Shropshire and Wrekin Fire and Rescue Authority
Strategy and Resources Committee
1 February 2018

Capital Programmes 2018/19 to 2022/23 and Prudential Guidelines

Report of the Treasurer

For further information about this report please contact James Walton, Treasurer, on 01743 258915, or Joanne Coadey, Head of Finance, on 01743 260215.

1 Purpose of Report

This report presents the capital programmes for 2018/19 to 2022/23, for consideration by the Committee in the context of Prudential Guidelines.

2 Recommendations

The Committee is asked to recommend that the Fire Authority:

a) Confirm the 2018/19 onward programmes, set out in Appendix A (exempt paper 14), and the associated revenue costs, as part of its final precept deliberations;
b) Approve the Prudential Indicators and the Treasury Strategy for 2018/19;
c) Approve the Minimum Revenue Provision 2018/19; and
d) Note the review of the Treasury Management Practices and Main Principles for 2018/19.

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 The Capital Programme

The Capital Programme for 2018/19 and later years has been reviewed by officers, and the schemes that require approval are shown at Appendix A. The schedule also provides some background to the proposed schemes, some of which require reviews before any expenditure is undertaken, and others, which are replacement items. Further information on the schemes proposed for 2018/19 is available from officers.

As members will be aware, costs and timescales associated with the major development programme at Telford have not yet been confirmed. In order to make provision for the scheme in future years of the programme, an indicative scheme was included in previous programmes.

All of the proposed schemes in 2018/19 are to be funded from revenue, and therefore there are no revenue consequences to consider. However some borrowing will be required for the Telford scheme and those other schemes due to start from 2019/20

The revenue costs associated with the Capital Programme in later years will be added to the final revenue package presented to the Fire Authority later in the month.

The Fire Authority agreed in October 2014 that future savings would be contributed to the unearmarked Capital Reserve, to fund development of the Stafford Park site.

5 Treasury Management Strategy Statement

Background

The Authority is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties commensurate with the Authority's low risk appetite, providing adequate liquidity initially before considering investment return.

The second main function of the treasury management service is the funding of the Authority's capital plans. These capital plans provide a guide to the borrowing need of the Authority, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans, or using longer-term cash flow surpluses.

CIPFA defines treasury management as:

"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

Reporting requirements
The Authority is currently required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

Prudential and treasury indicators and treasury strategy (this report) - The first, and most important report covers:
- the capital programme (including prudential indicators);
- a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

A mid-year treasury management report – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision. In addition, the Authority will receive quarterly update reports.

An annual treasury report – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Scrutiny
The above reports are required to be adequately scrutinised before being recommended to the Authority. This role is undertaken by the Strategy & Resources Committee.

Capital Strategy
In December 2017, CIPFA issued revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities will be required to prepare an additional report, a Capital Strategy report, which is intended to provide the following:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

The aim of this report is to ensure that the Authority members fully understand the overall strategy, governance procedures and risk appetite entailed by this Strategy.

The Capital Strategy will include capital expenditure, investments and liabilities and treasury management in sufficient detail to allow all members to understand how stewardship, value for money, prudence, sustainability and affordability will be secured.

Treasury Management Strategy for 2018/19
The Treasury Management Strategy for 2018/19 covers two main areas:

Capital issues

- the capital plans and the prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury management issues

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Authority;
- prospects for interest rates;
- the borrowing strategy;
- the investment strategy; and
- creditworthiness policy

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, MHCLG MRP Guidance, the CIPFA Treasury Management Code and MHCLG Investment Guidance.

Training
The CIPFA Code requires that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. A training session is being planned by Treasury Management officers at Shropshire Council, and relevant members and officers will be invited.

Treasury Management Consultants
The Fire Authority employs Shropshire Council to manage its treasury functions, who in turn have appointed Link Asset Services Treasury Solutions as their independent advisor. It is recognised that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources.

