GREATER MANCHESTER FIRE & RESCUE AUTHORITY

POLICY, RESOURCES AND PERFORMANCE MEETING: 2 FEBRUARY 2012

AUTHORITY: 16 FEBRUARY 2012

Subject: CAPITAL PROGRAMME 2012/13 to 2014/15 – PRUDENTIAL INDICATORS and MINIMUM REVENUE PROVISION (MRP) STATEMENT 2012/13

Report of Treasurer in consultation with the County Fire Officer and Chief Executive

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THE PRUDENTIAL CODE

1. Since April 2004 fire authorities have had the power to borrow to fund capital schemes without central government approval, but prior to doing so, we are required to determine whether or not it is prudent to do so. The mechanism for this is to look at a series of indicators known as prudential indicators intended to measure the extent of our debts and our ability to pay them back. We set these out at the time of setting the revenue budget and capital programme whether or not we are actually planning to use these powers to borrow.

2. The purpose of this report is to set out the requirements to determine prudential indicators for the forthcoming financial year 2012/13. The main requirements are as follows:

    - To determine estimates of capital expenditure for the forthcoming year and the two years thereafter. (See Table 1)
    - To determine the capital finance requirement (mainly, the amount of capital expenditure to be financed by borrowing) for each of these years. (See Table 4)
    - To estimate the ratio of capital financing costs to net revenue streams and the impact on precepts. (See Tables 5 and 6)
    - To set an operational boundary for external debt for the forthcoming year and the two years thereafter. (See Table 7)
    - To set an authorised limit for external debt for the forthcoming year and the two years thereafter. (See Table 8)
    - To set prudential indicators in respect of Treasury Management. (See Tables 9 and 10)

3. In setting prudential indicators, the Authority is required to have regard to the following:

    - Service Objectives, e.g. strategic planning for the Authority
    - Stewardship of assets, e.g. asset management planning
    - Value for money, e.g. option appraisal
    - Prudence and sustainability, e.g. implications for external borrowing
    - Affordability, e.g. implications for precepts.
    - Practicality, e.g. achievability of the forward plan

4. The contents of this report are consistent with the revenue budget report for 2012/13 to 2014/15.

Determination of estimates of capital expenditure 2012/13 to 2014/15

5. Table 1 & 1a set out the overall estimated level of capital expenditure and the revisions from the previously approved programme. It should be noted that these estimates and the underlying programme have been set for the purposes of producing prudential indicators.

6. The estimates are derived from the current approved capital programme with certain annual projects e.g. Station rebuilds and vehicle replacements, being continued into the later years of the overall programme. The indicative capital programme also includes the addition of a number of building work schemes, which are consistent with the approved Authority Asset Management Plan. A detailed analysis of the proposed capital programme is attached to the Budget Estimates report elsewhere on the agenda.

Table 1. (Revisions to Programme approved November 2011)

	2011/12	**2012/13**	**2013/14**	**2014/15**
	£m	**£m**	**£m**	**£m**
Approved Programme November 2011	**8.166**	**5.483**	**6.205**	**6.025**
Bury Fire Station build	-0.100	0.100		
Day Crewing Plus	-0.400	-1.000	-0.400	
Minor works	-0.040			
Blackley refurbishment	-0.020			
Asset Strategy Group	0.074	0.250	0.250	
ICU IT	-0.175	0.175		
MIC Vehicles	-0.050			
P&P Community Engagement equipment	0.056			
Training schemes	-0.600	0.600	1.000	
IT			0.150	
Sustainability	-0.125	0.125	0.250	
Community Safety Vehicles	-0.065	0.065		
Diversity	-0.045	0.045		
Programme now submitted	**6.676**	**5.843**	**7.455**	**6.025**

Table 1a Summary Capital Programme 2011/12 to 2014/15

	2011/12 **£m**	**2012/13** **£m**	**2013/14** **£m**	**2014/15** **£m**
Premises related	4.210	3.658	3.080	3.450
Operational Training related	0.691	0.600	1.000	0
IT related	0.925	0.370	0.150	0.150
Vehicles and Equipment	0.850	1.215	3.225	2.425
Total	**6.676**	**5.843**	**7.455**	**6.025**

7. The Prudential Code recognises that, in making its capital investment decisions, the Authority must have explicit regard to option appraisal, asset management planning, strategic planning and achievability of the forward plan.

