

REPORT OF THE
Cabinet
PART I

A. Revenue Budget and Precept 2011/12

1. Executive Summary

1. This report proposes recommendations to the County Council on the setting of the 2011/12 budget and council tax. Budgets have been prepared in accordance with the strategy agreed by the Cabinet in July 2010 and confirmed in December 2010, following the 2011/12 grant settlement.
2. The County Council faces a £55m funding gap this year from Government funding reductions, the cost of new responsibilities and additional service demands.
3. The proposed budget requirement to be met by formula grant and council tax for 2011/12 is £715.6m, which is £26.3m (3.5%) below the adjusted 2010/11 budget. Though services have budgeted to achieve savings of 8%, this does not translate into an 8% reduction in the budget, mainly because of the allowances also included in the budget for inflation, social care demographic pressures and for contingencies. A budget at this level would enable the council tax to be frozen at its 2010/11 level, £1037.88 at Band D, enabling the County Council to claim a Government grant of £13.2m for freezing its council tax.
4. Most local authorities are likely to take up the council tax freeze grant offered by the Government, so that there will be little, if any, change to the pattern of council tax levels between authorities in 2011/12. This will result in the County Council's council tax remaining within the lower quartile of equivalent County Councils.
5. All services have prepared budgets within the cash limits set by the Cabinet. This requires services to:
 - make savings towards the Phase 1 efficiency target of £15m agreed by Cabinet in February 2010 in order to seek to protect services and to reflect the expectation of a public sector pay freeze set out in the Coalition Government's Emergency budget.
 - achieve savings of 8% on their previous provisional budgets for 2011/12, maximising the scope for savings from the various corporate efficiency workstreams agreed by the Cabinet.
 - for services supported by specific or area based grants in 2010/11, further reductions of £3.6m to reflect reductions in specific grant which exceed the value of savings in grant-related expenditure included in the relevant service's 8% budget reduction proposals.
6. Children's Services are expected to meet the target agreed by the Cabinet for dealing with the in-year funding shortfall in 2010/11 resulting from the grant cuts announced in June, by implementing in full their planned savings by 31 March 2011. However redundancy costs, estimated at £3.7m will be incurred in 2010/11 to enable savings of approximately £8m to be achieved

prior to 2011/12. It is recommended that Children's Services cash limit be increased at the year end to underwrite any overspending resulting from the restructuring required to meet the in year grant cuts, as agreed in principle by Cabinet in July.

7. Adult Services are now anticipating that management action will be effective in enabling demographic and other demand pressures, to be managed within the 2010/11 cash limit, assisted by additional Department of Health funding of £4.3m to support partnership working with the NHS to deal with winter pressures, to prevent unnecessary hospital admissions and speed up hospital discharge.
8. Other services are planned to achieve underspendings in 2010/11. All Departmental underspends can be utilised in 2010/11 or carried forward to 2011/12 to meet non-recurring costs associated with the County Council's change programme
9. One-off savings of £5.3m are anticipated in the current year from lower capital financing charges and interest on balances. This is offset by the cost associated with Children's Services 2010/11 restructuring, estimated at £3.7m, to be financed corporately, and by the contingency of £2.2m proposed for higher winter maintenance spending. The resulting reduction in balances of £0.6m can be reinstated in 2011/12.
10. There are significant risks associated with the 2011/12 budget. The risks relate to the scale of the savings being sought in the first year of the County Council's Efficiencies and Expenditure reduction programme. These are unprecedented in the recent experience of the County Council coupled with the potential increase in demand for services and the immediate withdrawal of Government grants to Children's Services. Allowance has been made in a central risk contingency for identifiable risks associated with specific savings proposals together with a general allowance for potential delays in the delivery of the overall level of planned savings. A central contingency has also been created to cover risks associated with the level of costs arising from demographic and complexity of care needs factors relating to Adult Services.
11. The Cabinet in considering the implications for the corporate strategy of service budget proposals has proposed an addition of £0.6m to the Children's Services budget to recognise continuing budget pressures associated with the number of looked after children and social worker caseloads. The use of £600,000 from the council tax Second Home Reserve is also proposed to develop a scheme to support Care Leavers who are NEET (not in employment, education or training) into employment. Further proposals have also been made to reduce the cost of the Democratic structure by £456,000 bringing the total reduction to £1,156,000, equivalent to 24% of the current cost.
12. There is a one-off forecast additional council tax collection surplus for 2011/12. There is also a recurring council tax projected increase for 2011/12 of £2m per annum related to an increase in the taxbase. Following consultation on the December grant settlement, a further allocation of

£0.446m was made to the County Council related to Concessionary Fares, although there is still a net underfunding of some £1.2m.

13. In 2011/12 the continuing £2.4m is proposed on a one-off basis, alongside £0.9m from the one-off resource to augment the Organisational Change Reserve in line with the Cabinet decision in December to extend the voluntary redundancy scheme to posts below Grade H alongside the strategy to reduce expenditure over the two year period.
14. The remaining one-off resource is proposed to be used to restore the general fund balance to £18m by March 2012 (£0.7m) and the balance of £0.4m to be transferred to the Corporate Policy Reserve.
15. There is a remaining balance of £2.556m recurring alongside £0.4m of one-off funding to be transferred to the corporate policy reserve to support any further high priority initiatives that may require urgent support during the course of the year, to be supplemented by any 'in-year' savings related to the implementation of the £300k staffing reduction related to the Democratic Infrastructure reduction. These reserves are available to mitigate the impact of grant reductions.
16. A paper regarding the Medium Term Financial Strategy covering 2012/13 and beyond will be considered in June/July which is in advance of the normal budget setting timescales due to the significant changes in the Government funding levels. The financial strategy will look to reduce expenditure over a two year period, recognising the difficulties of a four year strategy which is implied by the Coalition Government's recent Comprehensive Spending Review announcement. For planning purposes the Medium Term Strategy will be developed on the basis of a continuation of a reduction of 8% on Departmental Cash Limit budgets, excluding expenditure funded by non-formula grants.
17. Balances are estimated at £18.0m at 31 March 2012, based on the planned use of balances approved in February 2010 in support of the budget in 2011/12. Balances at this level are in line with the current risk assessment, having regard to the contingencies also held within the budget to recognize the risks associated with the delivery in full of the planned level of savings. The balances are 2.5% of the overall budget which is at the lower end of the good practice guide of between 2.5 – 5%. The County Council's approach to the use of reserves was recently commended by the Minister for Housing and Local Government.

2. Background

1. The summary in section 1 sets out the main features of the budget. The rest of the report provides more analysis of the budget proposals, supported by the detailed budgets set out in the draft budget book.
2. The County Council's budget strategy has evolved during the year as the scale of reductions in public expenditure and the timescale over which the Government is seeking to achieve them has gradually unfolded.

3. A provisional budget for 2011/12 and 2012/13 was approved by the Cabinet in February 2010. This included an additional £3.4m for demographic pressures affecting social care and assumed no growth or spending reductions for other services. A reduction in formula grant of 2% in 2011/12 was assumed. A balanced budget was achieved consistent with a council tax increase of 1.9% per annum, below the Government's inflation target, on the basis of a corporate programme of efficiency savings targeted to generate savings of £15m per annum in 2011/12 and 2012/13. Efficiency savings in advance of 2011/12 of £8.6m were incorporated in the 2010/11 budget.
4. The previous Government's budget in March 2010 indicated that larger reductions in Government grant were likely to be required to eliminate the structural deficit within the public finances over the period of the next two Parliaments. Immediately following the elections, the Coalition Government announced some in-year local authority grant reductions for 2010/11 in early June and then presented an Emergency Budget at the end of June. This set the context for the Spending Review to be undertaken over the summer and for decisions on the allocation of resources between spending departments to be announced in October. A more ambitious timescale was set for eliminating the structural deficit over the period ending in 2014/15, the final year of the Spending Review period.
5. The Cabinet had reviewed the Medium Term Financial Strategy assumptions in May 2010 to take account of the previous Government's planned squeeze on public sector pay and the likelihood of grant reductions well above 2%. In July 2010, following the Coalition Government's Emergency Budget, the Cabinet agreed an Efficiencies and Expenditure Reduction Programme. The programme incorporated planned budget reductions of 8% for each service compared with the provisional budget for 2011/12 in anticipation that the County Council's Government grant might be reduced by more than 15% in 2011/12. The forecast loss of Government grant took account of two factors, that the County Council as a floor authority could expect a maximum reduction in Government grant and that any proposals to take account of levels of grant dependency in the allocation of grant would also result in bigger cuts in the County Council's grant.
6. The Cabinet agreed to establish a number of corporate efficiency workstreams with a view to achieving as large a proportion of the savings target from these workstreams as possible, targeting reductions in the running costs of the organisation, in order to minimise the impact on front line services and jobs.
7. The Spending Review announcement in October 2010 confirmed that Government grants to local authorities would be subject to above average reductions in order to protect priority services. A reduction of 28.8% in formula grant in real terms over the period 2011/12 to 2014/15 was announced, compared with an average reduction of 8.3% in departmental expenditure limits across the whole of government.. The local government reductions were also 'front-loaded' with a reduction of 20% to take place in the first two years. The Government announced that it intended to give a

grant equivalent to a 2.5% council tax increase in 2011/12 to all local authorities that agreed to freeze council tax at the 2010/11 level.

8. A two-year Revenue Support Grant consultation for 2011/12 and 2012/13 was announced on 13 December 2010 and a presentation was given to the December meeting of the Cabinet. Adjusted to take account of data corrections to the baseline transfer in the final settlement, the main features of the grant consultation were as follows:
 - no change to the broad principles of the four block model, but variable floors introduced for County Councils based on grant dependency. The County Council's grant reduction is the maximum 14.3% in 2011/12 (£30.9m), and 10.4% (£19.0m) in 2012/1
 - a baseline transfer of £3.3m in respect of central services relating to the transfer of schools to academy status and the transfer of planning functions to the South Downs National Park, neither of which will be matched by an equivalent reduction in spending need in 2011/12
 - a baseline transfer of funding for concessionary fares, which after allowing for a 14.3% reduction, provides funding of £1.2m less than the cost of the minimum scheme required to meet statutory requirements
 - a Government presentation of the grant settlement focussing on an assessment of the change in each local authority's overall spending power, rather than the loss of grant, indicating a reduction of 0.96% in the County Council's spending power in 2011/12. There is a question regarding the validity of the presentation, regarding the extent to which other resources are available to replace the loss of formula, area based and specific grants, relying heavily on the inclusion of funding of £12.7m included within the NHS budget for joint working between health and social care.
9. The County Council has made representations on each of these aspects of the settlement. It is unlikely that any fundamental changes to the grant allocation will result from the consultation, though some data corrections to the baseline transfer were announced on 31 January, mainly to increase the concessionary fares baseline transfer, which add £446,000 to the County Council's formula grant for 2011/12.
10. The grant settlement also included some significant changes affecting area based and specific grants, which have either been discontinued, merged or assimilated into formula grant – leaving four significant non-schools grants: an early intervention grant (£38.1m) including early years funding previously ring-fenced within the Schools Block; a Learning Disability and Health Reform grant (£41.9m), based on funding transferred from the NHS; a Private Finance Initiative (PFI) grant towards the Street Lighting PFI (£9.4m) and the council tax freeze grant (£13.2m).
11. After allowing for the effect of changes in functions and funding arrangements between 2010/11 and 2011/12, the overall loss of specific and area based grants in 2011/12 has been assessed at £11.6m (26.2%), made up as follows:

	£m
Discontinuation of Children's Services grants	-5.5
Reduction in Early Intervention grant	-3.5
Grants transferred into formula grant at below their 2010/11 level:	
Adult Services	-1.9
Transport	-1.2
Reduction in Community Safety grant	-0.3
Increase in Learning Disability and Health Reform grant	0.8
	-11.6

The specific grant reductions have therefore been mainly targeted at the non-schools Children's Services budget.

12. Services had been set 8% savings targets for 2011/12 to cover anticipated losses of both formula grant and specific/area based grants and in determining the extent to which specific/ area based grant reductions should be 'passported' to services in addition to the 8% savings target, account has been taken of the extent to which reductions in grant related expenditure were included in service budget savings proposals. £3.9m of the £11.6m reduction in grant has been 'passported' to Adult Services (£1.2m), Children's Services (£1.8m), Environment (£0.7m) and Policy and Resources (£0.2m)
13. The County Council's recent practice has been to have a three- year budget plan, in which the first year is a firm budget for the financial year just about to commence, but which also for planning purposes includes provisional budgets for the following two years. This year it is proposed to recommend a budget solely for 2011/12 at this meeting and to present a budget plan for a further three years in the Summer, to cover the remainder of the spending review period. This will provide the opportunity to consider more fully the savings options in future years and to refine the basis of forecasting for 2013/14 and 2014/15, the years beyond the current two- year grant settlement. Cabinet in December approved the development of this financial strategy for consideration in June/July that looks to reduce expenditure over a two- year period, recognising the difficulties of a four- year strategy which is implied by the Coalition Government's recent CSR announcement.

14. As the scale of the grant reductions faced by the County Council in 2011/12 are of a similar magnitude to those forecast in July 2010, the Cabinet in December confirmed that service budgets should be prepared on the basis of the 8% savings targets originally set for planning purposes in July, adjusted for the passporting of specific and area based grant reductions on the basis set out in paragraph 2.12 above. The table below summarizes the savings targets and the resulting budget guidelines for 2011/12.

