

COMMENTARY ON REVISED DRAFT PRUDENTIAL CODE (2) – PCSG 27 02/03

INTRODUCTION

- 1 This revised draft of the Prudential Code – PCSG 27 02/23 – is the second full revision of the 2001 exposure draft of the Code and is work in progress towards the second exposure draft of the Code.
- 2 This commentary outlines the changes that have been made since the first redraft – PCSG 19 02/03 – and the reasons for the changes.
- 3 The Prudential Code Steering Group is asked to consider this second redraft.

MINUTES OF THE MEETING OF THE PCSG HELD ON 16 OCTOBER 2002

- 4 The changes agreed at the October meeting of the Steering Group have been actioned within the current redraft.

MINUTES OF THE MEETING OF THE TREASURY MANAGEMENT PANEL HELD ON 18 OCTOBER 2002

- 5 As reported to the October meeting of the PCSG, the first redraft of the Prudential Code was also taken to the October meeting of the Treasury Management Panel. The relevant minute from that meeting is attached as Appendix A to this report for information. The Panel endorsed the work of the PCSG, suggested some minor amendments and will receive the recommendations of the Steering Group for the second exposure draft in due course.

PRIMARY LEGISLATION

- 6 Since the October meeting of the Steering Group, the draft Local Government Bill for England and Wales and amendments to the Local Government in Scotland Bill that would give effect to the prudential framework have been published. The current draft has been amended to refer to these provisions and to marry in with them.
- 7 It is recommended that the PCSG asks the ODPM, National Assembly for Wales and Scottish Executive to comment on the redraft specifically from this perspective, to ensure that the second exposure draft is consistent with the latest position vis-à-vis legislation.

ROAD TESTING THE DRAFT PRUDENTIAL CODE

- 8 All local authorities that are road testing the draft Prudential Code have been asked to provide any further information under Chatham House rules by end December 2002 and authorised returns by end December 2002 if possible with a final deadline of end January 2003. All authorised returns received before the meeting will be circulated to members of the Steering Group either before or at the meeting and future responses will be circulated to members. All information provided to the Secretariat under Chatham House rules has already been taken into consideration within the current redraft.

- 9 Appendix B to this commentary report contains a letter dated 28 November 2002 to the local authorities that are road testing the draft Code, which outlines the form of the road testing, together with a copy of the proforma that road testers have been asked to complete. It should be noted that this was a road test and not a pilot. In particular, the results from authorities are based on their existing plans and commitments and do not reflect or indicate future decisions under a live prudential system. Also, the road testing was undertaken on the 2001 exposure draft of the Code, as amended in respect of the treasury management indicators by the PCSG at their July meeting.
- 10 The Steering Group is asked to consider whether any further changes are necessary to the revised Code as a result of the road testing.

CLARITY

- 11 In addition to the changes made in the first redraft, further action has been taken with respect to greater clarity within the current draft.
- 12 In line with comments made by Parliamentary Counsel and by some road testers, the Code has been restructured so that process and governance issues, and the matters to be taken into account when setting or revising prudential indicators, appear before the sections on the detailed prudential indicators for capital expenditure, external debt and treasury management. This is helpful in setting the detailed indicators within the wider context.
- 13 Within the redraft, this change to the order has been made without highlighting and all subsequent changes to the text are highlighted. This assists transparency for the changes made within the text, since if the ordering change was highlighted everything in these sections would appear as a change and detailed changes made to the text would not be apparent.

AFFORDABILITY

- 14 Following discussion at the October meeting, further work has been undertaken with the LGA on the question of affordability and the fact that the figures for individual local authorities will be very different from each other. The differences between authorities will not necessarily reflect differences in affordability between them. Significantly, there will be differences in support for capital expenditure from government.
- 15 Further work has also been undertaken on the indicator that reflects the impact of financing costs on the Council Tax, in particular with the LGA and with local authorities that are road testing the draft Code in Scotland. Thanks are due particularly to Archie Strang and Linda Hardie at South Lanarkshire Council.
- 16 A similar indicator has been introduced in respect of the impact on council rents within the HRA.

THE PRUDENTIAL CODE AND THE HRA

17 Since the October meeting of the PCSG, it has been announced that the prudential framework will apply to the HRA in Scotland. Together with previous statements made in respect of England and Wales, this means that the prudential framework will apply to the HRA throughout England, Wales and Scotland.

