Nottinghamshire and City of Nottingham
Fire and Rescue Authority

PRUDENTIAL CODE FOR CAPITAL FINANCE 2025/26

Joint Report of the Chief Fire Officer and Treasurer to the Fire Authority

Date: 28 February 2025

Purpose of Report:

To inform Members of the Authority's obligations under the CIPFA Prudential Code for Capital Finance.

To seek the approval of Members of the proposed capital plans, prudential limits and monitoring processes set out in the report.

Recommendations:

That Members approve the Prudential Limits for 2025/26 (see Section 10 for details).

CONTACT OFFICER	
Name :	Bev Bull Head of Finance and Treasurer to the Fire Authority
Tel :	0115 8388100
Email :	bev.bull@notts-fire.gov.uk
Media Enquiries Contact :	Corporate Communications Team 0115 8388100 corporatecomms@notts-fire.gov.uk

1. BACKGROUND

1.1 The Local Government Act 2003 set out a framework for the financing of capital investments in local authorities which came into operation from April 2004. Alongside this, the Prudential Code was developed by the Chartered Institute of Public Finance and Accountancy (CIPFA) as a professional code of practice to support local authorities' decision making in the areas of capital investment and financing. Authorities are required by regulation to have regard to the Prudential Code.

1.2 The objectives of the Prudential Code are to ensure that:

- Capital plans and investment plans are affordable and proportionate;
- All borrowing and other long-term liabilities are within prudent and sustainable levels;
- Risks associated with investment are proportionate to financial capacity;
- Treasury management decisions are in accordance with good professional practice.

1.3 In exceptional cases, the Code should provide a framework which will demonstrate where the objectives may not be ensured, so that timely remedial action can be taken.

1.4 The Prudential Code was revised in December 2021. One of the key changes in the 2021 edition of the Prudential Code is the explicitly stated requirement that authorities must not borrow to invest primarily for financial return.

1.5 The Prudential Code includes a requirement for authorities to produce a Capital Strategy. The 2025/26 Capital Strategy formed part of the Medium-Term Financial Strategy which was approved by the Fire Authority on 13 December 2024.

1.6 The Prudential Code sets out a number of indicators which authorities must use to support decision making. These are not designed to be comparative performance indicators. In addition, the CIPFA Treasury Management Code of Practice and guidance notes sets out a series of treasury indicators. The prudential and treasury indicators should be considered in parallel, and they are therefore included together in this report.

1.7 In addition to the indicators that are required by the Prudential Code and the Treasury Management Code of Practice, this report includes local indicators for internal borrowing and investment benchmarks which will help the Authority to more effectively manage the risks involved with certain elements of treasury management activity.

1.8 This report sets out the proposed prudential and treasury limits for the Authority for the 2025/26 financial year along with the implications of the

proposed Capital Programme, which will be presented with the budget report also on the agenda.

1.9 Reports which monitor the Authority's performance against these indicators will be presented to the Finance and Resources Committee throughout the year.

2. REPORT

2.1 International Financial Reporting Standard 16 (IFRS 16) has been incorporated into the CIPFA Code of Practice on Local Authority Accounting from 1 April 2024. As a result, some leased assets may now be brought onto the balance sheet. Such assets will be known as "right of use assets". The inclusion of right of use assets on the balance sheet will impact several of the indicators detailed in this report. A review of current contracts has been carried out, and none are within the scope of IFRS 16. Therefore, no right of use assets are expected to be brought onto the 31 March 2025 balance sheet. It is possible that such assets may be recognised in the future, depending on the nature of any contracts that are entered into.