Determination of the capital financing requirement

8. The Prudential Code requires that estimates of the capital financing requirement should be produced – the balance between use of capital receipts, borrowing and revenue resources.

9. The starting point for these calculations is the aggregation of certain figures in the latest balance sheet, in this case 31 March 2011. This figure is then affected each year in the following way:

   - It increases as capital expenditure is incurred.
   - It is reduced to the extent that expenditure is financed by government grants, capital receipts, direct revenue funding and use of external contributions.
   - It is reduced by the statutory charge to revenue (Minimum Revenue Provision) and by any additional voluntary charge to revenue.

10. An assessment has been made of the financing sources that will fund the capital expenditure estimates. In making this assessment the following assumptions have been made:

   - The supported borrowing allocation given by Central Government has ceased from 2012/13, therefore there will be no funds available from this source.

   - Unsupported borrowing may be required pending the outcome of discussions with CLG on the future of capital grants for the Authority. For 2012/13 CLG have indicated that Capital Grants will be allocated on the same basis as 2011/12, therefore it is anticipated that £2.881m will be received in 2012/13. In future years, CLG have indicated that there may be a bidding round for Capital Grants. No Capital Grants have been included within the programme for future years. Assuming the grant is not available then prudential borrowing of £0.999m for 2013/14 and £6.025m for 2014/15 will need to be considered.

   - Capital Grant allocations as notified by Central Government.

   - Capital receipts from agreed disposals and anticipated disposals from the release of future surplus sites have been estimated.

   - The Capital Fund will provide (and will be sufficient to provide) the balance of funding for the years 2011/12 and 2012/13, and a significant contribution to capital expenditure in 2013/14.

Table 2 summarises the estimated funding sources for the capital programme.

Table 2. (Resourcing the capital programme)

	2011/12	2012/13	2013/14	2014/15
	£'m	£'m	£'m	£'m
Total spending requiring funding	**6.676**	**5.843**	**7.455**	**6.025**
Borrowing – supported	1.365	0		
Capital Grant Allocations	2.881	2.926		
Borrowing – unsupported	0	0	0.999	6.025
Capital receipts	0	1.260		
Direct Revenue Financing	0.331	1.600		
Capital Fund	2.099	0.057	6.456	
Total resources used in funding	**6.676**	**5.843**	**7.455**	**6.025**

11. The adequacy of the Capital Fund to meet this programme funding requirement is demonstrated in the following table, showing the impact of demand on the fund in the years 2011/12 to 2014/15.

Table 3. (Capital Fund balances)

	2011/12	2012/13	2013/14	2014/15
	£'m	£'m	£'m	£'m
Balance at start of year	7.612	6.513	6.456	0
Transfers to Fund	1.000	0	0	0
Demand on fund from capital programme	-2.099	-0.057	-6.456	0
Balance at end of year	6.513	6.456	0	0

12. As a consequence of this spending programme and its funding, the capital financing requirement is estimated to change as follows over the period of this review.

Table 4. (The estimated capital financing requirement)

	Total capital financing requirement
	£'m
Estimated at 31 March 2012	45.304
Change in 2012/13	-2.707
Estimated at 31 March 2013	42.597
Change in 2013/14	-1.654
Estimated at 31 March 2014	40.943
Change in 2014/15	3.480
Estimated at 31 March 2015	44.423

Estimating the ratios of capital financing costs to net revenue streams and the impact on precepts.

13. The Authority is required to calculate for 2012/13, 2013/14 and 2014/15 the relationship between financing costs and the net revenue stream.

    Financing costs refer mainly to:
    - Interest payable on external borrowing and other long-term liabilities.
    - The Minimum Revenue provision and any voluntary contributions.
    - Investment income.

    Net revenue stream refers to:
    - The amount in the Income and Expenditure Account to be met from Government grants and local taxpayers. Assumed in this report to equate to the budget requirement.

    Table 5 below sets out the calculations:

Table 5. (Ratio of capital financing costs to revenue streams)

	2012/13	2013/14	2014/15
Estimated financing costs (£'m)	3.879	3.879	3.879
Estimated net revenue stream (£'m)	108.345	103.790	101.854
Ratio of financing costs to net revenue (%)	3.58	3.74	3.81

14. In addition, the Authority is required to show the incremental impact of capital investment decisions on the precept. For the purposes of this report the incremental impact has been calculated as the financial consequences of any unsupported borrowing together with any revenue consequences other than financing costs associated with the overall programme.