18 The commentary on the revised draft Prudential Code considered by the Steering Group at their July meeting (Paper PCSG 19 02/02) included the following in respect of the Prudential Code and the HRA:

“67. In order to prepare the second exposure draft of the Prudential Code, it would be extremely helpful to know:

(a) Whether it will be necessary to separate HRA and non-HRA debt. If so, then a method for local authorities to determine this on a notional and defined basis will be necessary through a means external to the Prudential Code.

(b) Whether, alternatively, the means of separating HRA and non-HRA items for the purposes of the prudential framework will be undertaken through distinguishing between HRA and non-HRA capital expenditure and the capital financing requirement. If so, then a defined basis for calculating the HRA capital financing requirement would be required.”

19 The arrangements for the HRA are matters for the UK Parliament, Welsh Assembly Government and Scottish Executive. The detailed arrangements under the prudential framework for the HRA have yet to be decided. However, officers at the ODPM, National Assembly for Wales and Scottish Executive have indicated that it will not be necessary to separate HRA and non-HRA debt, but that the means of separating HRA and non-HRA items for the purposes of the prudential framework will be undertaken through distinguishing between HRA and non-HRA capital expenditure and capital financing.

20 The following is an extract from an e-mail from Tony Anderson, ODPM, and included with his permission:

“I think you can take it that we do not envisage local authorities having separate HRA and non-HRA debt, or that they will need to designate loans specifically for HRA or non-HRA purposes. This would be a backward step, not in line with general treasury management principles (and of course not how local authorities operate anyway).

That means that we need to work out a system for calculating the HRA’s contribution to an authority’s debt costs (and, it follows, how we propose to subsidise that). My feeling is that we’ll want to build on something like the present credit ceiling framework,

perhaps along the lines of the capital financing requirement, and distinguishing between HRA and non-HRA capital expenditure.”

- 21 This enables the requirements of the Prudential Code in respect of the HRA to be included within the second exposure draft for consultation. Amendments have been made within the current draft to require HRA authorities to separate out HRA and non-HRA elements in respect of the prudential indicators for:
- estimates of the ratio of financing cost to net revenue stream
 - actual ratio of financing costs to net revenue stream
 - estimates of impact of financing costs on the Council Tax/Council Rents
 - estimates of capital expenditure
 - actual capital expenditure
 - estimates of capital financing requirement
 - actual capital financing requirement.
- 22 In each case, the separation into HRA and non-HRA elements is required to be undertaken as determined under statute. This could then be either through secondary legislation, or through a government/devolved administration code or guidance with which the authority is required to comply. It would be helpful if, once finalised, cross references between the relevant statute/regulation/code/guidance and the Prudential Code are made.

PRUDENTIAL INDICATORS FOR TREASURY MANAGEMENT

- 23 The Treasury Management Panel at their October meeting agreed with the recommendation of the Steering Group that the Prudential Code should continue to contain the current cross reference to the TM Code and in addition the prudential indicators for treasury management.
- 24 This recommendation was linked to the Steering Group’s consideration and simplification of the detailed format of the prudential indicators. Following on from road testing, the current draft contains amended indicators for treasury management for consideration by the Steering Group.
- 25 Revised text for the final paragraph of the treasury management section has been drawn from the guidance sent to all local authorities in Wales on 3 September by the Welsh Assembly Government, *The Local Authorities (Capital Finance) (Approved Investments)(Amendment)(no.2)(Wales) Regulations 2002 – Final Guidance on Longer Term Investments*.

THE PRUDENTIAL CODE AND THE TREATMENT OF RELATED ENTITIES (LOCAL AUTHORITY COMPANIES, TRUSTS, LIMITED LIABILITY PARTNERSHIPS, ETC)

- 26 The commentary on the revised draft Prudential Code considered by the Steering Group at their July meeting (Paper PCSG 19 02/03) included the following in respect of the Prudential Code and the treatment of related entities:

“71 The CIPFA/LASAAC Joint Committee is undertaking work on the consideration of group accounts in local authorities. The Joint Committee’s work programme is such that the earliest date for its consultation on group accounts is September 2003.

