PORTFOLIO HOLDER DECISION MEETING

FRIDAY 4 MAY 2007
10.00 AM

COMMITTEE ROOM 3
HARROW CIVIC CENTRE

MEMBERSHIP	**Leader**

Issued by the Democratic Services Section,
Legal and Governance Services Department

Contact: Daksha Ghelani, Senior Democratic Services Officer
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HARROW COUNCIL

PORTFOLIO HOLDER DECISION MEETING

FRIDAY 4 MAY 2007

AGENDA - PART I

PROCEDURAL

1. **Declarations of Interest:**
   To receive declarations of personal or prejudicial interests, arising from business to be transacted at this meeting, from:

   (a) all Members of the Committee, Sub Committee, Panel or Forum;
   (b) all other Members present in any part of the room or chamber.

2. **Minutes:** (Pages 1 - 2)
   That the meeting held on 22 March 2007, having been circulated, be taken as read and signed as a correct record.

3. **Petitions:**
   To receive petitions (if any) submitted by members of the public/Councillors under the provisions of Executive Procedure Rule 15 (Part 4D of the Constitution).

4. **Public Questions:**
   To receive questions (if any) under the provisions of Executive Procedure Rule 16 (Part 4D of the Constitution).

   (Note: Paragraph 16 of the Executive Procedure Rules stipulates that questions will be asked in the order notice of them was received and that there be a time limit of 15 minutes).

5. **Matters referred to the Executive Member:**
   (if any)

   In accordance with the provisions contained in Overview and Scrutiny Procedure Rule 23 (Part 4F of the Constitution).

6. **Reports from the Overview and Scrutiny Committee or Sub-Committees:**
   (if any)

BUSINESS DEVELOPMENT

KEY 7. **Debt Repayment and Restructuring:** (Pages 3 - 24)

GENERAL

8. **Any Other Urgent Business:**
   Which cannot otherwise be dealt with.

AGENDA - PART II - NIL

<u>Local Government (Access to Information) Act 1985:</u> In accordance with the Local Government (Access to Information) Act 1985, this meeting is being called with less than 5 clear working days' notice by virtue of the special circumstances and ground for urgency stated below:-

<u>Special Circumstances/Grounds for Urgency:</u> Under Access to Information Procedure Rule 5.2, where a meeting is convened at shorter notice than set out in Rule 4, copies of the agenda and reports shall be open to inspection from the time the meeting is convened.

On the advice of Sector Treasury Services Ltd., the Council wishes to carry out some debt repayment and restructuring. The timing of implementation is critical – if interest rates move the outcome will change. Sector have recommended that debt repayment and restructuring be implemented as soon as possible in order to maximise the savings.

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PORTFOLIO HOLDER DECISION MEETING 22 MARCH 2007

Councillors: * Chris Mote

* Denotes Member present

[Note: Councillors Margaret Davine and Bill Stephenson also attended this meeting to speak on the item indicated at Minute 21 below].

PART I - RECOMMENDATIONS - NIL

PART II - MINUTES

15. **Declarations of Interest:**

RESOLVED: To note that no interests were declared in relation to the business to be transacted at this meeting.

16. **Minutes:**

RESOLVED: That the minutes of the meeting held on 30 November 2006 be taken as read and signed as a correct record.

17. **Petitions:**

RESOLVED: To note that no petitions were received under the provisions of Executive Procedure Rule 15 (Part 4D of the Council's Constitution).

18. **Public Questions:**

RESOLVED: To note that no public questions were put at the meeting under the provisions of Executive Procedure Rule 16 (Part 4D of the Council's Constitution).

19. **Matters referred to the Executive Member (if any):**

RESOLVED: To note that no matters had been referred to the Executive Member for reconsideration in accordance with the provisions contained in the Overview and Scrutiny Procedure Rule 22 (Part 4F of the Council's Constitution).

20. **Reports from the Overview and Scrutiny Committee or Sub-Committees (if any):**

RESOLVED: To note that no reports had been received.

21. **Urgent Key Decision - Consultation on possible changes to Adult Community Care Services:**

It was noted that the meeting had been convened at short notice for the reasons set out in the agenda.

The Director of Adult and Community Care Services introduced the report, which required the Leader of the Council to determine whether to amend the decision of Cabinet on 15 March 2007 to consult on two options in relation to the Eligibility Criteria under 'Fair Access to Care Services' consultation.

The Leader of the Council explained that, following further advice and, in light of the Council's challenging financial situation, it would be misleading to consult on the option to retain the 'status quo'. However, should the Council's financial situation improve, the matter could be re-visited.

In accordance with Executive Procedure Rule 25.5 (Part 4D of the Council's Constitution), the Leader of the Council invited Members present to address the meeting. They made the following comments:-

- the stakeholders, who had taken part in the pre-consultation, had requested that the option to retain the 'status quo' be consulted on and that this option ought to be retained for the purposes of the wider consultation exercise in order to retain the confidence of the stakeholders. It was then for the Cabinet to decide on their preferred option when the outcome of the consultation was known;

- if the Leader of the Council was minded to amend the decision of the Cabinet, then it should be subject to a caveat;

- a Portfolio Holder had only recently prided on the consultation with stakeholders;

In response, the Leader of the Council stated that he intended to write to all the stakeholders who had taken part in the pre-consultation stage on this matter. He re-iterated that it would be misleading to consult on an option, which was unlikely to be adopted.

