

Finance Committee

Meeting Venue:
Committee Room 4 – Ty Hywel

Meeting date:
24 May 2012

Meeting time:
12:50

Cynulliad
Cenedlaethol
Cymru

National
Assembly for
Wales



For further information please contact:

Helen Finlayson
Committee Clerk
02920898409
FinanceCommittee@wales.gov.uk

Agenda

Private briefing (12:50 – 13:00)

1. Introductions, apologies and substitutions (13:00 – 13:05)

2. Devolved Funding: Borrowing Powers and Innovative Approaches to Capital Funding (13:05 – 13:45) (Pages 1 – 14)

FIN(4) 08–12 – Paper 1 – Scottish Local Government Directors of Finance

Scottish Local Government Directors of Finance (Via Video Conference)

Bruce West, Head of Strategic Finance, Argyll & Bute Council

Ian Black, Head of Finance and IT, East Dunbartonshire Council

3. Devolved Funding: Borrowing Powers and Innovative Approaches to Capital Funding (13:45 – 14:30) (Pages 15 – 36)

FIN(4) 08–12 – Paper 2 – Welsh Local Government Association

Will McLean, Strategic Partnerships & Engagement Lead, Monmouthshire County Council

Peter Davies, Assistant Head of Finance, Monmouthshire County Council

Jon Rae, Director of Resources, WLGA

4. Papers to note (Pages 37 – 44)

FIN(4) 08–12 – Paper 3 – Correspondence from HM Treasury – Devolved Funding

FIN(4) 07-12 - Minutes of previous meeting

5. Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

Item 6.

6. Discussion of evidence - Devolved Funding: Borrowing Powers and Innovative Approaches to Capital Funding (14:30 - 15:00)

National Assembly for Wales Finance Committee:

Inquiry into Prudential Borrowing and Innovative Approaches to Capital Funding

A Submission by:

The CIPFA Directors of Finance Section

April 2012

the people
in public finance

CIPFA Local Government Directors of Finance Section is the professional forum which comprises the Section 95 Officers under the Local Government (Scotland) Act 1973 of all 32 local authorities in Scotland. The Section provides opinions on matters concerning the management and operation of Scottish local government finance and also serves as a learning forum for the exchange of experience and information on these issues.

Any questions arising from this submission should be directed to:

Marjory Stewart
Chair, Directors of Finance Section
Dundee City Council
Dundee House
50 North Lindsay Street
Dundee

Tel: 01382 433555
Email: marjory.stewart@dundeecity.gov.uk

1. **Introduction**

- 1.1 The CIPFA Directors of Finance Section welcomes the opportunity to provide evidence to the Committee's inquiry. We note that the Committee is specifically interested in:
- The lessons learned from local authorities on prudential borrowing; and
 - Innovative capital models from elsewhere in the UK
- 1.2 These two areas will be the principal focus of this submission. We describe the practical operation of prudential borrowing over a period of eight years since its introduction in Scotland.
- 1.3 Scottish local authorities have been at the forefront within the UK in seeking alternative models for financing large capital projects. One recent model, the Non Profit Distributing Organisation model (NPDO) is set out for the benefit of the Committee as an example of innovation.
- 1.4 The introduction of prudential borrowing takes place against the background of a wider UK capital control mechanism. That wider mechanism could be exercised at a future point in the form of a national borrowing limit. We therefore set out the agreed proposals which exist in Scotland in the event of the need for the introduction of a national borrowing limit. We contrast this with the draft proposals which are currently proposed for Wales.
- 1.5 We begin our submission with background information on the statutory framework for prudential borrowing in Scotland.

2 BACKGROUND TO PRUDENTIAL BORROWING IN SCOTLAND

- 2.1 The enactment of Sections 35 to 37 of The Local Government in Scotland Act 2003¹, introduced a new system of capital controls in Scotland with effect from April 2004. At the same time the previous control mechanism which was based on central government control was abolished².
- 2.2 The equivalent legislation which was introduced in Wales was the Local Government Act 2003³. The Committee will wish to note however that in Scotland legislative control is on capital expenditure while in Wales, legislative control is on borrowing.
- 2.3 Further regulation in Scotland (as in the rest of the UK) prescribed that the application of the new control mechanism by local authorities would be based on the application of the CIPFA Prudential Code for Capital Finance in Local Authorities⁴.
- 2.4 The policy intention as well as the practical effect was to transfer responsibility for decision-making on capital expenditure from central government (in the form of the then Scottish Executive) to local authorities.
- 2.5 The core objectives of Prudential Code are to provide a framework for local authority capital finance that will ensure for individual local authorities that⁵:
- Capital expenditure plans are affordable;
 - All external borrowing and other long-term liabilities are within prudent and sustainable levels
 - Treasury management decisions are taken in accordance with professional good practice
- 2.6 The Code is supplemented by a suite of locally set prudential indicators which operate as a control mechanism to ensure that these core principles are adhered to and reported.
- 2.7 The Code was fully revised in 2009 following a period of consultation and now incorporates changes as a result of the move towards International Financial Reporting Standards and emphasises the links with strategic planning and asset management and further emphasis is given to the importance of:-
- Service objectives, i.e. strategic planning for the authority
 - Stewardship of assets, e.g. asset management planning
 - Value for money, e.g. option appraisal
 - Prudence and sustainability, e.g. implications for external borrowing and whole life costing
 - Affordability, e.g. implications for council tax, rents etc
 - Practicality, e.g. achievability of the plan

¹ Local Government in Scotland Act Part 7, Sections 35, 36 and 37.

² Local Government (Scotland) Act 1973, Section 94

³ Local Government Act 2003 Part 1

⁴ The Prudential Code for Capital Finance in Local Authorities, 2011 Edition

⁵ The Prudential Code for Capital Finance in Local Authorities, 2011 Edition, page 5, para 1

- 2.8 Since the introduction of prudential borrowing, both the political and wider fiscal backdrop has altered. In 2007, Scotland elected a minority Scottish National Party (SNP) government and in 2011 SNP was elected as Scotland's first post-devolution majority government. One of the key policies adopted by the Scottish Government was a council tax freeze and this has been in place since 2008¹. Additionally and perhaps most significantly, Scottish Government spending on capital resources reduced by 24.8% in 2011/12 and is forecasted to reduce until 2014/15². It is against that background that this submission is compiled.

¹ Renewing Scotland: The Government's Programme for Scotland 2011-2012, page 5

² Scottish Government & Office of Budget Responsibility (OBR)

3. PRUDENTIAL BORROWING IN SCOTLAND

Practical Operation of Prudential Borrowing

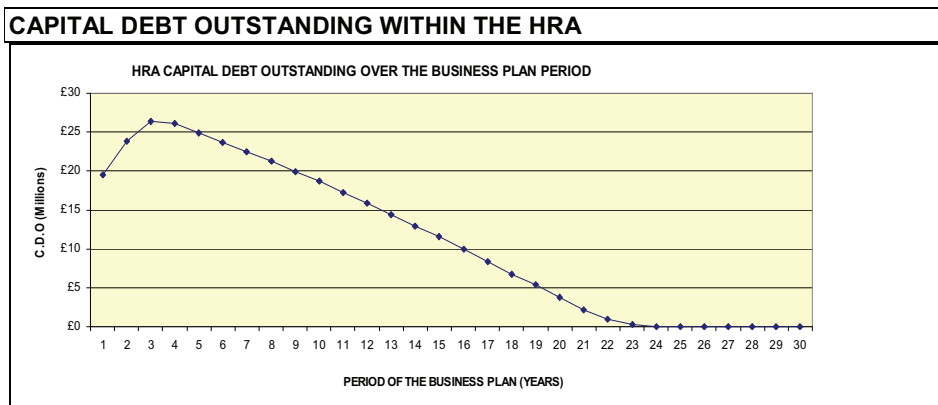
- 3.1 This section of our submission sets out a practical summary of how prudential borrowing operates in Scotland. As an indicator of scale, local authorities spent more than £2 Billion in Scotland on capital expenditure in 2010/11, of which around half was met from borrowing¹. The following case study based on a "live" example describes how local authorities take account of asset management and option appraisal best practice as part of an integrated approach to asset management and capital planning.
- 3.2 In developing a Capital Investment Strategy, a standard business case and scoring process to measure the merits of individual capital projects (a Capital Prioritisation and Options Appraisal Framework) is applied to determine priorities. A dedicated Council-wide group assess business cases against objective criteria.
- 3.3 Seven separate but specific asset management plans are constructed covering the key asset areas of Corporate Property, School Estate, Roads (including lighting and structures), Greenspace, ICT , Housing, and Vehicle Fleet. These detailed asset appraisals assist in developing the Capital Investment needs thereby strengthening the strategic approach by making recommendations on a long-term Capital Investment Strategy.
- 3.4 Revenue implications of the Capital Programme are incorporated into future years Revenue Budget, fully integrating Revenue and Capital budget processes. This is reflected in a Corporate Asset Management Plan which sets out how all assets will be managed.
- 3.5 A significant concern is that of a backlog in investment and maintenance and finite resources with which to address these issues. Property condition surveys and an assessment of the road network indicate nationally across Scottish local authorities this could represent a figure in excess of £2 billion, albeit a significant proportion of this is of low priority. Additionally asset rationalisation programmes are in place to down-size property portfolios.
- 3.6 Following the collection and analysis of this data on asset usage and conditions recommendations can be presented to elected members on the proposed Capital Investment Programme.
- 3.7 Up to 2010-11 Scottish Government provided revenue resources within the Financial Settlement to meet the debt costs associated with a notional borrowing value. This allowed local authorities to undertake an element of "supported borrowing". From 2011-12 it was agreed that this arrangement should end with these resources converted into additional Capital Grant. Now, all local authority borrowing is financed from within the local authority.
- 3.8 Taking a multi-year approach (usually 3 to 5 Years) a resultant Capital Investment Strategy ensures all future Capital Investment plans are developed in the context of improving the linkages to Council priorities and objectives and that account is taken of the proposals in the Corporate Asset Management Plan. The linkage from overall priorities on service delivery to the Prudential Code can be

¹ An Overview of Local Government in Scotland, Audit Scotland, page 23

further exemplified when the provision and financing of housing services is considered.