72 The outcome of the Joint Committee’s work will need to be incorporated within the Prudential Code in due course. However, it is suggested that the implementation of the prudential framework need not await the completion of this work.

73 The current SORP requires the preparation of summarised group accounts as supplementary information to the main accounts, where this is appropriate. Such accounts are currently prepared by few local authorities but the amounts involved can be material.”

27 The Prudential Code, as previously drafted, would require local authorities to take the implications flowing from any related entities into consideration when taking their decisions within the prudential framework. For the avoidance of any doubt on the issue, the following paragraph has been added within the revised draft:

“Where the authority has interests in companies or other similar related entities, the authority needs to have regard to its financial commitments and obligations to those companies/entities.”

and as a footnote to that paragraph:

“Local authorities with, in aggregate, material interests in subsidiary and associated companies and joint ventures, will also need to have regard to the group accounting requirements of the CIPFA/LASAAC Code of Practice on Local Authority Accounting.”

TRANSFERRED DEBT

28 Following discussions with the LGA and ODPM, the treatment of transferred debt has been further clarified within the definitions section of the revised draft.

CAPITAL FINANCING REQUIREMENT

29 Since the October meeting of the PCSG, further work has been undertaken on the capital financing requirement by the CIPFA Secretariat and through the road testing of the draft Code. Thanks are also due to Martin Easton and to Stephen Sheen who have undertaken further work in this area.

30 It is helpful to compare the capital financing requirement with, in England and Wales, the credit ceiling as calculated under the 1989 Act and, in Scotland, the amount outstanding on the loans fund as calculated under the 1975 Act.

- 31 Key differences between the capital financing requirement as defined in the 2001 exposure draft of the Prudential Code and both the credit ceiling and the outstanding balance on the loans fund relate to capital transactions where relevant accounting entries have not been put through the accounts specified in the 2001 exposure draft, ie
- fixed assets
 - deferred charges
 - fixed asset restatement reserve
 - capital financing reserve
 - government grants deferred.
- 32 Examples of such transactions include:
- some authorities have liabilities in respect of old deferred purchase/covenant schemes, where balances are separately identified on the balance sheet
 - some authorities have separately identified on their balance sheet an account titled ‘other capital contributions deferred’ that is actually a sub-set of the ‘government grants deferred’ account
 - some authorities have accounts in respect of mortgages given to third parties that are separately identified in the balance sheet.
- 33 All of these balances relate to capital transactions and it is suggested that they ought to be included within the capital financing requirement. Wording has been added within the current draft for consideration within the definitions section of the revised draft.
- 34 There are also key differences between the credit ceiling only and the capital financing reserve that relate to transactions required or allowed by statute that do not lead to items in the accounts of local authorities on their balance sheets. Examples relate to certain types of credit arrangement, and where local authorities have charged premiums to the PCL with a consequent increase in their credit ceiling. It is suggested that it is not the case that either the capital financing requirement or the credit ceiling is wrong : rather, that they are measuring slightly different but related matters, the capital financing requirement being driven by the balance sheet and the credit ceiling by detailed statute. It is recommended that no changes are made to the capital financing requirement for these differences.
- 35 At their October meeting, the PCSG considered and rejected the possibility of including pre-payments for revenue items such as premiums that are recorded as assets on the balance sheet of some local authorities within the definition of the capital financing requirement. This has been clarified within the current draft.
- 36 It is proposed that the appendix on the capital financing requirement (previously capital expenditure unfinanced) from the 2001 exposure draft of the Prudential Code be retained and expanded. Also, some of the text within the revised Code has been further clarified.
- 37 The PCSG is asked to confirm whether the term ‘capital financing requirement’ should be used within the second exposure draft or if an alternative should be used.

THE PRUDENTIAL CODE AND FRS 17

- 38 The issues that arise in respect of the Prudential Code and FRS 17 were identified within Paper PCSG 12 02/03 and have previously been discussed by the Steering Group. At their meeting in October, the Steering Group agreed to consider these issues at a future meeting, following an exploratory meeting with HM Treasury.
- 39 A separate meeting to discuss these issues was held by the Secretariat with representatives from HM Treasury, ODPM and the Audit Commission on 17 October 2002. The notes of that meeting are attached as Appendix C to this report and are intended to assist the PCSG in considering and deciding on this matter for incorporation within the second exposure draft of the Prudential Code for consultation.
- 40 In line with the recommendations of that meeting and for the consideration of the Steering Group, the current revised draft of the Prudential Code:
- (a) highlights that the revenue consequences of retirement benefits will be taken into consideration when a local authority considers the affordability of its capital plans
 - (b) excludes the pension reserve from the definition of 'other long term liabilities' for the prudential indicators in relation to external debt.