In response to questions from Members, the Director of Adult and Community Care Services stated that consultees would have an opportunity to provide constructive feedback during formal consultation. In addition, the consultation would set out details of which groups of people would not be affected by the proposed changes.

RESOLVED: (1) To amend the decision of the Cabinet on 15 March 2007 to consult on two options and that officers consult only on the following option: "To meet only 'critical band' assessed needs and to stop paying for any assessed needs at 'substantial band' or below";

(2) that a letter be sent to those consulted at the pre-consultation stage to explain the decision taken at this meeting.

Reason for Decision: To respond to concerns expressed by a senior Councillor and to allow the planned consultation to proceed.

(Note: The meeting having commenced at 4.04 pm, closed at 4.21 pm)

(Signed) COUNCILLOR CHRIS MOTE

Ref: PHD 086/06

Subject:	Debt Repayment and Restructuring
Responsible Officer:	Myfanwy Barrett, Director of Financial and Business Strategy
Portfolio Holder:	Chris Mote, Leader
Key Decision:	Yes
Urgent/Non Urgent:	Urgent
Power to be exercised:	Portfolio Holder Responsibilities (Allocation of Responsibilities) – Paragraph 3 of the Delegated Powers of Portfolio Holders Appendix to the Executive Procedure Rules – Part 4D of the Constitution. (Special Urgency Rule also applies – para. 16 of the Access to Information Procedure Rules)
Exempt:	No
Enclosures:	Report from Sector Treasury Services

SECTION 1 – SUMMARY AND RECOMMENDATIONS

RECOMMENDATIONS:

The Leader is asked to:

- Agree to implement the recommendations of Sector Treasury Services arising from the balance sheet review, subject to approval to the accounting treatment from the External Auditor
- Delegate to the Director of Financial and Business Strategy any decisions required on the timing of implementation

REASON: To ensure effective management of the Council's long term borrowing and deliver savings in 2007-08.

SECTION 2 - REPORT

1. Sector Treasury Services is a company within the Capita group which specialises in treasury management advice. Sector were commissioned recently to conduct a balance sheet review for the Council. They completed their work in April. Their report is attached.

2. Sector are recommending that the Council repays £98m of Public Works Loans Board (PWLB) maturity loans and replaces them with longer dated loans totalling £60m at lower coupon rates. This is a net reduction in long term borrowing of £38m, and will be financed through realising investments.

3. This proposal generates general fund savings in the order of £7.2m over 31 years. Due to the phasing of discounts on repaid loans and the split between the general fund and HRA, this saving is not spread evenly over the period. The saving in 2007-08 is in the order of £780k. The exact figures will vary depending on interest rates at the point of implementation.

4. The proposal was considered and supported by the Budget Review Working group, chaired by the Deputy Leader, David Ashton, on 23 April. The Council's external auditor has also been consulted on the accounting treatment of the debt restructuring. The auditor raised a number of queries which have been responded to. No action will be taken until the auditor has confirmed that he is content with the proposed accounting treatment.

5. Whilst the Director of Financial and Business Strategy has delegated authority for treasury management decisions, the scale of this exercise warrants formal approval.

6. Sector will support the Council throughout the implementation process and give advice on the timing of repayment and borrowing decisions. As the timing of repayment and borrowing is critical to the outcome and as these decisions are required very quickly, the Leader is asked to give a delegation to the Director in this respect. Such decisions will be made in consultation with Sector.

7. The Council's power to borrow money is contained in Section 1 of the Local Government Act 2003. In borrowing any money the council must have regard to the Prudential Code for Capital Finance in Local Authorities.

8. This decision is consistent with the Prudential Code and the Council's approved Treasury Management Strategy which states that:

- Borrowing will be managed with a view to achieving a competitive interest rate and appropriate maturity profile.
- New borrowing will be taken out to finance capital expenditure in line with the approved capital programme and prudential indicators.

9. This proposal is within with the Council's approved Authorised Limits and Operational Boundaries for external Debt under the Prudential Code. Borrowing may precede repayment when the decision is implemented resulting in a short term increase, but the net impact is a reduction in borrowing of £38m.

10. As Sector are part of Capita, the review was carried out at no cost to the council and the saving will be counted as a BTP saving.

11. Sector have been asked to submit a proposal to provide strategic treasury advice on an ongoing basis. This will be reviewed and subject to a separate report.

SECTION 3 - STATUTORY OFFICER CLEARANCE

Name:……Myfanwy Barrett Signature:……………………………... Date: …3 May 2007…………..	☐	Chief Financial Officer
Name:………Hugh Peart………… Signature:…………………………….. Date: ……3 May 2007……………..	☐	Monitoring Officer

SECTION 4 - CONTACT DETAILS AND BACKGROUND PAPERS

Contact:

Background Papers:

Report of Sector Treasury Services

IF APPROPRIATE, does the report include the following considerations?