Housing

- 3.9 In Scotland, the Housing Revenue Account (HRA) is a statutory, ring-fenced account. By statute, all tenant rent and costs related to operating the housing service (including debt charges) must be applied to the HRA. However the Prudential Code principles also extend to the HRA.
- 3.10 In 2005 a thirty year Business Plan was developed which demonstrated that the Council had sufficient investment resources to bring stock up to the level required in the Scottish Housing Quality Standard by 2015. Subsequent reviews of the Business Plan reflecting material changes have been conducted periodically and continue to demonstrate a viable HRA and SHQS compliance.
- 3.11 The scope of the Business Plan also importantly demonstrates participation in the Scottish Government’s new-build housing programme which provides an element of funding to incentivise local authorities to undertake house-building programmes, with the balance largely financed by additional borrowing utilising the Prudential Code.
- 3.12 The outcomes of the most recent reassessment of the Business Plan concluded that incorporating changes to Right to Buy, capital receipts and a prudent debt repayment profile, a more flexible and ambitious HRA Business Plan could be adopted. A key positive finding was that not only does the Business Plan still pass all financial tests but there is also further scope for additional borrowing to enhance new-build housing within the HRA. The following table sets out the summary position of the overall Capital Debt outstanding within the HRA as a result of the additional prudential borrowing incurred to finance the new-build programme.



- 3.13 It can be seen from the above table that housing debt will peak in year 3, 2014/15, and will then decline over the future period thereafter, indicating there is further investment capacity within the HRA. At no point does the annual debt charge associated with loan repayment rise above 40% of HRA turnover. The significance of that figure is that 40% is a locally adopted Prudential Indicator of affordability.

Prudential Borrowing and the Role of Elected Members

- 3.14 Elected members are required to provide appropriate scrutiny and review of their local authority’s Treasury Management and Capital Investment Plans, including a

review of performance against the Prudential Indicators. Commonly this scrutiny activity is undertaken at an Audit committee, with the findings of that process then reported to a meeting of the Council for final agreement. This ensure that robust governance arrangements are in place and all stakeholders have a full appreciation of the implications of investment decisions. The indicators are an appropriate measurement with a long-term financial perspective, and are therefore complex. Therefore, it is important that Council officers provide appropriate training and briefings to elected members to ensure the key factors and assumptions underpinning these strategies are clear and understood.

The Role of Capital Receipts

- 3.15 Capital receipts are worthy of specific reference. The focus upon improved asset management which has been a feature of the introduction of the prudential regime has enabled local authorities to be able to identify alternative uses for assets and to identify surplus assets. This has coincided with the general downturn in the market for development.
- 3.16 The consequence for local authorities in Scotland is that the level of capital receipts has reduced from around £0.5 Billion in 2007/08 to around £100M in 2010/11¹. This has resulted in greater reliance on prudential borrowing to keep investment plans on track since 2008². In simple terms, local authorities in Scotland have borrowed to compensate for both a timing delay in achieving asset sales and a reduction in overall capital receipts.

¹ Scottish Government Capital Finance Working Group, Paper 49, 20 Sept 2011, para 5

² Scottish Government Capital Finance Working Group, Paper 49, 20 Sept 2011, para 10

4. IMPOSITION OF A NATIONAL BORROWING LIMIT

Background

- 4.1 At the outset of this submission we described the policy intention of the prudential regime to transfer responsibility for capital expenditure to local government. One of the key learning points from the practical operation of the prudential regime is that against that background of local responsibility, government has retained power to impose limits on capital expenditure. Local authorities therefore require to be prepared in the event of any limit being imposed.
- 4.2 Section 36 of the Local Government in Scotland Act 2003¹, includes a power to enable Scottish Ministers to impose a national limit on capital expenditure. It is understood that such a control would be imposed at a macro level by HM Treasury 'for national economic reasons'. This in turn would trigger use of Section 36 by Scottish Ministers. To date this power has not been utilised.
- 4.3 The Scottish Government, as advised by HM Treasury, and in anticipation of the possibility that a limit may be imposed at some point in the future determined that a protocol should be developed to set out how such a limit would operate in practice. A protocol between the Scottish Government and local government was finalised in June 2008 and it detailed the administrative arrangements which would be put in place in the event of a need for a national limit².
- 4.4 The protocol was developed with input from key stakeholders in Scotland and was finalised in June 2008. The protocol is both transparent and understandable in that the level of detail enables clarity on the administrative arrangements to be put in place in the event of a national limit being required.

Comparison of National Limit Protocols

- 4.5 We note that while there is a finalised protocol in Scotland, no such protocol exists in England and in Wales, only a brief protocol exists in draft form³. The protocols contain similar wording with the same broad intention although the respective levels of detail, as well as status differs. The committee will wish to examine these differing arrangements further.

¹ Local Government in Scotland Act 2003, Section 36

² National Limit on Local Authority Borrowing, Protocol Between Scottish Government and Scottish Local Authorities, 27 June 2008

³ Draft National Limit on Local Authority Borrowing, Protocol Between the Welsh Government and the Welsh Local Authorities (undated)

4.6 The CIPFA Directors of Finance Section provided professional input into the development of the protocol in Scotland. Based on that knowledge we have compared the Scottish protocol with the draft Welsh protocol as follows:

Observation	Scotland	Wales	Comment
Status of Protocol	Final (since June 2008)	Draft	-
Parties to the Protocol	Scottish Government, Directors of Finance, COSLA, CIPFA, Audit Scotland	Welsh Government, WLGA	Key stakeholders in Scotland have contributed to the protocol. There is a 'buy-in' to any resulting process.
Transparency of Protocol	Available on Scottish Government website	Not yet publicly available	-
Timing of Imposition of Limits	Specified that "...any limit ..would be set in advance and apply to the following financial year only."	(Welsh Government) "...would expect advance notification" Noted that WLGA will be required to comment on proposals within 5 working days.	Clarity in Scottish protocol that the limit would be set in advance. Less certainty in the draft Welsh protocol.
Level of Detail included within the protocol	Detailed paper including definitions and parties to whom applicable	Short paper only.	Level of detail in Scotland has enabled advance debate and subsequent clarity on issues which may yet have to be addressed in Wales.
Clarity and Specification of Allocation Methodology	Detailed methodology described including data required and calculation methodology for individual authority allocations.	Proposed methodology yet to be determined per para 10 of the draft protocol.	

- 4.7 The key issues which emerged from the comparison was that devolved administrations and local authorities are in differing states of readiness for any national limit imposition. Although devolved administrations are entitled to take their own decisions, any imposed limit will of course be UK-wide.
- 4.8 A further implication for the Committee to consider, in the event of additional borrowing powers being granted, will be whether a detailed and transparent protocol for national government is desirable and whether it should be developed. The Scottish local government protocol provides a useful benchmark against which a national protocol could be developed.

5. INNOVATIVE FUNDING MODELS: NON-PROFIT DISTRIBUTING ORGANISATION MODEL (NPDO)

Introduction

- 5.1 Whilst the main focus for this submission has been prudential borrowing, we note that the Committee also intend to address alternative funding models from elsewhere in the UK. Over the last four years local authorities in Scotland have contributed to the development of a new model, referred to as a non-profit distribution model (NPDO). In this submission we briefly set out the underlying features and, on a case study basis, we describe how this has operated in one Scottish local authority. This NPDO model was developed over 7 years ago and the core principles are still used through the national HUB development initiative and Scottish Futures Trust and there have been some developments since then.
- 5.2 The model which is a derivative of early private finance schemes has the following identifiable features:
- Profits earned by the Special Purpose Vehicle company (SPV) are paid to a charity
 - Achievement of similar or Improved value for money as a standard PPP
 - A more transparent governance structure to ensure NPDO principles are adhered to by the SPV

NPDO – A Practical Case Study

- 5.3 When options were being appraised to deal with the backlog in maintenance of a local authority's school estate, traditional PPP was seen to have a number of drawbacks particularly relating to the expense and the possibility of windfall surpluses accruing to the private rather than the public sector.
- 5.4 The NPDO approach maximises the opportunity for the local community to benefit from SPV profits by removing the need for equity shareholders and diverting all surpluses generated during the concession period to a charity devoted to educational aims. In all other regards this is similar to a traditional PPP which is important in terms of marketability of the scheme. The local authority has a contractual relationship with a SPV. This contractual relationship is based upon the standard PPP contract.
- 5.5 In the case of this particular authority, the release of funding was dependent upon the contract being compliant with the Scottish Schools Standard Contract (SSSC). The adoption of a contract consistent with standard PPP contracts was seen as a key element of ensuring there was a market for the project especially given the volume of schools PPP contracts brought to the market at around the same time.

Financing

- 5.6 The project is entirely financed by borrowing. None of the shareholders have a return in the SPV that will yield them an investment return beyond that earned as interest on monies lent to the SPV. Around 90% of the funding is referred to as senior debt and this has been borrowed at a rate similar to other more traditional PPP projects.
- 5.7 The remaining 10% is referred to as junior or subordinated debt. This has less security than the senior debt and has a higher rate of interest. This is because it

exposes the lender to a greater risk. Lenders of senior debt get their interest and principal repaid before the lenders of junior debt.