CONCLUSION

- 41 The Prudential Code Steering Group is asked to consider the second redraft of the Prudential Code.

**EXTRACT FROM MINUTES OF TREASURY MANAGEMENT PANEL 18
OCTOBER 2002**

4 PRUDENTIAL CODE FOR CAPITAL FINANCE IN LOCAL AUTHORITIES

4.1 The Chairman introduced this item. He emphasised the importance of the role of the Treasury Management Panel in relation to the Prudential Code. The Code is being developed through the Prudential Code Steering Group, which reports to the TMP. The TMP will have responsibility for recommending to the Institute that the finalised Prudential Code is appropriate for the Institute to approve. The Prudential Code will be an integral part of the statutory regulatory framework for local authority borrowing and capital investment. It is an extremely important issue for local government and for the Institute.

4.2 The Panel received presentations from Tony Knights, the Chairman of the PCSG, and Maureen Wellen, the Secretary to the PCSG on the development of the Prudential Code and the detail of its current [draft] form. The slides used in those presentations are appended to these minutes.

4.3 The following issues arose in discussion:

- there will be new responsibilities both for full Council and for the Chief Financial Officer
- the position with respect to FRS 17 needs to be finalised. This will be particularly significantly in relation to unfunded schemes
- the role of the external auditor in the new system will be important
- in relation to exposure to variable and fixed rate interest, the importance of taking the position of borrowing net of investments, as advocated in the current draft, was stressed
- international accounting developments mean that marking to market in the accounts may become a feature in the future
- most local authority borrowing is from the PWLB
- in addition to the requirements of the Prudential Code, existing safeguards that will continue are also important, for example the balanced budget requirement and the mechanism of the S114 officer's report to Council
- there will be a need to ensure both capacity and training for the operation of the new system
- future central government and devolved administration support for local government capital investment is important.

4.4 In relation to capacity and training, Tony Knights recognised the issue. He stressed that the Prudential Code builds on the good practice processes common throughout local government such as medium term plans and the adoption of the Treasury Management Code. The Prudential Code crystallises much good practice that is already going on. The Institute is making its own arrangements in respect of the provision of training for finance staff. It should also be recognised that there will be a big bonus in freeing up the expert time currently spent on the detailed capital controls, which the government has recognised are an obstacle to effective capital investment.

APPENDIX A

- 4.5 The Chairman suggested that as the Panel works through final process for the approval of the Code that it would be helpful to have assurance that the necessary training is being provided. A report to the Panel at some stage over the next 6-9 months on this would be helpful. This was agreed.
- 4.6 John Rippon stressed that issues in relation to capacity, training and the ability of public service bodies to recruit are all important. Also, the new framework will see a fundamental change from detailed regulations to greater freedoms. Periods of transition pose particular risks and there will be a need for vigilance in the early years of the new system. A mechanism is required to see how things are going so that the framework can be supplemented if necessary.
- 4.7 The Chairman commented that these issues go beyond the Code itself to the overall framework, involving in particular CIPFA, the ODPM and Audit Commission, and the equivalent bodies in the devolved administrations. It was agreed that the role of audit will be important.
- 4.8 In relation to the draft Code, the Panel had before them the revised, work in progress, draft being considered by the PCSG on 16 October. Members of the Panel commented that the right balance was being struck for example:
- the role of the elected member and the chief financial officer
 - the treasury management indicators
 - the definitions, which rely on the proper practices embedded within the local authority accounting SORP instead of detailed regulation.
- 4.9 The TMP was asked to consider, in particular, an issue with respect to the prudential indicators for treasury management. Some respondents to the first exposure draft have queried whether the indicators for treasury management would fit better in the Treasury Management Code than the Prudential Code. At their May meeting, the TMP agreed that this is a matter for the TMP to consider and that the Panel would do so at its October meeting, following further discussion at the Steering Group. The PCSG considered this matter further at their July meeting. Whilst recognising that there is a minority view that the Prudential Code should only contain a cross reference to the TM Code, the PCSG decided to recommend to the Treasury Management Panel that the Prudential Code should continue to contain the current cross reference to the TM Code and in addition the prudential indicators for treasury management. This recommendation is linked to their consideration and simplification of the detailed format of the prudential indicators for treasury management. The TMP approved the recommendation of the PCSG.
- 4.10 In relation to the content of the draft Prudential Code, the Panel made the following detailed comments:
- in paragraph 38 it should be emphasised that this is not intended as an exhaustive list
 - in addition to the three year framework, the Code should require consideration of known significant variations outside the three year timeframe.