15. A potential provision for unsupported borrowing has been identified in 2013/14 and 2014/15. Any additional costs of borrowing are at this stage anticipated to be funded from within existing resources.

Table 6. (Impact on precepts)

		2012/13	2013/14	2014/15
Estimated budget requirement with capital programme at estimated levels, assumes any additional borrowing costs are met from within existing resources. (£ 'm)	A	108.345	103.790	101.854
Estimated budget requirement with capital programme estimates excluding unsupported borrowing. (£'m)	B	108.345	103.770	101.610
Non financing costs arising from capital programme included in "A" (£'m)	C	0	0	0
Effect on budget requirement of removing unsupported borrowing and other revenue costs (£'m)	(A-B) +C	0	0.020	0.244
Year on year effect on precept (£.p) *		0.00	0.02	0.30

* this impact is indicative as any additional borrowing will be funded from within existing resources.

Setting the Authorised Limit and Operational Boundary for external debt

16. The Authority is required to set these two limits to its external debt. External debt refers to borrowing and other long-term liabilities.

17. Both the authorised limit and operational boundary need to be consistent with the Authority's plans for capital expenditure and financing and with its Treasury Management policy statement and practices.

18. The operational boundary is to directly link into the Authority's plans for capital expenditure, the estimates of the capital financing requirement and the estimate of the cash flow requirements for all other purposes, including revenue.

19. The operational boundary represents the likely level of external debt that may be reached during the course of the year, it is not a limit.

20. The figures for the authorised and operational limit are calculated using the existing levels of debt and estimating those factors that could impact on this such as new external borrowing and the application of the Authority's own resources to support the capital programme.

21. Table 7 sets out the calculation of the operational boundary for the years 2012/13 to 2014/15.

Table 7. The Operational Boundary

	2011/12	2012/13	2013/14	2014/15
	£'m	£'m	£'m	£'m
Amounts outstanding 1 April 2011	**8.998**			
Previous year operational boundary	0	8.788	7.738	12.540
Additional borrowing	0	0	0.999	6.025
Maturing loans	-2.298	-2.000	0	-4.000
Replacement loans	0	2.000	0	4.000
Use of Capital Fund for capital programme	2.099	0.057	6.456	0
Revenue Contribution	1.331	1.600	0	0
Supported Borrowing	1.365	0	0	0
Revenue set aside (Statutory MRP)	-1.500	-1.514	-1.460	-1.352
Revenue set aside (Voluntary addition)	-1.207	-1.193	-1.193	-1.193
Estimated operational boundary 31 March	**8.788**	**7.738**	**12.540**	**16.020**

22. The calculation of the Authorised Limit should provide headroom over and above the operational boundary to allow for unusual cash movements. It is therefore recommended that the Authorised Limit allows for a 5% variation (rounded up to the nearest £0.5m) on the operational boundary to allow for such headroom. On this basis the Authorised Limit would be as shown in Table 8.

Table 8. The Authorised Limit

	Borrowing
	£'m
For 2012/13	8.5
For 2013/14	13.5
For 2014/15	17.0

Treasury Management Prudential Indicators

23. The Authority determines a Treasury Management Policy Statement (i.e. how we manage our borrowing and cash investments) prior to the start of the financial year and this will continue to be done. Under the prudential code, there are certain aspects of this policy that need to be determined now and which are the subject of this report.

    These indicators are in respect of:

    - The Treasury Management Code of Practice.
    - Interest rate exposures.
    - The maturity structure of borrowing.
    - The total principal sums invested for periods longer than 364 days.

Code of Practice

24. It is confirmed that the Authority has adopted the CIPFA Code of Practice for Treasury Management in the Public Services.

Interest rate exposures

25. The Authority is required to set upper limits to its exposures to the effects of changes in interest rates for both fixed interest rate and variable rate loans.

26. It has been Authority policy to borrow at fixed rates of interest and it is recommended that this will continue. Table 9 sets out the calculation of the upper limits for fixed rate and variable rate loans for the period in question.

