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## Report of the DIRECTOR OF CORPORATE SERVICES

### Executive Board

Date: 18<sup>TH</sup> OCTOBER 2006

### Subject: TREASURY MANAGEMENT BORROWING LIMITS

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**Electoral Wards Affected:**

**Specific Implications For:**

Equality and Diversity

Community Cohesion

Narrowing the Gap

Eligible for Call In

no

Not Eligible for Call In

(Details contained in the report)

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## EXECUTIVE SUMMARY

1. This report seeks to increase the Authorised and Operational borrowing limits which were set by Council in February 2006.
2. In accordance with the Local Government Act 2003, the Council is required to set borrowing limits for external debt having regard to CIPFA's prudential code.
3. The treasury operations so far this year indicate that the limits set in February 2006 may not be sufficient to enable flexibility in timing of debt rescheduling and the report recommends increasing the Authorised limit for 2006/07 to £1,590m and the Operational Boundary for 2006/07 to £1,490m.
4. Since the Council is able to borrow in advance for future years there needs to be sufficient flexibility to enable sums borrowed to be invested until they are required. Currently the limit set for investments for periods longer than 364 days is £100m. This report recommends increasing this limit to £150m.

## **1.0 Purpose Of This Report**

- 1.1 The treasury operations so far this year indicate that the borrowing limits set in February 2006 may not be sufficient to enable flexibility in timing of debt rescheduling. This report seeks approval to increase the Authorised borrowing limit and Operational boundary for 2006/07.

## **2.0 Background Information**

- 2.1 Under the Local Government Act 2003, the authorised limit represents the legislative limit on the Council's external debt. It should be set with sufficient headroom above the operational boundary to allow flexibility for planned borrowing to be undertaken, in order for prudent treasury management decisions to be taken and temporary cashflow fluctuations to be managed.
- 2.2 The operational boundary should reflect the maximum anticipated level of external debt consistent with budgets and cashflow forecasts. It should be seen as a management tool for ongoing monitoring of external debt, and may be breached temporarily due to unusual cashflow movements. However, a sustained or regular trend above the operational boundary should trigger a review of both it and the authorised limit.
- 2.3 The Treasury Policy and Strategy Statement for 2006/2007 was approved by full Council on 28th February 2006 and set the authorised limit and operational boundary for external debt. Both of these boundaries are made up of two elements, covering borrowing and other long term liabilities. The Director of Corporate Services has authority to make adjustments between the two elements provided that the overall limits remain unchanged. This report seeks approval to increase the Authorised borrowing limit and Operational boundary for 2006/07. The limits for 2007/08 and 2008/09 will be reviewed when the treasury strategy for 2007/08 is presented to the Executive Board in February 2007.

## **3.0 Main Issues**

- 3.1 The Authorised limit and Operational boundary were set in February 2006 and were set at a level to enable the Council to borrow in advance for 2007/08 and 2008/09, should rates prove to be advantageous. Table 1 below sets out the revised forecast total external borrowing requirement for 2006/07 to 2008/09.
- 3.2 The need for the increased limits has arisen through a change in the amount of borrowing needed to fund the capital programme and also to provide sufficient flexibility to borrow in advance on debt rescheduling opportunities.
- 3.3 Since the limits were set in February 2006 there has been an increase in the amount of borrowing needed to fund both the Housing Revenue Account and General Fund capital programmes. In particular the ALMOs were successful in securing additional borrowing support for the decency programme. Also, some capital resources assumed to fund the General Fund capital programme are now less likely to be achieved and therefore additional borrowing may be required. A capital programme update position and a Treasury Strategy update will be presented to Executive Board in November 2006.