	8% budget reduction	Budget guideline
	£000	£000
Adult Services	-24,410	324,615
Children's Services (excluding Schools)	-13,564	172,928
Culture, Communities and Rural Affairs	-2,722	30,535
Environment	-5,309	111,056
Policy and Resources	-6,295	71,361
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	-52,300	710,495
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The remainder of the report is structured as follows:

- revised budget for 2010/11 (paragraph 3)
- 2011/12 savings and redeployment proposals (paragraph 4)
- annual review of charges and the maximisation of income (paragraph 5)
- workforce implications (paragraph 6)
- further budget proposals (paragraph 7)
- performance and risk management (paragraph 8)
- earmarked reserves (paragraph 9)
- balances (paragraph 10)
- 2011/12 overall budget proposals (paragraph 11)
- implications for 2012/13 to 2014/15 (paragraph 12)
- treasury management strategy and annual investment strategy for 2011/12 (paragraph 13)
- prudential indicators (paragraph 14)
- consultation (paragraph 15)

3. Revised budget 2010/11

1. Budgets are monitored regularly by Executive members and Cabinet reviews high risk demand led budgets and associated activity levels, together with employee budget and financial health indicators on a quarterly basis.
2. The Cabinet agreed a revised policy for the carry forward of underspendings in October 2010, allowing services to carry forward 100% of any underspendings against the cash limit providing they are used to support the change agenda, in consultation with the County Treasurer.
3. Culture, Communities and Rural Affairs, Environment and Policy and Resources have set out to achieve savings against their 2010/11 cash limits, in advance of the budget reductions required in 2011/12. These savings will be primarily used to fund all or part of the up front costs of restructuring, thus enabling a higher level of salary savings to be achieved in 2011/12.
4. Adult Services have taken management action to contain budget pressures during 2010/11 and anticipate that the outturn for 2010/11 will be contained at or within the cash limit. The position has been assisted by the decisions of the Secretary of State for Health to make additional funding of £4.3m available for social care spending that benefits health in 2010/11.
5. The Cabinet in June agreed that Children's Services cash limit for 2010/11 should be reduced by £4.9m to reflect the in-year reduction in the Children's Services element of area based grant. However in recognition of the timescale associated with implementation of the proposed reductions, it was agreed that providing the required savings were achieved on a continuing basis by 31 March 2011, that the cash flow pressure on the budget in 2010/11 would be met corporately. The latest forecast is that savings of approximately £8m on a continuing basis will have been achieved by the end of 2010/11 to cover the in year grant reduction and other unavoidable service pressures, but that restructuring costs, excluding the effect of the higher cost of the voluntary redundancy scheme, of approximately £3.7m will not be able to be absorbed within the cash limit. It is recommended that in accordance with the policy agreed in June, that the in year funding shortfall of £3.7m be met corporately.
6. The County Council budgets for highway winter maintenance on the basis of the average expenditure over the past four years adjusted for inflation. So that Environment can plan the highway maintenance programme without having to allow for the uncertainty about the cost of winter maintenance activity, any variation against the four year average accrues to or is met from the Council's balances. As a result of the heavy snow in December, expenditure is expected to exceed the 2010/11 budget by at least £2.2m and provision has been made in the contingency for additional spending at this level.
7. As indicated in the previous budget monitoring report to the Cabinet, lower capital financing costs will be incurred in 2010/11 than budgeted. A reduction of £5.3m is anticipated for three reasons; lower borrowing levels in 2009/10 than anticipated due to slippage in capital expenditure, short term interest rates remaining at their current low level for longer than assumed and

additional balances on which interest is being earned both reflecting underspendings in 2009/10 and further planned service underspendings in 2010/11.

8. The table below summarizes the net effect of those changes which will result in a call of £0.6m on the County Council's balances:

	£m
Children's Services restructuring costs arising from the in-year grant reductions	3.7
Winter maintenance activity	2.2
Lower capital financing costs	-5.3
Reduction in balances	0.6

Paragraph 7 of the report contains a proposal to reinstate balances by £0.7m in 2011/12 to the risk assessed level of £18m.

4. **2011/12 service budgets – savings and redeployment proposals**

1. Executive members have presented budgets within the budget guidelines summarised in paragraph 2.14. The guidelines are based on the provisional budget guidelines for 2011/12 agreed by the Cabinet in February 2010, adjusted for the effect of the in-year grant reductions in 2010/11, the 8% reduction in service budgets proposed by the Cabinet in July 2010, the effect of reductions in 2011/12 Government grant, funding and function transfers and for minor variations in the 2011/12 base budget. The table below summarises the changes:

	£m
2011/12 Provisional Service budgets approved in February 2010	696.5
2010/11 in-year grant reductions	-6.2
8% budget reduction	-52.3
Passporting of 2011/12 Government grant changes	-3.6
Funding and function transfers – learning disability , concessionary fares and early years	73.9
Other base budget changes	2.2
2011/12 service budget guidelines	710.5

2. The Efficiency and Expenditure reduction programme approved by the Cabinet in July contained a number of corporate efficiency workstreams, designed to support services in meeting their budget reduction targets, while minimising the impact on front line services. £28.8m (54%) of the savings proposals are derived from the corporate efficiency workstreams, as summarized in the table below:

Corporate workstreams	£m
Senior management restructuring	7.9
Recruitment moratorium and support services restructuring	4.4
Communications	1.0
Democratic infrastructure	0.9
Grants	1.2
Inspection and regulation	0.2
Contract negotiations	9.7
Income and charging	0.6
Support and administration	1.0
Business/shared services	0.4
Learning, training and development	0.6
IT cost reduction	0.9
	28.8
Departmental savings	24.8
Total savings – including £1.3m procurement savings relating to Waste Management contract	53.6

3. The projected savings from the corporate workstreams are therefore expected to provide more than 50% of the overall savings, and are broadly in line with the corporate workstream saving forecast reported to the Cabinet in December. The following paragraphs highlight the main feature of each service' proposals.

Adult Services

4. In addition to identifying savings of £24.4m to meet the budget guideline, Adult Services continue to be affected by the impact of demographic pressures from an ageing population and from increased numbers of young

people with disabilities living into adulthood. An increase of 776 care packages is forecast at an estimated increased cost of £13.8m, which together with other unavoidable pressures of £2.1m, adds £15.9m to budget pressures. These budget pressures can be largely funded in 2011/12 from the anticipated grant of £12.7m from the NHS Primary Care Trust for improved integrated working between health and social care and from former specific grants that have been recycled into formula grant but had been expected to discontinue. The position will be more difficult in 2012/13 as the NHS grant is reduced to £12.2m and therefore will not provide a means of funding further additional demographic and complexity pressures.

5. The £13.8m assessment of demographic and complexity pressures does not include all the possible impacts associated with demographic trends. Some of the impacts are more uncertain – the timing of increased demand, the extent of increased numbers of ordinary residence cases, increased learning disability needs and the level of winter pressures. It is therefore proposed to deal with these risks through the central contingency rather than allocating a cash limit to Adult Services at this stage. Adult Services will be able to drawdown on this contingency subject to providing evidence of increased demographic and complexity growth. A contingency of £13.8m has been assessed, which can be covered by a means of a transfer from Adult Services cash limit of £11.5m leaving a balance of £2.3m dependent on the implementation of the revised contribution policy currently the subject of a consultation.

Children's Services - Schools

6. The majority of separate specific grants in addition to the dedicated school grant (DSG) have been assimilated into DSG on a 'flat cash basis', based on maintaining in cash terms, 2010/11 funding per pupil. Additional to this is the Pupil Premium being introduced in 2011/12, payable to schools at a rate of £430 per pupil to cover all pupils eligible for free school meals and looked after children, together with a £200 premium for children from service families.
7. The total schools budget for 2011/12 is £812.6m, just marginally higher than the adjusted budget for 2010/11 of £810.0m, after allowing for the transfer of early years funding out of the schools block and the transfer of extended schools funding into the schools block. The budget proposals identify one-off headroom of £11.0m in 2011/12, and a further £1.2m on a continuing basis, much lower than in previous years.

Children's Services – Non-schools

8. Children's Services was the service most affected by the in-year grant reductions announced in June 2010, and the 2011/12 grant settlement has also been particularly challenging for Children's Services, for three main reasons:
- Extended schools sustainability and subsidy grants – these grants were previously managed as part of the non-schools budget although mainly spent in schools in support of extended school activity. Children's Services in developing their 8% savings plans had assumed that spending being supported by these grants would be reduced significantly in 2011/12. The Department for Education (DofE) however decided to transfer the funding into the schools budget, preventing savings being made in the non-schools budget in this area. Children's Services were therefore required to identify additional savings of £8.7m to comply with their cash limit.
 - Reductions in other grants – the majority of the non-schools Children's Services grants have either been discontinued in the 2011/12 grant settlement (£5.5m) or merged into the new Early Intervention Grant, including early years funding formerly within the schools block, which was then subject to a reduction of £3.5m on the baseline figure. Having regard to savings already proposed within the 8% savings proposals relating to grant-related expenditure, a further reduction of £1.8m has been 'passported' to the Children's Services cash limit.
 - Academy top slice – the County Council's formula grant has been top sliced by £3.2m in 2011/12 to reflect the anticipated funding transfer from the non-schools budget for central services when schools opt to become academies. A further top-slice of £2.5m is proposed in 2012/13. Adopting an approach to transferred funding that has no link to the number of schools actually transferring to academy status is unsatisfactory and the County Council has made representations on this point in its response to the grant settlement consultation. However on the assumption that the Government will not modify its approach, it is proposed that the impact of the grant reduction be absorbed corporately in the first instance, pending the actual transfer of schools to academy status, when a budget adjustment will be made. To the extent that Children's Services and the central support services are successful in marketing the relevant services to academies, it will be possible to generate additional income to help to cover the loss of budget. It will also be necessary to provide corporate funding to cover the work required to be undertaken by the County Council in order to support the set up of Academies, which will be covered within the Corporate Risk Contingency.
9. Children's Services have also been required to identify savings to offset unavoidable budget pressures relating to Children Looked After (£2.9m), Family Support Services (£0.2m) and Home to School Transport (£0.4m). The planned reduction in numbers of looked after children in 2010/11 to an

average of 1,043 following a period of sustained growth in 2009/10, has not occurred, although the further growth in the first quarter of 2010/11 has been reversed. The 2011/12 budget allows for 1,100 looked after children broadly in line with activity levels in the current year.

10. In view of the scale of the additional savings of £8.7m that Children's Services were required to identify following the grant settlement in order to meet the cash limit, the Cabinet agreed in December that cash flow support would be required in 2011/12. This would both allow for the lead-in time required to implement change and the likely restructuring costs required up front. An approach is proposed similar to that adopted in relation to the in-year grant reductions in 2010/11, with a target for full implementation of planned savings in 2011/12 by 31 March 2012, so that the full value of the savings required can be achieved in 2012/13.

Culture, Communities and Rural Affairs (CCRA)

11. CCRA has a savings target of £2.7m in 2011/12, £1.5m of the proposed savings relate to the corporate workstreams and the remaining departmental savings mainly relate to the Libraries and Information Service, generated both from past restructurings, the planned further restructuring of the mobile library service and a planned reduction in spending on materials.

Environment

12. Environment have identified savings of £6.7m in 2011/12, £1.4m above their savings target, thus providing some one-off resources in 2011/12 to help meet the cost of the change agenda, including restructuring costs. In addition to the focus on the corporate workstreams, a county-wide review of subsidised bus services is planned, aimed at achieving savings of £1.2m during 2011/12 and a similar level of additional savings in 2012/13, from the full year effect of the review.

Policy and Resources (P&R)

13. As the corporate workstreams have been heavily focussed on back office and support services efficiency savings, the P&R budget proposals are mainly directed at the corporate workstreams. The overall level of savings provides a contingency of £0.6m in 2011/12 to help meet any unbudgeted costs of change. Included within the proposals are savings of £60,000 on members expenses and the discontinuation of the HATs community chest, saving £700,000.

5. Annual review of charges

1. Fees and charges have been raised where there is scope to do so in policy and economic terms, and the inflation allocation has been calculated on the basis that charges are increased in line with the allowance for inflation on gross expenditure, before the allowance for efficiency savings relating to pay, averaging 2.3%.

2. Details of income reviews and charges were set out in the budget reports for Executive members and in the summary below:

Income from fees and charges

	Total 2010/11	Mandatory charges 2011/12	Discretionary charges 2011/12	Total 2011/12
	£m	£m	£m	£m
Adults	52.9	46.0	13.0	59.0
Children's	7.0	2.0	4.1	6.1
CCRA	7.3	-	7.1	7.1
Environment	12.5	0.2	12.3	12.5
P&R	14.9	1.1	16.9	18.0
Total – Fees and Charges	94.6	49.3	53.4	102.7

6. **Workforce Implications**

- The workforce statement on Page A7 of the draft budget book summarizes the workforce implications of the budget proposals. The overall reduction attributable to the savings proposals within the budget, include changes to business unit staffing, represents a reduction of 696 FTEs. This is the staffing level consistent with the financial provision in the budget for pay costs but only reflects the part year effect of changes expected to take place during 2011/12. The full year reduction which amounts 1,171 FTEs provides a better measure of the impact of the budget on the future size of the workforce.
- The table below summarises the forecast reduction in the workforce.

