REPORT OF THE CABINET

The Cabinet met on 16 December 2008 and 26 January 2009. Attendances:-

Councillor Jones (Chairman) (2)
Councillors Bentley (2), Elkin (2), Glazier (2), Kirby (2), Lock (2), Reid (2), Mrs Stroude (1) and B Tidy (2).

1 Reconciling Policy and Resources

1.1 The Cabinet has considered a report on reconciling policy and resources including the Capital Programme 2009/10 to 2013/14, the Revenue Budget 2009/10 and the draft three year portfolio plans. The draft capital programme (attached as Appendix 1 to this report) and Revenue Budget (attached as Appendix 2 to this report) have been produced as a result of the work that has been underway since summer 2008 on Reconciling Policy and Resources using the council tax and savings assumptions that were agreed by the County Council as part of its three year plan in February 2006.

1.2 The Scrutiny Committees, and their Reconciling Policy and Resources boards, have discussed the emerging portfolio plans and the Cabinet considered the views of the Scrutiny Committees (Appendix 4 of the report to the Cabinet previously circulated to all councillors) prior to making its recommendations. The draft portfolio plans (Appendix 3 of the report to the Cabinet previously circulated to all councillors) have been approved by the Cabinet and Chief Officers have been authorised to finalise the plans in consultation with the relevant lead member. The draft plans will be used as the basis for the preparation of the Council Plan, a draft of which will be submitted to the Cabinet in March.

1.3 The draft Capital Programme and Revenue Budget documents reflect the Policy Steers agreed by the County Council in December 2008 and have taken into account the strategic risks that were reported to the Cabinet in November 2008.

1.4 Consultations have been carried out with the Trade Unions and the views of business ratepayers have been sought on the budget proposals. The detailed views expressed during the consultation process have been considered by the Cabinet and have previously been circulated to all members.

1.5 The Cabinet considered and agreed proposals by the Lead Member for Corporate Resources in relation to the use of flexibility within the budget. These have been included in Appendix 2 to this report.

1.6 The Cabinet has reviewed fees and charges for 2009/10 in accordance with agreed policy. The list of approved fees and charges has previously been circulated to all members.

1.7 The Cabinet recommends the County Council:

✡ (1) approve the Capital Programme in relation to schemes in progress or about to start and those to start in 2009/10 and 2010/11 and to note the schemes provisionally included in the capital Programme in future years as set out in Annex D of Appendix 1;

(2) note the prudential indicators as set out in Annex E of Appendix 1;

(3) approve the revenue budget estimates for 2009/10 as set out in Annex C of the commentary on the Revenue Budget circulated to all members (Appendix 2), which includes the use of budget flexibility set out in Annex C1 of Appendix 2;

(4) in accordance with the Local Government Finance Act 1992 to agree that:

(i) the amount calculated by East Sussex County Council as its net budget requirement for the year 2009/10 is £327,984,000;
(ii) the amount calculated by East Sussex County Council as the basic amount of its council tax (ie for a band D property) for the year 2009/10 is £1,127.49 and represents a 3.5% increase on the previous year;

(5) the borough and district councils be advised of the relevant amounts payable and council tax in other bands in line with the Regulations, and as set out in Annex C2 of Appendix 2, and to issue precepts accordingly; and

(6) to note the medium term challenge and task as outlined in Annex G1 of Appendix 2

2 Services for School Governors

2.1 The Cabinet has considered the report of the Children's Services Scrutiny Committee on its review of services to school governors. The report is included elsewhere on the agenda (see agenda item 6). The full scrutiny report has previously been circulated to all members.

2.2 The primary objective of the review was to assess and make recommendations on how best the authority can ensure that all governing bodies have the necessary skills and abilities to fulfil their overall responsibility of helping the school provide the best possible education for pupils.

2.3 The Cabinet has welcomed the report which provides a valuable insight into how governors view the support they receive from Governor Services. Implementation of the recommendations, as set out in the Director's report, will result in service improvements.

2.4 In welcoming the findings of the Scrutiny Committee, the Cabinet has considered a report by the Director of Children's Services (as set out in Appendix 3 to this report, circulated separately to all members) on the specific recommendations and endorsed it as its response to the recommendations.

2.5 The Cabinet, in welcoming the report, **recommends** the County Council to -

✡ approve the response of the Director of Children's Services on the implementation of the recommendations in the Scrutiny Committee's report.