Governance

- 5.8 The board of the SPV comprises up to 5 directors appointed by the providers of the subordinated debt. Each of the private sector partners in the project has a minimal shareholding. This allows them to appoint directors to the board. In addition to the directors appointed by the subordinated lenders there is an independent director (ID) appointed by Partnerships UK and a stakeholder director (SD), appointed by the Authority in the first instance, but who will be appointed by the charity when this is established.
- 5.9 The ID's role is to ensure that the SPV conforms to the NPDO principles enshrined in the Memorandum and Articles of Association and the Project Agreement. The ID is also responsible for initiating any refinancing of the project. The SD is responsible for ensuring the charity's interests are protected at SPV board level and that surpluses are passed to the charity in line with the Project Agreement.
- 5.10 The board of directors do not manage the SPV directly but appoint a management company to manage the contract and various sub contractors on behalf of the SPV. As part of the project the private sector partners had to agree to a resolution agreeing not to take a dividend or return based on their shareholding but to transfer any profits beyond a certain level to charity. The amount of profit that can be retained by the SPV is set at a level to provide an incentive to management and to provide for operational stability of the SPV.

The Charity

- 5.11 It is envisaged that a charity, separate to the SPV, will be set up to receive monies when any surplus funds are generated, although the exact charity is not specified in the SPV's company documents. The charity's probable objectives have been drafted and are expected to cover the following:
- for the public benefit to advance education and social welfare through the provision and/or finance of educational facilities, equipment and/or services;
 - to provide and/or finance the provision of facilities, equipment and services to advance the education of people who have any disability or infirmity or who suffer from ill health;
 - to promote community participation in healthy recreation by providing and/or financing facilities, equipment and services for playing sport;
 - to promote community participation in the arts and culture by providing and/or financing facilities, equipment and services in relation to arts and culture;
 - to advance the physical education of young people by providing and/or financing facilities, equipment and services for playing sport;
 - to promote access for and inclusion of disadvantaged groups and individuals to educational facilities, equipment and services; and
 - generally to provide, participate in and/or finance the provision of educational facilities, equipment and services for the benefit of the public.

Comparison with Standard PPP Contract

5.12 The following table summarises both the differences and the similarities in comparison to a standard PPP contract.

Similarities to Standard PPP	Differences with Standard PPP
Based around a DBFO contract between the public sector and a SPV.	100% debt funded
Consistent with SSSC for local NPDO	No equity return to SPV shareholders
High level of debt finance for SPV	SPV profits transferred to charity
Same risk / reward profile as PPP for accounting treatment	Independent and stakeholder directors on SPV board
VFM advantage of NPDO over public sector model comparable to traditional PPP scenario.	Sharing of refinancing gains extends to junior debt (not available in standard PPP because equity cannot be refinanced)

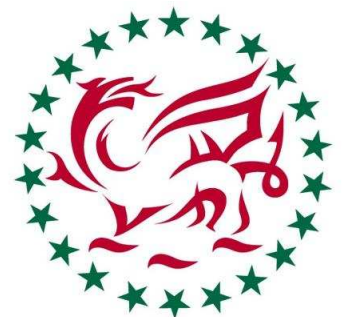
5.13 Going forward there are likely to be developing consequences which have yet to emerge including likely lengthy negotiations with funders on security and the practical consequences with no efficiency savings passed on to shareholders.

Finance Committee

FIN(4)-08-12 - Paper 2

Prudential Borrowing and innovative approaches to capital funding

March 2012



INTRODUCTION

1. The Welsh Local Government Association (WLGA) represents the 22 local authorities in Wales, and the three national park authorities, the three fire and rescue authorities, and four police authorities are associate members.
2. It seeks to provide representation to local authorities within an emerging policy framework that satisfies the key priorities of our members and delivers a broad range of services that add value to Welsh Local Government and the communities they serve.

Background and the Prudential Code

3. Under Sections 1 and 12 respectively of the Local Government Act 2003, local authorities have the power to borrow and invest for (a) any purpose relevant to their functions, and (b) the purpose of the prudential management of their financial affairs.
4. The prudential system for local authority capital finance was introduced on 1 April 2004 and enables local authorities to decide for themselves how much they can afford to borrow based on a prudent assessment of their capital needs. The duty to determine the level of affordable borrowing places reliance on self-regulation under professional codes of practice including the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code for Capital Finance in Local Authorities.
5. This new prudential system replaced the capital financing regime set out in Part IV of the Local Government and Housing Act 1989, whereby capital expenditure funded by borrowing (and all other forms of credit) was controlled through the issue by the Welsh Government of credit approvals, i.e. authorities were only able to borrow to the extent authorised by the Welsh Government. Any borrowing needs a revenue resource to pay for it over the period of the loan so without extra revenue to fund the costs of borrowing (for instance through tax raising) scarce revenue resources will be used up.

What is the total level of prudential borrowing across Wales and the prudential borrowing limit in each year since the inception of the scheme?

6. In this evidence and in any subsequent oral evidence presented to the Finance Committee it should be noted that the following terms will be used in describing local authority borrowing. The Prudential Code 2004 relates to the **total borrowing** of

an authority; there are two limits on **total external debt**; the 'Authorised Limit' and the 'Operational Boundary' **both of these 'limits' are calculated and set by the local authority** for the forthcoming and following two financial years. In calculating these limits the authority will ensure that they are consistent with future plans for capital expenditure and their treasury management statement and practices.

7. The 'Authorised Limit' is defined by the CIPFA Code as:

Authorised limit for external debt = authorised limit for borrowing + authorised limit for other long term liabilities

8. The 'Operational Boundary' is defined in the following way:

Operational Boundary for external debt = operational boundary for borrowing + operational boundary for other long term liabilities.

9. The operational boundary is the authority's prudent (but not worse case) expectation of their maximum level of external debt. It will be informed by capital expenditure plans, capital financing requirements and cash flow projections. It is a key tool for in year monitoring. The authorised limit is the higher figure and provides headroom over and above the operational boundary sufficient for example, unusual cash movements, which if breached is referred to members for resolution.

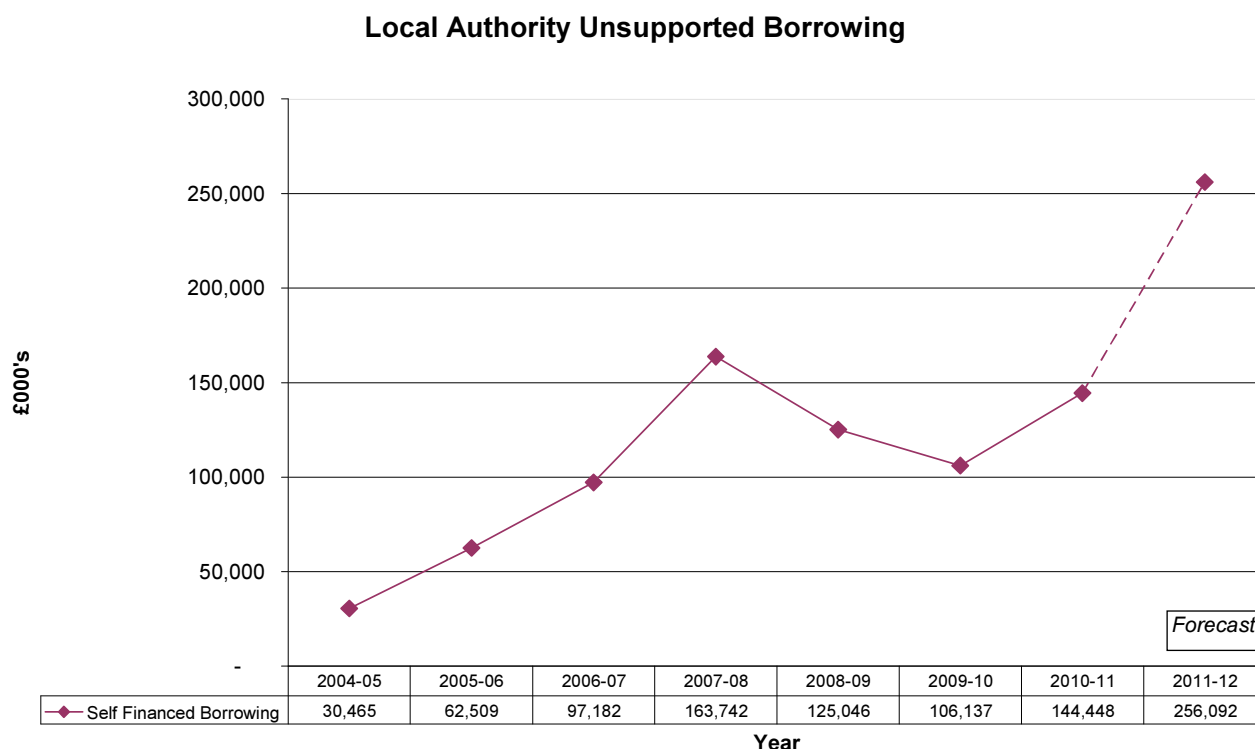
Unsupported borrowing

10. In presenting this evidence the WLGA, working with the Society of Welsh Treasurers (SWT) has answered the questions from the position that the questions relating to 'prudential borrowing' are actually concerned with 'unsupported borrowing' i.e. the borrowing undertaken by an authority that is not supported by a government grant. This is a crucial distinction as when using unsupported borrowing authorities must find the necessary financing from within their existing resource total.

11. The take up of unsupported borrowing does vary between local authorities and some authorities have done only limited amounts. This may be due to a cautious approach to borrowing generally, other available forms of financing such as capital receipts, or a political aim locally to keep council tax increases down. Authorities are also free to undertake unsupported borrowing to fund projects partially funded by the Welsh Government grants but again taking into account the councils overall financial position.