- 4.11 The Panel endorsed the work of the PCSG to date and expressed their thanks to Tony Knights and the Steering Group. It was noted that there will be a 2nd exposure draft of the Code during 2003 and that the PCSG would recommend this to the Panel for publication for consultation prior to finalisation of the Code.

**ROAD TESTING THE DRAFT PRUDENTIAL CODE
TEXT OF LETTER SENT ON 28 NOVEMBER 2002 TO CHIEF FINANCE
OFFICERS OF LOCAL AUTHORITIES THAT ARE ROAD TESTING THE DRAFT
PRUDENTIAL CODE**

Completion of roadtesting

This letter gives an update on roadtesting to date and outlines the process for the completion of the roadtesting of the draft Prudential Code for capital finance in local authorities which CIPFA is undertaking with local authorities in 2002. In particular, it asks you to complete a further proforma and, once completed, authorise the publication by CIPFA of information relating to your authority.

First of all, I would like to thank you for your participation in roadtesting. The process of roadtesting has to date provided, and will continue to provide, valuable input into the development of the CIPFA Prudential Code.

In my letter to all Chief Finance Officers of Local, Police and Fire Authorities in England Wales and Scotland dated 24 January 2002, I outlined the form that roadtesting would take, including the following:

“Each participating authority will be asked to road test the draft Code for a 4 to 6 month period. The road testing will be undertaken by the local authority itself, with a ‘help-line’ to CIPFA Secretariat staff. Road testing will involve both technical and strategic dimensions:

- the technical dimension will include calculating the numerical prudential indicators for the authority. This will: test the definitions in practical application; illustrate their quantum and how they inter-relate together in a real environment; and demonstrate the ease or otherwise with which they can be monitored. We will also ask each authority to record its current practice for charging for depreciation.
- the strategic dimension will examine how the prudential framework relates to strategic planning, asset management planning and option appraisal; and the procedures that would be adopted by the authority for decision making.

Please note – the phrase ‘road testing’ is being used rather than ‘undertaking pilots’ because participating authorities will remain subject to their current control frameworks, ie they will not be setting their own prudentially determined limits for borrowing during road testing.”

My earlier letter also outlined that there would be two one day workshops for local authorities that are roadtesting the draft Code.

APPENDIX B

The first workshop took place in May 2002. Separate events were held for groups of local authorities in Scotland (Edinburgh), Wales (Cardiff), North England (York) and South England (London). The objectives of the first workshop were:

- To introduce volunteer authorities to the roadtesting programme.
- To explore the strategic processes required by the [draft] Prudential Code.
- To explore each prudential indicator required by the [draft] Prudential Code to enable a greater all round understanding of the prudential approach, and in particular to enable volunteer authorities to calculate the required indicators during the roadtesting period.
- To explore possible alternatives to the detailed measures proposed in the [draft] Prudential Code.
- To explain CIPFA's requirements for documentation and feed back during the roadtesting period, and the help and assistance available from the Institute.

The second workshop was held in November 2002 in the same locations. The objectives of the second workshop were, in the morning sessions, for local authorities to feedback and discuss their experience of roadtesting with CIPFA. In the afternoon, representatives from (as appropriate) ODPM, the National Assembly for Wales, Scottish Executive, HM Treasury, LGA, WLGA, COSLA, the Audit Commission and Audit Scotland were invited.

Local authorities participating in roadtesting were asked to prepare, before the second workshop, returns on a proforma of the experience of roadtesting to date. These returns, and all input to the roadtesting to date except for the afternoon sessions of the second workshop have been treated under Chatham House rules.