1.	Consultation	Yes
2.	Corporate Priorities	N/A
3.	Manifesto Pledge Reference Number	N/A

Signature: ………………………………………………………………………

Position Director of Financial and Business Strategy

Name (print) Myfanwy Barrett

Date: 3 May 2007

FOR PORTFOLIO HOLDER/LEADER

* I do agree to the decision proposed

* I do not agree to the decision proposed

* Please delete as appropriate

Notification of personal interests (if any):

(Note: if you have a prejudicial interest you should not take this decision)

Additional comments made by and/or options considered by the Portfolio Holder

Signature: ………………………………………………………………………….

Leader

Date:

LONDON BOROUGH OF HARROW

2005/2006 Consolidated Balance Sheet Review

Desk Top Report

April 2007

Sector Treasury Services Limited

Prepared by Sector Treasury Services April 2007

London Borough of Harrow

Analysis of Consolidated Balance Sheet as at 31st March 2006.

Notes to CBS Analysis

Introduction

1. The main purpose of this report is to analyse the balance sheet and in particular the relationship between the Authority's assets and liabilities. Included within the liabilities is the Authority's external borrowing and this is also compared to the Authority's underlying need to finance its capital programme (Capital Financing Requirement) and the surplus or deficit cash that this relationship generates as expressed within the assets or liabilities of the Authority.

2. This analysis will then provide the foundations for establishing whether savings could be made from changing the dynamics of the balance sheet in relation to the capital financing strategy and / or the relationship between assets and liabilities.

Findings

1. We have based our findings on the London Borough of Harrow's (LBH) draft Statement of Accounts for the financial year ended 31st March 2006.

2. The primary focus of this analysis is to provide the Authority with an independent calculation of its Capital Financing Requirement (CFR).

   Based on our calculations the CFR is shown to be **+£151.866million.**

3. As at the end of March 2006, LBH had external debt totalling **£222.889m**. If reference is made to the figure that has been calculated for the CFR, it can be seen that the debt is above the measure of debt liability (CFR) by £71.02m.

4. To identify recent trends, we have calculated the opening Capital Financing Requirements for the 2004/05 and 2005/06 financial years. These are the post Prudential Framework positions for LBH.

5. By comparing the 2005/06 Closing Capital Financing Requirement with the CFR as at 31st March 2005, it can be seen that it increased by £39.054m during the 12 month period.

This is a result of the following year on year changes

	2004/05	2005/06	Year on Year Movement
CFR Calculation			
Fixed assets	914,762	1,058,160	143,398
Deferred Charges			
Fixed Asset Restatement Account	(571,557)	(681,888)	(110,331)
Capital Financing Account	(179,969)	(169,266)	10,703
Government Grants Deferred A/c	(50,424)	(55,140)	(4,716)
Capital Financing Requirement	112,812	151,866	39,054

6. The Capital Financing Requirement reflects the Authority's underlying need to borrow for a capital purpose. It increases when any capital expenditure is incurred, but reduces at the same time if this expenditure is resourced at the time it is incurred or if funds are set aside to repay debt (e.g. MRP).

An increase in the CFR may not necessarily lead to any additional borrowing, as the debt liability can be met from an authority's own resources (commonly known as internal borrowing – see paragraph 10 below). Any decision on how to fund the shortfall in capital finance would need to form part of the integrated treasury management strategy.

7. LBH Capital Financing Requirement over last three financial years

Using the information supplied by the Authority, we can confirm that the Capital Financing Requirements used by LBH in the last three financial years are as follows

Financial Year	***LBC Harrow CFR £'000s***	***Sector Treasury CFR £'000s***	***Variance £'000s***	***Comments***
2003/04	101,236	102,136	900	Minor Variance to be confirmed
2004/05	111,921	112,812	891	Minor Variance to be confirmed
2005/06	150,551	151,866	1,315	Minor Variance to be confirmed

At the time of writing this report, the LBH figures for the last three financial years are not matched to Sector Treasury Services estimates. The CFR we have calculated is based on figures taken from the audited statement of accounts. We will contact the Authority and arrange for a meeting to discuss the variance and update the table if appropriate.

It is noted that the variance between the previous three financial years is not material and would not impact on the proposed debt repayment strategy covered later in this report.

8. Capital Financing Requirement – Forward Estimates current and next two financial years

LBH have provided Sector with the estimated level of the Authority's Capital Financing Requirement (CFR) over the next three financial years. These figures are shown below.

Financial Year	***LBH CFR £'000s***	***Increase '£000***
2006/07	188,885	38,334
2007/08	213,017	24,132
2008/09	231,182	18,165

For the purposes of this report, it is assumed that any increase in the level of LBH's Capital Financing requirement will be funded with new borrowing. This would leave the gap between debt and debt liability at the current 2005/06 outturn position.

This will be discussed further in section 15 of this report, when we consider the future debt strategy.