PRUDENTIAL INDICATORS FOR AFFORDABILITY

2.2 **Estimates of the Ratio of Financing Costs to Net Revenue Stream**

	2023/24 Actual £000s	2024/25 Estimate £000s	2025/26 Estimate £000s	2026/27 Estimate £000s	2027/28 Estimate £000s	2028/29 Estimate £000s
Financing Costs	2,466	2,612	3,674	4,203	4,914	5,436
Net Revenue Stream	53,204	57,399	58,976	59,629	61,127	62,691
	Ratio of Financing Costs to Net Revenue Stream					
Ratio	4.6%	4.6%	6.2%	7.0%	8.0%	8.7%

2.3 This ratio is expected to rise over the coming years from 4.6% in 2023/24 to 8.7% in 2028/29. Financing costs include minimum revenue provision (MRP) costs, plus interest payable. The MRP cost is driven by the level of capital expenditure in the previous financial year and the useful life of the assets purchased. Financing costs are expected to increase year-on-year to reflect the increase in borrowing required to fund the ongoing capital programme (see section 2.5). The net revenue stream (comprised of council tax, national non-domestic rates and non-specific revenue grants) is expected to increase at a slower rate, hence the increase in the ratio. Previously the Authority had sought to limit this ratio at 8.0%, but the Medium-Term Financial Strategy report which was approved by the Fire Authority on 13 December 2024 removed this limit. Instead, the limit will be set annually, and will be

considered in the context of the overall budget position and affordability. It is recommended that the ratio for the period to 2025/26 be set at 6.2%.

2.4 The estimated ratio for 2025/26 assumes a council tax increase of £5. The estimates for 2026/27 onwards assume annual council tax increases of 2.95%.

PRUDENTIAL INDICATORS FOR CAPITAL EXPENDITURE AND EXTERNAL DEBT

2.5 **Estimate of Total Capital Expenditure and Capital Funding**

	2023/24 Actual £000s	2024/25 Estimate £000s	2025/26 Estimate £000s	2026/27 Estimate £000s	2027/28 Estimate £000s	2028/29 Estimate £000s
Capital Expenditure	**6,971**	**7,728**	**8,490**	**8,147**	**5,171**	**7,361**
Funded by:						
Borrowing	(6,323)	(6,075)	(5,480)	(7,937)	(5,061)	(7,351)
Revenue / Reserves	(513)	(1,284)	0	0	0	0
Capital Grant	(132)	(369)	0	0	0	0
Capital Receipts	(3)	0	(3,010)	(210)	(110)	(10)
Total Funding	**(6,971)**	**(7,728)**	**(8,490)**	**(8,147)**	**(5,171)**	**(7,361)**

2.6 The estimates for 2025/26 to 2028/29 form part of the budget report on this agenda.

2.7 The Capital Programme is funded from a mixture of borrowing, capital receipts and reserves. This combination will be reviewed on an ongoing basis to ensure the best long-term options are achieved for the Authority. This will include consideration of borrowing rates, reserve levels and revenue and capital receipt availability.

2.8 **Capital Financing Requirement**

	31/03/24 Actual £000s	31/03/25 Estimate £000s	31/03/26 Estimate £000s	31/03/27 Estimate £000s	31/03/28 Estimate £000s	31/03/29 Estimate £000s
CFR Opening Position	30,533	35,331	39,785	43,001	48,389	50,485
In Year Capital Borrowing Requirement	6,323	6,075	5,480	7,937	5,061	7,351
MRP Repaid in Year	(1,525)	(1,621)	(2,264)	(2,549)	(2,964)	(3,186)
CFR Closing Position	**35,331**	**39,785**	**43,001**	**48,389**	**50,485**	**54,651**
External debt	32,900	34,354	38,570	43,958	46,054	50,220

Under/(over) borrowing (i.e. Internal Borrowing)	2,431	5,431	4,431	4,431	4,431	4,431

2.9 The Capital Financing Requirement is the amount required from external sources to fund capital expenditure and represents the Authority's underlying need to borrow for capital purposes. It will therefore be the aggregate of all capital expenditure, less any revenue or reserve contributions, capital grants or capital receipts. The above table shows that the Capital Financing Requirement (CFR) steadily increases during the period from 2023/24 to 2028/29. The CFR increases when annual capital expenditure exceeds the funding available from capital receipts, government grants and revenue sources, and decreases when the funding exceeds the expenditure. The movement in the estimated CFR figures is mainly driven by the varying levels of estimated capital expenditure for each year, with the most significant increase taking place in 2026/27 when capital expenditure is expected to be £8.147m. Capital expenditure is actually expected to peak in 2025/26 at £8.490m, but the high level of capital receipts expected in that year (£3.010m) reduces the increase in the CFR.

