



Finance and Central Services Department
Local Government Finance & Performance Division

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Finance Circular No. 5/2003

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Our ref: 2BB0/001/001

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Dear Sir/Madam

PREPARATORY REQUIREMENTS FOR THE INTRODUCTION OF A NEW REGIME FOR CAPITAL EXPENDITURE IN 2004

1. I am writing to let you know about the steps that need to be taken in preparation for the introduction of the prudential capital regime (as provided for in Part 7 of the Local Government in Scotland Act 2003) currently planned for 1 April 2004.
2. Scottish local authorities have, since 1 April 2003, been required to determine, and keep under review, the maximum amount they can afford to allocate to capital expenditure (as provided for under section 35(1) of the Act). An increasing number of councils have begun to develop prudential indicators in accordance with the CIPFA Prudential Code for Capital Finance. This Code of Practice represents an important milestone in the development of the new regime. A second draft of the Code is already in circulation, with responses requested for 15 May. The Code is expected to be finalised this autumn.
3. The Code is designed for the use of local authorities, not central government. Scottish local authorities will be expected to determine their own capital expenditure. But this needs to be undertaken in recognition that Scottish local authority capital expenditure and any borrowing which supports it are relevant to action taken to control the UK economy as a whole, and to other decisions specific to Scotland. This means a certain amount of information about planned and actual expenditure is needed to inform and give comfort to central government and will be required by the Scottish Executive.

September 2003: Estimates of Capital Expenditure 2004-2007

4. We need each local authority to produce forecasts of capital expenditure for the following 3 years **by 30 September 2003**, as described in the table attached at Annex A, and to submit these forecasts to the Scottish Executive. These minimum reporting requirements are required to support



the Chancellor's pre-budget statement in November in which he needs to demonstrate the affordability of the UK's public spending plans.

5. As such, the key requirement is for information on total forecast HRA and non-HRA capital investment, and its sources. But it would be useful also to have early indication of your planned allocations between service headings to show what will be spent where. The aim is to establish an early indication of how councils are considering using the flexibility of the Prudential regime to support investment between service headings. It is recognised that these plans will be tentative for the most part, and are likely to be modified as councils progress their budget processes.

6. Annex A also seeks information about the proposed financing arrangements for the capital investment plans, from borrowing, capital receipts, etc. Councils are also asked to provide an indication of whether their capital plans include any assumed increase in council tax beyond their previously announced indicative levels.

7. Although this exercise is intended to produce indicative figures rather than fully worked-up budgets, we would be grateful if every effort could be taken to ensure that the aggregate totals are your best estimates. 8. You will be able to draw on:

- S94 consent and housing forecasts previously offered in the settlement for 2004/5 and 2005/6
- Information about loan charge support included in the settlement for 2004/5 and 2005/6
- Forecast capital grant allocations for 2004/5 and 2005/6¹
- Capital strategies and asset management plans
- Indicative council tax and house rent assessments
- Information contained in PPP agreements

8. For 2006/7, the prudent assumption would be that the same level of central government funding will be available as for 2005/6.

HRA

9. Although Annex A includes provisional reporting arrangements for the HRA, we are presently consulting on these reporting arrangements as part of the consultation paper, 'Modernising Scotland's Social Housing', which issued on 27 March. Specifically, we are inviting comments on the possibility of a forecast of capital expenditure over a longer period than 3 years. Comments on the HRA proposals should be sent as a response to the consultation paper, which can be found on the SE website at <http://www.scotland.gov.uk/consultations/housing/mssh-00.asp> Page 17 covers the reporting arrangements for the Prudential Regime. The consultation period closes on 30 June, and we will write to you again about requirements in relation to HRA information after that.

December – March 2004: The first prudential budget

10. Ministers will need to have confidence that the prudential capital regime is being reflected in the budget setting process this winter. Some form of reassurance will be needed that decisions relevant to the setting of rents and council tax for 2004/5, the first year of the full operation of the new regime, have been made in accordance with the Prudential Code and other requirements.

11. I will write to you again about this issue as soon as final decisions are made about how best to achieve this, following discussion in the Capital Reforms Implementation Group.

¹ According to information available at the time of the return
Regime preparation requirements

Regime preparation requirements



From 1 April 2004: Future monitoring requirements

12. There will be further consultation on the future monitoring requirements for local authority non-housing capital expenditure. The abolition of s94 consents and the introduction of the new prudential regime, together with new arrangements being developed between the Scottish Executive and HM Treasury for the management of capital expenditure, mean that we need to review the financial returns made to the Scottish Executive by Scottish local authorities where they relate to capital. These returns will need to support the new system, enabling effective monitoring at the macro level, better informed policy development in the Executive, and providing a basis for future Spending Review decisions about grants and loan charges support.

13. We will review these information requirements in accordance with the guidance paper 'Getting it Right' and aim to ensure that all changes made to the information demanded of Scottish local authorities comply with good practice and the principle of minimising the burden of unnecessary information demand. We are also taking the opportunity to consider how well any new returns will fit in with the introduction of Whole of Government Accounts returns in 2005. The issue will be discussed by the Capital Reform Implementation Group and the SCOTSTAT Working Group on Local Government Financial Statistics and I will write to you again about it.

14. If you have any non-HRA queries, please contact Mary Newman or Noel Rehfisch in Local Government Finance and Performance Division, Area 3-J (0131 244 7056 or 0131 244 7002). Comments on the HRA proposals should be sent as a response to the consultation paper referred to in paragraph 9.

Yours sincerely



CHRISTIE SMITH
Head of Local Government Finance & Performance