



**OFFICE OF THE
DEPUTY PRIME MINISTER**

The Chief Executives
County Councils in England
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London Borough Councils
City of London
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Dear Chief Executive

Developments in Capital and Asset Management Planning

As you are all aware, much has been going on in the world of capital finance, not least the replacement of the current system. I am using this opportunity to provide an overview of some of the wider strategic issues and developments which you will want to be aware of and which are of importance for the future, as well providing an update on developments in capital and asset management planning for 2003.

This information is pertinent to all local authorities and it is important that local authority officials involved in capital planning and asset management read this document .

Prudential System

1. The Local Government Bill currently going through Parliament will abolish credit approvals and replace them with a local prudential system. This new system is about self-regulation rather than control by central government on the amount an authority can borrow to support capital investment. It will require individual local authorities to decide how much they can prudently borrow in line with the Prudential Code being developed by the Chartered Institute of Public Finance and Accountancy (CIPFA). It is hoped to implement the prudential system from April 2004 but this is dependent on the progress of the legislation. Local Authorities should in any case be beginning to prepare for implementation and familiarising themselves with the guidance. The second draft of the guidance is available at www.cipfa.org.uk/pt/pt_details_c.html/news_id=15685).
2. Local Authorities will determine their total level of borrowing in accordance with the guidance of the Prudential Code. Having set a limit on the level of debt that can be incurred, authorities will be required to adhere to these limits. They will not be able to undertake new borrowing that would breach these limits and so will be permitted to increase their ceiling for affordable debt-in year, only if the new figure is still within prudential limits.

3. The locally set limit on an authority's borrowing will take account of all sources of estimated future revenue income and the potential calls on the use of that revenue. Subject to identified corporate investment priorities, the amount of revenue income not required for other spending purposes will be available to support the cost of new borrowing for capital investment.
4. The draft prudential code recognises that in making capital investment decisions local authorities must have explicit regard to: option appraisal, asset management planning, strategic planning for the authority and the achievability of the forward plan. Robust strategic capital planning will therefore underpin the future framework of the prudential system by identifying how those plans are affordable, prudent and sustainable.
5. The capital strategy will form an integral part of the strategic financial and service planning that will become part of the annual budget setting process and support decisions on a local authority's capital investment under the prudential system. Local authorities will need to integrate their capital and revenue budget planning processes so that coherent decision making can take place on the level of borrowing that is prudent, affordable and sustainable for the authority. Decisions to take on additional borrowing will flow from an analysis of the strategic assessment of the authority's present asset base, identification of investment needs, prioritisation of those needs set within the context of available capital resources including capital receipts, capital grant and revenue contributions.

Whole of Government Accounts

6. The Government is working towards producing Whole of Government Accounts (WGA). This will assist in ensuring that best practice accounting methods are used to construct accounts covering the public sector as a whole, including local government, and that fiscal reporting is as transparent as possible. Since Local Authorities are part of the public sector it is important for completeness, that local authorities are part of WGA. Preparatory work is currently being undertaken with HM Treasury, CIPFA, and the Audit Commission. Although the timetable for this extension to WGA has not yet been finalised, the first dry run year is likely to be 2004/5, coinciding with the introduction of the Prudential Framework for local authority capital finance.
7. Whole of Government Accounts will be commercial-style accounts covering the whole of the public sector. Like departmental resource accounts, WGA will be produced on an accruals basis and will use generally accepted accounting principles (GAAP), adapted where necessary for government. Government will be treated as if it were a single entity by eliminating all significant transactions between public sector entities.
8. WGA will provide better quality and more transparent information to assist with the development of fiscal policy, to facilitate better management of public services and to assist with the more effective distribution of resources. In particular, WGA will provide audited data to underpin the operation of the Golden Rule, (over the economic cycle, the government will only borrow to invest and not to fund current spending) and allow the public sector balance sheet to be used in fiscal management.

9. Preparing WGA will require convergence of accounting practice across public sector bodies. Significant work is required to ensure consistency of approach in accounting practices. However, Local Authority accounting will need to align with GAAP in, amongst other areas, how the costs of assets are charged for. A consultation paper on support for capital investment to be released later in the Spring (see below) will outline some approaches and issues relating to depreciation based accounting for fixed assets. Again detailed knowledge of local authority asset bases including valuation, condition and maintenance backlog plays a vital role in this exercise. Robust processes will rely on sound asset management plans backed by databases providing valid, relevant and up to date core data on assets.
10. Harmonising accounting practices and ensuring best accounting practice will enhance comparability of performance information across the public sector, increasing the ability of individual bodies to benchmark their own performance against that of others. It will also enable targets to be set and measured on a consistent basis. This overview of the public sector finances provided by WGA will also improve government's accountability to Parliament and taxpayers, and form an important element in the Modernising Government agenda.
11. Further information on WGA can be found at www.wga.gov.uk