Operational Boundary and Authorised Limit for External Debt

2.10 The operational boundary is the Authority's estimate of its total external debt, including other long-term liabilities (such as finance leases) which are separately identified. This is to reflect the most likely scenario and not the worst case. It is possible for the operational boundary to be temporarily breached to take account of unusual movements in cash flow but this should not be a regular occurrence. A variation from the operational boundary is permissible but will be reported to Fire Authority.

2.11 The operational boundary includes allowances to borrow to fund the capital programme, replace maturing debt and to allow for any short term borrowing that may be needed to cover the cashflow of the authority.

2.12 The authorised limit is essentially the same as the operational boundary but allows headroom over and above it to take account of unusual movements in cash flow, and therefore should be the maximum amount of external debt that the Authority is exposed to at any given time. Any proposed variation from the authorised limit must be authorised by the Fire Authority.

2.13 **Operational Boundary and Authorised Limit**

	2024/25 £000s	2025/26 £000s	2026/27 £000s	2027/28 £000s	2028/29 £000s
Operational Boundary					
Borrowing	39,700	46,034	46,168	48,164	52,730
Other long term liabilities	200	200	200	200	200
Total External Debt	39,900	46,234	46,368	48,364	52,930

Authorised Limit					
Borrowing	43,670	50,637	54,651	54,651	58,003
Other long term liabilities	1,000	1,000	1,000	1,000	1,000
Total External Debt	44,670	51,637	51,784	53,981	59,003

2.14 **Actual External Debt as at 31/03/24**

	2023/24 £000s
Actual borrowing	32,900
Actual other long term liabilities	0
Total – Actual External Debt	**32,900**
Operational Boundary	36,901
Authorised Limit	41,591

INDICATORS FOR TREASURY MANAGEMENT

2.15 The Service carries out its own treasury management in accordance with the CIPFA Code of Practice for Treasury Management. The Authority has adopted a low-risk approach to treasury management, which seeks to ensure that investments are secure and that there is sufficient liquidity of funds to enable the Authority to carry out its business.

Gross and Net Debt

2.16 The actual amount of external long-term borrowing as at 31 March 2024 was £29.9m, with short-term borrowing totalling £3m. There were no other longer-term liabilities at this date. At the same date, the level of investments was £8.6m, giving a net debt position of £24.3m.

2.17 The Treasury Management Strategy 2025/26 report, also on this agenda, outlines the proposal to borrow over the next four years to finance the capital programme and to replace maturing loans. The decision about when to borrow will depend upon interest rate forecasts. For the purposes of setting indicators, assumptions have been made about when borrowing may take place. In reality the timing will be determined by Officers in conjunction with the Authority's treasury advisors.

2.18 The proportion of net debt to gross debt can highlight where an Authority is borrowing in advance of need, as it shows the extent to which funds have been borrowed and then invested. Whilst the Authority is permitted to borrow in advance to finance the capital programme, where borrowing rates are higher than investment rates this creates a "cost of carry". Therefore, when this is that case the cost of carry is reduced by keeping the proportion of net debt to gross debt as high as is practicable. For information, the proportion of

net debt to gross debt as at 31 March 2024 was 74%, and it is forecast to be 84% at the end of the current financial year. It is proposed that the Authority sets the following limits for the proportion of net debt to gross debt:

2.19 **Proportion of Net to Gross Debt**

	2025/26	2026/27	2027/28	2029/29
Lower limit for proportion of net debt to gross debt	50%	50%	50%	50%
Upper limit for proportion of net debt to gross debt	85%	85%	85%	85%

Interest Rate Risk Exposure

2.20 In terms of borrowing, it has been considered prudent to use Public Works Loans Board (PWLB) fixed interest loans on most occasions. This is because the PWLB generally offers rates which cannot be obtained elsewhere in the marketplace. Unlike lending, borrowing is a low risk activity so future borrowing arrangements will be entered into on the basis of what is most advantageous for the Authority at the time. Any proposals to borrow from alternative sources to the PWLB will be discussed with the Authority's treasury advisors.

2.21 Borrowing in the past has been at fixed interest rates although variable rates are not ruled out should they be considered financially advantageous at the time of financing. A maximum limit of 30% of borrowing from variable rate sources is proposed.