12. Given the ever tightening level of public finances and the continued growth in demand for public services in Wales there is a huge amount of pressure on a small amount of capital funding. The disaggregation of different borrowing streams is difficult from a technical, treasury management perspective but also from a strategic and planning perspective where they should be considered together. Decisions on the determined level of capital expenditure should be taken considering both supported and unsupported borrowing as a part of the level of affordable debt.
13. Figure 1 sets out the levels of new unsupported borrowing undertaken by all Welsh local authorities (including Police, Fire and National Park Authorities) since the beginning of the scheme.

Figure 1¹



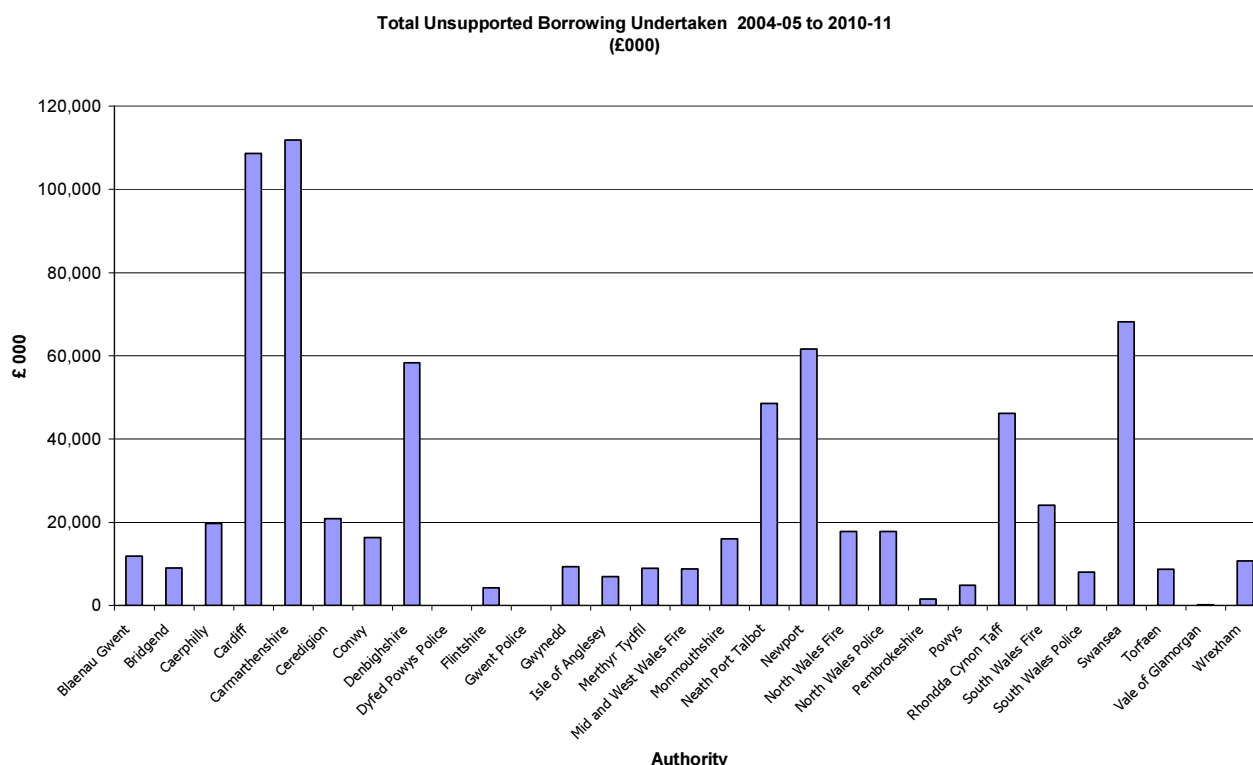
14. Since 2004-2005 (to 31/3/2011) authorities have financed **£730million** of capital expenditure through unsupported borrowing. This has increased from £30million in 2004-2005 (3.54% of total capital expenditure) to £144million in 2010-2011 (14.48% of total capital expenditure). It is expected that in 2011-2012 authorities will use over a **quarter of a billion pounds (£256million)** and this **will represent 24%** of their total capital expenditure.

¹ Data taken from Capital Outturn and forecast returns 2004-2012

15. It is evident from the chart that following the emergence of the global financial crisis in 2007 – 2008 there was a marked reduction in some authorities’ appetite for unsupported borrowing given the uncertainties surrounding the public finances. The increase seen in 2010-2011 represents recognition that the financial settlement in the Comprehensive Spending Review 2010 saw Wales’ capital severely reduced. In light of these cuts and a significant reduction in the availability of other sources of finance such as capital receipts, authorities were forced to use more unsupported borrowing to ensure that service critical schemes were started and completed. This trend is repeated in 2011-2012.

16. Individual authorities have developed differing positions regarding the use of unsupported borrowing and can be seen in figure 2. (A full listing of all unsupported borrowing undertaken by Welsh authorities since the schemes inception can be found at Annex 1)

Figure 2²

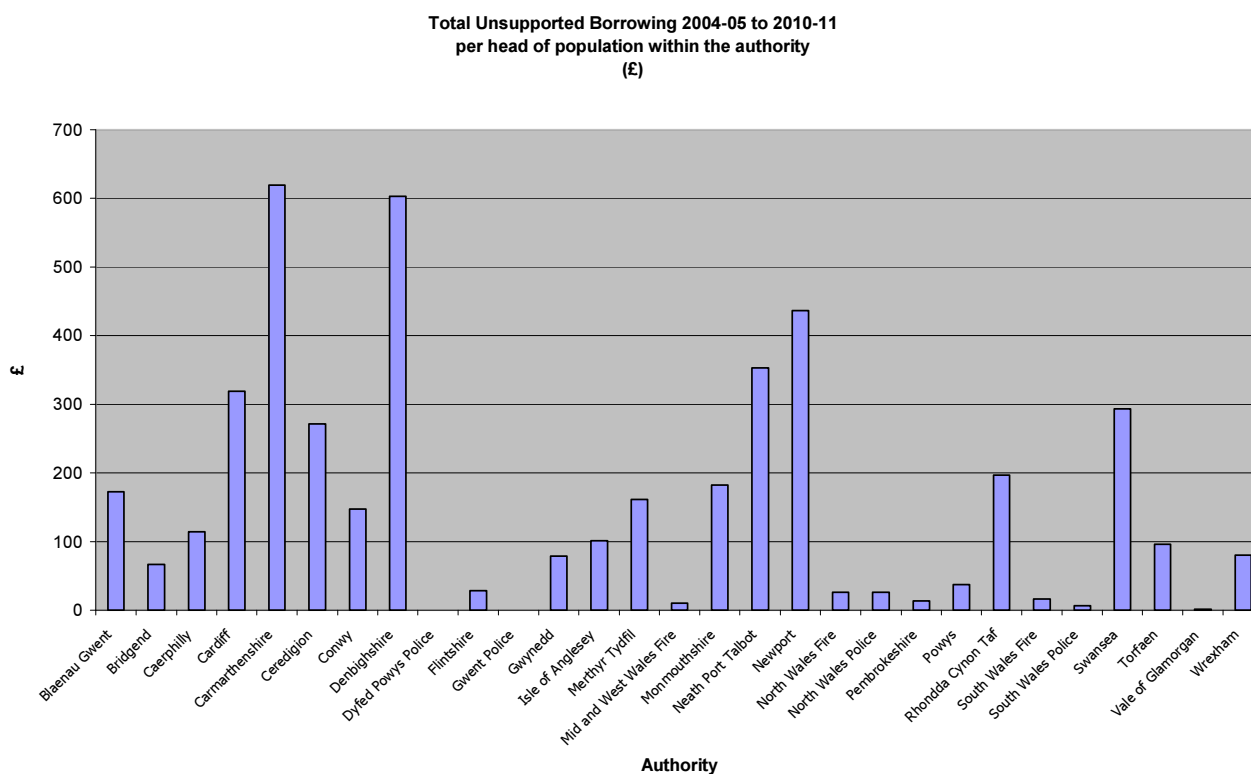


17. Figure 3 illustrates the levels of unsupported borrowing undertaken per head of the population. The differential occurs because each authority will approach its capital financing requirements from their own perspective. They will have differing circumstances in terms of previous investment levels and current investment