**Table 1 – Total External Borrowing Requirement**

<b>ANALYSIS OF BORROWING 2006/07-2008/09</b>	<b>2006/07</b>	<b>2007/08</b>	<b>2008/09</b>
	<b>This report</b>		
	<b>£m</b>	<b>£m</b>	<b>£m</b>
<b>External Borrowing at 1 April</b>	1,054	1,270	1,400
New Borrowing for the Capital Programme - HRA	119	111	35
New Borrowing for the Capital Programme – Non HRA	121	47	28
Debt redemption costs charged to Revenue (Incl HRA)	( 21)	(25)	(26)
Reduced/(Increased) level of Revenue Balances	( 3 )	(3)	(3)
<b>External Borrowing at 31 March</b>	<b>1,270</b>	<b>1,400</b>	<b>1,434</b>

- 3.4 The Council is active in looking for opportunities to prematurely repay loans and replace them at more advantageous rates to reduce interest costs and generate one off savings. To enable this to be done effectively the authorised limit needs to include sufficient flexibility to allow re-financing of loans to take place before loans are repaid, should rates be advantageous and market conditions allow. Currently the limits include a small allowance for this which is proving to be insufficient.
- 3.5 The operational boundary should reflect the maximum level of external debt consistent with budgets and cashflow forecasts. As some borrowing has already been done in advance to fund the 2007/08 capital programme, this must now be reflected in the operational boundary together with any future advance borrowing that is likely.
- 3.6 The proposed borrowing limits for 2006/07 are set out below:

	<b>2006/07 February 2006 £m</b>	<b>2006/07 This Report £m</b>
<b>Authorised Limits</b>		
Borrowing	1,410	1,550
Other Long Term Liabilities	40	40
<b>Total</b>	<b>1,450</b>	<b>1,590</b>
<b>Operational Boundary</b>		
Borrowing	1,260	1,460
Other Long Term Liabilities	30	30
<b>Total</b>	<b>1,290</b>	<b>1,490</b>

- 3.7 The Council is asked to approve the limits set out above, and to delegate authority to the Director of Corporate Services to make adjustments between the borrowing and other long term liabilities boundaries provided that the overall boundary remains unchanged. Any such adjustments will be reported to the next available Council meeting following the change.
- 3.8 With effect from the 1<sup>st</sup> April 2004, to coincide with the introduction of the Prudential code, legislation and guidance on Local Government Investments was issued. This legislation allows Councils with external debt to hold investments for more than 364 days, a freedom not previously allowed. Further freedoms were also introduced which give Councils greater flexibility and hence access to higher returns, provided

that any investment strategy is consistent with the Prudential framework. The Prudential code requires that Councils set limits on investments for periods longer than 364 days. In February 2006, in view of the new strategy to consider borrowing in the current year for part of the 2007/08 requirement, this limit was set at £100m.

- 3.9 The capital programme borrowing requirements for 2007/08 and 2008/09 are now higher than assumed in setting the above limit. Should rates be advantageous, this limit needs to be sufficient to allow borrowing for future years, with this advanced funding being invested until it is required. It is proposed therefore to increase this limit to £150m.
- 3.10 Within these overall limits, the Council's treasury policy restricts the amount which can be invested at any one time with individual borrowers, in order to minimise the exposure to risk. The Council's treasury consultants provide regularly updated lists of credit ratings for potential borrowers, drawn from an international credit rating agency. The current agreed treasury policy is to lend up to £15m to institutions with an excellent credit rating (typically UK clearing banks or other large financial institutions), and up to £5m for up to 3 months to institutions with good credit ratings.

#### **4.0 Implications For Council Policy And Governance**

- 4.1 The operation of the Treasury Management function is governed by provisions set out under part 1 of the Local Government Act 2003 whereby the Council is required to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities.
- 4.2 The Prudential Code requires that full Council set certain limits on the level and type of borrowing before the start of the financial year together with a number of Prudential indicators. Any in year revision of these limits must similarly be set by Council.

#### **5.0 Legal And Resource Implications**

- 5.1 There are no direct resource implications of increasing borrowing limits. However, by increasing the borrowing limits as proposed, the Council will be in a better position to take advantage of treasury management opportunities which could generate revenue interest savings for the Council.

#### **6.0 Conclusions**

- 6.1 The treasury borrowing and investment limits currently in place are insufficient to enable the most cost effective management of the borrowing function. It is therefore proposed that borrowing limits are increased as set out in section 7.

#### **7.0 Recommendations**

That the Executive Board :

- 7.1 Recommend to Council the revised borrowing limits for 2006/07 as set out in Section 3.
- 7.2 Recommend to Council the revised investment limit for 2006/07 as set out in Section 3.