Government Support for Capital Investment

12. The government is reviewing how capital investment in local government is supported. The abolition of credit approvals and their replacement with the prudential system requires some changes to be made. It therefore seems opportune to consider alternative mechanism for delivery of government support for capital investment. As was clearly stated in the 2001 White Paper *Strong Local Leadership- Quality Public Services*, Government support for capital investment will continue. The move to the prudential system is intended to supplement Government supported investment, and not replace it. Whatever changes are made in the future to the mechanism of government support following consultation later in the Spring, the commitment remains to delivering the bulk of capital investment to local authorities through the single capital pot.
13. Support for local authority capital investment is at present funded through Formula Grant (i.e. revenue support grant (RSG) + redistributed business rates), and Housing Revenue Account Subsidy (HRAS), reflecting the revenue costs of borrowing, and for some types of expenditure either wholly or in part through capital grants. Options will be proposed in a consultation document in the Spring of this year on how that support will be delivered in the future. In the light of the proposed move to WGA, we will be taking the opportunity to consider depreciation based support and we will also be considering changes to the balance of the way in which government support is funded.
14. Effective public service provision requires the devolution of power to service providers to encourage flexibility and creativity, particularly in meeting customer needs and responding to local circumstances. ODPM has led on work to develop the 'single capital pot', to facilitate this process in providing the bulk of capital support as unringfenced so that it can be used flexibly within local authorities. In SR2002, the Government reiterated its commitment to ensuring that support is provided in flexible,

cross service resources through the single capital pot. For 2003/4 the level of resource being delivered through the pot is in excess of 60% and the government is committed to increasing the level of unringfenced resource delivered through the pot to two thirds by the end of the spending review period.

Comprehensive Performance Assessment (CPA) for Districts

15. The proposed elements of the CPA for district councils include self-assessment, peer challenge, two high level diagnostic assessments in major areas - housing and public space, an assessment of the benefits service, an auditor's judgement, and a corporate assessment.
16. The CPA process will be informed by information from other evidence sources. This will include the auditor judgement on how resources are deployed within local authorities and on the process supporting the use of these resources. In examining how capital resources are deployed, auditors will be looking at how corporate capital planning processes support and deliver robust capital programmes and asset management.

Single Capital Pot Guidance 2003

Action for all Local Authorities

17. Even if there is no requirement to submit a plan for assessment to your Government Office in 2003. Government Offices will continue to collate core statistical and revenue and capital information including data on capital assets from all local authorities for central government. This data is essential in helping to inform future spending review decisions on capital investment. All local authorities will also be required to continue to provide returns on their property PIs.
18. Authorities assessed as excellent under the Comprehensive Performance Assessment framework will not need to submit plans in 2003. Authorities who received a "good" assessment in the Single Capital Pot process for either their Asset Management Plan or Capital Strategy will be relieved of the burden of submitting that particular plan.
19. However, although plans will not be assessed in these circumstances, Strategic Capital Planning and Asset Management remain important and will underpin the framework of the new prudential system as outlined above (paras 1-5) and which subject to the parliamentary timetable, may be introduced from April 2004.
20. The majority of the guidance remains the same as that issued last year for the second round. However, some minor changes have been made in the light of feedback from local authorities. This year's guidance has been updated in co-operation with ACES, COPROP, FPS, RICS, CIPFA and the LGA and incorporates local authority feedback and comments through the Government Office feedback process.

Main changes from last year's guidance

21. We have updated the text to reflect changes to the Single Capital Pot including:

- Increases to the level of unringfenced funding for **all local authorities** as a result of Spending Review 2002;
- Extra freedoms for CPA assessed "excellent" and "good " authorities
- The impact of plan relaxation for CPA assessed "excellent" authorities;
- Changes to the property Performance Indicator definitions reflecting concerns raised by local authorities through various fora;
- Confirming the abolition of the discretionary element of the Single Capital Pot.

22. We have also confirmed the requirement for all authorities (see paras 20 and 21 of guidance) to provide core property data as per the old context sheet and to continue to provide Property performance indicator data.

23. Copies of this letter are being sent to principal local authorities in England and to those bodies on the attached list. The single capital pot will apply in respect of principal authorities (Counties, District and Unitary Councils and London Boroughs) although the guidance is copied to other Part IV authorities (e.g. single purpose authorities) for information.

Any enquiries about this and other guidance relating to the Single Capital Pot should be address to Peter Hart on 020 7944 3370 peter.hart@odpm.gsi.gov.uk and Chris Howsham on 020 7944 3140 chris.howsham@odpm.gsi.gov.uk

Copies of this and previous guidance on the single pot are available on our website at www.local.odpm.gov.uk/finance/capital/singpot.htm.

Yours sincerely

PAM WILLIAMS

Copy List

LGA

ALG

NALC

CIPFA

Audit Commission

4Ps

FPS

RICS

SCALA

ACES

Institute of the Clerk of Works

Association of Chief education Officers

Association of Directors of Social Services

Chartered Institute of Housing

CSS

TAG

Institute of Highways and Transport