	Full year staffing reduction (FTEs)
Adult Services	-376
Children's Services – Non-schools	-458
CCRA	-37

	Full year staffing reduction (FTEs)
Environment	
- Revenue budget	-100
- Capital Programme	-11
Policy and Resources	
- Revenue Budget	-136
- Business units	-53
	1,171

7. Further budget proposals

Collection Fund and taxbase

1. The District Councils as the billing authorities for the collection of council tax in Hampshire are not required to declare their collection fund surpluses or deficits and set the following year's net taxbase until January. Consequently budget planning is based on a forecast of the collection fund surplus and taxbase increase. For 2011/12, the forecast collection fund surplus was £1.5m, slightly lower than the £2.1m actually achieved in 2010/11. In the event the district councils have collectively declared a surplus of £3.5m, £2m more than forecast. This provides one-off additional resources in 2011/12.
2. The council taxbase for 2011/12 was forecast to increase by 0.25%, lower than the 0.7% increase in 2010/11, on the assumption that the lower level of house building since the downturn in the property market, might adversely affect the rate of increase in the taxbase. However the level of the net taxbase increase has only reduced to 0.6%, the effect of which is also to generate additional income on a continuing basis of £2m, at current council tax levels. The increase in formula grant in the final settlement provides an additional continuing sum of £0.4m.
3. The Cabinet agreed to earmark £10m in an Organisational Change Reserve by means of a transfer from the Corporate Policy and Invest to Save Reserves, in order to meet the known liability resulting from a decision to target staff reductions, not achieved through the recruitment moratorium, by way of voluntary measures. It can therefore be anticipated that this reserve will have a short-term life span in support of the change programme over the next two financial years. £3.3m of the reserve is forecast to be used in 2010/11 and it is proposed that the additional continuing resources of £2.4m from the higher taxbase and formula grant be used to augment the reserve in 2011/12 and would then be available to help bridge the budget gap in

2012/13. In addition it is proposed that £0.9m of the additional proceeds of £2m from the higher collection fund surplus be utilised for the same purpose in 2011/12 to reinstate the reserve at £10m for 2011/12. £0.7m of the remaining sum could be used to restore the budgeted general balance to £18m at 31 March 2012, leaving the balance of £0.4m to be transferred to the Corporate Policy reserve.

4. This is consistent with the Cabinet decision on 22 December to extend the voluntary redundancy scheme to posts below Grade H and the decision to develop a financial strategy that looks to reduce expenditure over the two year period, recognising the difficulties of a four year strategy which is implied by the Coalition Government's recent Spending Review announcement.

Leader's recommendations

5. The Leader recommended to Cabinet having reviewed service, redeployment and savings proposals, allocating £600,000 to Children's Services in 2011/12. In 2010/11 a contingency of £1m was included in the budget to recognise the uncertainty associated with forecasting the cost of providing care for looked after children. The 2011/12 budget guideline included an allowance of 1% (£750,000 for Children's Services) for social care demographic pressures, and it is proposed to allocate a further £250,000 to Children's Services. This is in recognition of the continuing budget pressures facing children's social care, as numbers of looked after children have not decreased in 2010/11. It also proposed to allocate a further £350,000 to employ additional Children's social workers in the interest of ensuring that all social workers have manageable case loads.
6. A further proposal is to make £600,000 available from the council tax second homes income reserve to develop a scheme to support Care Leavers who are NEET (not in employment Education or Training) into employment through an apprentice scheme which will be developed over the coming months. The Medium Term Financial Strategy will look to ensure a sustainable future for their scheme.
7. The Leader also proposed to the Cabinet further budget reductions regarding the cost of the Democratic Structure amounting to £456,000, bringing the total annual reduction in the Democratic Structure to £1.156m, equivalent to 24% of the current cost. The additional budget reduction relates to £156,000 resulting from a reduction in Members budgets of £2,000 per annum from £10,000 to £8,000 from 1 April 2011 and to a £300,000 staffing reduction which will be implemented following due process over the course of the coming financial year.
8. A further £2.556m has been added to the corporate policy reserve to support any further high priority initiatives that may require urgent support during the course of the year, to be supplemented by any 'in- year' savings related to the implementation of the £300,000 staffing reduction.

Capital financing costs

9. The Government has changed the policy for support of local authority capital investment in 2011/12 so that all support is channelled through capital grants rather than by a combination of capital grants and borrowing allocations, the latter being reflected in formula grant. This is a policy change that is welcomed by the County Council as it deals with the problem of Government support for borrowing being ineffective because of floor damping.
10. Capital financing costs in respect of supported borrowing will therefore reduce over time as the County Council is required to make provision for repayment of loans linked to past capital investment, but will not be required to incur any new borrowing in respect of supported capital expenditure. The Cabinet in December agreed that officers should explore the options for developing a new capital strategy to reflect the changing context for local authority capital investment. The strategy will be developed during 2011 and it is proposed that in order to facilitate making use of some unsupported borrowing to underpin the strategy that capital financing costs are included in the 2011/12 budget at their planned level.

Risk contingency

11. A central contingency is included within the budget alongside the cash limited budgets for services, where additional or reduced spending is envisaged but where inclusion of the spending or saving within the cash limit is contingent upon the outcome of some future event. This approach has been adopted to cover some aspects of inflation, the waste management contract, allowance for interest rate changes and for any spending or savings plans which are subject to future member approval. As indicated in paragraph 4.5 it is proposed to include an Adult Services demography and complexity contingency within the 2011/12 budget and in addition a specific risk contingency associated with the 2011/12 savings programme.
12. The risk contingency will have two elements, it is partly designed to recognise the cash flow support that Children's Services will require in 2011/12 because of the lead-in time and restructuring costs associated with the additional savings of £8.7m required as a result of the changes in the grant settlement. If all the remaining savings within service budget proposals are achieved a sum of £8.6m is available as a general contingency either against delay in achieving budgeted savings or to cover higher than planned restructuring costs. This represents just under 20% of the related savings. Including a risk contingency on this basis also mitigates against the need to budget for a higher level of balances.

Specific grants

13. The Cabinet also agreed to 'passport' to the relevant services the impact of two late amendments to specific grants, involving the introduction of a new Inshore Fisheries and Conservation grant of £204,000 and a reduction of £262,000 in the Community Safety grant.

8. Performance and Risk management

1. The budget has been set in the context of the priorities of the corporate strategy and as indicated in paragraph 4.2, the corporate efficiency work streams agreed by the Cabinet in July 2010 have played a central role in the formulation of the savings proposed in the budget.
2. Section 25 of the Local Government Act 2003 requires the Chief Financial Officer (the County Treasurer) to report to the County Council when setting its council tax on:
 - the robustness of the estimates included in the budget
 - the adequacy of the financial reserves in the budget
3. The County Council is required to have regard to this report in approving the budget and council tax. The draft report is included in Appendix 1.
4. The main areas of risk are:
 - Equal pay claims – an equal pay reserve has been established and capitalisation directions will be applied for to spread any higher costs over a number of years. The budget assumes that the current claims will be resolved during 2011/12.
 - Budgeted savings – service budgets contain savings of £52.3m in respect of the 8% savings target. This is a substantially more challenging level of savings in one year than in any recent period. The corporate risk contingency of £8.6m provides some mitigation against the risk of savings not being fully achievable in line with the budget assumptions.
 - Children's Services grants – late notification of substantial further reductions of £8.7m has resulted in the potential need for one year cash flow funding to recognize both the timescales required and the cost of change.
 - Inflation – service budgets assume non-pay inflation will average 2.5% in 2011/12. There is a risk of higher levels of general inflation with RPI and CPI currently increasing at year on year rates of 4.8% and 3.7% respectively.
 - Demand led budgets – though there is a risk of higher levels of demand for statutory services particularly affecting social care, the budget includes some mitigating measures to deal with those budget pressures.
5. The detailed risk assessment is set out in Appendix 1 and indicates a prudent level of underlying balances at around £18m, 2.5% of net expenditure, taking account of other measures within the budget. Balances at this level, as proposed, together with the earmarked reserves and contingencies within the budget, will be sufficiently robust for the County Treasurer's assurance required by the 2003 Act.

9. Earmarked Reserves

1. Earmarked reserves (excluding schools) are budgeted to fall from £120.5m at 31 March 2010 to £86.8m at 31 March 2012. The major uncertainty concerns the largest reserve, the Equal Pay reserve, set aside to meet any successful equal pay claims arising from the County Council's implementation of the national single status agreement. It is anticipated that the Employment Tribunal will consider the current claims during 2011/12 and that as a result 2011/12 will be the critical year in determining the extent of the County Council's liability for equal pay claims. The 2011/12 budget has been drawn up on the basis that the reserve will be utilised in 2011/12.
2. Full details of each of the main reserves are set out on Page A11 of the draft budget book.

10. Balances

1. Budgeted balances at 31 March 2011 are £21.1m, reducing to £17.3m at 31 March 2012 with the planned use of underspendings in 2008/09 and 2009/10 to support the council tax in 2011/12. The risk assessed level of general balances in 2011/12 is £18m, equivalent to 2.5% of the budget requirement and the proposal to utilise £0.7m of the higher collection fund surplus to add to the general balance results in estimated balances of £18m at 31 March 2012, in line with the risk assessment.

11. 2011/12 overall budget proposals

1. Taking into account the changes identified in the earlier sections of this report, the final budget proposals for 2011/12, compared with 2010/11 adjusted for funding and function changes in 2011/12, are:

Service cash limits 2011/12

	2010/11 Adjusted	2011/12
	£000	£000
Schools	809,974	812,635
Adult Services	349,386	313,064
Children's Services – non-schools	185,418	173,528
CCRA	33,037	30,535
Environment	116,999	111,056
P&R	81,049	71,805
	<hr/>	<hr/>
	1,575,863	1,512,623

Other budgets compared with 2010/11 can be summarised as follows:

Other budgets 2011/12

	2010/11	2011/12
	£000	£000
Revenue contributions to capital	29,018	25,636
Capital financing	52,796	60,769
Other budgets – flood protection, landfill allowances, coroners etc	1,484	1,666
Trading account (surpluses) / deficits etc	923	1,539
Dedicated Schools grant	-720,378	-825,013
Specific and area based grants	-201,834	-107,609
Contingency		
Inflation, waste management contract and other general contingencies	14,854	12,442
Equal Pay	-	48,520
Phase 1 efficiency savings	- 1,660	-4,914
Adult Services demography and complexity -	-	13,793
Corporate Risk contingency	-	17,300
Contribution to /(from) earmarked reserves	-797	-38,094
Contribution to/(from) balances	-8,346	-3,073
	<hr/>	<hr/>
	-833,940	-797,038

2. Bringing all these budgets together results in an overall budget requirement of £715.6m, which is a 3.5% reduction on the 2010/11 adjusted budget of £741.9m.

2011/12 Budget requirement

	2010/11	2011/12
	£000	£000
Service budgets	1,575,863	1,512,623
Other budgets	-833,940	-797,038
Budget requirement	741,923	715,585

3. The budget requirement will be met, as shown in the next table, compared with 2010/11's adjusted budget, incorporating a freeze in council tax.

	2010/11 adjusted	2011/12
	£000	£000
Budget requirement	741,923	715,585
Formula grant	-216,629	-185,652
Net surpluses on collection funds	-2,062	-3,506
Precept	523,232	526,427
Taxbase Band D equivalent dwellings	504,135	507,214
Council (tax per Band D)	1,037.88	1,037.88
Increase over previous year	1.9%	-

4. It is anticipated that all of the local authorities in Hampshire covered by the council tax freeze grant will opt to freeze their council tax in 2011/12 at the 2010/11 level. Town and Parish Councils are not covered by the scheme and could increase their council taxes. The average Band D council tax in Hampshire is unlikely to change significantly from the average in 2010/11 of £1,425.

5. The trends in council tax compared with budgets and local and national grant variations in recent years are as follows:

% variations in council tax, grant and budgets				
	Government National Grant	County Council		
		Grant	Budget	Council Tax
	%	%	%	%
2005/06	5.3	5.0	4.7	3.5
2006/07	3.8	2.0	5.2	4.7
2007/08	3.7	2.7	5.4	4.9
2008/09	3.5	2.0	4.4	4.5
2009/10	2.8	1.75	2.3	1.9
2010/11	2.6	1.5	2.3	1.9
2011/12	-9.9	-14.3	-3.5	0.0

6. The County Council's financial profile remains very similar to that of last year
- its formula grant per head is second lowest of comparable County Councils
 - its council tax is likely to remain in the lower quartile of County Councils, as all County Councils are likely to freeze their council tax in 2011/12.

12. Implications for 2012/13 to 2014/15

1. A further report will be brought to the Cabinet on the Medium Term Strategy for 2012/13 to 2014/15 in June/July. This will seek to implement the Cabinet's strategy of achieving the spending reductions required by the Government's Spending Review over two years by targeting a further 8% reduction in service spending in 2012/13, reflecting the Government's policy of front loading local government grant reductions. This will also recognize the difficulties of a four-year strategy, which is implied by the Coalition Government's Spending Review announcement. Monitoring the implementation of the planned 2011/12 savings will be a critical factor in assessing the implications of this strategy. Though the budget proposed at this meeting only covers 2011/12, it includes an assessment of the full-year effect of savings being implemented in 2011/12, identifying further savings of £24.6m from the full year effect of the measures.

13. Treasury management strategy and investment strategy for 2011/12

1. The County Council is required to adopt a treasury management strategy and an annual investment strategy for 2011/12 and these are set out in Appendix 2 for approval. The strategy has been reviewed in the light of the appointment of treasury management advisers. The revised borrowing strategy reflects the intention of taking a more active approach to managing the portfolio of existing borrowing.

14. Prudential indicators

1. The prudential code ensures that:
 - capital programmes are affordable in revenue terms
 - external borrowing and other long-term liabilities are within prudent and sustainable levels
 - treasury management decisions are taken in line with professional practice

Some of the upper limits have been raised to reflect the revised Treasury Management and Investment Strategy.

2. Appendix 2 also contains the prudential indicators required by the code for the County Council.

15. Consultation

1. A variety of forums and methods have been utilised to hear the views of the public, the employees and the Unions on the efficiency programme and cost reduction proposals. A summary of the Strategy and key messages was reported to the Cabinet.

RECOMMENDATIONS

That :

1. the Treasurer's report under Section 25 of the Local Government Act 2003 be taken into account when the Council determines the budget and precept for 2011/12 (Appendix 1).
2. the revenue budget for 2011/12 (as set out in the attached draft budget book) be approved.
3. the total budget requirement for the general expenses of the County Council for the year beginning 1 April 2011, be £715,585,000.
4. the County Council's Band D council tax for the year beginning 1 April 2011 be £1,037.88, as in 2010/11.

