MONITORING OF TREASURY MANAGEMENT SERVICE AND ACTUAL PRUDENTIAL INDICATORS 2005/06

EXECUTIVE MEMBER: Councillor Elaine Woodburn

LEAD OFFICER: Sue Borwick

REPORT AUTHOR: Catherine Nicholson

Summary:

1. The attached reports covers the operation of the Council's prudential indicators for 2005/06 and its treasury function for the first six months of this financial year.

Recommendation: That Exec

1. Notes the report and approves the revised prudential indicators and limits.
2. Approves the transfer back in house of the funds currently held by an External Fund Manager – (Investec) so that they can be managed internally.

Impact on delivering Copeland 2020 objectives: Statutory requirement. Links directly to the budget process and funding of the capital programme

Impact on other statutory objectives (e.g. crime & disorder, LA21): As above

Financial and human resource implications: In order to maximise investment income due to the Council, it is believed that a better return could be achieved by managing the investments in-house, rather than using the current External Fund Manager.

Project & Risk Management: In order to maximise security of our funds, we work closely with our Treasury Advisers, Butlers, to ensure that a robust and up to date Counter Party List is adhered to when placing Council funds.

Key Decision Status

- **Financial:** No
- **Ward:** No

Other Ward Implications: None

BACKGROUND

1.1 The Prudential Code for Capital Finance in Local Authorities began on 1st April 2004 and introduced a greater freedom for the Council's capital expenditure. Part of the requirements of the Code is for reporting procedures to be implemented to monitor the progress and status of the capital expenditure plans. This report fulfils that requirement and shows the status of the Prudential Indicators as at 30th September 2006. The indicators were first reported to Full Council on 28th February 2006.

2. CAPITAL EXPENDITURE AND FINANCING OF THE EXPENDITURE

2.1 The table below shows the Prudential Indicator (PI) which highlights the actual 2005/06 capital expenditure position and the updated estimated capital programme for 2006/07 to 2008/09. The financing of the capital programme is also shown. Changes to the capital expenditure estimates relate to projects approved by Executive during the year.

	2005-06 Actual	**2006/07 Original**	**2006-07 Revised**	**2007-08 Revised**	**2008-09 Revised**
Capital Expenditure					
Total Expenditure	3,917307	3,066,000	3,066,000	2,276,000	2,276,000
Financed By:					
Capital Receipts	404,756	1,290,180	1,290,180	650,000	650,000
Capital Grants	2,085,705	1,776,000	1,776,000	1,476,000	1,476,000
Capital Reserves					
Revenue	617,846			150,000	150,000
Net Capital Requirement	**809,000**	**0**	**0**	**0**	**0**

3. THE COUNCIL'S BORROWING NEED (THE CAPITAL FINANCING REQUIREMENT)

3.1 The table below shows the Council's Capital Financing Requirement, which is the Council's underlying external indebtedness for a capital purpose. It flows directly from the capital expenditure plans above, and will also be adjusted for annual revenue charge for debt repayment (the Minimum Revenue Provision).

	2005-06 Actual	2006-07 Original	2006-07 Revised	2007-08 Revised	2008-09 Revised
Capital Financing Requirement – CFR					
Total CFR	0	0	0	0	0
Net Movement in CFR	-738,091	0	0	0	0
PI – External Debt					
Borrowing	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000
Other long term liabilities	0	0	0	0	0
Total Debt 31 March	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000

4. LIMITS TO BORROWING ACTIVITY

4.1 The first key control over the Council's activity is a Prudential Indicator to ensure that over the medium term, net borrowing will only be for a capital purpose. Net external borrowing should not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for 2006/07 and the following two financial years. This allows some flexibility for limited early borrowing for future years.

	2005-06 Actual	2006-07 Original	2006-07 Revised	2007-08 Revised	2008-09 Revised
Gross Borrowing	5,000,000	5,000,000	5,000,000	5,000,000	5,000,000
Investments	-18,376,000	-18,000,000	-18,000,000	-18,000,000	-18,000,000
Net Borrowing	-13,376,000	-13,000,000	-13,000,000	-13,000,000	-13,000,000
CFR	0	0	0	0	0

4.2 The Head of Finance and Business Development reports that the Council complied with this prudential indicator in 2005-06, and no difficulties are envisaged for the current or future years. This view takes into account current commitments, existing plans, and the proposals in the Budget Report.