9. Net Borrowing and the Capital Financing Requirement

Using the figures contained in the 2005/06 Consolidated Balance Sheet, we have also calculated the Authority's net borrowing. Our findings are shown below:

<u>LBH Net Borrowing Position 31st March 2006</u>

Net borrowing		
External borrowing		222,889
External investments	(80,713)	
Bank overdraft	3,895	
Cash in hand	(1,130)	
		(77,948)
Net borrowing		144,941

If we compare this figure with the debt liability we calculated in section 5) above, we can confirm that as at 31st March 2006, net borrowing was £6.925m below the CFR at this date.

<u>LBH Net Borrowing Position 31st March 2005</u>

Net borrowing		
External borrowing		180,435
Less		
External investments	(91,883)	
Bank overdraft	457	
Cash in hand	(1,584)	
		(93,010)
Net borrowing		87,425

These are only snapshots at a point in time, but the latest calculation provides confirmation that the Authority did comply with the Prudential Code requirement in 2005/06 to ensure that net borrowing is below the CFR. When combined with the evidence provided by the 2004/05 consolidated balance sheet (see above), it indicates that over the medium term the Authority is only borrowing for capital purposes.

It should be noted that the gap between Net Borrowing and the Capital Financing Requirement has been narrowing in recent years. In the first year of our analysis, there was £50.085m headroom and this has fallen to £6.925m in 2005/06. This is a material reduction and is consistent with the investment analysis shown later in our report which shows a similar fall in investment balances.

We would advise the Authority to keep this position under review and consider this in conjunction with options to reduce the levels of excess borrowing.

10. Working Cash Flow

As part of the balance sheet review, we have calculated the Authority's working cash flow surplus as at 31st March 2006. This is to say that debtors/payments in advance were outweighed by creditors/receipts in advance by **£4.028million**.

Note – The working cash flow surplus was £3.737million at the end of the previous financial year.

As this is not a significant year on year increase and the Working Cash Flow surplus is not a material item, we would not recommend any further analysis of this item.

11. Fund Balances

LBH also had £23.709million in "Fund Balances" at 31st March 2006. In other words the Authority had sums set aside in its various reserves, provisions and balances. However when this is adjusted for the Working Cash Flow surplus and stocks held, **Net Fund Balances amount to £27.571million.**

12. Surplus Monies

As indicated above the Authority had Net Fund Balances of £27.571million at 31st March 2006. If this figure is then compared with the £80.713million of investments held at the same date, we can identify that LBH has **"Surplus Monies" totalling £53.142million.**

This sum is in effect “excess” borrowing, which can be further explained through the relationship between the Authorities CFR and Debt. If reference is made to the Authority’s Consolidated Balance Sheet and the CFR as calculated in 5) above, it can be seen that the Authority had a **debt liability of £151.866m** but the level of external debt was **£222.889m**.

The variance between these two positions at the end of 2005/06 financial year amounted to £71.02m. Further analysis of the balance sheet has identified how these resources are being utilised.

	£'000s
Cash Overdrawn	3,895
Internal Investments	
Suspense Accounts	
Premium	(17,575)
Cash in Hand	(1,130)
Surplus Monies	(53,142)
Long Term Debtors	(3,062)
TOTAL	(71,014)

For Information, excess borrowing amounted to £68.449million as at 31st March 2005.

In addition, at the end of 2003/04 financial year, the level of excess borrowing was £68.130million. This indicates that the level of borrowing is a medium term position and warrants further investigation.

Borrowing above CFR may be caused by "excess" borrowing caused by more PCL being received under the previous Capital Control System than was applied to reduce external borrowing. This would simply represent a cash resource carried forward into the new system, available to finance new capital spending as though it were a capital receipt.

Excess borrowing will also arise if it relates to anything which is not in the CFR, such as transferred debt.

If the Authority chose to use the cash backed capital resource to fund future capital then they would only need to make the fixed asset accounting entry. This is as a result of the earlier entries to place the set aside capital receipts in the capital financing account.

Any accounting entries will depend upon whether the cash is used to reduce future external borrowing or to finance new capital spend. In prudential terms, it should be the former but this needs to be considered as part of the future Treasury Management Strategy.

Sector will put forward a view on how best to deal with the current ‘excess’ borrowing position in the debt strategy section of this report.

13. Capital Receipts/Grants Unapplied

It is noted that LBH had £5.199m unapplied capital resources held in the capital receipts/grants unapplied account at the end of the 2005/06 financial year.

As part of our discussions at our meeting on 11th January 2007, it was noted that these resources are earmarked developer's funds. As a result they would not be available for early set-aside to provide a temporary reduction in minimum revenue provision.

An additional issue that we would like to consider is the use of capital receipts to pay a premium charged in relation to any amount borrowed. This power is now available following changes in the Local Government Act 2003 and in particular regulation 23 of Statutory Instrument 2003 No 3146.

This change provides similar powers granted to debt free authorities, allowing them to use PCL to finance premiums.

Sector's view is that an Authority can either finance premiums[1] as they are paid, or as they charged (amortised) to the revenue account.

If the Authority intends to use capital receipts as part of its future debt rescheduling strategy, it may be prudent to retain some funds in the capital receipt reserve to finance debt premiums.

14. Investments

It is noted that investments reduced by 12.16% during 2005/06 and as at 31st March 2006, they amounted to £80.713m.