[See also the report of the Scrutiny Committee for Children's Services, paragraph 1, page 21]

3 Conservators of Ashdown Forest Budget 2009/10

3.1 The Cabinet has received the Conservators' draft budget for 2009/10 and considered both the overall position and the balance of funding to be made available to the Conservators from the Trust and the Council's own resources. The 'Trust Funds' are legally distinct from the County Council's general resources.

3.2 The draft budget for 2009/10, previously circulated to all members, shows the Trust Fund contribution at the recommended level of £65,100 (this includes the additional £10,000 grant approved by Cabinet in February 2007 for the three year period to 2009/10).

3.3 The County Council's Reconciling Policy and Resources process has commenced and due to the pressure on the Council's resources and the need to make considerable budget savings, it is recommended that the Council's own contribution to the conservators, after allowing for inflation at 2%, is reduced by £10,000 to £78,700. This matches the provision in the Transport and Environment Department's draft budget. Taking into account both the recommended contributions of £65,100 and £78,700 the Conservators budget would show a shortfall of £15,100. It is not unreasonable to assume that a contribution will be forthcoming from Wealden District Council similar to that in previous years although this was not shown in the budget considered by the Cabinet.

3.4 The Conservators' final budget will be amended to reflect these recommendations and the Cabinet has agreed that final approval be delegated to the Deputy Chief Executive and Director of Corporate Resources in consultation with the Lead Member for Corporate Resources. The recommendations are reflected in the reconciling policy and resources report in paragraph 1 of this report.

4 Treasury Management Strategy 2009/10

4.1 Under Section 3(1) of the Local Government Act 2003 and the Prudential Code for Capital Finance 2004, the County Council is required to determine its authorised borrowing limit, to adopt treasury management prudential indicators and limits and agree its treasury management strategy and policy statement each year.

<u>Strategy and amendments to strategy for 2008/09 to date</u>

4.2 The strategy for 2008/09, agreed in January 2008, included two changes to the investment arrangements to take account of the increased risk. The first change related to the credit ratings used to gauge the financial viability and strength of banks and other organisations, the second was to further restrict the period of some investments.

4.3 Due to the worsening situation in the financial markets further changes were put into place and were approved by the County Council in July 2008. As a result of the continuing deterioration of the banking sector, the reduced ratings of some banks and the collapse of the Icelandic banks, further changes were agreed in November 2008.

4.4 As the money markets had been particularly volatile it was necessary to review and adjust the investment tactics on a daily, sometimes hourly basis.
The following revisions were made in November and are still current (but see paragraph 4.12):

- Except for existing term investments or those with the Government Debt Management Account Deposits Facility (DMADF) at the Bank of England all new investments were to be on daily access terms.
- Only UK banks which are eligible for the Government's Credit Guarantee Scheme and meet the following minimum rating criteria to be used:

Ratings agency	Long term	Short term
Fitch	AA-	F1+
Moody	AA3	P-1
Standards and Poors	AA-	A-1+

- All new investments of surplus funds to be limited to Nat West, HBOS, and Abbey (maximum £25m exposure to each) with the balance at DMADF. Reinvestment of the current term deposits will be in accordance with this strategy (which means they will be invested with DMADF)

Formulating a Strategy for the remainder of 2008/09 and for 2009/10

Borrowing

4.5 The County Council has had a strategy to borrow to support the Capital Programme and it lends out other cash (rather than using internal borrowing). Historically this meant that the interest rate earned on cash balances was higher than the interest rate paid on loans from the Public Works Loans Board (PWLB). In the current financial climate, this interest rate differential has been removed. No new PWLB borrowing has taken place since January 2008 and is unlikely in the current climate unless long term PWLB rates reach a very low level (where the long term benefit would exceed the short term costs). Indeed, as well as using the existing cash balances to finance capital spending (rather than new borrowing) it is also considered prudent to repay early some £13m of relatively expensive PWLB loans which are due to mature in the next 5 years. This would reduce the overall counterparty risk on lending, and give some modest savings (even after paying the PWLB premium for early redemption).

Investment

4.6 There are fixed deals taken before our change to a mainly overnight investment strategy that will continue into 2009/10. These six deals amounting to £30m are deposited with Lloyds HBOS (£15m.), HSBC (£5m.) and Toronto Dominion (£10m.) and are currently considered as an acceptable risk.

