Financial Strategy Advisory Group

29 September 2023

ACTUAL TREASURY POSITION AND PRUDENTIAL INDICATORS 2022/23

1. Introduction

The Local Government Act 2003 introduced a new system of capital controls for Local Authorities. The key principle of the system of controls is that local authorities have the freedom to borrow for capital investment purposes providing that they can demonstrate that borrowing is affordable, sustainable and prudent.

The Act requires all local authorities to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code. The Code is a professional code that sets out a framework for self-regulation of capital spending. It sets out the approach that all authorities must take in undertaking integrated medium-term revenue and capital budget planning and a set of indicators that must be considered and/or approved in order to demonstrate that annual capital investment and treasury management decisions are affordable, sustainable and prudent.

Members' involvement through the process is essential in order that the Council can demonstrate that capital expenditure plans are affordable, external borrowing is prudent and sustainable and that treasury decisions are taken in accordance with good practice. The structure and content of the treasury management report complies with the requirements of the Code for 2022/23.

To facilitate the decision-making process and support capital investment decisions the Prudential Code requires the Council to agree and monitor a minimum number of prudential indicators. These indicators are mandatory but can be supplemented with local indicators if this aids interpretation and many will cover three years forward. The indicators cover affordability, prudence, capital expenditure, external debt and treasury management. These indicators will also form the basis of in year monitoring and reporting.

The indicators are purely for internal use by the Council and are not to be used as comparators between councils, as any comparisons will not take account of local factors and so will be meaningless. In addition, the indicators should not be taken individually; rather the benefit from monitoring will arise from following the movement in indicators over time and the year-on-year changes.

This appendix provides a commentary on each prudential indicator relevant to the Council and sets out the actual 2022/23 prudential indicators for approval as part of the Council's requirement to comply with the Prudential Code.

2. Affordability Prudential Indicator

Prudential indicators are required to assess the affordability of the capital investment plans. These indicators provide an indication of the impact of the capital investment plans on the overall Council finances.

Actual and Estimates of the Ratio of Financing Costs to Net Revenue Stream

This is an indicator of affordability and highlights the revenue implications of capital expenditure by identifying the proportion of the net revenue budget required to meet financing costs, net of investment income.

ACTUAL TREASURY POSITION AND PRUDENTIAL INDICATORS 2022/23

Ratio of Financing Costs to Net Revenue Streams	2021/22 Actual	2022/23 Estimated	2022/23 Actual
General Fund	9%	8%	7%

The ratios above reflect the net cost of borrowing after allowing for investment income. 2022/23's ratio is lower than 2021/22 principally because 2022/23's showed a significant increase on interests generated cash balances. In practice, the financing costs are fully funded by further income generated from both the Council's and Epsom & Ewell Property Investment Company's investment property acquisitions.

3. Capital Expenditure and the Capital Financing Requirement

The Prudential Code requires the calculation of the Council's Capital Financing Requirement (CFR). This figure represents the Council's underlying need to borrow for capital purposes. The year-on-year change is influenced by the capital expenditure incurred and how it is financed. The expected movement in the CFR over the next three years is dependent on the level of supported and unsupported capital expenditure decisions taken during the budgeting cycle.

The CFR forms one of the required prudential indicators. It includes the related capital expenditure and financing figures for each year, and the external debt for each year, which are mandatory prudential indicators.

In 2016/17 the Council agreed to borrow up to £80m to finance the acquisition of commercial properties within the Borough. In 2017/18, the Council agreed to borrow up to a further £300m to finance property investments through Epsom & Ewell Property Investment Company Limited. To date, the Council has acquired four investment properties for a combined £30m in-borough and two investment properties for a combined £60m out-of-Borough, all funded from borrowing. As a result, the CFR has increased substantially since 2015/16, when it had been nil.

Following statutory investment guidance in April 2018, Council agreed in February 2020 to cease any further out-of-Borough investment property acquisitions, where the main purpose is purely to profit, in order to meet the statutory guidance.

The Committee is asked to receive the actual CFR and actual debt figures set out below:

Financial Strategy Advisory Group

29 September 2023

ACTUAL TREASURY POSITION AND PRUDENTIAL INDICATORS 2022/23

Capital Financing Requirement	2021/22 Actual	2022/23 Estimated	2022/23 Actual
	£'000	£'000	£'000
Capital Expenditure:			
Capital programme expenditure	1,735	3,896	1,814
Assets acquired under finance leases	34	0	13
Total Capital Expenditure	**1,769**	**3,896**	**1,827**
Capital Financing:			
Capital receipts	229	973	270
Capital grants	455	1,579	616
Capital reserves	653	1,791	326
Revenue	398	434	602
Total Capital Financing	**1,735**	**4,777**	**1,814**
Minimum revenue provision	1,416	1,439	1,460
Capital Financing Requirement at 31 March	**88,985**	**88,865**	**87,551**
External Debt:			
External borrowing	64,427	64,427	64,427
Other short/long term liabilities	2,287	1,877	1,869
Total External Debt at 31 March	**66,714**	**66,304**	**66,296**
Internal borrowing	22,181	22,181	21,255
Capital Financing Requirement at 31 March	**88,895**	**88,485**	**87,551**

4. External Debt

A key control over the Council's activity is to ensure that over the medium-term net borrowing will only be for a capital purpose. The Council needs to ensure that net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of additional capital financing requirement for 2022/23 and next two financial years.