5. the County Council's council tax for the year beginning 1 April 2011 for properties in each tax band be:

	£
Band A	691.92
Band B	807.24
Band C	922.56
Band D	1037.88
Band E	1268.52
Band F	1499.16
Band G	1729.80
Band H	2075.76

6. precepts be issued totalling £526,426,934.20 on the billing authorities in Hampshire, requiring the payment in such instalments and on such dates set by them previously notified to the County Council, in proportion to the taxbase of each billing authority's area as determined by them and as set out below:

Basingstoke & Deane	64,655.00
East Hampshire	48,332.33
Eastleigh	44,368.15
Fareham	42,796.00
Gosport	27,595.10
Hart	37,967.18
Havant	42,925.00
New Forest	73,047.60
Rushmoor	31,671.86
Test Valley	45,875.00
Winchester	47,980.46

7. the treasury management and annual investment strategies (as set out in Appendix 2), together with the prudential indicators for 2011/12 be approved and that the Monitoring Officer be authorised to make any changes to the terms of reference of the Audit Committee in the constitution in order to give effect to the new challenge and scrutiny role required as a result of the revised CIPFA requirements.

B Capital programme 2011/12 to 2014/15

1. Executive Summary

1. This report sets out for approval the proposed capital programme for 2011/12 to 2014/15, based on the guidelines agreed by Cabinet on 22 December 2010 including support for capital schemes from the Government.
2. The report collates the service capital programmes prepared by Executive members. It shows that the projected payments arising from the capital programme can be financed within existing resources, without resorting to the use of temporary prudential borrowing.
3. The proposals take account of the County Council's capital strategy and the Prudential Code for Capital Finance in Local Authorities including the capital financing position, the level of debt outstanding and the consequences for the revenue budget and council tax. The prudential indicators are included in Appendix 2 of the report.
4. The main points of the report are:
 - the proposed capital programmes are in line with the guidelines set by Cabinet in December 2010 for the locally resourced programme, together with schemes supported by Government capital grants
 - the coalition Government has issued all its support for local authorities' capital investment in the form of capital grants from 2011/12 onwards, with no use of supported borrowing allocations
 - the level of capital receipts is forecast to recover to an extent over the next few years but initially this will primarily allow the sale of sites already earmarked to rationalisation schemes or to fund previously approved prudential borrowing
 - the Executive Lead Member for Children's Services has proposed using additional prudential borrowing totalling £7.2m between 2010/11 and 2014/15 to finance school schemes in development areas in Andover, Waterlooville and Aldershot in advance of contributions from developers. This borrowing is expected to be repaid by 2014/15 but could be more than the current forecast of £7.2m and be outstanding for longer if the developer contributions are delayed
 - the proposed programme includes £10m per annum for Project Resilience for the structural maintenance of highways, to be funded by efficiency savings which will cover prudential borrowing costs, as agreed by Cabinet in May 2010
 - also included is a £1m per annum programme for Hampshire Transport Management vehicles and £1.56m for IT Services Hosted Schools Solution project. Both will be funded by prudential borrowing, with the loans repaid from charges to the business units' customers
 - for the County Council in total, loans outstanding for prudential borrowing will rise to £112m by 2014/15. The repayment of the 'bridging loans' included in this total will depend on the continued

recovery of the property market. The current assumptions are that they will be fully repaid by 2014/15

- the total value of the proposed capital programme over the four-year period from 2011/12 to 2014/15 is £492m
- as agreed by Cabinet in December 2010, a medium term review of the capital programme will be undertaken over the next few months, for future consideration by the Leader and Cabinet in June/July 2011, as part of the Medium Term Financial Strategy for 2012/13 and beyond.

2. Background

1. At its meeting on 22 December 2010, Cabinet set guidelines for the new capital programme for 2011/12 to 2014/15 at the same reduced level as the current capital programme. This reflected the continued uncertainty about the level of capital receipts likely to be available to finance the locally resourced capital programme.
2. Executive members have now prepared proposals for:
 - a locally resourced capital programme for the four-year period from 2011/12 to 2014/15 within these guidelines and other resources available to services
 - a programme of schemes supported by Government capital grants.

3. Expenditure and resources cashflow - summary

1. Table 1 shows the annual capital expenditure flows from the proposed capital programme, compared with the financing resources available.

Table 1 – Capital expenditure and resources

	2010/11	2011/12	2012/13	2013/14
	£000	£000	£000	£000
Expenditure	185,332	189,040	177,907	136,632
Resources	185,852	189,067	177,982	136,694
Shortfall (+) / Surplus (-)	-520	-27	-75	-62
Planned use of capital reserve	400	-	-	-
Surplus of resources to be transferred to the capital reserve	-120	-27	-75	-62
Capital reserve balance at the end of the year	-120	-147	-222	-284

	2014/15	2015/16
	£000	£000
Expenditure	124,842	74,067
Resources	124,863	74,137
Shortfall (+) / Surplus (-)	-21	-70
Planned use of capital reserve	-	-
Surplus of resources to be transferred to the capital reserve	-21	-70
Capital reserve balance at the end of the year	-305	-375

2. The small surpluses of capital resources in each year demonstrates that the stable financing position for the capital programme has been maintained. No temporary prudential borrowing is currently required to balance payments and resources during the period.
3. The forecasts are likely to change as schemes within the programme progress and the position will be reassessed at the next review of the capital programme.
4. Progress during 2011/12 on all capital payments and resources will be closely monitored and reported to the Leader and Cabinet during the year. Executive members will also review progress on their capital programmes at regular intervals during the year.

4. Prudential borrowing

1. Prudential borrowing agreed to date and now proposed is in accordance with the existing framework for the use of prudential borrowing under the Prudential Code for Capital Finance.
2. New proposals for prudential borrowing include:
 - £7.2m to finance part of the cost of school schemes in advance of developers' contributions
 - £10.0m per annum to finance Project Resilience for structural maintenance of highways, as previously agreed by Cabinet in May 2010
 - £1.0m per annum to finance the Hampshire Transport Management vehicle purchase programme
 - £1.56m to finance the IT Hosted Schools Solution project.

3. With these new proposals, the prudential borrowing outstanding after deducting bridging loans repaid to 31 March 2010 will be £198m. Of this, £127m will be repaid from savings in the revenue budget, including the Enhance nursing care homes project, waste management infrastructure and the structural maintenance of highways.
 4. The County Council's existing framework for the use of prudential borrowing will be considered as part of the mid term review of the capital programme later this year.
5. **Guideline cash limits for the capital programme**
1. 'Locally resourced' schemes are those financed from the County Council's own resources such as capital receipts, contributions from the revenue budget, reserves and other funds. They do not include schemes supported by capital grant from the Government.
 2. The guidelines for the locally resourced programme were confirmed by Cabinet in December 2010 at the levels previously set for the programme. They had been reduced by one-third in February 2009 in response to the lower forecasts of capital receipts likely to be available to support the capital programme. This followed the sharp decline in the demand for development land as a result of the financial crisis in 2008. That reduced level has been maintained, with no uplift for inflation, as uncertainty remains about future capital receipts.
 3. Overall, the reduction in guidelines is £8.4m per annum which means that, with the impact of the global financial crisis, the capital programme is £50m lower over the six years from 2009/10 to 2014/15.
 4. The guidelines set by Cabinet for each service are shown in Table 2.

**Table 2 – Guidelines for locally resourced capital programmes
2011/12 to 2014/15**

	2011/12	2012/13	2013/14	2014/15
	£000	£000	£000	£000
Adult Services	598	481	481	481
Children's Services	90	90	90	90
Culture, Communities and Rural Affairs	417	448	448	448
Environment	6,008	5,847	5,847	5,847
Policy and Resources	6,509	6,494	6,494	6,494
Total	13,622	13,360	13,360	13,360

5. Subsequent virements to or from revenue proposed by Executive members and other adjustments are listed in the sections below on each service's proposed capital programme.

Government supported programme

6. The Government announced in its Spending Review in October 2010 that all its support for local authorities capital expenditure from 2011/12 will be issued in the form of capital grants and not as borrowing allocations. This can be welcomed as it overcomes the disadvantage for the County Council that it did not receive full revenue grant support towards loan charges arising from the so-called Government supported borrowing allocations.
7. Although the Government's Spending Review covered the four years from 2011/12 to 2014/15, the Government has not announced its capital grant allocations for the full year period, as summarised in Table 3.

Table 3 – Government capital grant announcements

Adult Services	2011/12 and 2012/13 only
Children's Services	2011/12 only, pending the outcome of the James review of school investment
Environment	2011/12 and 2012/13, with indicative allocations for 2013/14 and 2014/15
Policy and Resources	as Children's Services

8. In each case, services have assumed that Government grants will continue at similar levels in the later years of their four-year capital programmes. The proposed programmes will need to be reconsidered when the Government has announced the levels of its support for these later years.

6. The programmes submitted

1. The total starts value of the four-year programme submitted by Executive members is £492m, as shown in Table 4. It includes £365m of schemes supported by Government grants.

Table 4 – Starts programmes submitted 2011/12 to 2014/15

	Land	Works, Fees, Furniture and Equipment			Total programme including Land
		Locally resourced programmes	Schemes supported by Government allocations	Total Works, Fees etc	
	£000	£000	£000	£000	£000
2011/12	747	25,228	98,150	123,378	124,125
2012/13	746	38,094	100,373	138,467	139,213
2013/14	746	37,747	80,149	117,896	118,642
2014/15	746	22,449	86,413	108,862	109,608
Total	2,985	123,518	365,085	488,603	491,588

2. The proposed programmes are in line with the guidelines set in December 2010 and are set out in detail in the attached capital programme.
3. The capital expenditure flows from these programmes and from the works currently in progress are summarised on Page C12 of the capital programme, together with the resources available to finance those expenditure flows.
4. The following sections summarise the programmes prepared by Executive members and highlight the issues arising.

7. Adult Services

1. The proposed programme for Adult Services is in line with the guidelines for the locally resourced programme.
2. Prior to 2011/12, the Government issued a capital grant for adult social care of £0.731m per annum. This grant was retained corporately to fund, in part, the locally resourced capital programme including the capital repairs programme that covers Adult Services' properties. In addition, the Government previously allocated a number of separate capital grants for Adult social care.
3. From 2011/12, the Government has consolidated all these capital grants into a single unringfenced grant for capital investment in community capacity. The Government has announced the amount of this grant at £2.417m for 2011/12 and £2.483m for 2012/13.

4. At this stage, these grants have been retained corporately. The use of the grants will be considered as part of the proposed mid term review of the County Council's overall capital strategy.

8. Children's Services

1. The proposed programme for Children's Services of £175m over the next four years is supported primarily by the Government with capital grant allocations, as Table 5 shows.

Table 5 – Children's Services capital programme – resources available

	2011/12	2012/13	2013/14	2014/15	Total
	£000	£000	£000	£000	£000
Resources carried forward					
- from 2010/11					
- previously agreed	833	-	-	-	833
- additional	20,482	-	-	-	20,482
- from 2011/12	-16,835	16,835	-	-	-
- from 2013/14	-	-	-3,945	3,945	-
Government's capital grants:					
- Basic Need - new pupil places	11,606	11,606	11,606	11,606	46,424
- Capital Maintenance	11,709	11,709	11,709	11,709	46,836
- Schools' Devolved Capital	4,069	4,069	4,069	4,069	16,276
- Havant Academy	8,678	-	-	-	8,678
Local resources:					
- guideline	90	90	90	90	360
- capital receipt anticipated	-916	4,572	2,065	-	5,721
- developer funded schemes (see paragraph 8.13 below)	1,214	11,570	14,576	2,039	29,399
- provision for land	100	100	100	100	400
Total	41,030	60,551	40,270	33,558	175,409

2. Prudential borrowing totalling £7.220m will be necessary to finance schemes in advance of the receipt of developers' contributions, based on current forecasts of the timing of capital payments and contributions. This is considered in more detail in paragraph 8.13 below.
3. The Executive Lead Member for Children's Services proposes carrying forward capital resources of £20.482m from the programmes for 2010/11 and earlier years to 2011/12, in addition to the £0.833m previously agreed. These resources have been added to the proposed programme for 2011/12 in this report. The deferred schemes are listed in Table 6.

Table 6 – Children's Services schemes to be deferred from 2010/11 to 2011/12

	Project cost	Resources to be carried forward
	£000	£000
Building Schools for the Future (BSF)	2,500	2,500
Secondary – non BSF	2,030	2,030
Primary Capital Programme	6,055	5,855
Education and inclusion service general	342	342
Specialist facilities improvements	300	228
Primary inclusion project	1,250	1,250
New pupil places primary	1,800	1,800
Fareham and Gosport inclusion project	4,000	4,000
Special school improvements	2,000	1,604
Purchase of temporary classrooms	500	223
Stubbington Study Centre	500	500
Other equipment	150	150
Total project cost	21,427	
Total resources carried forward		20,482

Government capital grants

4. The coalition Government has consolidated its support for schools capital from 2011/12 onwards into three main capital grants for basic need (new pupil places), capital maintenance and schools' devolved capital.
5. The previous Government's allocations for the Primary Capital Programme, Sure Start, extended schools, youth capital fund, the targeted capital fund and the disabled children grant (Aiming High) have been terminated.
6. All the Government's support will be in the form of capital grants, with no borrowing allocations in future.

Capital Maintenance funding

7. The Government has replaced its funding for Modernisation and Condition work (formerly known as New Deal for Schools or NDS) with a capital grant for Capital Maintenance. With the agreement of the Executive Members, this has been divided between the Children's Services and Policy and Resources capital programmes using the 46% : 54% proportions agreed for the NDS allocations in July 2003.
8. The total grant available for Capital Maintenance is shown in Table 7. The Government has so far only announced its allocations for 2011/12. For the purposes of preparing the capital programme, it has been assumed that this level of capital grant will continue for 2012/13 to 2014/15.