2.22 The total value of lending is not expected to exceed £17m, which is likely to peak around July and August 2025. However, it is difficult to assess what the likely investment profile might be as this depends upon capital expenditure timings as well as the level of pension top up grant received from the Government, and the timing of borrowing. All investments are made in line with the Treasury Management Strategy.

2.23 **Limits for Interest Rate Exposures**

	Benchmark %	2025/26 %	2026/27 %	2027/28 %	2028/29 %
Upper Limit for fixed rate exposures	100%	100%	100%	100%	100%
Upper Limit for variable rate exposures	30%	30%	30%	30%	30%

2.24 In addition to the upper limit for variable rate exposures in relation to external debt, the Authority has adopted a local indicator which sets a limit for the acceptable level of internal borrowing. This is because the use of internal

borrowing exposes the Authority to interest rate risk, as there is a chance that cash balances may need to be replenished at a time when interest rates are higher. In this respect, internal borrowing is effectively variable rate debt. The level of internal borrowing is calculated as follows:

Capital Financing Requirement – External Borrowing = Internal Borrowing

2.25 At 31 March 2024 the Authority had total borrowing of £32.9m and a CFR of £35.3m. Internal borrowing was therefore £2.4m.

2.26 It is proposed that the Authority sets the following limits for internal borrowing:

	2024/25 %	2025/26 %	2026/27 %	2027/28 %
Upper Limit for internal borrowing as a % of the Capital Financing Requirement	20%	20%	20%	20%

Investment Benchmarking

2.27 The Treasury Management Strategy 2025/26, which is also on this agenda, sets out the following local benchmarks to assess the security, liquidity and yield of its investments:

- **Security:** a risk benchmark of **0.05%** historic default when compared to the whole investment portfolio.
- **Liquidity:** a "Weighted Average Life of Investments" benchmark of **approximately 3 months**, with an upper limit of **0.40 years**.
- **Yield:** internal returns to be above a benchmark of the **3 month compounded Sterling Overnight Index Average (SONIA) rate**

2.28 Further details of these benchmarks can be found in the Treasury Management Strategy 2025/26.

Loan Maturity

2.29 There is no requirement for a direct linkage between the assets financed and the term of loans taken out. Upper limits in terms of loan maturity are set to ensure that the Authority is not exposed to the risk of having to repay loans and then re-borrow in the short term when interest rates might be high.

2.30 It is recommended that the maturity structure limits remain unchanged for 2025/26. The Authority holds a loan of £4m which is structured as a "Lender Option Borrower Option" (LOBO) loan. Whilst the end date of the loan is March 2078 there are options every five years for the lender to revise the interest rate. The Authority may choose to repay the loan without penalty if the amended rate is not advantageous. The next opportunity for the revision

of the interest rate is 7 March 2028. The limits for these years will be kept under review to reflect that the investment may mature on these dates.

2.31 **Limits on the Maturity Structure of Borrowing**

	Upper Limit	Lower Limit
Under 12 months	20%	0%
12 months to 5 years	30%	0%
5 years to 10 years	75%	0%
10 years to 20 years	100%	0%
Over 20 years	100%	30%

Principal Sums Invested for Periods Longer than 365 Days

2.32 Investments arising from borrowing to support the capital programme are unlikely to exceed one year in duration, however for surplus cash which supports reserves it may be desirable to invest monies for a slightly longer period to achieve a level of certainty around interest receipts and perhaps beneficial interest rates. Such decisions will be influenced by market conditions at the time and the liquidity of funds will be of paramount importance. It is proposed that Officers should be able to invest monies for longer than a year if this appears to be an advantageous strategy, but that a maximum limit of £2m be applied to any such investments. This will contain the Authority's exposure to the possibility of loss arising from having to seek early repayment of investments.