² Data taken from Capital Outturn returns 2004-2011

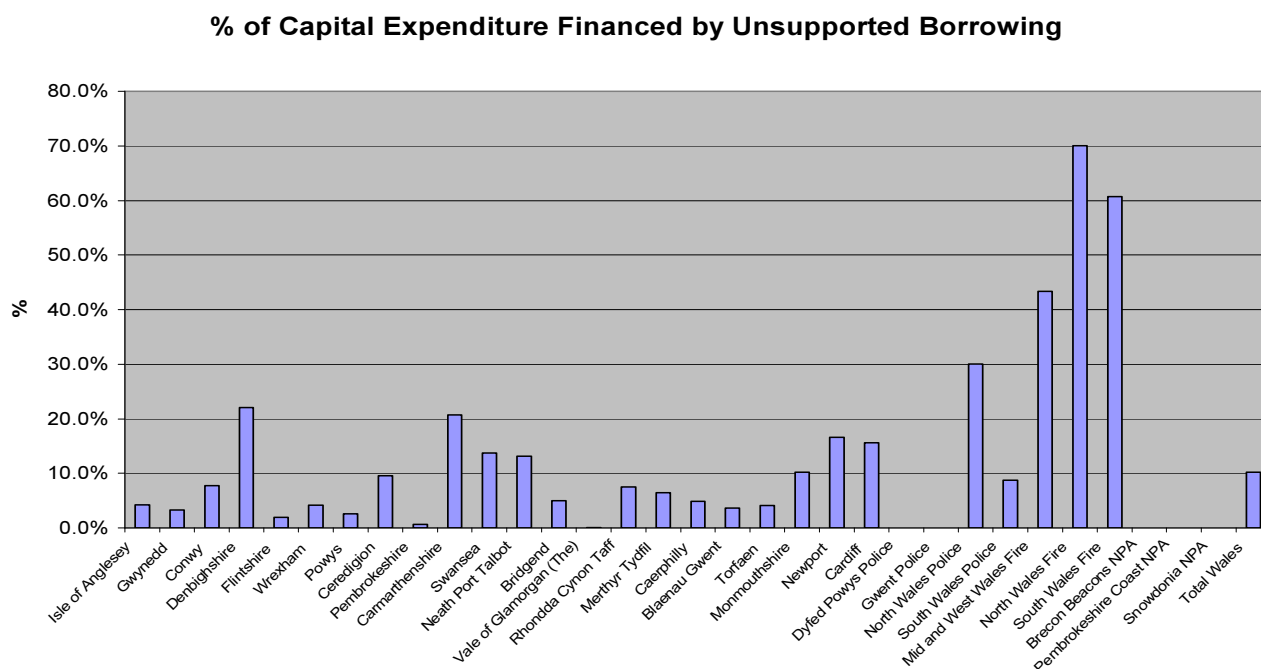
priorities. There will also be a range of differing views of risk and risk appetites. The Authority must use its own professional judgement to determine that the funding raised is "Sustainable, Affordable and Prudent" taking into account the councils overall financial position.

Figure 3³



³ Data taken from Capital Outturn returns 2004-2011

Figure 4⁴



18. Figure 4 shows the percentage of capital expenditure financed by unsupported borrowing.

19. Carmarthenshire’s position as the highest user of unsupported borrowing, both in absolute and relative terms, relates to specific policy and financing decisions in four key areas. These are; the Modernising Education Provision Programme (refurbishment and new build of education establishments), the HRA Programme (Meeting the WQHS on Council housing), the recent Highways Improvement WG funding and the Fleet Replacement Programme (purchase of new/replacement vehicles) which, in many cases, replaces leasing arrangements.

20. The local authority that has undertaken the smallest amount of unsupported borrowing is the Vale of Glamorgan. This has been a conscious decision at the authority where, to date, other funding streams have been utilised. However, the authority recognises that in the future the pressures of meeting the Welsh Quality Housing Standard (WQHS), the funding challenges presented by the 21st Century Schools initiative and the Local Government Borrowing Initiative highway scheme will mean a greater amount of unsupported borrowing being used.

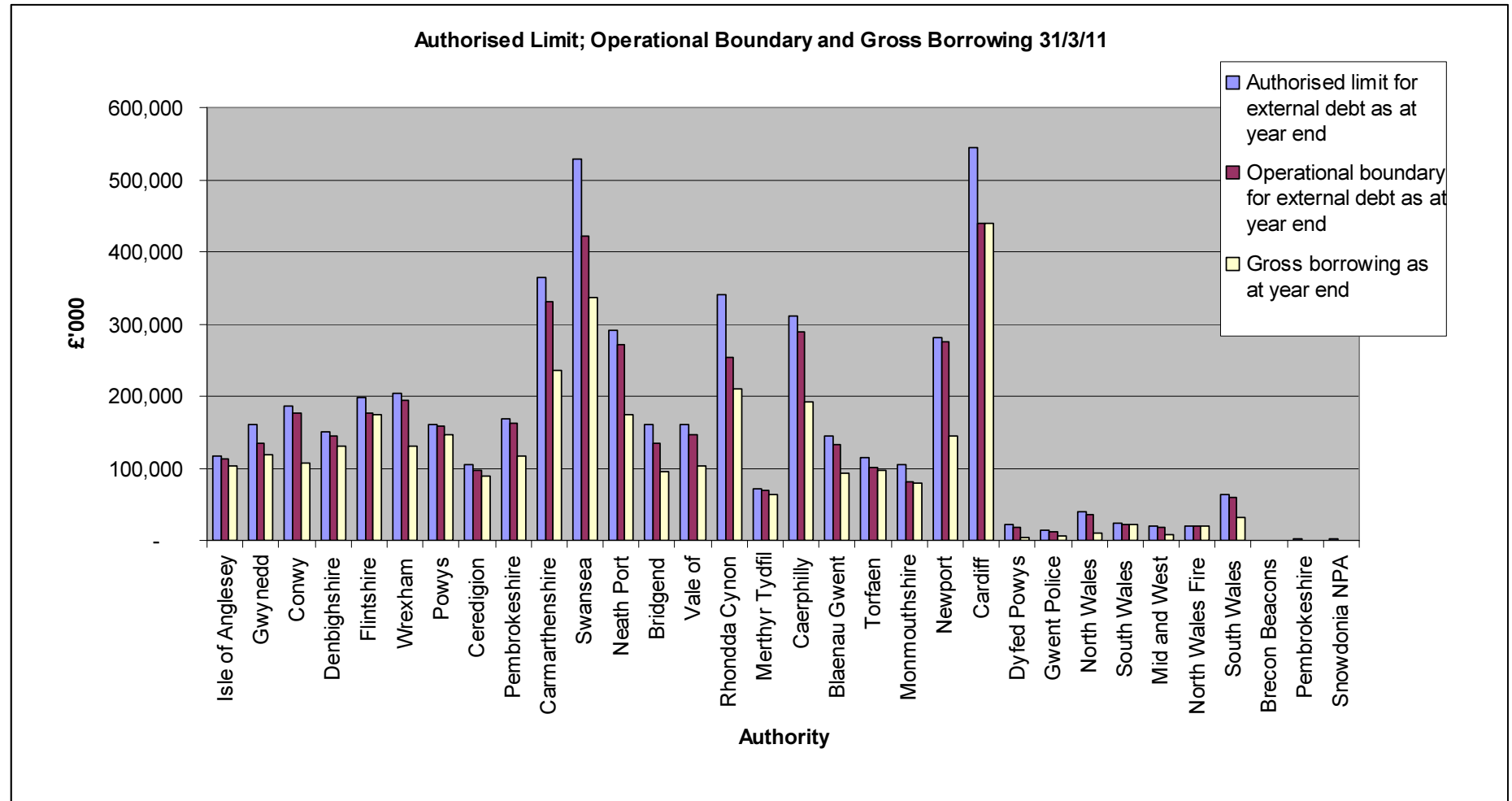
21. In considering the question of limits, figure 5 sets out the authorised limit, operational boundary and total borrowing for each authority for the financial year

⁴ Data taken from Capital Outturn returns 2004-2011

ending 31 March 2011. The total authorised limit for Welsh authorities in the financial year 2011 was £5.06billion and the operational boundary was £4.48billion. In that year the actual external borrowing was £3.48billion. The authorised limit and the operational boundary are not limits for the amount of total borrowing that an authority can undertake but relate to the **level of external debt** at any given time.

22. There is an emerging trend amongst authorities that they use internal borrowing whenever possible as this is a more cost effective option than borrowing from the market as the cost is solely the loss of investment income, which at the moment could be as low as 0.25%. Many treasury management strategies will encourage the effective use of internal borrowing.

Figure 5⁵



⁵ Data taken from Capital Outturn returns 2004-2011

What measures are taken to determine and keep under review prudential borrowing limits, including the processes, consideration of revenue implications and how this is undertaken?

23. There is no statutory limit to an authority's prudential borrowing, unsupported or supported, and all borrowing is considered as part of the authority's broader capital programme. All authorities will have to ensure their compliance with the CIPFA prudential code and demonstrate this compliance during external audit of their accounts each year. The overall amount of external borrowing, of which unsupported borrowing forms a part, is calculated each year as the Capital Financing Requirement. One of the Prudential Indicators required by CIPFA's Prudential Code is the amount of borrowing costs (MRP and External interest) as a proportion of the budget and this is used as an important headline indicator.
24. A suite of Treasury Management and Prudential Indicators are produced by authorities before the start of the financial year. These ensure that capital investment decisions are affordable, prudent and sustainable. The Indicators are set within the Treasury Strategy Statement. They are also monitored at an appropriate frequency (often quarterly) and reported to the appropriate political level, Executive / Cabinet or Council. The operational boundary itself will be monitored on a daily basis once daily money market transactions have taken place as a part of the normal treasury management activities undertaken by local authorities.
25. Any unsupported borrowing is approved as part of the discussions on the whole Capital Programme. It is another means of financing along with supported borrowing, grants and contributions and capital receipts.
26. The management of a capital programme will have a series of approval processes and form a key part of the budget setting process; this will involve both officer and member considerations. The Executive / Cabinet will have a significant role but the broader considerations will also be informed by the full budget processes which will engage all members in the scrutiny and agreement of the budget. The management of capital expenditure is becoming increasingly sophisticated in Welsh authorities and there is an understanding that capital investment decisions need to contribute to the achievement of the authority's strategic objectives. Authorities will seek to link their asset management plan, capital strategy and treasury management strategy which should all be based on the same consistent assumptions regarding capital expenditure and financing profiles.

27. There are a range of approaches developed across Wales in how unsupported borrowing is used and how its use is approved. The key consideration in all of these is that the borrowing is affordable and the revenue costs are either:

- met from existing resources because it is an authority priority; or
- met from the benefits of the capital investment.