6 Prudential Guidelines

Capital Prudential Indicators
The Authority's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

Capital expenditure
This prudential indicator is a summary of the Authority's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle

	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/23 Estimate £000
Capital expenditure	1,376	4,381	745	1,837	2,000	800

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Capital reserves	745	707	0	0
Net financing for the year	0	1,130	2,000	800

The indicators below demonstrate the affordability of the capital programmes proposed by the Authority, by showing the impact of the programmes on its overall finances.

	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Ratio of financing costs to net revenue stream	2.79%	3.04%	3.53%	3.93%
Impact of capital investment decisions on Band D council tax	43p	87p	£1.63p	£2.36p

The Authority's borrowing need (the Capital Financing Requirement)
The Capital Financing Requirement (CFR) is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each assets life, and so charges the economic consumption of capital assets as they are used.

	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Capital Financing Requirement	3,888	3,617	8,063	8,892	10,530

Borrowing
The Authority must ensure that sufficient cash is available to meet its service activity. Treasury management officers at Shropshire Council manage the Authority's cash, which includes the Authority's capital strategy. This will involve both the monitoring of cash flow and, where capital plans require, the organisation of appropriate borrowing facilities.

	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
External Debt	5,698	5,698	7,395	8,223	9,742

Treasury Indicators: limits to borrowing activity

The operational boundary
This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Operational Boundary	5,698	7,395	8,223	9,742

The authorised limit for external debt

A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the Authority. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Authorised Limit	6,617	11,063	11,892	13,530

7 Treasury Strategy 2018/19

Economic Background

The Monetary Policy Committee (MPC) delivered a 0.25% increase in Bank Rate at its November meeting, also giving forward guidance that that they expected to increase Bank Rate only twice more by 0.25% by 2020 to end at 1%.

Public Works Loan Board (PWLB) rates are likely to rise gently, although forecasting remains difficult with so many external influences currently weighing on the United Kingdom.

Borrowing Strategy

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

In terms of PWLB rates, the overall trend in the longer term will be for rates to rise slowly, when economic recovery is firmly established, accompanied by rising inflation and a steady Bank Rate.

The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring even higher borrowing costs.

There will remain a cost to any new borrowing, which causes an increase in investments, as this will incur a revenue loss between borrowing costs and investment returns.

External versus Internal Borrowing

The Fire Authority's approach to borrowing has continued to be the use of cash surpluses and reserves to finance new capital expenditure, so as to run down cash balances and minimise counterparty risk incurred on investments. However some borrowing will be necessary during the planning period.

Investment Strategy

The Fire Authority's investment policy will have regard to Communities and Local Government (CLG) Guidance on Local Government Investments (the Guidance) and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral 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 will not be undertaken.

This is the initial strategy for 2018/19, and will only be revised by 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 the 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 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.

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.

The Authority will not invest any funds with a counterparty for more than 365 days.

8 Minimum Revenue Provision 2018/19

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 these regulations, an authority is required to set aside an amount of MRP, which it considers prudent. Interpretation within the guidance states:

"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 2018/19, 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 policy set out below 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. This method will be continued into the coming year.

10 Treasury Management Policy

The Treasurer has responsibility for Treasury Management, and as such carries out operations in accordance with the Authority's Treasury Strategy, above. This responsibility includes the preparation of the Treasury Management Practices, and the schedules specifying the systems and routines to be employed.

The main principles of the Treasury Management Practices were reviewed by officers and approved in February 2016. The principles have been reviewed this year by officers, when no amendments were necessary. However a further review will be carried out in line with the new Prudential Code and Capital Strategy. They will continue to be reviewed and presented to the Fire Authority on an annual basis.

11 Financial Implications

Financial implications are as set out within this report.

12 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”.

13 Initial Impact Assessment

An Initial Impact Assessment form has been completed.

14 Equality Impact Assessment

Officers have considered the Service’s Brigade Order on Equality Impact Assessments (Human Resources 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 is not, therefore, required.

15 Appendices

Exempt Paper 14
Appendix A
Capital Programmes 2017/18 to 2021/22 and Prudential Guidelines

Appendix B
Debt Charges for Capital Programmes 2017/18 to 2021/22

16 Background Papers

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