The following table sets out the actual levels of borrowing and investment for 2022/23:

	2021/22 Actual	2022/23 Estimated	2022/23 Actual
	£'000	£'000	£'000
Gross Borrowing at 31 March	66,714	66,344	66,296
Investments at 31 March	35,000	15,454	27,400
Net Borrowing at 31 March	31,714	50,890	38,896
Capital Financing Requirement	**88,895**	**88,485**	**87,551**

Financial Strategy Advisory Group

29 September 2023

ACTUAL TREASURY POSITION AND PRUDENTIAL INDICATORS 2022/23

The Head of Finance reports that the Council complied with the requirement to keep net borrowing below the CFR in 2022/23, and no difficulties are envisaged for the current or future years. This view takes into account current commitments and plans in the budget report.

A further two Prudential Indicators control the overall level of borrowing. These are:

The Authorised Limit

The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the absolute maximum amount of debt that the Council can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

The Operational Boundary

The operational boundary is based on the Council's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring.

The Committee is asked to receive the authorised and operational limits set out below:

External Debt Boundaries	2021/22 Actual	2022/23 Estimated	2022/23 Actual
	£'000	£'000	£'000
Authorised Limit for External Debt			
Borrowing for commercial properties	64,427	145,000	64,427
Other short/long term liabilities (finance leases)	2,287	3,000	1,869
Total Authorised Limit for External Debt	**66,714**	**148,000**	**66,296**
Operational Boundary for External Debt			
Borrowing for commercial properties	64,427	88,895	64,427
Other short/long term liabilities (finance leases)	2,287	1,877	1,869
Total Operational Boundary for External Debt	**66,714**	**90,772**	**66,296**

5. Treasury Management Indicators

The purpose of the treasury management prudential indicators is to contain the activity of the treasury function within certain limits, thereby reducing the risk or likelihood of an adverse movement in interest rates or borrowing decisions impacting negatively on the Council's overall financial position. However, if these are set to be too restrictive, they will impair the opportunities to reduce costs or maximise investment income.

Financial Strategy Advisory Group

29 September 2023

ACTUAL TREASURY POSITION AND PRUDENTIAL INDICATORS 2022/23

The treasury management service is an important part of the overall financial management of the Council's affairs. Its importance has increased as a result of the freedoms provided by the Prudential Code. It covers the borrowing and investment activities and the effective management of associated risks. Its activities are strictly regulated by statutory requirements and a professional code of practice, the CIPFA Code of Practice for Treasury Management in Local Authorities.

The Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice at its meeting in April 2012 and Council approved the latest treasury management strategy and procedures in February 2022.

The treasury management policy requires an annual strategy to be reported to Members outlining the expected treasury activity for the forthcoming year. A further report is produced after the year end to report on actual activity for the year.

The treasury management strategy identifies four prudential indicators in respect of treasury management:

Upper Limits on Fixed Rate Exposure

This indicator identifies a maximum limit for the Council's exposure to fixed interest rates for borrowing based upon the debt position net of investments.

Upper Limits on Variable Rate Exposure

This indicator identifies a maximum limit for the Council's exposure to variable interest rates for borrowing based upon the debt position net of investments. The Council has no plans to enter into any variable rate borrowing arrangements.

Maturity Structures of Borrowing

This indicator sets out the gross limits on borrowing which are set to limit the Council's exposure to large, fixed rate sums falling due for refinancing.

Total Principal Funds Invested for Periods Longer Than 364 Days

This indicator limits the amount of long-term investments which can be sold in each year, to reduce the need for early sale of an investment.

Financial Strategy Advisory Group

29 September 2023

ACTUAL TREASURY POSITION AND PRUDENTIAL INDICATORS 2022/23

Figures are for the financial year unless otherwise titled in italics	2021/22	2022/23	2022/23
	Actual	Estimated	Actual
	£'000	£'000	£'000
Capital Expenditure	1,769	3,896	1,827
Capital Financing Requirement (CFR) ***at 31 March***	88,895	87,456	87,551
Treasury Position at ***31 March***			
External borrowing	64,427	64,427	64,427
Other short/long term liabilities	2,287	1,877	1,869
Total Debt	**66,714**	**66,304**	**66,296**
Investments	35,000	15,454	27,400
Net Borrowing	**31,714**	**50,850**	**38,896**
Maximum Debt (Actual) compared to Authorised Limit (Original Indicator)	66,714	148,000	66,296
Average Debt compared to Operational Boundary (Original Indicator)	66,714	90,772	66,296
Ratio of financing costs to net revenue stream	9%	8%	7%
Upper limits on fixed interest rates ***(against maximum position)*** **as above**	66,714	67,828	66,296
Upper limits on variable interest rates ***(against maximum position)*** **as above**	0	0	0
Maturity structure fixed rate borrowing ***(%)***	**2021/22 Actual**	**2022/23 Estimated**	**2022/23 Actual**
Under 12 months	0%	0%	0%
12 months to 2 years	0%	0%	0%
2 years to 5 years	0%	0%	0%
5 years to 10 years	8%	8%	8%
10 years and above	92%	92%	92%
Maximum principal funds invested over 364 days ***(against maximum position)***	0	£10m	0