4.3 A further two prudential indicators control or anticipate the overall level of borrowing. These are:

4.4 **The authorised limit –** This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

4.5 **The operational boundary –** This indicator is based on the probable external debt during the course of the year; it is not a limit and actual borrowing could vary around this boundary for short times during the year. CIPFA anticipate that this should act as an indicator to ensure the authorised limit is not breached.

Authorised limit for external debt	**2006-07 Original**	**2006-07 Revised**	**2007-08 Revised**	**2008-09 Revised**
Borrowing	5,000,000	5,000,000	5,000,000	5,000,000
Temp Rev and Capital estimate	3,500,000	3,300,000	3,300,000	3,300,000
TOTAL	**8,500,000**	**8,300,000**	**8,300,000**	**8,300,000**

Operational boundary for external debt	**2005-06 Revised**	**2006-07 Estimated**	**2007-08 Estimated**	**2008-09 Estimated**
Borrowing	5,000,000	5,000,000	5,000,000	5,000,000
Contingency	500,000	500,000	500,000	500,000
TOTAL	**5,500,000**	**5,500,000**	**5,500,000**	**5,500,000**

5. AFFORDABILITY PRUDENTIAL INDICATORS

5.1 The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans on the overall Council's finances.

5.2 **Actual and estimate of the ratio of financing costs to net revenue stream –** This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream. The estimates of financing cost include current commitments and the proposals from the budget report.

Ratio of Financing Costs to Net Revenue Stream	**2005-06 Actual**	**2006-07 Original**	**2006-07 Revised**	**2007-08 Revised**	**2008-09 Revised**
General Fund	-10%	-9%	-9%	-8%	-8%

5.3 **Estimates of the incremental impact of capital investment decisions on the Council Tax –** This indicator identifies the trend in the cost of proposed changes in the three year capital programme recommended in the budget report compared to the Council's existing approved commitments and current plans. They are required to be approved annually and will be reported to Full Council at the same time as the next Budget and Council Tax Setting Report.

6. TREASURY MANAGEMENT PRUDENTIAL INDICATORS

6.1 The first treasury indicator requires the adoption of the CIPFA Code of Practice on Treasury Management. This Council adopted that Code on 14th March 2002.

6.2 The Upper Limits on Variable Rate Exposure indicator is the maximum limit for variable interest rates based upon the debt position net of investments.

6.3 The Upper Limits on Fixed Rate Exposure is similar to the indicator above, but covers maximum limit on fixed interest rates.

	2005-06 Original	2006-07 Revised	2007-08 Revised	2008-09 Revised
Prudential indicator limits based on debt only				
Limits on fixed interest rates	£5,000,000	£5,000,000	£5,000,000	£5,000,000
Limits on variable rates	£0	£0	£0	£0

7. MATURITY STRUCTURES OF BORROWING

7.1 These gross limits are set to reduce the Council's expose to large fixed rate loans (those instruments which carry a fixed interest rate for the duration of the instrument) falling due for refinancing.

Maturity Structure of Fixed Borrowing	**2006/07 Revised Lower Limits**	**2006/07 Revised Upper Limits**
Under 12 Months	0%	50%
12 Months to 2 years	0%	0%
2 years to 5 years	0%	0%
5 years to 10 years	0%	0%
10 years and above	0%	100%