Table 7 – Capital Maintenance

		2011/12	Later years
		£000	£000
Children's Services	46%	11,709	11,709
Policy and Resources	54%	13,745	13,745
Total	100%	25,454	25,454

The Government's total capital support for the Children's Services

9. The Government has provided grants of £61.5m in support for capital investment in Children's Services in Hampshire for 2011/12, as Table 8 shows. This is a reduction from the £87.2m allocated by the previous Government for 2010/11, in the form of capital grants and borrowing allocations. The total of £87.2m for 2010/11 is before adjusting for amounts advanced to 2009/10 and the coalition Government's in-year reductions for 2010/11.

Table 8 – Government support for capital spending on Children’s Services

	2010/11	2011/12
	£000	£000
New pupil places	6,231	11,606
Schools’ devolved capital	21,049	4,069
Capital Maintenance (formerly NDS)	16,034	25,454
DSG funded capital repairs	11,719	11,719
Havant Academy	-	8,678
Children’s social care	144	-
Schools access initiative	2,447	-
Sure Start grant	7,787	-
Sure Start grant – condition	477	-
Youth capital fund grant	514	-
Primary capital programme	11,825	-
Extended schools grant	1,049	-
Targeted capital fund	6,300	-
Disabled children grant	1,588	-
Total Government support	87,164	61,526

Havant Academy

10. The Executive Lead Member for Children’s Services approved in November 2010 the inclusion in the 2011/12 capital programme of a major refurbishment project at Havant Academy. The estimated value of the project, to be met in full from Government grant, was £10.085m. The Department for Education (DfE) has subsequently reviewed the resources available for this and other academy projects nationally and has imposed a funding reduction of £0.504m, leaving a total project cost, including ICT provision, of £9.582m. ICT funding of £0.904m will be made available directly to the Academy by the DfE and will not, therefore, form part of the Children’s Services capital programme. The revised value of the building

project is £8.678m, including fees and the project is expected to start on site in early summer 2011. This scheme has been included in the proposed programme for 2011/12.

Park Community School, Havant

11. Major structural issues have been identified at Park Community School in Havant where the majority of the buildings are constructed in a pre-cast concrete system and are nearing the end of their useful life. Temporary measures have been in place for some time to mitigate the effects. The buildings are now ranked as the highest condition and capital replacement priority of all secondary schools in the County.
12. A costed feasibility study is being prepared to replace the buildings and provision of £10m has been included in the Children Services capital programme for 2012/13, funded from the Government's Capital Maintenance grant. It is anticipated that Policy and Resources will make a matching funding contribution from its allocation for strategic maintenance of schools. This will be a welcome improvement for school buildings estate in Havant.

Prudential borrowing for the Children's Services capital programme

13. A number of school schemes have been included in the proposed capital programme for 2011/12 to 2014/15 which will be partly funded from developers' contributions. They include new primary schools in Fleet, Andover, Waterlooville and Aldershot, together with work in Winchester and Romsey. Developers are expected to provide £29.4m towards the £34.2m cost of these schemes, with the balance to be met from the Government's capital grant allocations.
14. These schemes are mainly required to meet the growth in pupil numbers arising from localised development pressures. On the basis of current forecasts of capital payment flows, it is likely that some prudential borrowing will be required to bridge the timing gap before some of the developers' contributions are received. It is currently expected that £7.220m will need to be borrowed as bridging loans, as summarised in Table 9.
15. Most of this prudential borrowing is forecast to be required in 2011/12 and 2012/13, and it is expected to be fully repaid by 2014/15. The position will need to be kept under review, including the availability and timing of both developers' contributions and Government support, when the capital programme is considered again next year.

Table 9 – Prudential borrowing for schemes funded by developers' contributions

	2010/11	2011/12	2012/13	2013/14	2014/15	Total
	£000	£000	£000	£000	£000	£000
Borrowing	300	3,981	2,420	519	-	7,220
Repayments	-	-	-3,074	-2,107	-2,039	-7,220
Loans outstanding (cumulative)	300	4,281	3,627	2,039	-	-

Pressures on the Children's Services capital programme

16. The Executive Lead Member for Children's Services reports that there are sufficient resources to fund all schemes which need to be started in 2011/12. The position for 2012/13 and following years will be managed by moving the available resources to meet the pattern of demand for investment.

9. Culture, Communities and Rural Affairs

1. The proposed capital programme for Culture, Communities and Rural Affairs is in line with the guidelines set by Cabinet for the locally resourced capital programme, with the addition of provision in 2011/12 (£0.339m) and 2012/13 (£0.150m) for the second and third years of the programme of works at the Basingstoke Canal agreed by the Executive Member for Policy and Resources in April 2010.

10. Environment

1. The resources available to fund the Environment capital programme are summarised in Table 10.

Table 10 – Environment capital programme – resources available

	2011/12	2012/13	2013/14	2014/15	Total
	£000	£000	£000	£000	£000
Government support:					
Local transport plan grant	30,815	30,214	29,036	30,591	120,656

	2011/12	2012/13	2013/14	2014/15	Total
	£000	£000	£000	£000	£000
Local resources:					
Prudential borrowing for					
Project Resilience	10,000	10,000	10,000	10,000	40,000
Guideline programme	6,008	5,847	5,847	5,847	23,549
less virements to revenue					
- winter maintenance	-648	-648	-648	-648	-2,592
- to fund the financing costs					
of prudential borrowing					
for Project Resilience	-348	-1,044	-1,740	-2,436	-5,568
Total local resources	15,012	14,155	13,459	12,763	55,389
Total resources	45,827	44,369	42,495	43,354	176,045

2. The Executive Member for Environment proposes adjusting the starts programmes for each year to make sure that the resultant expenditure flows fully use the resources available. These adjustments are summarised in Table 11.

Table 11 – Environment’s proposed capital programme

	2011/12	2012/13	2013/14	2014/15	Total
	£000	£000	£000	£000	£000
Resources available (as Table 10)	45,827	44,369	42,495	43,354	176,045
Phasing of starts programmes to match funding available	-681	+476	+2,210	-971	+1,034
Proposed programme	45,146	44,845	44,705	42,383	177,079

3. The programme includes £10m per annum for Project Resilience for the structural maintenance of highways, to be funded by efficiency savings which will cover prudential borrowing costs, as agreed by Cabinet in May 2010.
4. The proposed four-year programme also includes schemes wholly or partly funded by developers' or other contributions totalling £24.7m, including £8.6m in 2011/12. Schemes have only been named where there is reasonable confidence in the security of funding and programme dates.

Major transport schemes

5. There are no new major transport schemes proposed in the 2011/12 to 2014/15 programme.

Household waste recycling centres

6. The Environment capital programme includes provision in the 2012/13 programme for the relocation of the Waterlooville Household Waste Recycling Centre at a cost of £0.9m.

11. Policy and Resources

1. The allocation of the proposed Policy and Resources capital programme between schemes is largely based on the priorities in the existing programme. The main corporate priority continues to be the maintenance of the core buildings in the County Council's built estate, through the capital repairs programme. It supports the delivery of services countywide and specifically aims to address the priorities identified in the Corporate Risk Assessment. This ensures that key structural, health and safety and sustainability issues are addressed.

Business units

2. An annual allocation of £1.0m has been included in the proposed capital programme to purchase vehicles for Hampshire Transport Management. HTM began purchasing new vehicles, instead of leasing them, in 2009/10. This generates a saving of around 4% annually and benefits customers through reduced hire charges. The capital cost will be met initially by prudential borrowing which will be repaid from HTM's charges to customers.
3. The proposed programme for 2011/12 includes £1.56m for the IT Hosted Schools Solution project. This involves the design and delivery of the entire ICT estate at individual schools, including the provision of equipment. A successful pilot was carried out during 2010/11 at a primary school and a secondary school. It is intended to extend the pilot across several schools in 2011/12 and it could potentially be taken up by a significant number of Hampshire schools. The £1.56m covers the initial capital investment and it will be funded by prudential borrowing. The ongoing management element of the service will be covered by IT Services' trading account and funded by customer charges, together with the financing costs of the prudential borrowing.

Advance and advantageous land

4. The proposed provision for advance and advantageous purchases of land is £0.65m in each year from 2011/12 to 2014/15.

12. Conclusions

1. Regular reports will be made during the year on the implementation of the programme, including the progress of major projects, the level of capital expenditure and resources in 2011/12 and the progress on obtaining the capital receipts necessary to finance the capital programme.
2. As agreed by Cabinet in December 2010, a medium term review of the capital programme will be undertaken over the next few months for future consideration by the Leader and Cabinet in June/July 2011, as part of the Medium Term Financial strategy for 2012/13 and beyond. This will consider the forecast levels of capital receipts, prudential borrowing protocols, other financing models including how private finance could be leveraged into future infrastructure planning and how existing assets could be developed to create new service opportunities.

RECOMMENDATIONS

That:

1. the capital programme for 2011/12 and the provisional programmes for 2012/13, 2013/14 and 2014/15 be approved as set out in the attached capital programme document and subject to the conditions set out in section B.3 of the County Council's Financial Procedures on the responsibilities for managing the capital programme and, where appropriate, to the approval of the Executive Member for Policy and Resources to proposals by Executive members to retain more than a 25% share of capital receipts
2. expenditure on preliminary design and planning work for major transport schemes be permitted when they have achieved a place in the County Council's Local Transport Plan, subject to the cost being met within existing Government allocations
3. authority be given to incur expenditure on land purchases as follows:
 - (a) up to the sum specified in respect of sites still required for the schemes included in the capital programme for the period 2011/12 to 2014/15 provided that the relevant scheme has been the subject of a feasibility or design project appraisal approved by the relevant Executive member
 - (b) up to the amount included in the programmes for 2011/12 to 2014/15 in respect of advance and advantageous land purchases.

Section 25 report, Local Government Act 2003

1. Section 25 of the Act requires the Chief Financial Officer (the County Treasurer) to report to the County Council when setting its council tax on:
 - the robustness of the estimates included in the budget
 - the adequacy of the financial reserves in the budget.
2. The County Council is required to have regard to this report in approving the budget and council tax. It is appropriate for this report to go first to Cabinet and then made available to the County Council in making its final decision.
3. The CIPFA guidance on reserves and balances provides the general framework for considering the adequacy of reserves. A risk assessment has been made of the cost and demand pressures on budgets, insurance liabilities, achievement of budget savings and adverse winter conditions which support the proposed level of balances of approximately £18m. This assessment is set out as an Annex to the Appendix.
4. Similarly the level of reserves is scrutinised each year and the protocol on the purpose, use, control and review of each reserve has been agreed. Schools have one of the largest reserves at a projected £36.8m supporting their delegated budgets funded by ring-fenced specific grant. The most important reserves for other services in terms of the medium term view are the grant equalisation reserve (used to help match grant loss), the equal pay reserve, corporate efficiency reserve and the insurance reserve.
5. Section 25 concentrates primarily on the uncertainty within the budget year rather than the greater uncertainties in future years. However future uncertainties, particularly for the County Council as a 'floor' authority also inform the need for reserves and balances in the medium term. The current financial position involving significant savings targets increases the risk of overspending, together with demand led spending pressures during a recession and potentially higher inflation.
6. The budget report is the conclusion of a detailed process of prior consultation and consideration through out the current year by Cabinet.
7. The County Council's policy on balances is to hold a minimum prudent level which on the basis of 2011/12's risk assessment is 2.5% of net expenditure. This is a level which is comparable with the last three years, and remains relatively low compared with other equivalent local authorities. The risks associated with being a floor authority and thus receiving the biggest reduction in government grant and of needing to achieve significant savings in service expenditure to balance the budget continue to justify this level of reserves. The risks associated with the achievement of budgeted savings have increased significantly this year, though partly offset by reduced risk of recessionary impacts on the County Council
8. The level of uncertainty for the budget year is narrowed down as the budget strategy is developed during the year and defined in the performance and risk management and earmarked reserves paragraphs in the budget report.
9. In setting the budget the County Council should have regard to the strategic, operational and financial risks facing the County Council. The County Council has an overall risk management framework which covers these issues. The forward

budget plan and reserves take into account the main risks and uncertainties, including:

- Inflation
 - a pay freeze has operated in 2010/11 and the budget assumes a continuing pay freeze in 2011/12 and 2012/13 on the basis set out by the Chancellor of the Exchequer in the Emergency Budget in June 2010.
 - price inflation has been set at 2.5%. Given the sharp increase in both the retail and consumer price indices during the last year, containing price increases at an average 2.5% may prove challenging, depending upon market factors.
 - short-term interest rates have been budgeted to average 1.3% in 2011/12, 0.8% above the current base rate, as an upward movement in base rate is expected to begin during 2011/12.
- Pay drift
 - increments are not budgeted for and services will need to secure efficiency savings to offset these. Past trends suggest that this can be managed.
 - there is a substantial potential liability from equal pay claims arising from the pay and benefits review. None of the claims has yet been considered by the employment tribunal and an equal pay reserve estimated at £47.1m at 31 March 2011 has been built up for non-school claims. School balances will assist in meeting claims in respect of school-based staff. An application for a capitalisation direction will be made in 2011/12 to protect against the risk of successful claims exceeding the capacity to fund them from the relevant reserves. A settlement in excess of this figure will require a capitalisation direction to enable the revenue impact to be phased over more than one financial year in order to avoid compensating job or service cuts, though there is no guarantee that the Government will provide an adequate capitalisation direction. The Government has also taken steps to assist local authorities to spread these costs by introducing regulations which allow the effect of accruals for equal pay liabilities to be disregarded for council tax setting purposes.
- Employer contributions to the Hampshire Local Government Pension will remain at their current level for the three year period, 2011/12 to 2013/14, equivalent to 19.1% of pensionable pay, following the actuarial review at 31 March 2010.
- Savings and redeployments built in to the budget
 - The savings required in 2011/12 are on a significantly larger scale than in recent years. These will be subject to rigorous review by Executive Members and by the Cabinet, and savings plans will need to be approved and monitored during the course of the year.