4.7 It is important to take account of the current and predicted future state of the financial sector. The state of the money markets has not improved over the last few months. The following factors must be taken into account:

- The economy has fallen into recession after a period of sustained growth.
- House prices have dropped in the past year and the inflation rate will fall further in 2009/10.
- The Banking sector still has serious problems and there is still uncertainty of lending within and between banks.
- The bank base rate which started 2008/09 at 5.25% has reduced five times and now stands at 1.5% (the lowest rate it has ever been).
- The base rate may not be at its lowest point and future rate cuts may occur.
- Borrowing rates have fallen but not as quickly as the bank base rate.

- The County Council is now receiving a lower rate of interest on its lending than it is paying on its borrowing.

4.8 If the current strategy for 2008/09 agreed in November was continued into 2009/10, the vast majority of the County Council's investments would be with the Government Debt Management Account Deposits Facility (DMADF). The rate of interest on these deposits for all periods quoted (overnight to six months) has been consistently lower than the bank base rate by 0.5% to 1.25%. The reluctance of the DMADF to pay a reasonable rate of interest and the impact of the fall in base rates from 5.25% at the start of the financial year to a current figure of 1.5% has serious consequences on the budget for Treasury Management. This is dealt with in the Reconciling Policy and Resources elsewhere (see paragraph 1 of this report)

4.9 The strategy going forward must continue with the policy of ensuring minimum risk but will also need to deliver more than DMADF rates if the aim is to secure investment income of at least base rates on the Council's cash balances. Different types of investments have been appraised including their positive and negative merits, how they work and rates and periods of their deposits. Details of the following types of investment were set out in Annex 1 of the report considered by the Cabinet (previously circulated to all members):

- DMADF deposits
- Government securities – Gilts
- Treasury backed money market funds
- British banks and types of deposits
- Other banks
- Other local authorities
- Money market funds
- Use of external managers

Other approaches to investment will continue to be kept under review.

4.10 As Annex 1 of the report to the Cabinet highlighted the achievement of base rate will require the level of deposits in acceptable investments paying in excess of base rate to be up to twice the level of deposit in the DMADF account which pays less than base rate and the proposed strategy set out later reflects this requirement.

4.11 The existing Treasury Management Strategy treats the whole cash balance as one fund whereas the balance is made up of a number of different elements:

1) Fire Authority cash balances
2) Certain reserves which receive interest (e.g. Schools LMS balances, corporate waste reserve, insurance reserve)
3) Other County Council balances and reserves

It is proposed to treat these three groups differently in the future. The Fire Authority deposits will be invested in line with its own separate Treasury Management Policy (rather than being subsumed within the limits contained in the County Council Policy). The deposit of the interest earning reserves (based on their opening balance for the year) will all be with DMADF and the rate paid on those reserves will accordingly be the DMADF rate earned (below base rate). The balance of County Council funds will be invested in line with the Treasury Management Strategy set out below with the aim of achieving interest of at least base rate.

Proposed Strategy for the remainder of 2008/09 and for 2009/10

4.12 In the current economic climate it is essential that a very prudent approach is maintained. This will be primarily achieved through investing with DMADF and on an overnight basis with selected banks and funds which meet the Council's rating criteria. It is also important to recognise that movements within the money markets can happen with no notice and the Deputy Chief Executive and Director of Corporate Resources may have to amend this strategy in order to safeguard Council funds. As in the past any such actions will be reported to the next Cabinet meeting. An example of that is exercising a judgement to place more weight on UK Government's moral guarantee to high street banks if there are marginal movements in credit rating for the same high street banks.

4.13 It is not expected that any new external borrowing will be undertaken in the next 15 months however the limits set out in paragraph 4.17 would allow such borrowing. External borrowing will only take place if the rates available are so low that the long term benefits will significantly exceed the short term cost. As well as using internal borrowing to finance new capital investment it is further proposed to repay some £13m of existing PWLB loans. Further cost effective repayment opportunities will be taken if and when they emerge.