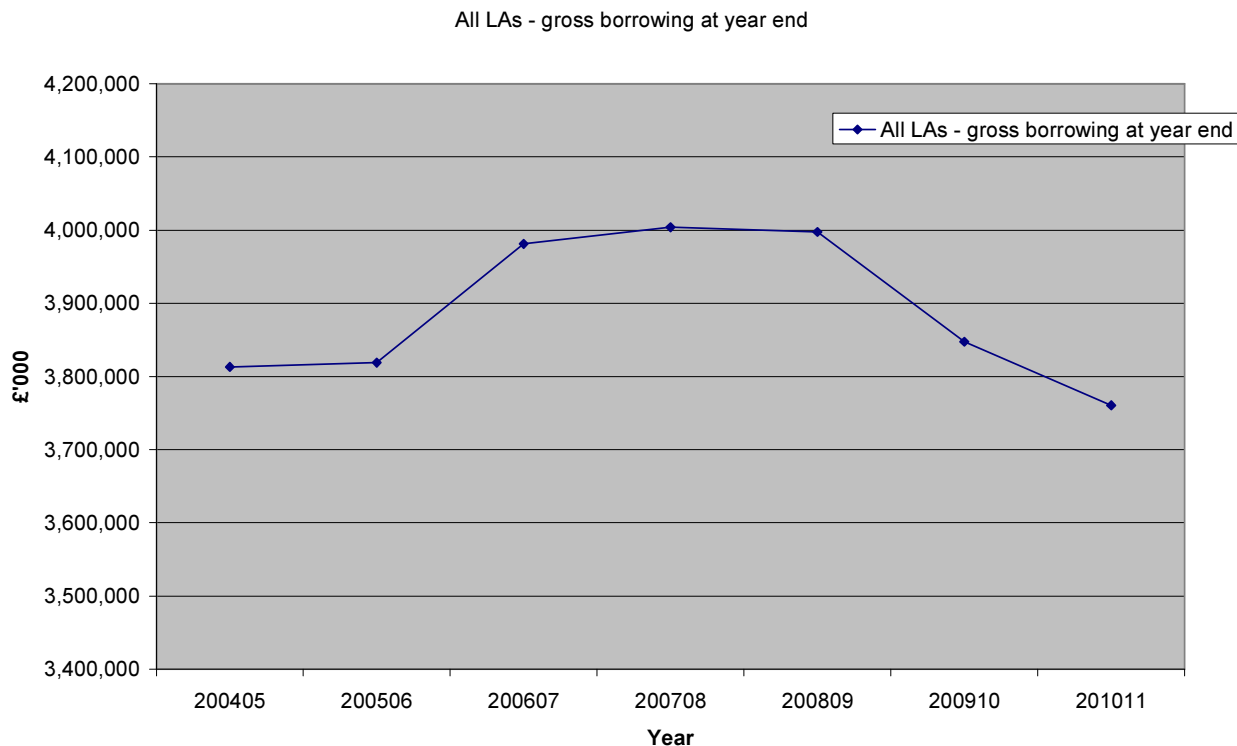
28. In order to control the savings and ensure a 'corporate' focus is maintained a number of authorities identify the revenue savings of a specific project and these are then "vired" from the spending portfolio to a central debt management budget for the period of the prudential borrowing and are controlled centrally.

29. Critically, in all authorities the revenue implications are considered when a project is proposed and the revenue funding identified. The funding is also considered as part of the medium term financial plan. Some authorities have made a policy decision that they will not increase Council Tax to finance unsupported borrowing.

What is the level of outstanding debt at 31 March 2011 and the implications in terms of annual repayments due in the future?

30. As at the 31 March 2011 the **total gross borrowing** outstanding (**both unsupported and supported borrowing**) was £3.76 billion. This has fallen from a high of £4 billion in 2007-2008. The reducing level of gross borrowing seen in figure 6 contrasts with the rising levels of unsupported borrowing identified in figure 1. It represents a conscious decision on the part of authorities to reduce their levels of external borrowing as a value for money consideration (to reduce reducing interest payments) and a consequence of treasury management strategies to maximise the use of internal resources such as internal borrowing. Furthermore, historic debts, brought forward from previous authorities, are falling out.

Figure 6⁶



31. In 2010-2011 local authorities budgeted £340million for debt management (both supported and unsupported), this represents 4.7% of net revenue authority expenditure. The level was predicted to remain at the same in 2011-12.

What is the average cost of servicing prudential borrowing, in terms of total amount borrowed compared to total amount repaid over the lifetime of the borrowing?

32. Because Welsh authorities operate integrated treasury management strategies and meet the standards set out in the CIPFA Treasury Management Code of Practice it is not possible to separate and identify the average cost for unsupported borrowing. At any time an authority will look across its borrowing requirement and seek to achieve the most cost efficient borrowing to meet their needs. Furthermore, in following accounting practice it is not possible to match specific borrowing to a specific asset.

33. Welsh authorities have developed robust business planning processes which will identify a funding requirement and the cost of borrowing the funds necessary to implement the changes and this will be considered as a part of the decision making process. There are a range of mechanisms that authorities can use to assess

⁶ Capital forecast forms; Welsh Government

business cases such as internal rate of return or net present value but these decisions are separate to the actual financing. The critical rule is that the result of the business case must be greater than the opportunity cost of the borrowing.

Provide a brief overview of the nature of projects / purposes for which funds from prudential borrowing have been used

34. There is a high degree of similarity in the schemes that Welsh authorities have chosen to use unsupported borrowing for and these will be outlined further in this section. Furthermore there were a number of common drivers for the use of unsupported borrowing:

- Opportunity – through sound financial planning authorities have been able to take advantage of their borrowing powers to take decisions that provide greater efficiency within their organisations. Examples of opportunity could be buying a building when the cost of the debt is less than the lease charge, and managing vehicle fleet through purchase rather than lease.
- Return – There are some decisions that are taken because the investment will make a return for the authority. Examples could be investment in energy efficient buildings, the release of funding through consolidating education provision into a reduced number of schools eliminating surplus places or investment in leisure centres where upgraded facilities create higher income streams or reduced running costs.
- Member choice/priority – There will be occasions where local politicians determine a policy choice and the decision is supported through investment in unsupported borrowing when this resource could have been spent elsewhere.

35. The main areas where unsupported borrowing has been used are:

- **The purchase of vehicles, plant and equipment** – savings due to capital charges being less than the lease cost;
- **Leisure Facilities** – new and improved services are funded through unsupported borrowing and the greater footfall and membership provides the income to support the borrowing;
- **Education and rationalisation of surplus places** – through consolidating school places old and expensive buildings can be closed, there are consequently fewer buildings to support and maintain and these are often

cited as having reduced energy costs and providing an enhanced learning environment;

- **Energy efficient premises** – old office accommodation can be expensive to maintain and heat through moving to newer premises reductions in maintenance and energy costs will cover additional capital charges;
- **Photovoltaic (PV) Cells** – a number of authorities have fitted PV cells to both council buildings and council houses to reduce energy costs and provide income through the feed in tariff scheme;
- **Improved street lighting stock** – authorities are able to invest through the reduced running costs of new stock
- **Housing** – for those authorities who have either chosen to retain their housing stock or have been unsuccessful in their transfer ballots unsupported borrowing funding through the Housing Revenue Account (HRA) and tenants' rents is the key means of achieving the Wales Housing Quality Standard.
- **Invest to save schemes** - authorities have chosen to use unsupported borrowing to finance internal schemes that will promote efficiency within the organisation, eg as a part of IT investment and change processes.

LGBI – Highways Infrastructure Improvements

36. In 2011-2012 the Welsh Government and the WLGA designed and agreed a scheme to promote investment in local authority highways. It provided authorities with additional resource to allow an increase of unsupported borrowing to finance expenditure on highways infrastructure. The programme will, over a three year period, provide approximately £170m additional funding. This was the first scheme of its type; it is reliant upon authorities providing robust business cases for their investment plans and these being considered at a regional level through the transport consortia. The scheme has received a positive response from local government as a means of improving highways infrastructure across Wales. Furthermore, through effective supply chain management it will create a stimulus in the Welsh economy.

Are there any lessons learned or concerns would wish to highlight in relation to prudential borrowing?

37. Since the introduction of the Prudential Code authorities have developed their use of unsupported borrowing. The freedom provided by the introduction of the Prudential Code encouraged a new way of thinking about capital investment decisions and how they link with wider strategic objectives and plans. It also required the development of a new set of skills in order to make best use of the powers for the benefit of local communities. This has been undertaken in a prudent way ensuring that the decisions made today have not left an unaffordable legacy for future generations. The affordability indicators of the Prudential Code are an important monitoring mechanism for authorities but they will be established locally. The Prudential Code states that authorities should have regard for the following matters:

- affordability, eg implications for the Council Tax
- prudence and sustainability, eg implications for external borrowing
- value for money, eg option appraisal
- stewardship of assets, eg asset management planning
- service objectives, eg strategic planning for the authority
- practicality, eg achievability of the forward plan

38. Unsupported borrowing has proved to be a valuable option for local authorities in progressing business cases, saving money and enabling change. But it is critical that the 'golden rule' of unsupported borrowing is adhered to i.e. that the borrowing should not be undertaken unless there is a sufficient, sustainable revenue stream committed to support it. Furthermore it is important that "fixed" costs such as capital charges do not become too great a proportion of the revenue budget as that makes efficiency savings harder to achieve as there is less ordinary revenue expenditure to be saved.

39. This is a very important consideration; although the use of unsupported borrowing has increased as authorities try to bridge the gap between capital investment need and the available funding, there is a revenue 'tail' associated with all borrowing. There is a need to balance capital investment needs with any potential to to constrain the delivery of mainstream services.