- Efficiency savings and other savings
 - The 2011/12 and 2012/13 provisional budgets approved by the County Council in February 2010 included a corporate efficiency target of £15m per annum. Advance savings were achieved in 2010/11 and are budgeted to be achieved in 2011/12, enabling £7.4m to be transferred to the corporate efficiency reserve in 2011/12.
- Income
 - there is an annual review to maximise income and increase income at least in line with costs which is referred to in paragraph 5 of the report and was reported in greater detail to executive members
- Achievement of budget plan
 - There is a well established and sound history of very close achievement of outturn to budgets, and though Children's Services are predicting an overspending in 2010/11, this is the result of the scale of in year grants made by the Department for Education.
- Strength of financial information and reporting arrangements
 - budget monitoring and control is well established, particularly in reporting and taking action over the second half of the financial year. Corporate co-ordination of budget monitoring focuses on demand led budgets, overall employee budgets and the achievement of planned savings.
 - other action plans have been put in place to consolidate and improve financial controls.
- Capital programme
 - capital strategy, asset management plans and the local transport plan have all previously been accredited with the highest scores in the former comprehensive performance assessment.
 - the slow down of the property market produced a temporary shortfall of capital financing resources in 2008/09 and 2009/10. Additional revenue contributions to capital were made in both in 2008/09 and 2009/10 and allowance has been made in the budget for additional temporary unsupported borrowing to cover the delay in achieving planned disposals.
 - the Government's decision to provide support for capital schemes from 2011/12 solely by means of capital grant removes the problem of support through the formula grant system for borrowing allocations being ineffective, because of the damping of formula grant.
- Level of borrowing and outstanding debt
 - the issues are fully covered in the treasury management strategy and prudential indicators appendix to the budget report.
 - the current policy on temporary unsupported borrowing for specific projects results in the financing costs being contained within the

forward budget plan cash limits without an additional impact on the council tax payer.

- despite much lower capital receipts than originally planned since 2008/09, it has been possible to avoid the need for temporary unsupported borrowing to cover a general shortfall in capital financing resources.
- Contingent Liabilities
 - the County Council self-insures, so it finances all its own liability claims. The liabilities are uncertain but to cover these a provision is maintained for known liability claims and a reserve is maintained to deal with fluctuations in liabilities and in the level of fire damage reinstatement, which now stands at £11.9m.
- Annual Governance Statement
 - the Treasurer has the responsibility for ensuring that an effective system of internal financial control is maintained and operated in connection with the resources concerned.
 - the review of the effectiveness of the system of internal financial control is informed by the work of the managers within the County Council, by internal audit and the Audit Commission in its annual governance report and other reports.
 - the Audit Committee receives and reviews the annual governance statement and the external audit governance report.
- Audit Commission
 - gave an unqualified opinion on the 2009/10 accounts, and an unqualified opinion on the County Council's arrangements to secure economy, efficiency and effectiveness in its use of resources in 2009/10.
- Other risks
 - there are potential legal claims outstanding and other possible risks which past trends suggest can be met from balances if required. There is no known significant risk or liability which requires a provision, contingency or reserve not already allowed for in the budget report.
 - changes in function and funding arrangements. The main risk relates to the arrangements for transferring funding from the County Council in respect of central services to schools, as schools opt for Academy status. The loss has been allowed for in the 2011/12 budget without assuming any offsetting savings will necessarily arise in 2011/12.
 - though government grants have been confirmed for the next two years, the County Council's formula grant calculated from the formula is still £19.3m (10.4%) below the grant floor in 2011/12. The policy on the use of the grant equalisation reserve has provided mitigation against grant loss in previous years, but the contribution reaches its peak in 2011/12 and 2012/13.

10. Provided that the County Council considers the above factors and accepts the budget recommendations, including the level of earmarked reserves and balances, a positive opinion can be given under Section 25 on the robustness of the estimates and level of reserves.

Carolyn Williamson
County Treasurer
1 February 2011

2011/12 – Risk assessment of General Balances

	£m	%	£m	Comments
Inflation pay	332.7	-	-	Low risk of pay freeze assumption not holding in 2011/12
Non-pay	623.1	1.0	6.2	Allowance for higher non pay inflation, but with potential for absorption within the cash limit
Income	-196.4	-1.25	2.4	Risk of resistance to income generation assumption
Interest rates	28.8	2.0	0.6	Short-term interest rates may increase in 2011/12 above current levels, but the majority of interest costs relate to long term fixed rate borrowing and are mitigated by contingency provision
Demand led budgets	306.3	6.0	18.4	Allows for potential for absorption within cash limit
Insurance liabilities	4.8	25.0	1.2	
Achievement of cashable savings	62.9	10.0	6.3	Risk increased by scale of savings targeted but mitigated by risk contingency within budget
Winter maintenance	4.1	25.0	1.0	Risk of higher spending than the four year average borne from balances
			36.1	
Less likelihood of worst cases coinciding		50.0	-18.1	
Proposed target balances			18.0	

Appendix 2**Treasury Management Strategy Statement and Investment Strategy 2011/12 to 2013/14****1 Summary**

- 1.1 The Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Treasury Management Code) and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators on an annual basis. The TMSS also incorporates an Investment Strategy as required under Communities and Local Government's (CLG) Investment Guidance.
- 1.2 CIPFA has defined Treasury Management as:
"The management of the organisation'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."
- 1.3 The Council is responsible for its treasury decisions and activity. No treasury management activity is without risk. The successful identification, monitoring and control of risk are an integral element to treasury management activities and include Credit and Counterparty Risk, Liquidity Risk, Market or Interest Rate Risk, Refinancing Risk, and Legal and Regulatory Risk.
- 1.4 The strategy takes into account the impact of the Council's Revenue Budget and Capital Programme on the Balance Sheet position, the current and projected Treasury position (Annex B), the Prudential Indicators and the outlook for interest rates (Annex C).
- 1.5 As per the requirements of the Prudential Code, the Council has adopted the CIPFA Treasury Management Code at its meeting in February 2010. The Council has incorporated the changes from the revised CIPFA Code of Practice (November 2009) into its treasury policies, procedures and practices.
- 1.6 All treasury activity will comply with relevant statute, guidance and accounting standards.
- 1.7 The treasury management strategy has been reviewed in the light of the appointment of treasury management advisers, Arlingclose, by the County Treasurer, for the Council. The strategy for borrowing previously focused on the new capital financing requirements of the capital programme and the replacement of maturing loans. Going forward the intention is to take a more active approach to managing the portfolio of existing borrowing looking for opportunities which may arise in an environment of changing interest rates to refinance some borrowing to offer improved revenue costs of capital financing. Consequently, the prudential indicators related to borrowing limits have been reviewed to set reasonable upper limits and yet enable flexibility within delegated powers for the County Treasurer to secure opportunities which do arise.
- 1.8 The strategy reflects the changed capital financing environment for the Council with the move to capital grant from supported borrowing. It is necessarily reflecting the proposal to the Council to approve the capital programme for

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2011/12 only and as a planning framework for the forward three years pending the detail of the capital settlement. The settlement is likely to trigger a review of the forward capital programme and thus the capital financing requirements.

1.9 The prudential indicators which are all covered in this report are:

- incremental impact of capital investment decisions
- ratio of financing costs to net revenue stream
- authorised limit
- operational boundary
- upper limit for fixed interest rate exposure
- upper limit for variable interest rate exposure
- maturity structure of fixed rate borrowing
- upper limit for total principal sums invested over 364 days.

1.10 A glossary of terms is provided in Annex F.

1.11 **This Appendix recommends to the County Council that:**

- **The Treasury Management and Investment Strategies for 2011/12, although this would also be adopted for the rest of 2010/11, be approved (Borrowing and Debt Rescheduling - Section 3, Investments - Section 4).**
- **The Prudential Indicators be approved – (NB: the Authorised Limit is a statutory limit) – Annex A.**
- **The Minimum Revenue Provision (MRP) Statement be approved – Section 6.**
- **The use of Specified and Non-Specified Investments be approved – Annexes D & E.**
- **Approval be given to the monitoring and reporting arrangements as set out in Section 7, in particular the new arrangements for the Audit Committee to challenge and scrutinise the treasury management activity per the revised CIPFA requirements.**

2 Balance Sheet and Treasury Position

2.1 The underlying need to borrow for capital purposes, as measured by the Capital Financing Requirement (CFR), together with Balances and Reserves, are the core drivers of Treasury Management Activity. Table 1 analyses the movement in the CFR. Table 2 summarises the borrowing requirement for capital purposes. Both are based on the proposed Revenue Budget and Capital Programme.

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Table 1: Capital financing requirement

	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
Capital financing requirement at the beginning of the year:			
County Council	718.0	735.9	731.5
Managed on behalf of external bodies	37.2	35.4	33.8
	755.2	771.3	765.3
New borrowing (as per para. 2.4)	39.1	16.9	11.8
Street Lighting PFI	24.1	30.2	31.4
Repayment from revenue account and external bodies based on the minimum revenue provision	-27.4	-27.4	-26.4
Capital repayment on Waste Management contract	-3.7	-4.0	-4.4
Capital repayment on Street Lighting PFI	-2.2	-2.2	-2.3
Special capital repayments arising from repayment of prudential borrowing	-13.8	-19.5	-13.7
Capital financing requirement at year end	771.3	765.3	761.7

Appendix 2

Table 2: Borrowing requirement for capital purposes

	31/03/2011 Estimate £m	31/03/2012 Estimate £m	31/03/2013 Estimate £m	31/03/2014 Estimate £m
Total Capital Financing Requirement	755.2	771.3	765.3	761.7
Less: Existing Profile of Borrowing	-356.0	-351.0	-347.0	-341.0
Other Long Term Liabilities	-96.5	-114.7	-138.7	-163.5
Cumulative Maximum External Borrowing Requirement	302.7	305.6	279.6	257.2
Less: Balances & Reserves	-182.9	-142.4	-128.7	-128.2
Cumulative Net Borrowing Requirement/ (Investments)	119.8	163.2	150.9	129.0

- 2.2 The Council's level of physical debt and investments is linked to these components of the Balance Sheet. The current portfolio position is set out at Annex B. Market conditions, interest rate expectations and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position. The Council will ensure that net physical external borrowing (i.e. net of investments) will not exceed the CFR other than for short term cash flow requirements.

Estimates of capital expenditure

- 2.3 It is a requirement of the Prudential Code to ensure that capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax.

Table 3: Capital Expenditure

Capital Expenditure	2009/10 Actual £m	2010/11 Estimate £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
Total	167.6	185.3	189.0	177.9	136.6

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Capital expenditure is expected to be financed as follows:

Table 4: Capital Resources

Capital Financing	2010/11 Estimate £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
Capital receipts	13.1	31.1	26.8	12.7
Grants and other income	83.2	106.9	127.2	100.1
Revenue contributions	30.4	25.7	26.5	25.7
Contributions from reserves	3.3	0.0	0.0	0.0
Total Financing	130.0	163.7	180.5	138.5
Supported borrowing	54.9	21.9	2.0	0.0
Prudential borrowing	8.7	17.2	14.9	11.8
Less: repayments from capital receipts, etc.	-8.3	-13.8	-19.5	-13.7
Total Funding	55.3	25.3	-2.6	-1.9
Total Financing and Funding	185.3	189.0	177.9	136.6

- 2.4 Based on the capital expenditure plans set out in paragraph 2.3, the CFR is forecast to increase from £755.2m at 1 April 2011 to £761.7m at 31 March 2014, as set out in paragraph 2.1.
- 2.5 The capital financing requirement represents capital expenditure which has not been financed from capital receipts, the revenue budget, capital grants or external contributions. This can be financed either from external borrowing or by borrowing from internal balances. It includes the capital investment in respect of the Street Lighting PFI and Waste Management contract.
- 2.6 The Provision for the repayment of debt is charged to the revenue account based on a Minimum Revenue Provision (MRP), in most cases based on 4% of the capital financing requirement. The Council's policy on MRP to repay debt is covered in Section 6.

Appendix 2

- 2.7 Table 5 analyses the capital financing requirement between borrowing supported by the Government through the formula grant system and prudential borrowing. In normal circumstances, the focus of the County Council's consideration of the affordability of borrowing for capital purposes would be focussed on the level of prudential borrowing, as increases in the cost of supported borrowing from additional Government borrowing allocations would be matched by additional formula grant. However, this is not currently the case as the County Council's grant is determined by the criteria for setting a 'grant floor' rather than the formula itself.

Table 5: Capital financing requirement between supported and prudential borrowing

At 31 March	2010 Actual £m	2011 Estimate £m	2012 Estimate £m	2013 Estimate £m	2014 Estimate £m
Supported borrowing:-					
- County Council	496.6	531.0	530.4	510.7	489.9
- Other bodies	38.9	37.1	35.4	33.8	32.1
- Waste Contract	85.5	82.0	78.3	74.3	70.0
- Street Lighting PFI	0.0	14.5	36.4	64.4	93.5
Prudential borrowing	93.9	90.6	90.8	82.1	76.2
TOTAL	714.9	755.2	771.3	765.3	761.7

- 2.8 Table 6 analyses the prudential element of the capital financing requirement between categories.

Appendix 2

Table 6 analyses the prudential element of the capital financing requirement between categories.