4.14 The different elements of the total cash balances to be invested will be dealt with as follows:

1) Fire Authority – invested in line with their own specific policy and in the first instance assumed to mirror County Council policy at 3 below (estimated average £11m)
2) Interest on specific Council reserves – invested solely in DAMDF (estimated average £85m)
3) Balance of Council funds (estimated average £180m)

- Up to £120m maximum deposited on an overnight basis only with any of the following to the individual limits shown:

Bank / Fund	**Proposed Maximum Investment**
Barclays	£35m
Lloyds HBOS	£35m
Nat West (call account maximum)	£35m
Abbey	£35m
Treasury backed money market funds (AAA rated)	£35m
Money Market Funds (AAA rated)	£35m

Only banks which are eligible for the Government's Credit Guarantee Scheme and meet the following minimum rating criteria to be used (with the exception of Nat West, the Council's existing bankers, which currently fall below this criteria on the Standard and Poors rating only – but this will be kept under close review).

Ratings Agency	**Long Term**	**Short Term**
Fitch	AA-	F1+
Moody	AA3	P-1
Standards and Poors	AA-	A-1+

- The balance in excess of £120m to be deposited with DMADF.

Authorised Limit for borrowing in 2009/10

4.15 The Authorised Limit for borrowing determined for 2009/10 will be the statutory limit determined under section 3(1) of the Local Government Act 2003.

4.16 The limits set out later in this report have been based upon the amount of capital spending to be financed through borrowing in 2009/10 and following financial year. Whilst the Prudential Code would allow a higher limit than this (2009/10 and next two financial years) it is considered prudent at this stage to base the limits upon 2 years. This approach was agreed by the County Council in July 2004 and has worked well.

4.17 For 2009/10 it is estimated that the Authorised Limit for borrowing should be determined as usual although, as stated earlier, additional external borrowing is not expected to be undertaken,

		£m.
	Opening Balance at 1 April 2009	286
	New borrowing for capital programme	22
	Less repayment of debt	-11
A	Closing balance (no borrowing in advance)	297
B	Advance borrowing allowed (£10m plus net borrowing for following year) 21	
A + B	Operational Boundary	318
C	Short term borrowing	20
A + B + C	**Authorised Limit**	**338**

Prudential indicators and limits

4.18 There are self-imposed prudential indicators and limits that are set on an annual basis. The indicators which relate to treasury management are included below:

- Operational Boundary and Authorised Borrowing Limit (which also include short term borrowing)
- Interest rate exposures
- Maturity structure of debt
- Compliance with the treasury management code of practice
- Maturity structure of investments

(a) Operational Boundary and Authorised Limit for Borrowing

		Actual 2007/08	**Near Actual 2008/09**	**Estimate 2009/10**	**Estimate 2010/11**	**Estimate 2011/12**
		£m	**£m**	**£m**	**£m**	**£m**
	Opening Balance	260	274	286	297	306
	New borrowing for capital programme	25	23	22	21	21
	Less repayment of debt	-11	-11	-11	-12	-12

A	**Closing balance (no borrowing in advance)**	274	286	297	306	315
B	**Advance borrowing allowed (£10m plus net borrowing for following year)**	21	20	21	21	21
A+B	**Operational Boundary**	295	306	318	327	336
C	**Short Term (£20m)**	20	20	20	20	20
A+B+C	**Authorised Limit**	315	326	338	347	356
D	**Borrowing to date**	270	277			
D-A	**Remainder of planned borrowing**	**4**	**9**			

4.19 The proposed Operational Boundary for borrowing is based on the same estimates as the Authorised Limit but without the additional amount for short term borrowing included to allow, for example, for unusual cash movements. The Operational Boundary represents a key management tool for in year monitoring and long term borrowing control.

4.20 The Authorised Limit is consistent with the Council's current commitments, existing plans and the proposals for capital expenditure and financing, and with its approved treasury management policy statement and practices. They are based on the estimate of the prudent but not worst case scenario plus sufficient headroom (short term borrowing) over and above this to allow for day to day operational management, for example unusual cash movements or late receipt of income.

(b) Interest rate exposure

4.21 The Council will continue the current practice of seeking to secure competitive fixed interest rate exposure. It is proposed to continue to set limits which would allow variable rate borrowing and lending in case that becomes a more effective approach. The table below shows both borrowing and lending and a combined borrowing and lending table.