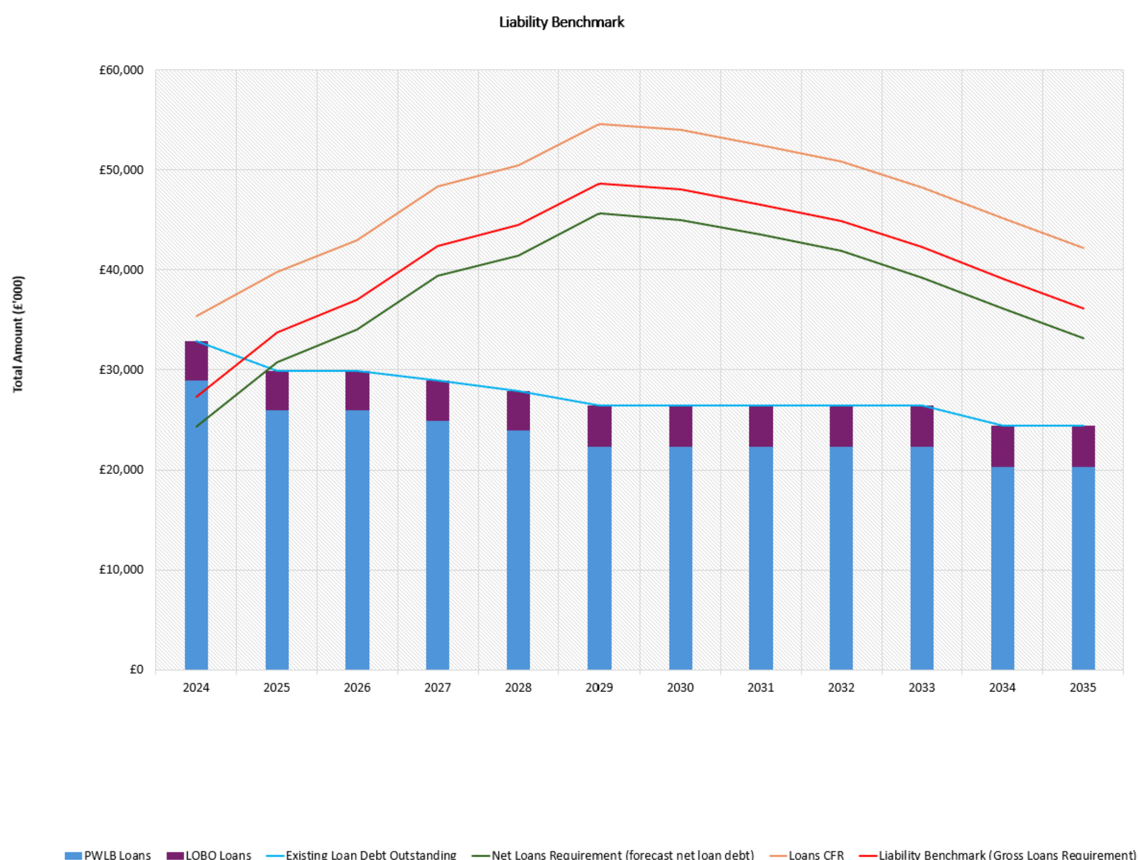
2.33 **Limits for Principal Sums Invested for Longer than 365 Days**

2025/26 £000s	**2026/27 £000s**	**2027/28 £000s**	**2028/29 £000s**
Prudential Limits for Principal Sums Invested for Periods Longer than 365 Days			
2,000	2,000	2,000	2,000

2.34 **Liability Benchmark**

The liability benchmark is a projection of the amount of loan debt outstanding that the Authority needs each year to fund its existing debt liabilities, planned prudential borrowing for capital expenditure and other cash flows. This is shown by the gap between the Authority's existing loans that are still outstanding at a given future date and the Authority's future need for borrowing (as shown by the liability benchmark). It therefore shows how closely the existing loans book fits the future need of the Authority based on its current plans. Any shortfall will have to be met by future borrowing; any excess will have to be invested unless borrowing is prematurely repaid. However, the Treasury Management Code of Practice does not require authorities to always minimise risks by closely matching their loan debt to the

liability benchmark. Factors such as interest rate expectations may lead an authority to prudently conclude that it is appropriate to have a maturity profile that does not exactly match the benchmark, or to borrow in advance of need to secure affordable interest costs. The liability benchmark is simply a tool to help the authority manage risk.