At 31 March	2010 Actual £m	2011 Estimate £m	2012 Estimate £m	2013 Estimate £m	2014 Estimate £m
Schemes to be financed from savings in the revenue budget and capital programme	42.9	40.3	48.7	57.5	62.5
Temporary borrowing on specific projects to be repaid from capital receipts / developer contributions	49.8	43.4	33.9	16.8	6.2
Trading unit capital investment financed from future charges	1.2	6.9	8.2	7.8	7.5
TOTAL	93.9	90.6	90.8	82.1	76.2

2.9 The proposals for prudential borrowing in 2011/12 and subsequent years are the result of the application of the County Council's policy on the use of prudential borrowing under the Prudential Code. Projects fall within four categories contained in the policy:-

- borrowing over a period of up to 10 years on an 'invest to save' basis where the capital project is expected to generate cash savings, increased income or the avoidance of otherwise unavoidable costs, which will enable the service's revenue cash limit to be reduced in order to accommodate the financing costs within the budget;
- temporary prudential borrowing pending the availability of capital receipts, grants or contributions, which will enable the borrowing to be repaid, including any interest costs not met from within the service revenue budget. Prudential borrowing has been incurred on a number of school projects in advance of capital receipts or developer contributions and in respect of other reinvestment projects. The County Council's policy requires service budgets to cover interest costs and minimum revenue provision from the revenue budget rather than rolling it up to be financed from the eventual capital receipt;

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- use of prudential borrowing to finance business unit capital expenditure where the financing costs will be recovered in charges made to users and met from their existing budgets. IT Services' use of prudential borrowing was approved in accordance with this policy.

Incremental Impact of Capital Investment Decisions:

- 2.10 As an indicator of affordability the table below shows the impact of capital investment decisions on Council Tax. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved capital programme with an equivalent calculation of the revenue budget requirement arising from the proposed capital programme.

Table 7: Incremental impact on Council Tax

Incremental Impact of Capital Investment Decisions	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate
	£	£	£
Borrowing costs	0.51	2.20	1.71
Running expenses and revenue contributions to capital	0.71	1.07	0.79
Increase in Band D Council Tax	1.22	3.27	2.50

- 2.11 The indicator has been calculated as if the impact of financing new capital investment by borrowing falls entirely on the Council Tax. As Government support is now all in the form of capital grant, all of the additional borrowing costs comprise prudential borrowing. The new prudential borrowing proposed will be matched by an equivalent reduction in current expenditure within the relevant service or will be covered from future capital receipts, grants or contributions.
- 2.12 The estimate for interest payments and Minimum Revenue Provision for the repayment of debt in 2011/12 is £64.0m and for interest receipts is £0.75m. The ratio of financing costs to the Council's net revenue stream is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs. The ratio is based on costs net of investment income.

Table 8: Ratio of financing costs to net revenue stream

Ratio of Financing Costs to Net Revenue Stream	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate
	%	%	%
Total	8.84	9.41	9.37

Appendix 2**3 Borrowing and Rescheduling Strategy**

- 3.1 The Council's balance of actual external debt at 31 December 2010 (gross borrowing plus other long-term liabilities) is shown in Annex B. This prudential indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.
- 3.2 The Authorised Limit sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) and is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit). The authorised limits for 2011/12 and beyond have been increased to provide the Council with maximum policy flexibility.

Table 9: Authorised Limit for external debt

Authorised Limit for External Debt	2010/11 Estimate	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate
	£m	£m	£m	£m
	780	860	850	850

- 3.3 The Operational Boundary links directly to the Council's estimates of the CFR and estimates of other cashflow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit. The operational boundaries for 2011/12 and beyond have been increased to provide the Council with maximum policy flexibility.

Table 10: Operational Boundary for external debt

Operational Boundary for External Debt	2010/11 Estimate	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate
	£m	£m	£m	£m
	660	780	770	770

- 3.4 The County Treasurer has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next meeting of the Council.
- 3.5 The Council will keep under review the following borrowing options:
- PWLB loans
 - Borrowing from other local authorities
 - Borrowing from institutions such as the European Investment Bank and directly from Commercial Banks
 - Borrowing from the Money Markets
 - Local authority stock issues

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- Local authority bills
- Structured finance.

3.6 On 20 October 2010, the Comprehensive Spending Review (CSR) increased the cost of new local authority fixed rate loans to 1% above the cost of the Government's borrowing. However, the PWLB remains an attractive source of borrowing, given the transparency and control that its facilities continue to provide. The types of PWLB borrowing that are considered appropriate for a low interest rate environment are:

- Variable rate borrowing
- Medium-term Equal Instalments of Principal (EIP) or Annuity Loans
- Long-term Maturity loans, where affordable.

Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimise borrowing costs over the medium to longer term and maintaining stability. The differential between debt costs and investment earnings, despite long term borrowing rates being at low levels, remains acute and this is expected to remain a feature during 2011/12. The "cost of carry" associated with medium- and long-term borrowing compared to temporary investment returns means that new fixed rate borrowing could entail additional short-term costs. The use of internal resources in lieu of borrowing may again, in 2011/12, be the most cost effective means of financing capital expenditure.

3.7 PWLB variable rates are expected to remain low as the Bank Rate is maintained at historically low levels for an extended period. Exposure to variable interest rates will be kept under regular review. Each time the spread between long-term rates and variable rates narrows by 0.50%, this will trigger a formal review point and options will be considered and decisions taken on whether to retain the same exposure or change from variable to fixed rate debt.

3.8 The rationale for rescheduling would be one or more of the following:

- Savings in interest costs with minimal risk
- Balancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

As opportunities arise, these will be considered by the County Treasurer's staff.

3.9 Borrowing and rescheduling activity will be reported to the Council.

3.10 The following Prudential Indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The upper limits for both fixed and variable rate exposure are based on the Operational Boundary and have been set to give the Council maximum policy flexibility. The limits have been changed to enable the potential for a refinancing from, e.g., variable to fixed rate borrowing.

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Table 10: Upper limits for fixed and variable interest rate exposure

	2010/11 Estimate £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
Upper Limit for Fixed Interest Rate Exposure	420	780	770	770
Upper Limit for Variable Interest Rate Exposure	420	780	770	770

- 3.11 The Council will also limit and monitor large concentrations of fixed rate debt needing to be replaced. Limits in the following table are intended to control excessive exposures to volatility in interest rates when refinancing maturing debt, whilst providing policy flexibility.

Table 11: Upper and lower percentage limits on the maturity structure of long-term fixed-rate borrowing outstanding in 2010/11

Maturity structure of fixed rate borrowing	Existing level at 31/12/10 %	Lower Limit for 2011/12 %	Upper Limit for 2011/12 %
under 12 months	4	0	50
12 months and within 24 months	1	0	50
24 months and within 5 years	7	0	50
5 years and within 10 years	12	0	75
10 years and within 20 years	29	0	75
20 years and within 30 years	43	0	75
30 years and within 40 years	4	0	100
40 years and within 50 years	0	0	100
50 years and above	0	0	100

Appendix 2**4 Investment Policy and Strategy**

4.1 The Council's investment priorities are:

- security of the invested capital;
- liquidity of the invested capital;
- an optimum yield which is commensurate with security and liquidity.

4.2 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the CLG Guidance. Potential instruments for the Council's use within its investment strategy are contained in Annexes D and E. The Treasurer, under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the core investment portfolio will be reported to the Council.

4.3 'Specified investments' offer both high security and liquidity. All such investments should be in sterling and with a maturity of no more than a year. Such short-term investments made with the UK Government or a local authority will automatically count as specified investments. In addition, short-term sterling investments with banks and building societies with high credit ratings will count as 'specified investments'.

4.4 During the year, the Council will have surplus cash balances to allow direct long-term investment on the money markets. The Investment Strategy will provide flexibility to invest cash for periods of up to two years in order to access higher investment returns in the current low interest rate environment. All such investments would be made with reference to the outlook for the UK Bank Rate and money market rates – see Annex C.

4.5 The maximum investment limit with any single counterparty of £60m referenced in Annex D has been derived using an assumption that the maximum overall cash balance available at any one time would not exceed £300m. If the overall cash balance were to exceed this figure during 2011/12, the maximum counterparty limits would be increased by the same proportion under delegated powers of the County Treasurer.

4.6 Same-day liquidity deposits with managed AAA-rated money market funds, which are currently listed as follows (although other AAA-rated money market funds may also be used if deemed necessary):

- RBS Global Treasury Sterling Fund;
- Standard Life Sterling Fund;
- Henderson Sterling Fund;
- Ignis Sterling Fund; and
- Prime Rate Sterling Fund.

No more than £30m should be placed with any one money market fund.

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- 4.7 The Council's current level of investments of £224.84m as at 31 December 2010 is presented at Annex B.
- 4.8 In any period of significant stress in the markets, the default position is for investments to be made with the Debt Management Office or UK Treasury Bills. (The rates of interest from the DMADF are below equivalent money market rates, but the returns are an acceptable trade-off for the guarantee that the Council's capital is secure.)
- 4.9 The Council would select countries, and the institutions within them (see Annex D), for the counterparty list after analysis and careful monitoring of:
- Credit ratings (minimum long-term A+ for counterparties; AA+ for countries)
 - Credit default swaps (where quoted)
 - GDP; Net debt as a % of GDP
 - Sovereign Support Mechanisms/ potential support from a well-resourced parent institution
 - Share prices (where quoted)
 - Macro-economic indicators
 - Corporate developments, news and articles, market sentiment
- 4.10 The Council will continue to analyse and monitor these indicators and credit developments on a regular basis and respond as necessary to ensure security of the capital sums invested.
- 4.11 The UK Bank Rate has been maintained at 0.5% since March 2009, and is anticipated to remain at low levels throughout 2011/12. Short-term money market rates are likely to remain at very low levels for an extended period which will have a significant impact on investment income.
- 4.12 The Council has placed an upper limit for principal sums invested for over 364 days, as required by the Prudential Code. This limit is to contain exposure to the possibility of loss that may arise as a result of the Council having to seek early repayment of the sums invested. The limit previously was zero and has been increased to £10m for 2010/11 rising to £60m for 2011/12 to allow policy flexibility, although the maximum investment being placed with one institution will be restricted to £20m. The limit is lower for subsequent years to reflect the anticipated drawdown of Council reserves.

Table 12: Total sums invested for more than 364 days

Upper Limit for total principal sums invested over 364 days	2010/11 Approved £m	2010/11 Revised £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
	Nil	10.0	60.0	50.0	40.0

Appendix 2

As required by the Prudential Code, CLG on Local Government Investments in England requires that an Annual Investment Strategy (AIS) be set.

5 Outlook for Interest Rates

- 5.1 The economic interest rate outlook is attached at Annex C. The Council will reappraise its strategy from time to time and, if needs be, realign it with evolving market conditions and expectations for future interest rates.

6 2011/12 Minimum Revenue Provision Statement

- 6.1 The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414) place a duty on local authorities to make a prudent provision for debt redemption. Guidance on Minimum Revenue Provision has been issued by the Secretary of State and local authorities are required to “have regard” to such Guidance under section 21(1A) of the Local Government Act 2003.

- 6.2 The four MRP options available are:

- Option 1: Regulatory Method
- Option 2: CFR Method
- Option 3: Asset Life Method
- Option 4: Depreciation Method

NB This does not preclude other prudent methods.

- 6.3 MRP in 2011/12: Options 1 and 2 may be used only for supported capital expenditure. Methods of making prudent provision for self financed expenditure include Options 3 and 4 (which may also be used for supported capital expenditure if the Council chooses).
- 6.4 The MRP Statement will be submitted to the Council before the start of the 2011/12 financial year. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement should be put to the Council at that time.
- 6.5 The Council will apply Option 1/Option 2 in respect of supported capital expenditure and Option 3/Option 4 in respect of prudential capital expenditure.

And

MRP in respect of leases brought on Balance Sheet under the IFRS-based Code of Practice will match the annual principal repayment for the associated deferred liability.

- 6.6 Option 3/Option 4 is particularly relevant from 2011/12 as any new borrowing is expected to be largely prudential.

Appendix 2**7 Monitoring and Reporting on the Treasury Outturn and Prudential Indicators**

Treasury activity is monitored quarterly and reported internally to the County Treasurer. The Prudential Indicators which are summarised at Annex A will be monitored through the year by the Treasurer.

The County Treasurer will report to the Council on treasury management activity / performance and Performance Indicators as follows:

- (a) a mid-year and year end review of treasury activity against the strategy approved for the year
- (b) The Council will produce an outturn report on its treasury activity no later than 30 September after the financial year end
- (c) The Audit Committee will be responsible for the new responsibility to challenge and scrutinise the treasury management activity and practices.

8 Other Items**Training**

CIPFA's Code of Practice requires the responsible officer, which is the County Treasurer, to ensure that all members tasked with treasury management responsibilities, including challenge and scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities.

Initial overview training sessions for all Councillors and the Audit Committee were held during 2010/11. Further training will be developed with Councillors over the coming year particularly to support the Audit Committee role, although this will be open to all Councillors to attend.

The training needs of the Council's treasury management staff are subject to regular review.

Investment Consultants

The County Treasurer uses Arlingclose Ltd as external treasury advisers for information, advice and assistance relating to borrowing and investment.