Table 9. (Calculation of upper and lower limits for fixed and variable rate loans)

	2012/13	2013/14	2014/15
	£'m	£'m	£'m
Fixed rate exposure			
Estimated fixed rate borrowing (at operational boundary)	7.738	12.540	16.020
Less :- value of investments held at fixed rates	0	0	0
Upper limit on fixed rate exposure	7.738	12.540	16.020
Variable rate exposure			
Estimated variable rate borrowing	0	0	0
Less :- value of investments held at variable rates	0	0	0
Upper limit on variable rate exposure	0	0	0

The maturity structure of borrowing

27. The Authority is required to set for the forthcoming year only both upper and lower limits with respect to the maturity structure of its projected fixed rate borrowing. The limits are to be expressed as percentages of total projected borrowing. The recommended limits are shown in Table 10.

Table 10. (Maturity structure of projected borrowing)

	Upper limit	**Lower limit**
	%	**%**
Under 12 months	0	0
12 months and within 24 months	0	0
24 months and within 5 years	50	0
5 years and within 10 years	50	0
10 years and above	100	50

28. The maturity profile that is actually chosen for new borrowing would depend on prevailing market conditions, the acceptance of the above limits will give reasonable flexibility in that it would allow:

- All new borrowing (but no less than 50%) to be taken out for 10 years or more.
- Up to 50% of new borrowing to be taken out for periods of 2 to 10 years.
- No borrowing for less than 2 years.

The total principal sums invested for periods longer than 364 days.

29. The Authority is required to set a prudential limit on sums invested for periods longer than 364 days. It is not envisaged that there would be any investments held for more than 364 days.

30. The Authority is requested to approve the various recommendations and limits set out in the report as follows:

- Setting the Authorised Limit and the Operational Boundary, as shown in Tables 7 and 8 of the report.

- Treasury Management Prudential Indicators, as shown in Tables 9 and 10.

<u>Minimum Revenue Provision (MRP) Statement 2012/13</u>

31. The Authority must adopt a formal policy on MRP - basically the amount we set aside to repay loans. The Authority has a duty to make a prudent MRP in the financial year.

32. As Members will be aware the Authority is required to comply with the accounting standards contained within the Accounting Code of Practices as published by CIPFA. There are a number of Policy options available for calculating the MRP and these are discussed in more detail below.

33. The following statement of policy covers the 2012/13 financial year. It is consistent with the decisions taken in the budget.

What is considered Prudent provision?

34. Provision for the repayment of debt is considered to be prudent where the period of repayment is either reasonably commensurate with that over which the capital expenditure to which it relates provides benefits, or in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

Options Available

35. Under the regulations there are four options for calculating MRP these are set out as follows:-

Regulatory Method

36. MRP is equal to the amount determined in accordance with the former regulations 28 and 29 of the 2003 Regulations, as if they had not been revoked by the 2008 Regulations. The MRP element of the RSG (Revenue Support Grant) is calculated on this basis. This was 4% of the outstanding debt.

Capital Financing Requirement (CFR) Method

37. The Capital Financing Requirement (CFR) is calculated from the Authority's Balance Sheet (rather than the outstanding debt) and represents the amount of deemed borrowing needed to fund its assets. MRP is equal to 4% of the non-housing CFR at the end of the preceding financial year.

    This is the method currently adopted by the Authority.

Asset Life Method

38. Where capital expenditure on an asset is financed wholly or partly by borrowing or credit arrangements, MRP is to be determined by reference to the life of the asset. There are two main methods by which this can be achieved, as described below.

39. Under both variations, authorities may in any year make additional voluntary revenue provision, in which case they may make an appropriate reduction in later years' levels of MRP.

    (a) Equal instalment method

    MRP is the amount given by the following formula:

$$\frac{A - B}{C}$$

    where-

    A is the amount of the capital expenditure in respect of the asset financed by borrowing or credit arrangements

B is the total provision made before the current financial year in respect of that expenditure

C is the inclusive number of financial years from the current year to that in which the estimated life of the asset expires.

(b) Annuity method

40. MRP is the principal element for the year of the annuity required to repay, over the asset life, the amount of capital expenditure financed by borrowing or credit arrangements. The Authority should use an appropriate interest rate to calculate the amount. Adjustments to the calculation to take account of repayment by other methods during the repayment period (e.g. by the application of capital receipts) should be made as necessary.