Over the three year period of this review, Investments peaked at £120.148m

The main reasons for this reduction of £39.435m are as follows:

Increase in financing of Debt Premium	£14.910m
Reduction in Balances/Reserves	£10.661m
Reduction in Unapplied Capital Receipts/Grants	£ 6.971m
Reduction in Cash Flow Surplus	£11.713m

In addition, as previously discussed, LBH currently has excess borrowing of £71.02m. If this amount was used, either in part or in full, to fund capital expenditure or redeem debt it would have a significant impact on future investment balances.

Again this issue will be covered in more detail in the debt strategy section of this report.

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[1] These are payments associated with premature debt repayment

We have not carried out any analysis of current investment performance, as it is outside the remit of this report.

15. LBH Historical Credit Ceiling position

We have been provided with the historical Aggregate Credit limit figures for the Authority and have used these to determine the movement in debt liability before 31st March 2007.

The relevant information is shown in the table below

A more detailed summary of the Aggregate Credit limits is shown in the appendices

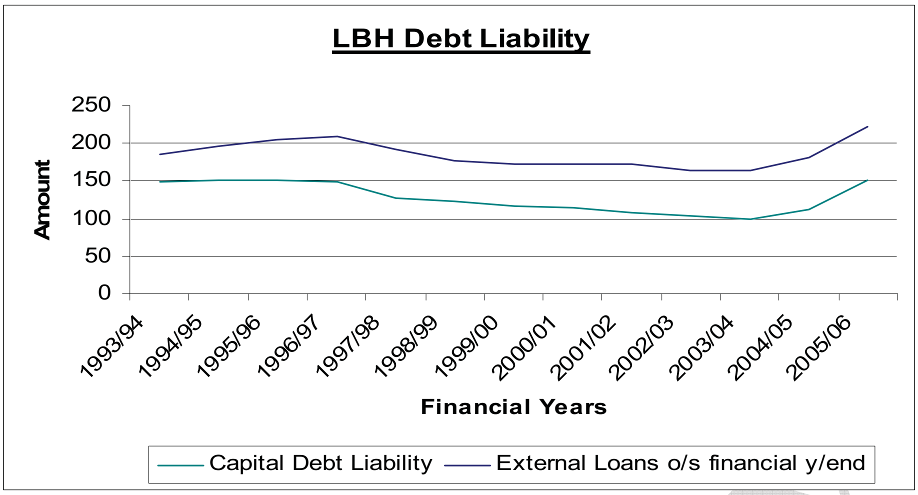
Financial Year	Capital Debt Liability	External Loans o/s financial y/end	Variance
1993/94	149.771	185.864	36.093
1994/95	151.092	196.053	44.961
1995/96	150.641	204.133	53.492
1996/97	148.013	208.825	60.812
1997/98	126.695	190.844	64.149
1998/99	122.306	177.723	55.417
1999/00	116.044	172.598	56.554
2000/01	114.524	172.246	57.722
2001/02	108.414	171.629	63.215
2002/03	103.943	163.006	59.063
2003/04	99.850	162.880	63.030
2004/05	111.986	180.435	68.449
2005/06	150.551	222.889	72.338

Using this information, we can confirm that the level of debt has been above the Authority's debt liability for each of the last 11 financial years.

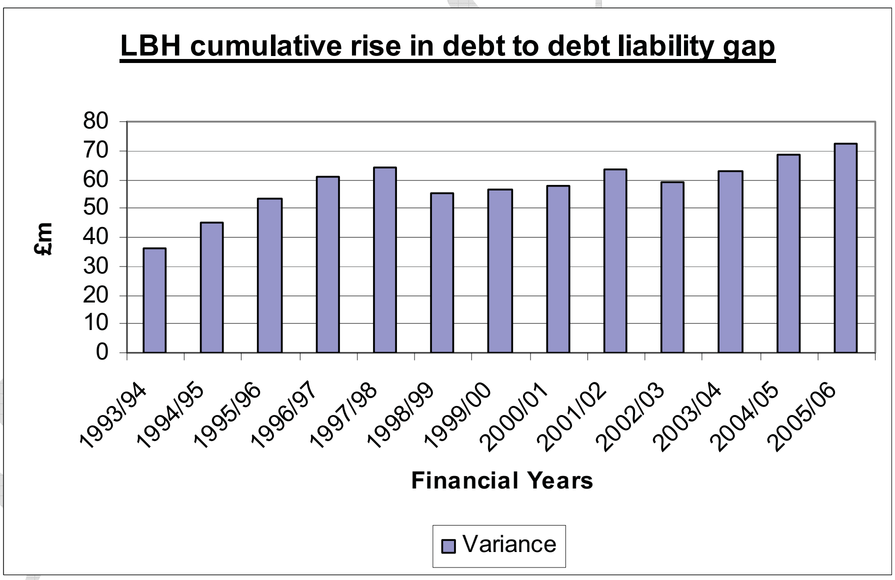
This information adds weight to our findings in section 3 of this report when debt was £71.02M above the Capital Financing Requirement[2]. In addition the level of external debt was £68.449M above CFR at the end of the 2004/05 financial year.