40. With decreasing core capital funding and reduced ability to raise capital receipts there is a very real danger that unsupported borrowing is seen as the only answer to capital shortfalls. Significantly increasing the financing costs to net revenue stream percentage or 'silting up the revenue budget with mortgage costs' is not a sustainable approach.
41. Given the complex relationship between capital and revenue expenditure and need it is inadvisable to consider one without the other.

Provide a brief overview of any alternative mechanisms the authority may be considering to finance capital investment in the future

42. Local authorities continuously seek alternative funding mechanisms to lever much needed resources into local areas and economies. This investment can be used to directly fund assets or to work in partnership with others, to allow greater levels of investment. Local authorities have considered and will continue to consider the mechanisms set out below.
43. **Tax Increment Financing** - The current approach to TIF being explored in England and Scotland proposes that 70% of the business rate uplift in a designated area is retained locally with the remaining 30% being returned to the centre. If through the CBD project Cardiff delivers 200,000 sq ft of new, occupied, development each year over the 5 year life of the Enterprise Zone, this could equate to around £1m of locally retained revenue per year, totalling £5m by the end of the life of the Enterprise Zone. £5m of revenue retained over 25 years would enable borrowing of circa £50m to invest in major infrastructure improvements.
44. **European Funding** - In light of the current economic crisis, and in particular the scale of the cuts Wales is facing in capital expenditure, the need to invest in capital infrastructure should be very high up on the list of priorities for the future European Structural Fund Programmes for Wales. We will need to be much more creative and innovative in how we use future European Funding as a catalyst for further investments from the private sector and be cleverer about how to achieve more sustainable investments.
45. The scale of the cuts across the public sector will make it more challenging to find match funding in the new programmes. As a result every opportunity to assist in this will need to be explored. A specific match funding pot will be essential for the next programming period but this has to align with the Structural Fund processes and be much more flexible and open than the current Targetted Matched Fund pot. Further,

clarity around other potential Welsh Government departmental match funding sources will be critical early on in the new programming period.

46. In the future programmes we will need to work together in order to lever maximum value from financial packages which utilise Welsh Government departmental budgets such as the Centrally Retained Capital Fund, funding for Regeneration Areas, the new Communities First Programme, education and skills, and other organisations' budgets such as the Big Lottery and Job Centre Plus etc to add value to the European Funding. This needs to include how to make more use of match funding the European Funds at source to make it easier for businesses and communities to access this much needed funding in the future.
47. This will also need to include more creative thinking about how we fund capital infrastructure projects in the future, including accessing funding from other EU sources such as the Connecting Europe Facility for Infrastructure investments and maximising the borrowing potential of local government, to act as a catalyst for further investments from the private sector.
48. **Joint European Support for Sustainable Investment in City Areas (JESSICA)** – Is essentially a partnership approach to investing in urban areas. It allows authorities to work with partners in both the public and private sector to find innovative funding solutions to project financing whilst using European structural funds. In Wales the Regeneration Investment Fund for Wales (RIFW) is a Welsh Government funded vehicle.
49. **Local Asset Backed Vehicle** – allow authorities to use their assets, rather than cash, to engage partners in investment vehicles. These have been used extensively in England with Croydon being a leading proponent of the model.
50. **Public Private Partnerships (PPP)** – for many in Wales the discussion regarding PPPs has become a binary argument focused on those either positive negative experiences of private finance initiative (PFI). The WLGA has worked with partners such as CBI Wales to understand the potential for greater private sector engagement recognising that there have been political restraints put upon its use in other parts of the Welsh public service.
51. **Securitisation** - is the disposal of future revenues. For example, someone receiving rents from properties might transfer the entitlement in exchange for an immediate lump-sum payment. From a technical accounting viewpoint, securitisation appears to be the sale of an asset (the future revenue stream) and the lump-sum received is

the sale proceeds, not borrowed money. But the strategy achieves the same result as borrowing and it might be thought that it could be used as an alternative to it. This is a very new funding model being looked at by some of the London Boroughs.

Do you have any views on potential implications on local authorities of the Welsh Government's stated intention to maximising local authorities borrowing power to boost capital available for infrastructure?

52. The WLGA has long advocated the potential role of local government in supporting the need for infrastructure investment in Wales to encourage inward investment, enable business in Wales to be more effective and create a stimulus to the economy. We have engaged fully with the Welsh Government to ensure that the Local Government Borrowing Initiative will be a success.

53. However, given the pressures on both capital and revenue funding the WLGA and SWT have concerns that any significant movement towards a greater usage of revenue finance to support capital expenditure will constrict future budgetary flexibility and inhibit choices. The funding gap associated with schemes such as 21st Century Schools and major transport infrastructure schemes (eg M4 relief roads and electrification of rail lines) are significant and the revenue consequence of borrowing to 'fill' those gaps would be significant.

How could local authority borrowing be used to boost the levels of capital available for Welsh infrastructure?

54. The pilot Local Government Borrowing Initiative has demonstrated a model for leveraging greater investment in Welsh highway infrastructure through a collaborative approach. However, the scope for this approach is not infinite given the pressures facing revenue budgets across Wales. In this pilot there was agreement between the Welsh Government and local government regarding the area of expenditure but the importance of local choice and democratic decision making in the investment choices cannot be overstated

What alternative mechanisms of leveraging capital funding being considered by the Welsh Government in the preparation of their Infrastructure Plan, including the possibility of boosting borrowing by local authorities and other organisations?

55. The WLGA believes that the Welsh Government should have borrowing powers with or without tax devolution. However we agree with the Holtham Commission that the case for allowing the Welsh Government to borrow becomes even stronger when aligned with the devolution of tax powers as it would have greater control over its

own revenue. In the meantime Welsh Government has worked in partnership with local government on piloting a Local Government Borrowing Initiative which is due to commence in 2012-13, with Welsh Government providing additional resources to councils to create headroom in their revenue budgets to enable them to undertake prudential borrowing for additional capital investment in highways infrastructure.

In exploring innovative capital models proposed elsewhere in the UK, how these have been developed, utilised, and, where possible, how they have performed.

56. The WLGA and SWT have undertaken a number of pieces of work to establish the viability of differing approaches to capital financing models. Some of this work has been undertaken under the auspices of the the Capital Finance and Investment Group (CFIG) a key part of the infrastructure of the Partnership Council and the Consultative Forum on Finance.
57. The ongoing work in Scotland regarding TIF and the current work of the Local Government Association in England (LGA) who are looking at local government creating its own bond issuing vehicle are recent examples. The joint WLGA / CBI working group spent several months understanding the potential advantages of the public sector working alongside the private sector in managing and delivering capital investment.
58. However, the decision to use any of the more 'innovative' models that are outlined in paragraphs 43 – 52 is in essence a local choice. The hugely challenging financial environment that all of the Welsh public service is working in means seeking value for money and continued flexibility to respond to budgetary challenges are authorities' key concerns. The use of unsupported borrowing managed effectively in house removes the need for a partner to achieve a commercial return on any investments. This means that whilst interest rates remain at historically low levels, authority-led solutions are the most popular. There are exceptions to this, for instance the current TIF proposal in Cardiff.
-

For further information please contact:

Will McLean, Programme Lead, Resources Team

will.mclean@wlga.gov.uk

Welsh Local Government Association

Local Government House

Drake walk

Cardiff

CF10 4LG

Tel: 029 2046 8600

New Unsupported Borrowing undertaken by Local Authorities in Wales

	2004-05 £ 000's	2005-06 £ 000's	2006-07 £ 000's	2007-08 £ 000's	2008-09 £ 000's	2009-10 £ 000's	2010-11 £ 000's
Isle of Anglesey				888	534	4,109	1,389
Gwynedd	2,418		923	1,707	798	2,309	1,225
Conwy	172	2,278	2,740	3,455	2,913	3,543	1,244
Denbighshire	1,314	5,821	8,767	13,795	9,500	7,784	11,349
Flintshire	571	786	1,238	162	311	409	757
Wrexham	3,340	255	1,491	13	196	2,387	3,014
Powys	921	2,505	1,471			0	0
Ceredigion	1,222	1,630	2,104	661	15,191	31	40
Pembrokeshire						806	778
Carmarthenshire	7,057	4,317	9,912	16,712	24,033	21,466	28,399
Swansea		428	22,591	35,330	6,743	3,166	0
Neath Port Talbot	559	3,053	15,886	11,104	6,971	6,425	4,517
Bridgend	1,172	453	93	184	1,432	1,139	4,543
Vale of Glamorgan	178					0	0
Rhondda Cynon Taff	64	13,267	4,858	8,740	8,656	2,874	7,738
Merthyr Tydfil	1,917	1,600	780	4,676		0	0
Caerphilly		5,000	3,956	8,656	1,680	514	0
Blaenau Gwent	420	975	1,427	3,016	1,660	2,949	1,373
Torfaen			5,921			143	2,631
Monmouthshire		525	1,632	98	1,397	4,672	7,719
Newport	1,161	3,319	4,582	16,877	4,348	8,978	22,380
Cardiff	3,506	9,310	611	31,112	10,920	23,174	30,080
TOTAL WALES LA	25,992	55,522	90,983	157,185	97,283	96,879	129,176

Dyfed Powys Police	.	.	-	-	-	-	-
Gwent Police	.	.	-	-	-	-	-
North Wales Police	1,733	5,117	3,222	3,459	2,472	1,576	206
South Wales Police	283	202	-	-	7,000	-	482
Mid and West Wales Fire	.	703	1,462	965	1,078	2,505	2,174
North Wales Fire	2,457	271	729	1,934	4,678	1,636	6,032
South Wales Fire	.	694	786	199	12,535	3,541	6,378
Brecon Beacons	.	.	-	-	-	-	-
Pembrokeshire Coast	.	.	-	-	-	-	-
Snowdonia NPA	.	.	-	-	-	-	-
Total Wales	30,465	62,509	97,182	163,742	125,046	106,137	144,448

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HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

Ms Jocelyn Davies
Chair of National Assembly for Wales' Finance Committee
Cardiff Bay
Cardiff
CF99 1NA

10 May 2012

A handwritten signature in blue ink, appearing to read 'Ben Davies'.