Borrowing	2008/09 Projected Outturn	2009/10 Estimate	2010/11 Estimate	2011/12 Estimate
Fixed Rate Exposure				
Upper Limit	100%	100%	100%	100%
Lower Limit *	100%	87%	85%	82%
Variable Rate Exposure				
Upper Limit	0%	13%	15%	18%
Lower Limit *	0%	0%	0%	0%

(* assumes all new borrowing is variable)

Lending

Fixed Rate Exposure				
Upper Limit	100%	100%	100%	100%
Lower Limit	0%	0%	0%	0%
Variable Rate Exposure				
Upper Limit	100%	100%	100%	100%
Lower Limit	0%	0%	0%	0%

Borrowing and Lending combined

Fixed Rate Exposure				
Upper Limit	100%	100%	100%	100%
Lower Limit	46%	42%	41%	40%
Variable Rate Exposure				
Upper Limit	100%	100%	100%	100%
Lower Limit	0%	0%	0%	0%

(c) Maturity structure of debt

4.22 The Council has set upper and lower limits for the maturity structure of its borrowings as follows.

	Lower limit	Upper limit	Current
Under 12 months	0%	25%	0%
12 months and within 24 months	0%	40%	1%
24 months and within 5 years	0%	60%	4%
5 years and within 10 years	0%	80%	8%
10 years and above	0%	100%	87%

(d) Compliance with the treasury management code of practice

4.23 East Sussex County Council has adopted the *CIPFA Code of Practice for Treasury Management in the Public Services*

(e) Maturity structure of investments – Investment of surpluses for a period of up to 5 years.

4.24 Investments will be made in line with the strategy set out above and are unlikely to be for any periods beyond 6 months (the current maximum length DMADF deal). The table below shows the maximum amount that could be lent out for over 1 year if DMADF do provide such a facility.

Year	Opening balance £m	Net movement Addition or (reduction) £m	Closing balance £m	Waste Maximum Over 1 year £m	Limit Over 1 year £m
2009/10	67	4	71	71	75
2010/11	71	(1)	70	70	75
2011/12	70	4	74	74	80
2012/13	74	6	80	80	85
2013/14	80	7	87	87	90

Capital Financing Requirement and Minimum Revenue Provision (MRP) Statement

The Council's Borrowing Need (the Capital Financing Requirement)

4.25 The prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of Council's underlying borrowing need. The Council is asked to approve the CFR projections below:

£m	2008/09 Revised	2009/10 Estimated	2010/11 Estimated	2011/12 Estimated
Total CFR	**286**	**297**	**306**	**315**
Movement in CFR	**12**	**11**	**9**	**9**
Movement in CFR represented by				
Net financing need for the year (above)	23	22	21	21
MRP/VRP and other financing movements	-11	-11	-12	-12
Movement in CFR	**12**	**11**	**9**	**9**

4.26 The Council is required to pay off an element of the accumulated General Fund capital spend each year through a revenue charge (the Minimum Revenue Provision - MRP), and also allowed to undertake additional voluntary payments (VRP), i.e., £200,000 in 2009/10.

4.27 CLG Regulations have been issued which require full Council to approve an MRP Statement in advance of each year. A variety of options are provided to councils to replace the existing Regulations, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement.

'For capital expenditure incurred before 1 April 2008 or which in the future will Supported capital Expenditure, the MRP policy will be:

- Based on based on the non-housing CFR, i.e., The Council currently set aside a Minimum Repayment Provision based on basic MRP of 4% each year to pay for past capital expenditure and to reduce its CFR.

From 1 April 2008 for all unsupported borrowing the MRP policy will be:

- Asset Life Method – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option will be applied for any expenditure capitalised under a Capitalisation Direction)'

Treasury Management Policy Statement for 2009/10

4.28 It is recommended that the Treasury Management Policy Statement for 2009/10 should be unchanged. The Statement is set out below

East Sussex County Council defines its treasury management activities as:

"The management of the organisation's cash flows, its banking, money market and capital market transactions, the effective management of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."
The County Council regards the successful identification, monitoring and management of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.

This authority acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

4.29 The Cabinet recommends the County Council to –

✡ (1) determine that for 2009/10 the Authorised Limit for borrowing shall be £338m;

(2) adopt the prudential indicators and limits set out above;

(3) approve the Minimum Reserve Provision Statement for 2009/10 as set out in paragraphs 4.25 to 4.27 above; and

(4) approve the Treasury Management Strategy and Policy statement for 2009/10 as set out above

26 January 2009 PETER JONES
Chairman