2.35 The above chart takes account of proposed capital expenditure up to 2034/35, and the resulting changes to both the CFR and the levels of borrowing for capital purposes. The CFR level reduces beyond 2029 as it is decreased by the annual minimum revenue payment charges relating to previous and proposed capital expenditure. The net loans requirement takes the Authority's net debt position as its starting point and then reflects changes to the level of planned borrowing for capital purposes to fund the proposed capital programme up to 2034/35. The liability benchmark consists of the net loans requirement, plus an allowance for liquidity (known as the liquidity buffer). Aside from capital expenditure, the firefighters' pension fund has perhaps the most significant impact on the Authority's cash flows. Therefore, Officers must take account of potential cash deficits relating to the pension fund when determining an appropriate level for the liquidity buffer.

2.36 The chart shows that the Authority's outstanding debt exceeded the liability benchmark in March 2024 due to the timing of borrowing (£3m was borrowed March 2024), but that the liability benchmark is expected to exceed the level of outstanding debt from March 2025 onwards. This indicates a requirement

to borrow during this period. The use of this chart encourages authorities to focus on a “net book” treasury management position whereby borrowing and investments are netted down (whilst maintaining appropriate investment balances for liquidity purposes). This reduces the treasury risks resulting from running debt and investment portfolios at the same time. It also means that the management of borrowing and investments is integrated so that both are reviewed together when monitoring and managing treasury risks. The projected liability benchmark is a useful tool for helping to determine a suitable maturity profile for the Authority’s debt when new borrowing decisions are made.

3. FINANCIAL IMPLICATIONS

The financial implications of this report are set out in full within the body of the report.

4. HUMAN RESOURCES AND LEARNING AND DEVELOPMENT IMPLICATIONS

There are no human resources or learning and development implications arising from this report.

5. EQUALITIES AND ETHICAL IMPLICATIONS

An equality impact assessment has not been undertaken because this is not a new policy or service. A previous assessment has shown that there are no specific equality impacts which arise directly from the Prudential Code.

6. ENVIRONMENTAL AND SUSTAINABILITY IMPLICATIONS

There are no environmental implications arising from this report. This report serves to ensure that the financial sustainability of the Authority is maintained.

7. LEGAL IMPLICATIONS

The Local Government Act 2003 imposes an obligation on the Authority to agree and monitor its prudential indicators.

8. RISK MANAGEMENT IMPLICATIONS

The risk exposures in this report relate primarily to three areas:

- The risk of over exposure of the Authority to interest rate fluctuations;

- The risk that the Authority has an unmanageable or unaffordable level of borrowing;
- The risk of tying up investments, thereby reducing liquidity and exposing the Authority to possible losses arising from early repayment of investments.

This report serves to set out those risks and ensure that they are managed.

9. COLLABORATION IMPLICATIONS

There are no collaboration implications arising from this report.

10. RECOMMENDATIONS

That Members approve the Prudential Limits for 2025/26 as follows:

Estimated Ratio of Financing Costs to Net Revenue Stream	6.2%
Estimate of Total Capital Expenditure to be Incurred	£8.490m
Estimate of Capital Financing Requirement	£43.001m
Operational Boundary	£46.234m
Authorised Limit	£51.637m
Upper limit for fixed rate interest exposures	100%
Upper limit for variable rate interest exposures	30%
Loan Maturity:	Limits:
Under 12 months	Upper 20% Lower 0%
12 months to 5 years	Upper 30% Lower 0%
5 years to 10 years	Upper 75% Lower 0%
Over 10 years	Upper 100% Lower 0%
Over 20 years	Upper 100% Lower 30%
Upper Limit for Principal Sums Invested for Periods Longer than 365 Days	£2,000,000

That Members approve the following local indicators for 2025/26:

Upper limit for internal borrowing as a % of the Capital Financing Requirement	20%
Limit for proportion of net debt to gross debt	Upper 85% Lower 50%
Investment security benchmark: maximum historic default risk of investment portfolio	0.05%

Investment liquidity benchmark: maximum weighted average life of investment portfolio	0.40 years
Investment yield benchmark	Internal returns to be above 3 month compounded SONIA rate

11. BACKGROUND PAPERS FOR INSPECTION (OTHER THAN PUBLISHED DOCUMENTS)

None.

Craig Parkin
CHIEF FIRE OFFICER

Bev Bull
TREASURER TO THE FIRE AUTHORITY