NATIONAL ASSEMBLY FOR WALES'S FINANCE COMMITTEE AND DEVOLVED FUNDING

Thank you for your letter dated 27 March and subsequent email from the Clerk to the Finance Committee and my officials on the 26 April.

2. With thanks for your understanding on the time it has taken for me to come back to you, please see below for further detail in response to each of the queries you raised.
3. A comparison of the existing borrowing powers of the three devolved administrations under the existing Statement of Funding Policy
Currently, local authorities in Wales and Scotland have borrowing powers under the Local Government Act 2003. The Northern Ireland Executive has borrowing powers under the Northern Ireland Loans Act 1975 and the Northern Ireland Miscellaneous Provisions Act 2006 in lieu of its local authorities. This is limited at £200m p.a. which can be used to fund capital expenditure and is agreed with the Treasury at every Spending Review.

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All three of the Devolution Acts – Scotland Act 1998, Northern Ireland Act 1998 and Government of Wales Act 2006 make provisions to enable the Devolved governments to borrow to manage short term cash flow. They also all benefit from UK Government borrowing that is undertaken to fund capital investment throughout the UK.

The current situation in respect of borrowing powers is therefore one of parity across the devolved administrations.

The Scotland Act 2012 introduces a new borrowing regime for Scottish Ministers from April 2015. It breaks the status quo described above on the basis that:

- Scottish Ministers will be responsible for raising around £6bn of devolved taxes from April 2015 onwards. This provides an independent source of revenue which Scottish Ministers can adjust as necessary to support Scottish borrowing;
- Volatility associated with tax raising powers which were previously managed at a UK level will, over time, be transferred to the Scottish Parliament in order to increase the accountability of the Parliament. Borrowing powers form part of the suite of tools available to Scottish Ministers to manage any errors in forecasting devolved Scottish taxes.

4. The extent to which the Welsh Government could be granted borrowing powers, taking account of any lessons learnt from the experience of local authority current borrowing powers

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Future borrowing powers for the Welsh Government are being considered by the Silk Commission alongside tax raising powers. As part of this process I expect the extent to which the Welsh Government could be granted additional borrowing powers to be considered.

5. The borrowing powers proposed to be devolved to the Scottish Government in the Scotland Bill and any controls or limits over how they should be exercised

Holding levels of taxation and spending constant, Scottish borrowing will increase UK borrowing. The Scotland Act and its non-legislative framework therefore places controls and limits on Scottish borrowing to ensure it is affordable for the UK. The Command Paper published alongside the Scotland Bill available at:

www.scotlandoffice.gov.uk/scotlandoffice/.../Scotland_Bill_Command_Paper.pdf sets out the controls on p.38 and p.39.

6. Any protocol which exists between the Treasury, the relevant devolved administrations and local authorities regarding arrangements for limits to be applied to local authority borrowing

There is no formal protocol governing prudential borrowing regimes for local authorities in England, Scotland and Wales, though paragraph 7.4 of the Statement of Funding Policy sets out the arrangements. This can be found at:

http://www.hm-treasury.gov.uk/spend_sr2010_fundingpolicy.htm

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7. Any innovative funding mechanisms for capital infrastructure being explored by the UK Government

The Budget announced a number of innovative funding mechanisms that the Government is considering or facilitating.

The Government will carry out a feasibility study into opportunities to increase the role of private investment in the strategic road network, with a progress update by Autumn Statement. The Budget announced a short list of options to improve capacity on the A14 which could be part-funded through tolling.

In addition, the Government has supported the establishment of a new Pension Infrastructure Platform, including up to a dozen of the UK's largest public and private sector pension schemes, which will make the first wave of its initial £2 billion of investment in UK infrastructure by early 2013.

References to the Budget are 1.219 (p39) for roads points and 1.225 (p42) for pension funds. The document can be found at:

<http://www.hm-treasury.gov.uk/budget2012.htm>

8. If the Welsh Government were given power to issue a bond, what control mechanisms would the Treasury wish to see put in place?

The case for a devolved administration borrowing from the bond market is not clear cut, and has potential implications that extend further than for other sources of borrowing. The Scotland Bill does not provide the power for the Scottish Government to borrow by way of bonds, but allows for Treasury ministers to grant this power in the future where this does not undermine the overall UK fiscal position or have a negative impact on total

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UK borrowing. The Government has committed to issue a consultation to explore the issues around Scottish bond issuance shortly.

9. The Scotland Bill consultation has focused considerably on the volume of permissible debt. The borrowing will be undertaken through the purchase of specific debt products. What products of debt are being considered as part of the consideration of giving borrowing powers to the Scottish Government as a result of the Scotland Bill, and will consideration be given to restricting the bodies from which the Scottish Government will be able to borrow?

The Scotland Act 2012 enables Scottish Ministers to borrow from the National Loan Fund and for capital purposes, commercial banks in addition to the National Loan Fund. The question of access to the bond market will be subject to a forthcoming consultation.

10. As you will know, a protocol exists between the Welsh Government and Welsh local government in terms of the procedures to be following if a national limit on local authority borrowing is required. If the Welsh Government were granted borrowing powers, would you envisage a similar protocol being introduced between the Treasury and the Welsh Government?

Future borrowing powers for the Welsh Government are being considered by the Silk Commission alongside tax raising powers. As part of that process I expect borrowing limits and controls including any protocols to be considered.

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11. If the Welsh Government were granted borrowing powers, and a national borrowing limit was set, how would you envisage that borrowing limit being shared between local and central government?

Future borrowing powers for the Welsh Government are being considered by the Silk Commission alongside tax raising powers. As part of that process I expect borrowing limits and controls to be considered.

12. Local government in Northern Ireland has recently been granted powers to undertake prudential borrowing. How is local government borrowing going to be taken account of within the limit for Northern Ireland Executive borrowing?

The new local government borrowing is in addition to the £200m limit placed on borrowing by the Northern Ireland Executive.

13. Securitisation has been used by at least two Scottish local authorities as a means of raising money based on the security of assets. Have you given any consideration to the use of securitisation as a method of raising finance in Wales?

No consideration has been given to the use of securitisation as a method of raising finance in Wales.

14. I hope this aids your inquiry and let me know if I can be of further assistance

But where

A handwritten signature in blue ink, appearing to read 'Danny Alexander'.

DANNY ALEXANDER

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Finance Committee

Meeting Venue: **Committee Room 4 – Ty Hywel**

Meeting date: **Wednesday, 16 May 2012**

Meeting time: **09:15 – 12:25**

This meeting can be viewed on Senedd TV at:

http://www.senedd.tv/archiveplayer.jsf?v=en_500000_16_05_2012&t=235&l=en

Cynulliad
Cenedlaethol
Cymru

National
Assembly for
Wales



Concise Minutes:

Assembly Members:

Jocelyn Davies (Chair)
Peter Black
Christine Chapman
Paul Davies
Mike Hedges
Ann Jones
Julie Morgan
Ieuan Wyn Jones

Witnesses:

Gerry Holtham, Infrastructure Investment Adviser
Jeff Andrews, Welsh Government
Andrew Jeffreys, Welsh Government
Stephen Jones, Local Government Association
Chris Williams, Development Director, Tidal Energy Ltd
Katherine Himsworth, Furnace Farm Ltd

Committee Staff:

Helen Finlayson (Clerk)
Daniel Collier (Deputy Clerk)
Martin Jennings (Researcher)
Eleanor Roy (Researcher)
Tom Jackson (Clerk)
Ben Stokes (Researcher)
Joanest Jackson (Legal Advisor)

1. Introductions, apologies and substitutions

1.1 The Chair welcomed Members and members of the public to the meeting.

2. Devolved Funding: Borrowing Powers and Innovative Approaches to Capital Funding

2.1 The Chair welcomed Jane Hutt AM, Minister for Finance; Gerry Holtham, Infrastructure Investment Adviser; Andrew Jeffreys, Deputy Director, Strategic Capital Investment; and Jeff Andrews, Specialist Policy Adviser.

2.2 The Committee scrutinised the Minister.

2.3 The Committee agreed to write to the Minister requesting further information on questions which were not reached.

3. Devolved Funding: Borrowing Powers and Innovative Approaches to Capital Funding

3.1 The Chair welcomed Stephen Jones, Director of Finance and Resources, Local Government Association.

3.2 The Committee questioned the witness.

4. Effectiveness of European Structural Funding in Wales

4.1 The Chair welcomed Chris Williams, Development Director, Tidal Energy Ltd. and Katherine Himsforth Director of Furnace Farm via Video Conference.

4.2 The Committee questioned the witnesses.

5. Papers to note

5.1 The Committee noted correspondence from the Deputy Minister for Agriculture, Food, Fisheries and European Programmes regarding JESSICA.

5.2 The Committee ratified the minutes of the previous meeting.

6. Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

Items 7 to 8.

7. Discussion of evidence – Devolved Funding: Borrowing Powers and Innovative Approaches to Capital Funding

7.1 The Committee discussed the evidence on its inquiry into Devolved Funding: Borrowing Powers and Innovative Approaches to Capital Funding.

8. Discussion of evidence – Effectiveness of European Structural Funding in Wales

8.1 The Committee discussed the evidence on its inquiry into the Effectiveness of European Structural Funding in Wales.