The final stage of roadtesting as outlined in my January letter, is for each participating authority to document its roadtesting activities for CIPFA, with that documentation becoming the property of CIPFA. It is CIPFA's intention to publish this documentation. This will assist the members of the Prudential Code Steering Group in finalising the second exposure draft of the Prudential Code for consultation. The documentation will also be published through CIPFA Publications. This will assist local authorities in preparing for the new framework and will provide further information to other stakeholders. In the publication of the results of roadtesting, we will make clear that the results are based on existing plans and commitments and do not reflect or indicate future decisions under a live prudential system – decisions that will be undertaken in a very different context where local government decides its own capital investment and borrowing within a prudential regime. We will also clarify that roadtesting was undertaken on the 2001 exposure draft of the Code, as amended in respect of the treasury management indicators by the PCSG at their July meeting.

In order to provide information for publication, please would you now complete the attached proforma. This is similar to the earlier proforma but with the following changes:

- a revised section 1, whereby the Chief Financial Officer authorises the publication of the information by CIPFA.

APPENDIX B

- a new section 4, which is optional, which invites comments on CIPFA's discussion paper on the role that depreciation could play in local government finance.
- a new section 5, which is also optional, which invites any other documentation that the authority wishes to provide in respect of roadtesting.

Please would all authorities complete sections 1, 2 and 3.

The publication of the Local Government Bill for England and Wales and the proposed amendments to introduce the prudential framework within the Local Government in Scotland Bill bring into focus the impetus to publish the second exposure draft of the Prudential Code in Spring 2003.

The following timetable for replies applies:

- **by end December 2002** : provision of any further information under Chatham House rules
- **by end December 2002 if possible with a final deadline of end January 2003** : return of attached proforma.

Due to the pressure on timetable it is not possible to guarantee the inclusion of returns received after these dates. If it is helpful, a partial return by end December 2002 with the full return by end January 2003 would assist.

Following the second workshop Peter Morley, who acts for CIPFA in this matter, or I will contact each authority individually by phone to discuss any issues arising.

Copies of this letter are being sent electronically to the roadtesters and will be made publicly available.

I am grateful for your involvement in roadtesting, which is very important to the process of developing the Prudential Code.

Yours sincerely

Mrs Maureen Wellen
Policy and Technical Manager, Capital and Treasury

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APPENDIX B

3	Your calculations for the numerical prudential indicators:								
	Notes for proforma on the following pages:								
1	It is assumed that most authorities will use 2001/2002 for the actual figures for the previous year, 2002/2003 for Year 1 etc.								
	However, other years for the purpose would be fine, eg 2000/2001 for actuals eg 2003/2004 for year 1								
	Please list which years have been used for your return:								
		Actuals							
		Year 1							
		Year 2							
		Year 3							
2	The prudential indicators listed above for treasury management reflect the decisions taken on the format of these indicators at the July meeting of the PCSG and notified to road testers.								
3	Paper PCSG 2 02/03 may be helpful to you in completing the forward prudential indicators for debt. This paper is available on the CIPFA web-site. Hard copy will be sent on request.								
	DEBT								
(a)	Prudential limit for external debt with prudential limit for borrowing and prudential limit for other long term liabilities separately identified					Borrowing £000	Other £000		
				Year 1					
				Year 2					
				Year 3					
(b)	Authorised limit for external debt with authorised limit for borrowing and authorised limit for other long term liabilities separately identified								
				Year 1					
				Year 2					
				Year 3					

APPENDIX B

	(c)	Estimates of maxima for external debt with borrowing and other long term liabilities separately identified					
				Year 1			
				Year 2			
				Year 3			
	(d)	Actual external debt after the year end with borrowing and other long term liabilities separately identified					
	(e)	Estimate of ratio of financing costs to net revenue stream				Ratio	
		HRA element (if relevant)					
				Year 1			
				Year 2			
				Year 3			
		Non-HRA element					
				Year 1			
				Year 2			
				Year 3			
	(f)	Actual ratio of financing cost to net revenue stream after the year end					
		HRA element (if relevant)					
		Non-HRA element					
	CAPITAL EXPENDITURE AND COMMITMENTS						
	(g)	Estimate of capital expenditure to be incurred				£000	
				Year 1			
				Year 2			
				Year 3			