A graph of movement in debt and debt liability (13 financial years) is shown below

[2] The Capital Financing Requirement is the current measure of a local authority's capital debt liability.



It is also important to consider whether this level of excess debt has been rising or falling over the period. We have used the figures provided by the Authority and this has been graphed to show the trend since the base year (1993/94). The graphical presentation demonstrates that the gap between the level of debt and debt liability has risen and fallen over the last 13 years. More importantly, the gap has not fallen below £20million since 1999/00 and has risen in each of the last three financial years.



This information supports Sector Treasury Service's view that the level of excess borrowing is a long term position and that resources are available to enable a debt repayment strategy to be considered.

The full details of the proposed debt strategy are set out in section 16 below.

16. Debt

We have been supplied with LBH's debt portfolio as at 31st Dec 2006

This identifies that the Authority's outstanding debt has risen by £9.652m and now stands at £242.541m

We accept that this part year position may not reflect movements in debt between now and the end of the financial year and also needs to be considered with expected increases in the level of the Authority's Capital Financing Requirement during the medium term budget cycle.

LBH Current Debt as at 31st Dec 2006

Current Debt Position				
PWLB Maturity	£158,000,000	4.26%	(£6,724,480)	
PWLB Annuity	£741,169	4.25%	(£31,500)	Assumed Rate Used
EIB	£0	0.00%	£0	
Market	£63,000,000	6.28%	(£3,954,510)	
Variable	£20,800,000	5.65%	(£1,175,200)	
TOTAL	**£242,541,169**	**4.900%**	**(£11,885,690)**	

As per our comments in section 1 of this report, the level of external debt was £71.02m above the Authority's capital debt liability as at 31st March 2006. In addition, we have assumed that any increase in the projected level of the Authority's capital financing requirement will be funded by new borrowing. This was covered in section 8 of this report.

The remainder of this section will deal with proposed strategies to generate revenue savings from the existing debt portfolio.

LBH has provided Sector with the latest debt portfolio and we have used these figures to investigate the possibility to reschedule, convert or repay some or all of the current debt

At the time of writing this report, the debt information supplied was incomplete. To complete the exercise, we require the start and maturity date for PWLB annuity loans. These have been requested and we will revise our figures when they are received.

Current Debt Position				
PWLB Maturity	£158,000,000	4.26%	(£6,724,480)	
PWLB Annuity	£741,169	4.25%	(£31,500)	Assumed Rate Used
EIB	£0	0.00%	£0	
Market	£63,000,000	6.28%	(£3,954,510)	
Variable	£20,800,000	5.65%	(£1,175,200)	
TOTAL	**£242,541,169**	**4.900%**	**(£11,885,690)**	

Current Investments & Income		
3m LIBID (Investment Rate)	4.75%	Assumed Bank Rate over life of proposal
Investments	£87,590,000	
Investments Income	£4,160,525	

General Fund Current Cost Position	
Total interest costs payable	(£11,885,690)
Interest rechargeable to HRA	£1,452,038
Investment income	£4,160,525
Net (cost)/income to GRA	**(£6,273,127)**

For information - Sector Treasury Services has based its calculations on the discount rates and the discount rates used are taken from PWLB rate sheet 068/07 (4th April 2007). It should be noted that these rates move on a daily basis and these movements will influence the actual level of savings achieved.

Debt Repayment and Rescheduling

Sector Treasury Services has looked at options to reschedule and/or repay some or all of the current debt.

The level of indicative savings is identified below

1. LBH Current Debt & Investment (including consolidated rate)

Debt & Investment Profile

Opening 1.4.06	1/4/2006
Opening HRA CFR (Item 8 Debit)	£28,060,000
Opening GRA CFR	£122,491,000
Opening Total Capital Financing Req	**£150,551,000**

Mid Year 06/07	
Mid year HRA CFR (Item 8 Debit)	£29,630,500
Mid year GRA CFR	£140,087,500
Mid Total CFR (less adjustment A)	**£168,330,670**

Average rate of interest on debt outstanding	4.90%
CRI	4.90%

Adjustment A	£1,387,330

Current Debt Position				
PWLB Maturity	£158,000,000	4.26%	(£6,724,480)	
PWLB Annuity	£741,169	4.25%	(£31,500)	Assumed Rate Used
EIB	£0	0.00%	£0	
Market	£63,000,000	6.28%	(£3,954,510)	
Variable	£20,800,000	5.65%	(£1,175,200)	
TOTAL	**£242,541,169**	**4.900%**	**(£11,885,690)**	

Current Investments & Income		
3m LIBID (Investment Rate)	4.75%	Assumed Bank Rate over life of proposal
Investments	£87,590,000	
Investments Income	£4,160,525	

