code, the indicators that have to be set and monitored relate to:
   - External Debt (Authorised Limit, Operational Boundary and Actual External Debt)
   - Financing Cost to Net Revenue Stream
   - Capital Financing Requirement
- Capital Expenditure
- Impact of Capital Investment Decisions on Council Tax
- Gross Debt and Capital Financing Requirement
- Gross and Net Debt
- Interest Rate Exposures
- Maturity Structure of Borrowing
- Principal Sums Invested for Greater than 364 Days
- Formal Adoption of the CIPFA Treasury Management Code of Practice

3 WHY HAS THE PRUDENTIAL CODE CHANGED?

3.1 There have been many changes in Local Government since the production of the initial Prudential Code, particularly around austerity and commercialism. The potential risks from both these areas have been recognised as particularly concerning by CIPFA.

3.2 When CIPFA were reviewing the Prudential Code last year, they saw that it was important to ensure that the changes were there to strengthen and improve the existing framework and that any changes within public sector service delivery and processes continued to reflect transparency, accountability and good decision making.

3.3 The Prudential Code plays a pivotal role in providing assurance that the decisions made around capital finance have at their heart the principles of:
   - Affordability
   - Sustainability
   - Prudence

3.4 The Code framework aims to be structured in a way that is flexible enough to support innovation, but to be durable enough to essentially provide assurance for those who operate within its principles and those who oversee that activity.

4 WHAT HAS CHANGED WITH THE REVIEW OF THE PRUDENTIAL CODE?

Capital Strategy

4.1 Key developments for the new version of the Code include the introduction of more contextual reporting through the requirement to produce a capital strategy along with streamlined indicators.

4.2 The introduction of a capital strategy allows individual local authorities to give greater weight to local circumstances and explain their approach to borrowing and investment. As with many authorities, being a new requirement, this is not a formal strategy that is currently produced.

4.3 However, many of the elements that would be included in such a strategy are already considered at many of the stages that we currently follow in setting our capital programme.

4.4 The capital strategy must form part of our integrated revenue, capital and balance sheet planning – so key to the production of our budgets. The strategy must also set out the long term context in which our capital expenditure and our investment decisions are made. As a result there will be links where appropriate from this strategy to our Treasury Management Strategy.
The strategy must also reflect on risk and reward and the impact on the achievement of our priorities. The Director of Resources must also report explicitly on deliverability, affordability and risk associated with the Capital Strategy.

Below is a summary of the main sections that would be anticipated in a Capital Strategy going forward

- **Capital Expenditure**
  - Governance
  - Long term plans
  - Asset management planning
  - Restrictions around funds
- **Investments and liabilities**
  - Approach, due diligence, risk appetite
  - Governance process for approval and monitoring
  - Summary of material investments, guarantees and liabilities
- **Treasury management**
  - Governance
  - Long term planning including MRP
  - Risk appetite, key risks and sensitivities
- **Skills and knowledge**

Our Capital Strategy will be developed over the coming months and brought back to committee for approval in order to play a role going forward.

**Adoption of CIPFA’s Treasury Management Code**

The new Code has removed the requirement for us to state that we have adopted CIPFA’s Treasury Management Code.

This is not a change to diminish the gravity of the Treasury Management Code, but more to reflect that in reality we have no option other than to adopt CIPFA’s Treasury Management Code, and so does not need to be specifically stated in any policy.

**Principles Apply to Mayors, Combined Authorities and Group Entities**

The new Code has made specific reference and given clarification that the principles of the Prudential Code also apply to Mayors, Combined Authorities and Group Entities.

**Requirement to Consider Explicitly Separate Ring-Fenced Funding streams**

Where ringfenced resources or separate funds exist, affordability must be considered only against those resources available to fund borrowing.

Under combined authority arrangements affordability may need to be considered against combined authority resources and the impact on underlying authorities. Where debt or guarantees relating to local enterprise partnerships (LEPs), subsidiaries or other corporate and non-corporate bodies exist, the impact on the council should be considered.
Deletion of Council Tax Indicator

4.13 Previously the Code required that we forecast the potential impact of our capital programme decisions on the council tax level. This indicator gave a forecast financial value per Band D property.

4.14 It has been recognised that this does not necessarily link to the decision making processes taken in setting the council tax level and has therefore been removed from the Code.

Other Matters

4.15 Other changes had been proposed on drafts of the new Prudential Code, however, these have not been taken forward in to the final version.

4.16 It does not include an explicit ban on borrowing for profit-making investment, as had previously been proposed. However, it is understood that there are likely government moves to prevent councils using loans to fund out-of-area property investments. There has recently been growing concern in the Treasury about the scale of council borrowing to fund commercial investments.

4.17 The Code includes the statement that councils “must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed”.

4.18 The government’s Local Authority Investment Code stipulates that where a local authority chooses to disregard the Prudential Code and Guidance and borrows or has borrowed purely to profit from the investment of the extra sums borrowed, the Treasury Management Strategy should explain:

- Why the local authority has decided not to have regard to this Guidance or to the Prudential Code in this instance; and
- The local authority’s policies in investing the money borrowed, including management of the risks, for example, of not achieving the desired profit or borrowing costs increasing.

4.19 The government’s Local Authority Investment Code also states that where a local authority classifies an investment as contributing to regeneration or local economic benefit, it should be able to demonstrate that the investment forms part of a project in its Local Plan.

CONCLUSION

5.1 There have been a number of changes to the Prudential Code in this latest review by CIPFA in order to better reflect the current landscape that we operate in of austerity and commercialism.

5.2 Risk is a key factor under the Code and this is reflected in other moves to ensure considerations around return on rental yields and borrowing to support such ventures.

5.3 The changes to the Prudential Code have other consequential impacts on the CIPFA Treasury Management Code. These have been reflected in our updated Treasury Management Strategy and Treasury Management Policies and Practices included elsewhere on the agenda for approval.

HEAD OF FINANCIAL SERVICES
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