41. MRP should normally commence in the financial year following the one in which the expenditure was incurred. The estimated life of the asset should be determined in the year that MRP commences and not subsequently be revised.

42. If no life can reasonably be attributed to an asset, such as freehold land, the life should be taken to be a maximum of 50 years. However, in the case of freehold land on which a building or other structure is constructed, the life of the land may be treated as equal to that of the structure, where this would exceed 50 years.

43. When borrowing to provide an asset, the Authority may treat the asset life as commencing in the year in which the asset first becomes operational. It may postpone beginning to make MRP until the financial year following the one in which the asset becomes operational. “Operational” here has its standard accounting definition. Investment properties should be regarded as becoming operational when they begin to generate revenues.

44. The Authority has adopted the Accounting Standards which require them to calculate the MRP on PFI assets based upon the Asset Life Annuity Method.

Depreciation Method

45. MRP is to be equal to the provision required in accordance with depreciation accounting in respect of the asset on which expenditure has been financed by borrowing or credit arrangements. This should include any amount for impairment chargeable to the Income and Expenditure Account.

46. For this purpose standard depreciation accounting procedures should be followed, except in the following respects.

47. MRP should continue to be made annually until the cumulative amount of such provision is equal to the expenditure originally financed by borrowing or credit arrangements. Thereafter the Authority may cease to make MRP.

48. On disposal of the asset, the charge should continue in accordance with the depreciation schedule as if the disposal had not taken place. But this does not affect the ability to apply capital receipts or other funding sources at any time to repay all or part of the outstanding debt.

49. Where the percentage of the expenditure on the asset financed by borrowing or credit arrangements is less than 100%, MRP should be equal to the same percentage of the provision required under depreciation accounting.

50. This method is currently employed by the Authority to calculate repayment of debt for supported borrowing on the purchase of short life assets such as vehicles and equipment.

Policy Statement for 2012/13

51. It is proposed to continue with the Capital Financing Requirement method for calculating MRP for supported borrowing for all the Authority assets except for:

- vehicles and equipment where the depreciation method of calculating the repayment provision shall be employed.

- PFI assets where the asset life annuity model is employed.

52. The Authority currently has no unsupported borrowing. The Treasurer has the discretion to make additional voluntary provision for debt repayment.

RECOMMENDATIONS

Prudential Indicators and Treasury Policy

53. The various prudential indicator requirements contained within this report are summarised explicitly within this section.

54. The Committee is recommended to set the following prudential indicators and treasury management objectives as set out in the table below: -

Table 11. (Summary of Prudential Indicators)

	Indicator	**2012/13**	**2013/14**	**2014/15**
	Capital Spending			
1.	Estimated capital expenditure (£m)	5.843	7.455	6.025
2.	Estimated capital financing requirement (£m)	42.597	40.943	44.423
	Capital Financing Ratios			
3.	Estimated ratios of capital financing costs to net revenue streams (%)	3.58	3.74	3.81
	Impact on Revenue			
4.	Incremental impact of Capital Expenditure Decisions on Precept (£.p)	0.00	0.02	0.30
	Treasury Management			
5.	Operational Boundary (£m)	7.738	12.540	16.020
6.	Authorised Limit (£m)	8.500	13.500	17.000
7.	Fixed Rate Exposure Limit (£m)	7.738	12.540	16.020
8.	Variable Rate Exposure Limit (£m)	Nil	Nil	Nil
9.	The Authority will continue with its policy to borrow only at fixed rates of interest			
10	The Authority determines the following maturity structure for new borrowing in 2012/13 :-			
		Upper limit	Lower limit	
		%	%	
	Under 12 months	0	0	
	12 months and within 24 months	0	0	
	24 months and within 5 years	50	0	
	5 years and within 10 years	50	0	
	10 years and above	100	50	
11	The Authority will not invest for periods of longer than 364 days			

Minimum Revenue Provision Statement 2012/13

55. The Committee is asked to recommend to the Authority that the above Statement on MRP is adopted for 2012/13.

Paul McKevitt
Treasurer

Steve McGuirk
County Fire Officer & Chief Executive

LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972

Document	Date	File or Other Ref.	Place of Inspection
CIPFA Code of Practice		www.cipfa.org.uk	

Paul McKevitt
Treasurer

Resources Directorate
WIGAN

FP/JC /Prudential Indicators Report
24 January 2012
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