2. Debt Restructuring/Repayment

Loans to be repaid

Loans to be Repaid — Redemption date: 10/4/2007

Loan ref.	Principal	Coupon	Maturity Date	Discount Rate	Discount	Years to Maturity	
489335	£10,000,000	4.600%	25/11/2030	4.850%	£349,448	23.64	
481657	£5,000,000	4.625%	12/10/2024	5.000%	£217,165	17.52	
489336	£9,500,000	4.600%	25/11/2031	4.850%	£339,355	24.64	
489491	£5,500,000	4.500%	21/12/2033	4.700%	£166,306	26.69	
489627	£5,000,000	4.600%	25/1/2027	5.000%	£249,640	19.81	
491115	£10,000,000	3.700%	25/11/2030	4.600%	£1,393,875	39.77	
491116	£10,000,000	3.700%	12/10/2024	4.550%	£1,406,427	40.77	
491117	£10,000,000	3.700%	25/11/2031	4.550%	£1,418,439	41.77	
49112	£5,000,000	3.700%	10/01/2056	4.500%	£782,819	47.77	
49111	£10,000,000	3.700%	10/01/2055	4.500%	£1,574,872	48.77	
490282	£8,000,000	4.400%	12/6/2023	5.000%	£528,426	16.19	
490754	£5,000,000	4.250%	4/11/2034	4.700%	£345,822	27.58	
483584	£5,000,000	4.380%	23/11/2025	5.000%	£376,025	18.64	
Total	**£98,000,000**	**4.14%**			**£9,148,619**	**31.78**	**Average**
						16.19	**Shortest**

The total value of loans to be repaid is £98million and they have an average life of 31.78 years. If these loans were repaid early LBH would achieve a discount of £9,148,619.

As this is a repayment and rescheduling exercise, the plan would be to only partially replace the loans with the cheapest PWLB fixed maturity loans, leaving a net repayment of £38million. It should be noted that any discount would be spread over a maximum of 10 years (DCLG Regulations 2007).

New Loan

New Loan	Principal	Coupon	
			5/4/07
PWLB 45 to 50 year	£60,000,000	4.50%	47.50
Total	**£60,000,000**	**4.50%**	**47.50**

PWLB - Restructuring Options

First Period

Average rate of interest on debt outstanding	5.15%
CRI	5.15%

Discount Share	
Discount	£9,148,619
GRA share	£7,443,481
HRA Share	£1,705,138

Revised Debt Position			
Current Borrowing	£242,541,169	4.90%	(£11,885,690)
New borrowing	£60,000,000	4.50%	(£2,700,000)
Average Life	47.50		
PWLB Repaid	(£98,000,000)	4.14%	£4,054,250
Average Life	31.78		
TOTAL	**£204,541,169**	**5.15%**	**(£10,531,440)**

Revised Investments	
3m LIBID (Investment Rate)	4.75%
Investments	£58,738,619
Investments Income	£2,790,084

The indicative savings below are based on PWLB rate sheet 068/07 and the assumptions made above.

General Fund Future Cost Position	
Total interest costs payable	(£10,531,440)
Interest rechargeable to HRA	£1,525,619
Investment income	£2,790,084
Discount Benefit	£744,348
Net (cost)/income to GRA	**(£5,471,389)**
Year 1 (cost)/benefit to GRA	**£801,738**
Time adjusted	**£781,970**

These savings would continue to accrue over the life of the replaced loans as follows:

Year	(Cost)/Benefit
2	£758,282
3	£714,827
4	£671,371
5	£627,915
6	£584,459
7	£541,003
8	£497,547
9	£454,091
10	£410,635
11	£57,390
12	£57,390
13	£57,390
14	£57,390
15	£57,390
16	£57,390
17	£57,390
18	£57,390
19	£57,390
20	£57,390
21	£57,390
22	£57,390
23	£57,390
24	£57,390
25	£57,390
26	£57,390
27	£57,390
28	£57,390
29	£57,390
30	£57,390
31	£57,390

And would total £7.2million over this 31 year period, based on the assumptions illustrated above.

As discounts are being amortised to revenue over a maximum period of 10 years, the estimated overall General Fund benefit over the first 10 years, included in the above savings analysis, would be £6.06m. The additional benefits from years 11 to 31 is mainly the net effect of a higher interest rate on the debt portfolio increasing the amount which can be charged to the Housing Revenue Account from the General Fund, which in turn the HRA is reimbursed in Housing Subsidy from the Department for Communities and Local Government to leave the HRA theoretically self funded.

We can provide detailed models to support these indicative General Fund savings and can update the models on a daily basis to provide accurate estimates of future savings. These updates will take account of volatility in the PWLB loan rates.

Debt Repayment

As discussed in section 5 of this report, LBH has been operating with a level of debt which is considerably higher than the Authority's actual debt liability. The cash resource which is linked to these additional loans is currently being invested to provide a revenue stream which is reducing the cost of carry of the loan portfolio.

We have included in the above option the repayment of loans totalling £38million. It is envisaged that over the medium term further loans would be repaid as part of the medium term strategy, but only when there was an opportunity to make material savings for the Authority. This position would be continued to be monitored.

Any savings Sector recommends are net of the Housing Revenue account Cashflows and show the savings attributable to the General Fund,

The forecast level of LBH investments, after the early debt repayment, would fall by the net repayment to the PWLB (Principal less discount receivable).

In addition the loan portfolio average rate and consolidated rate of interest (Item 8) would increase from 4.90% to 5.15%.

Average rate of interest	5.15%
CRI	5.15%

As the consolidated rate of interest (CRI) has risen, this will result in higher Item 8 debit charges. Sector Treasury Services would have to discuss this issue with LBH to ensure it is matched by an increase in HRA subsidy.