8. TREASURY MANAGEMENT IN 2006-07

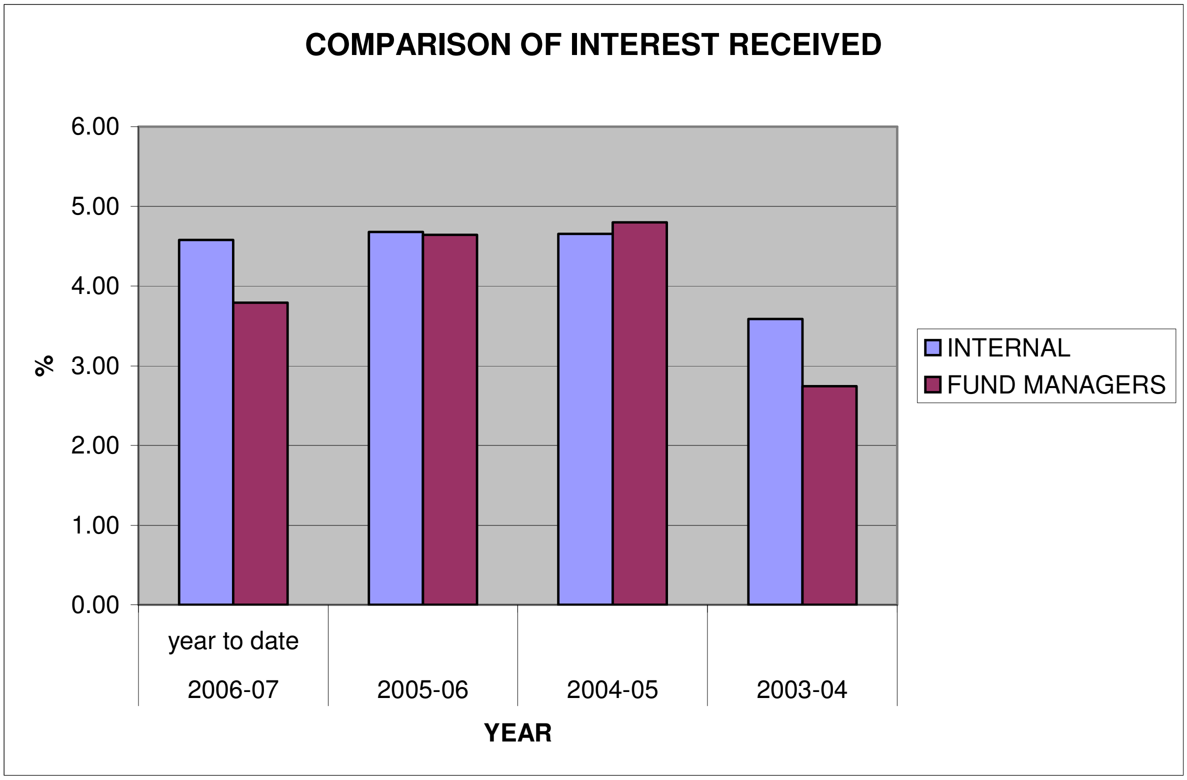
8.1 The Council still has the one remaining Market Loan in its debt portfolio, of £5 million. We continually assess the position of this loan with our Treasury Consultants, Butlers, to see whether we are securing the best terms for the Council. At the current time, the advice is to leave this loan in its present form.

8.2 Earlier in the financial year, a loan was repaid to the Council from Home Group, of approximately £2.2 million. Although this has increased the Council's cash balances, it has also left a shortfall in the interest the Council can receive. This is because the interest on the original loan was 11%, whereas market rates at the present time are approximately 4.5%.

8.3 However, during the year interest rates have risen by 0.5% above our budget estimates. This has meant that the actual interest we are receiving on our investments is over and above our estimates.

8.4 Back in 2000, Copeland decided to place £10 million with an External Fund Manager – Investec. This was because at the time it was believed that they would be able to generate a higher return on investments than could be achieved by in house staff, due to their size and experience on the financial markets.

8.5 However, performance of this fund over the last couple of years has been disappointing and our performance in house has consistently out performed the experts. (This has been the case with lots of external funds and not just the one we use.) The performance of both is pictured in the graph below.



8.6 Pressures on the budget for next year and beyond, now mean that we must strive to maximize the level of interest that we can earn and therefore we would recommend that the balance of monies with the Fund Manager is now recalled and we manage all the investments in-house. Appendix A details the levels of investments placed as at 30th September 2006.

8.7 We will continue to work closely with Butlers to ensure that our counter-party list (ie those financial institution/ organizations that we can place money with) is secure and enables us to secure the best return for the Council.

List of Appendices – Appendix A Investments

List of Background documents – Treasury Files

List of consultees: Corporate Team, Accountants, Leader