APPENDIX B

		Express either in absolute terms or as a					
		percentage of total borrowing less investments					
				Year 1			
				Year 2			
				Year 3			
	(n)	Lower limit for borrowing that is at fixed rates					
		less investments that are fixed rate investments					
		Express either in absolute terms or as a					
		percentage of total borrowing less investments					
				Year 1			
				Year 2			
				Year 3			
	(o)	Upper limit for year 1 for amount of projected borrowing					
		that is fixed rate maturing in each period.					
		Express as a percentage of total projected borrowing					
		that is fixed at the start of the period					
		Where the periods are				As %	
		Under 12 months					
		12 months & within 24 months					
		24 months & within 5 years					
		5 years +					
	(p)	Lower limit for year 1 for amount of projected borrowing					
		that is fixed rate maturing in each period.					
		Express as a percentage of total projected borrowing					
		that is fixed at the start of the period					
		Where the periods are					
		Under 12 months					
		12 months & within 24 months					
		24 months & within 5 years					

NOTES OF MEETING HELD ON 17 OCTOBER 2002 TO DISCUSS FRS 17 AND THE PRUDENTIAL CODE

Present

CIPFA : Tony Knights
John Stanford
Maureen Wellen

HM Treasury : David Loweth
Ian Carruthers
Nick Buxton
Kieran Rix

ODPM : Graham Fletcher

Audit Commission : Paul King
Paul Mayers

MATTERS DISCUSSED

- 1 The meeting discussed the issues that were raised in paper PCSG 12 02/03 in respect of FRS 17 and the Prudential Code. The aim of the meeting was to assist the PCSG when the Steering Group considers and decides on this matter for incorporation within the second exposure draft of the Prudential Code for consultation. The notes from the meeting are therefore being reported to the Steering Group.
- 2 The meeting agreed that the issues for consideration are as outlined in paper PCSG 12 02/03.
- 3 After discussion, the people present recommended the following to the Prudential Code Steering Group:
 - (a) The Prudential Code will require that the revenue consequences of retirement benefits are taken into consideration when a local authority considers the affordability of its capital plans. This is clear cut : it applies to funded and to unfunded retirement benefits; it applies to mandatory and to discretionary retirement benefits; ie it applies to all the revenue consequences of retirement benefits.
 - (b) The Prudential Code places reliance on the balance sheet of local authorities. The question arises whether the pensions reserve should or should not be included within the definition of 'other long term liabilities' required for the prudential indicators in relation to external debt. The representatives at the meeting recommend that the pensions reserve is not included within prudential indicators in relation to external debt because:

APPENDIX C

- (i) to do so would obfuscate rather than clarify the decision making process with respect to the Prudential Code for local authorities and the transparency of those decisions
- (ii) the nature and context of the assets and liabilities identified within the pension reserve are very different from those relating to capital finance and are separately identifiable. If they were required to be included within the indicators for the Prudential Code, they would need to be separate from the other indicators and not part of the same decision making process. In respect of the Prudential Code it is the affordability of the revenue consequences of retirement benefits that is the key, not the level of the pensions reserve
- (iii) FRS 17 recognises the different nature of the pension asset/liability. Paragraph 43 of Appendix IV to FRS 17 states:

“The different context in which the figures in the statement of total recognised gains and losses and balance sheet need to be viewed is also highlighted by their position in the accounts : the actuarial gains and losses are reported in the statement of total recognised gains and losses, not the profit and loss account (or earnings per share), and the pension asset/liability is presented at the foot of the balance sheet separately from and after all other net assets.”
[my underlining]
- (iv) not including the pensions reserve within the Prudential Code does not lead to lack of transparency for local authorities in respect of this reserve, since the pensions reserve will be required to be separately identified on the face of the balance sheet
- (v) the ODPM indicated that consideration would be given to requiring through regulation that the pensions reserve be excluded from the prudential indicators – NB it has now been confirmed within the explanatory notes to the Local Government Bill that this is the intention in respect of regulations to be made under the powers in that Bill
- (vi) it was agreed that the above comments apply to all liabilities that arise within the pensions reserve, whether from funded or unfunded benefits and whether from discretionary or non-discretionary elements.