Appendix 2 – Annex A

Summary of prudential indicators and treasury management indicators		2009/10 Actual	2010/11 Estimate	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate
Prudential indicators for capital expenditure						
Capital expenditure	£m	167.6	185.3	189.0	177.9	136.6
Capital financing requirement	£m	714.5	748.0	761.9	755.7	749.2
Prudential indicators for affordability						
Ratio of financing costs to net revenue stream	%	6.70	7.35	8.84	9.41	9.37
Incremental impact of capital programme on council tax	£	n/a	4.04	1.22	3.27	2.50
Prudential indicators for prudence						
Medium-term borrowing not to exceed capital financing requirement		County Treasurer will ensure this is not breached				
Treasury management indicators for external debt						
Actual external debt	£m	512.3	n/a	n/a	n/a	n/a
Authorised limits	£m	690.0	780.0	860.0	850.0	850.0
Operational boundaries	£m	570.0	660.0	780.0	770.0	770.0
Other treasury management indicators						
Adoption of revised CIPFA Code of Practice (2009)		Agreed by County Council in February 2010				
Upper limits – fixed rates	£m	363.0	420.0	780.0	770.0	770.0
Upper limits – variable rates	£m	195.0	420.0	780.0	770.0	770.0

Appendix 2 – Annex A

Maturity structure of fixed rate borrowing	Existing level	Lower	Upper		
	at	Limit	Limit		
	31/12/10	for 2011/12	for 2011/12		
	%	%	%		
Under 12 months	4	0	50		
12 months and within 24 months	1	0	50		
24 months and within 5 years	7	0	50		
5 years and within 10 years	12	0	75		
10 years and within 20 years	29	0	75		
20 years and within 30 years	43	0	75		
30 years and within 40 years	4	0	100		
40 years and within 50 years	0	0	100		
50 years and above	0	0	100		
Upper Limit for total principal sums invested over 364 days	2010/11 Approved £m	2010/11 Revised £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
	Nil	10.0	60.0	50.0	40.0

Appendix 2 – Annex B

EXISTING PORTFOLIO PROJECTED FORWARD

	Current Portfolio at 31/12/10 £m	31 Mar 11 Estimate £m	31 Mar 12 Estimate £m	31 Mar 13 Estimate £m	31 Mar 14 Estimate £m
External Borrowing:					
Fixed Rate – PWLB	-290.0	-283.0	-278.0	-274.0	-268.0
Fixed Rate – Market	0	0	0	0	0
Variable Rate – PWLB	0	0	0	0	0
Variable Rate – Market	-73.0	-73.0	-73.0	-73.0	-73.0
Total External Borrowing	-363.0	-356.0	-351.0	-347.0	-341.0
Other long-term liabilities					
Finance Lease (Waste Contract)	-85.5	-82.0	-78.3	-74.3	-70.0
IFRS Long Term Liabilities:					
Street Lighting PFI	-5.0	-14.5	-36.4	-64.4	-93.5
Total Gross External Debt	-453.5	-452.5	-465.7	-485.7	-504.5
Investments:					
Managed in-house					
Short-term monies (Deposits / monies on call / MMFs)	224.8	190.0	120.0	120.0	120.0
Long-term investments (maturities over 12 months)	0	10.0	40.0	30.0	20.0
Total Investments	224.8	200.0	160.0	150.0	140.0
(Net Borrowing Position)/ Net Investment position	-228.7	-252.5	-305.7	-335.7	-364.5

Appendix 2 –Annex C

Arlingclose's economic and Interest Rate Forecast – January 2011

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Official Bank Rate													
Upside risk	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	0.50	0.50	0.75	1.00	1.25	1.50	2.00	2.50	2.75	2.75	3.00	3.00	3.00
Downside risk	-	-	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
1-yr LIBID													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	1.65	1.90	2.15	2.40	2.50	2.50	2.75	3.00	3.25	3.50	3.50	3.50	3.50
Downside risk	- 0.25	- 0.25	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
5-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	2.75	3.00	3.25	3.50	3.75	4.00	4.00	4.00	4.00	4.00	4.25	4.25	4.00
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
10-yr gilt													
Upside risk	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	3.90	4.00	4.10	4.25	4.50	4.75	4.75	4.75	4.75	4.75	5.00	5.00	4.75
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
20-yr gilt													
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	4.50	4.75	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.25	5.25	5.00
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
50-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	4.25	4.50	4.75	4.75	4.75	4.75	4.50	4.50	4.50	4.50	4.75	4.75	4.50
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25

- The recovery in growth is likely to be slow and uneven.
- The initial reaction to the Comprehensive Spending Review (CSR) is positive, but implementation risks remain.
- The path of base rates reflects the fragility of the recovery and the significantly greater fiscal tightening of the emergency budget. With growth and underlying inflation likely to remain subdued, the Bank will stick to its lower for longer stance on policy rates.
- Uncertainty surrounding Eurozone sovereign debt and the risk of contagion will remain a driver of global credit market sentiment.

Underlying assumptions:

- The framework and targets announced in the CSR to reduce the budget deficit and government debt will be put to the test; meeting the 2010 borrowing target of £149 billion will be crucial to the gilt market's confidence in the credibility of the deficit reduction plans.
- Despite money supply being weak and growth prospects remaining subdued, the MPC have gravitated towards increasing rates in the new year as global inflation continues to rise along with household inflation.
- Consumer Price Inflation is stubbornly above 3% and is likely to spike above 4% in the first quarter of 2011 as a result of VAT, utilities and rail fare increases.

Appendix 2 Annex C

- Unemployment remains near a 16 year high, at just over 2.5 million, and is set to increase as the public sector shrinks. Meanwhile employment is growing but this is mainly due to part time work, leaving many with reduced income.
- Recently announced Basel III capital/liquidity rules and extended timescales are positive for banks. Restructuring of UK banks' balance sheets is ongoing and expected to take a long time to complete. This will be a pre-condition for normalisation of credit conditions and bank lending.
- Mortgage repayment, a reduction in net consumer credit and weak consumer confidence are consistent with lower consumption and therefore the outlook for growth.
- The US Federal Reserve downgraded its outlook for US growth; the Fed is concerned enough to signal further QE through asset purchases. Industrial production and growth in the Chinese economy are showing signs of slowing. Both have implications for the global economy.

Specified Investments

Specified Investments identified for use by the Council

Specified Investments will be those that meet the criteria in the CLG Guidance, i.e. the investment

- is sterling denominated
- has a maximum maturity of 1 year
- meets the “high credit quality” as determined by the Council or is made with the UK government or is made with a local authority in England, Wales, Scotland or Northern Ireland or a parish or community council.
- the making of which is not defined as capital expenditure under section 25(1)(d) in SI 2003 No 3146 (i.e. the investment is not loan capital or share capital in a body corporate).

“Specified” Investments identified for the Council’s use are:

- Deposits in the DMO’s Debt Management Account Deposit Facility
- Deposits with UK local authorities
- Deposits with banks and building societies
- Gilts: (bonds issued by the UK government)
- Bonds issued by multilateral development banks, e.g., European Investment Bank, World Bank
- Treasury-Bills (T-Bills)
- Local Authority Bills (LA Bills)
- AAA-rated Money Market Funds

For credit rated counterparties, the minimum criteria will be the lowest equivalent short-term and long-term ratings assigned by Fitch, Moody’s and Standard & Poor’s (where assigned).

Long-term minimum: A+(Fitch); A1 (Moody’s); A+ (S&P)

Short-term minimum: F1 (Fitch); P-1 (Moody’s); A-1 (S&P)

The Council will also take into account information on corporate developments of and market sentiment towards investment counterparties.

Appendix 2 Annex D

Country/ Domicile	Counterparty	Maximum Counterparty Limit £m
UK	NatWest	60
UK	Lloyds TSB	60
UK	Barclays Bank Plc	60
UK	HSBC Bank Plc	60
UK	Nationwide Building Society	60
UK	Clydesdale Bank	30
UK	Santander UK Plc	30
UK	Standard Chartered Bank	30
Australia	Australia and NZ Banking Group	10
Australia	Commonwealth Bank of Australia	10
Australia	Westpac Banking Corp	10
Canada	Bank of Montreal	10
Canada	Bank of Nova Scotia	10
Canada	Canadian Imperial Bank of Commerce	10
Canada	Royal Bank of Canada	10
Canada	Toronto-Dominion Bank	10
Finland	Nordea Bank Finland	10
France	BNP Paribas	10
France	Credit Agricole CIB (Credit Agricole Group)	10
France	Credit Agricole SA (Credit Agricole Group)	10
France	Société Générale	10

Appendix 2 –Annex D

Country/ Domicile	Counterparty	Maximum Counterparty Limit £m
Germany	Deutsche Bank AG	10
Netherlands	ING Bank NV	10
Netherlands	Rabobank	10
Sweden	Svenska Handelsbanken	10
Switzerland	Credit Suisse	10
US	JP Morgan	10

Please note this list could change if, for example, a counterparty/country is upgraded, and meets our other creditworthiness tools. Alternatively if a counterparty is downgraded, this list may be shortened.

Appendix 2 Annex E

Non-Specified Investments determined for use by the Authority

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Authority's use:

	In-house use	Use by fund managers	Maximum maturity
Deposits with banks and building societies	✓		2 years
CDs with banks and building societies	✓	✓	
Gilts			
Bonds issued by multilateral development banks	✓ (on advice from treasury advisor)		
Bonds issued by financial institutions guaranteed by the UK government			
Sterling denominated bonds by non-UK sovereign governments		✓	
Government guaranteed bonds and debt instruments issued by corporate bodies	✓	✓	
Non-guaranteed bonds and debt instruments issued by corporate bodies	✓	✓	

In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.

Glossary of Treasury Terms

Balances and Reserves	Accumulated sums that are maintained either earmarked for specific future costs or commitments or generally held to meet unforeseen or emergency expenditure.
Bank Rate	The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". This rate is also referred to as the 'repo rate'.
Bond	A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The price of a bond may vary during its life.
Capital Expenditure	Expenditure on the acquisition, creation or enhancement of capital assets.
Capital Financing Requirement (CFR)	The Council's underlying need to borrow for capital purposes representing the cumulative capital expenditure of the local authority that has not been financed.
Capital receipts	Money obtained on the sale of a capital asset.
Cost of carry	The cost of "carrying" or holding a position. For example, if one takes out borrowing at 5% and invests the money at 2%, there is a cost of carry of 3%.
CPI	Consumer Price Index – the UK's main measure of inflation.
Credit Rating	Formal opinion by a registered rating agency of a counterparty's future ability to meet its financial liabilities; these are opinions only and not guarantees.
Corporate Bonds	Corporate bonds are bonds issued by companies. The term is often used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies.
Diversification / diversified exposure	The spreading of investments among different types of assets or between markets in order to reduce risk.
ECB	European Central Bank.
Federal Reserve	The US central bank. (Often referred to as "the Fed").
General Fund	This includes most of the day-to-day spending and income.
Government Gilts	Gilts are bonds issued by the UK Government. They take their name from 'gilt-edged': being issued by the UK government, they are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity.
IFRS	International Financial Reporting Standards.

Appendix 2 Annex F

Maturity	The date when an investment or borrowing is repaid.
Maturity profile	A table or graph showing the amount (or percentage) of debt or investments maturing over a time period. The amount or percent maturing could be shown on a year-by-year or quarter-by-quarter or month-by-month basis.
Money Market Funds (MMF)	Pooled funds which invest in a range of short term assets providing high credit quality and high liquidity.
Minimum Revenue Provision	An annual provision that the Council is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets.
Non-Specified Investments	Term used in the Communities and Local Government Guidance and Welsh Assembly Guidance for Local Authority Investments. It includes any investment for periods greater than one year or those with bodies that do not have a high credit rating, use of which must be justified.
Premiums and Discounts	<p>In the context of local authority borrowing, (a) the premium is the penalty arising when a loan is redeemed prior to its maturity date and (b) the discount is the gain arising when a loan is redeemed prior to its maturity date. If on a £1 million loan, it is calculated* that a £100,000 premium is payable on premature redemption, then the amount paid by the borrower to redeem the loan is £1,100,000 plus accrued interest. If on a £1 million loan, it is calculated that a £100,000 discount receivable on premature redemption, then the amount paid by the borrower to redeem the loan is £900,000 plus accrued interest.</p> <p>PWLB premium/discount rates are calculated according to the length of time to maturity, current market rates (plus a margin), and the existing loan rate which then produces a premium/discount dependent on whether the discount rate is lower/higher than the coupon rate.</p> <p>*The calculation of the total amount payable to redeem a loan borrowed from the Public Works Loans Board (PWLB) is the present value of the remaining payments of principal and interest due in respect of the loan being repaid prematurely, calculated on normal actuarial principles. More details are contained in the PWLB's lending arrangements circular.</p>
Prudential Code	Developed by CIPFA and introduced on 01/4/2004 as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice.
Prudential Indicators	Indicators determined by the local authority to define its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators

Appendix 2 –Annex F

PWLB	Public Works Loans Board. It is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.
Quantitative Easing	In relation to the UK, it is the process used by the Bank of England to directly increase the quantity of money in the economy. It “does not involve printing more banknotes. Instead, the Bank buys assets from private sector institutions – that could be insurance companies, pension funds, banks or non-financial firms – and credits the seller’s bank account. So the seller has more money in their bank account, while their bank holds a corresponding claim against the Bank of England (known as reserves). The end result is more money out in the wider economy”. Source: Bank of England.
Revenue Expenditure	Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges.
RPI	Retail Prices Index. A monthly index demonstrating the movement in the cost of living as it tracks the prices of goods and services including mortgage interest and rent. Pensions and index-linked gilts are uprated using the RPI index.
Specified Investments	Term used in the CLG Guidance and Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than 1 year. UK government, local authorities and bodies that have a high credit rating.
Supported Borrowing	Borrowing for which the costs are supported by the government or third party.
Supranational Bonds	Instruments issued by supranational organisations created by governments through international treaties (often called multilateral development banks). The bonds carry a AAA rating in their own right. Examples of supranational organisations are the European Investment Bank, the International Bank for Reconstruction and Development.
Treasury Management Code	CIPFA’s Code of Practice for Treasury Management in the Public Services.
Temporary Borrowing	Borrowing to cover peaks and troughs of cash flow, not to fund spending.
Term Deposits	Deposits of cash with terms attached relating to maturity and rate of return (interest).
Unsupported Borrowing	Borrowing which is self-financed by the local authority. This is also sometimes referred to as Prudential Borrowing.
Yield	The measure of the return on an investment instrument.