It should be noted that the current differential between long and short dated interest rates means that the loss of investment income will be higher than the debt interest saving achieved by this proposal, although the value of the discount received would be greater.

Sector Treasury Services would be happy to discuss the objectives of the Authority in more detail to ensure that any strategy we propose does not increase the revenue burden in future years.

17. Accounting for Premia/Discounts

The accounting for premia and discounts incurred on the premature repayment of loans changed with effect from 1 April 2007, mainly as a result of the DCLG Regulation which was issued in March 2007. In addition, a Draft SORP was issued by CIPFA which has yet to be finalised.

Any rescheduling exercise after 1st April 2007 will be subject to proper practices contained in SORP 2007. This means that any premium or discount arising from an extinguishment of a loan will be taken direct to the income and expenditure account in the financial year that the transaction takes place

If the loan is modified (remains with same lender before and after a repayment and replacement or where a LOBO is blended and extended with same lender) and meets the SORP 2007 10% test, then any breakage costs (premium or discount) are used to adjust the carrying value of the loan (amortised cost). The write down to income and expenditure will be determined by the effective interest rate for the modified loan.

This deals with the accounting issues for the Income and Expenditure Account.

Where regulation overrides SORP from 1st April 2007 the required entries will go through the Statement of the movement on General Fund balance

This can be best illustrated using an example.

Where, for example, a PWLB loan is repaid and replaced and a £500k premium is incurred. In this example the original loan has 5 years to maturity and replacement loan is taken for 50years. The lender has not changed, so an authority carries out the 90\110% modification test. It fails the test as the discounted cash flows on the original loan and replacement loan are not within 10% of each other.

Using SORP, the £500k premium goes straight to Income and Expenditure account

But the DCLG Regulation applies and accordingly this allows the Authority to spread premium over life of replacement loan. The Authority elects this approach and is only required to charge £10k to revenue per year

So an adjustment of £490k (credit as it is a premium) is made to the Statement of Movement on the General Fund Balance in the year that the transaction takes place

The Income and Expenditure account receives no further charge

The Statement of movement on the General Fund balance will incur a 1\50th per annum charge until the premium is written down in full

The Authority can choose to accelerate the write down and could also choose the life of replaced loan

Discounts are capped, in terms of amortisation periods, at either the period outstanding on the original loan or 10 years, whichever is the lower period. This means that discounts cannot be taken direct to Income and Expenditure where regulation overrides SORP. The Regulation does not allow discounts to be accelerated into the revenue account at a faster rate.

In cash terms, the treatment of discounts under the Regulation will mean that whilst the same amount is received, the fact that the discount is ‘drip fed’ into the accounts over 10 years generates investment income which is recognised in the savings calculations and creates a stable revenue buget position over 10 years. If the discount were taken into the accounts in year one, and spent immediately through the revenue budget process, then there would be no investment income to recognise. In addition, whilst the revenue budget would benefit from a one off boost in income in year one only from the discount, it could create problems in future years as a result of either having to find alternative income to meet the funding of revenue expenditure which the discount funded in year one or alternatively revenue expenditure would have to be cut by this magnitude.

HRA recharges will be determined by the Item 8 Determination. The savings calculations used in this Report show the net effect on the General Fund, which is driven by the DCLG Regulation as this overrides SORP.

18. In Summary

LBH is currently classified as an indebted authority.

Using the figures in the 2005/06 Statement of Accounts, Sector has calculated a positive CFR as at 31st March 2006 of £151.9m.

The debt liability (CFR) increased by £39m during 2005/06 financial year.

External Debt is higher than the Authority's underlying debt liability by £71m. This represented a reduction of £3m during the 2005/06 financial year.

It may be prudent to have a balance of funds held in the capital receipt reserve to finance any costs associated with future debt rescheduling.

Investment balances have fallen by £39.435m during the last three financial years. This is a result of falling reserves/balances; capital grant/reserves unapplied; cash flow surplus and an increasing amount of cash tied up in financing the debt premiums.

The Debt Rescheduling/Repayment proposal indicate that **general fund savings of £7.2m** could be achieved by repaying £98m PWLB maturity loans and replacing these longer dated loans with loans totalling £60m at lower coupon rates.

Any savings from debt management would be subject to daily movements in PWLB discount rates and the rates in place at the time of executing the strategy. Accordingly, these savings are subject to change. Sector Treasury Services can provide updated figures upon request.

19. It is important that this exercise is not viewed as a one-off balance sheet fix but the first stage of a longer term strategy which regularly reviews the Authority's balance sheet and underlying capital financing and treasury management strategy with the objective of optimising the Authority's performance and keeping the balance sheet efficient. This will drive down the cost of capital financing for the Authority, thereby generating real and material savings to the Authority's General Fund, net of the recharge to the Housing Revenue Account, all within acceptable risk parameters which will be discussed and agreed with the Authority on a regular basis.

20. Any further work required by Sector Treasury Services to confirm the reasons for the financial positions provided in our summary above, would be chargeable, as it is not within the remit of this report.

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