Rother District Council **Agenda Item: 7.2**

Report to	-	Cabinet
Date	-	11 February 2019
Report of the	-	Executive Director
Subject	-	Capital Programme 2018/19 to 2023/24 and Capital Strategy

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Recommendation to COUNCIL: That

1) the Capital Strategy at Appendix A be approved and adopted; and

2) the revised Capital Programme at Appendix B be approved.

Head of Service: Robin Vennard
Lead Cabinet Member: Councillor Lord Ampthill

Introduction

1. This report updates Members on the new requirement to have a Capital Strategy and provide details of the latest Capital Programme. The Strategy aims to gives Members an overview of the Council's approach to capital. This requirement comes from the CIPFA 2017 codes for Prudential and Treasury Management.

Capital Strategy

2. The draft Capital Strategy at Appendix A is a new report for 2019/20, giving a high-level overview of how capital expenditure, capital financing and treasury management activities contribute to the provision of local public services, along with an overview of how associated risk is managed and the implications for future financial sustainability.

3. The Strategy gives a high level overview of the following areas:

(i) Capital Expenditure and its financing
(ii) The role of Asset Management
(iii) Projected Asset Disposals
(iv) Treasury Management
(v) Sets out the expected borrowing needs of the Council
(vi) Sets the borrowing limits for the Council
(vii) Sets out the expected returns on the cash investments
(viii) Outlining other liabilities on the Council
(ix) The impact of capital spending on the Revenue Budget
(x) Sets out the relevant knowledge and expertise of relevant officers and advisors.

4. The Strategy is based on the draft Capital Programme detailed below.

Capital Programme

5. The Council's capital programme at Appendix B totals some £63m, although £15m is yet to have funding secured. A significant part of this, some £35m relates to the Council's approved Property Investment Strategy (PIS0 Minute C18/13 refers). The PIS envisages £35m of borrowing to deliver its economic regeneration aspirations as well as generating a revenue stream for the Council. The forecast shows that once fully invested, £2.2m of income could be generated annually but this is offset by approximately £1.4m of interest and repayment costs. The capital programme also envisages utilising £2m of reserves in 2019/20 (£5m by 2023/24) to support expenditure. This will reduce the investment earnings of the Council through its treasury activities.

6. The draft Capital Programme clearly identifies the scope of ambition of the Council to invest over the next five years. It also shows where schemes are part or fully funded. Accurately forecasting spend is difficult for a number of these projects where there is a high level of uncertainty concerning issues such as funding, planning approval and land acquisition. Projects and schemes can only commit spending to the value of what is financed. The unfunded element of the programme is shown in the right hand column of the schedule in Appendix B. These projects will only be allowed to proceed once funding is secured. The following paragraphs updates Members on changes to previously approved schemes and new schemes:

Acquisitions, Transformation and Regeneration

7. **East Parade £695,000:** This project has been subject to previous reports to Cabinet and has approved funding from the Council of £295,000. It is proposed that the £400,000 funding gap for this project be met by the Bexhill Sea Angling Club who are seeking grant funding from Sports England as well as identifying other fund raising opportunities. Members will be updated on the outcome of these bids in due course.

8. **Property Investment Strategy £35m:** The strategy identified a spend of £35m for investing in the District. The programme shows that spend of £2.5m has been incurred to date and that a further £12.5m is planned for 2019/20. Four sites at the Beeching Road West Trading Estate, Bexhill have been purchased which will give the Council an immediate income as well as development opportunities for the future. The Council are also in negotiations with a number of commercial landlords to purchase tenanted and development sites across the district. These will be subject to the approval of the Property Investment Panel and are likely to be delivered in the early part of 2019/20 financial year.

9. **Blackfriars Housing Development £3.25m:** The funding for this project is the subject of a bid to the Housing Infrastructure Fund being managed by Homes England. Officers are currently negotiating the final conditions of the grant.

Housing and Community Services

10. **Camber Western Car Park £120,000:** The volume of traffic in the summer causes damage to the car park and creates an uneven and unstable composition of the surface. As a result a number of vehicles become trapped

annually requiring support from coastal officers to extricate them. A number of contractors have recommended reinforcing the ground in the affected areas with heavy duty grass blocks. To sustain the use of the car park and spread the costs it is proposed for works to take place in three stages, over three financial years, with the first stage taking place in 2019/20.

11. **Housing (purchases - temp accommodation) £2m:** It is a priority for the Council to reduce the cost of providing temporary accommodation. While a range of new measures are being developed to prevent homelessness and reduce the need to use temporary accommodation there is a parallel need to find more affordable models of housing provision. In July 2018 Cabinet accepted the recommendation of the Housing Task and Finish Group (Minute CB18/14 refers) for the Council to acquire emergency and temporary accommodation through the purchase of accommodation, in order to reduce the cost of provision to the Council.

Corporate Core including Executive Directors

12. **Accommodation Strategy (£ To Be Decided):** It is important to ensure that the Council is getting value for money from its use of office space. An initial review of office space has been carried out but further work is necessary before the process is finalised. In order to implement any changes a sum of money will be required for e.g. building works and office furniture.

13. **Lift for Amherst Road Offices £100,000:** Currently the only lift access to the upper floors is through the Job Centre Plus office. To enable full flexibility in use and potential letting of the upper floors it is therefore necessary to redesign the access to the lift.

Conclusion

14. The draft Capital Programme shows that despite the continued impact of the Government's austerity measures, the Council wishes to make a significant commitment to invest in the district to improve it economically and socially; to ensure it remains an outstanding place to work and live. The programme and the accompanying Capital Strategy do not come without significant risk. Members will need to recognise these risks and manage them to ensure the programme can be delivered.

Malcolm Johnston	Dr Anthony Leonard
Executive Director	Executive Director

Risk Assessment Statement

Failure to produce a Capital Strategy would mean that the Council would not be complying with the CIPFA Treasury Management and Prudential Codes of Practice and may, therefore, be at risk of making inappropriate investments leading to a potential major loss of resources or setting capital expenditure targets that would not be affordable for the Council.

Capital Strategy 2018/19 to 2023/24

Introduction

1. This Capital Strategy is a new report for 2019/20, giving a high-level overview of how capital expenditure, capital financing and treasury management activities contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability.

Capital Expenditure and Financing

2. Capital expenditure is where the Council spends money on assets, such as property or major equipment that will be used for more than one year. In local government this includes spending on assets owned by other bodies or individuals (e.g. disabled adaptations) and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are not capitalised and are charged to revenue in year. Further details of the Council's policies on capital expenditure are contained in its annual Statement of Accounts.

3. In 2019/20, the Council is planning capital expenditure of £19.9m, plus a further £1.2m subject to funding being secured, as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £'000

	2018/19 forecast	**2019/20 budget**	**2020/21 budget**	**2021/22 budget**	**2022/23 budget**	**2023/24 budget**
General Fund Serv	4,614	7,447	535	238	238	238
Regen Investments	2,512	12,488	20,000	0	0	0
TOTAL	**7,126**	**19,935**	**20,535**	**238**	**238**	**238**

4. The main capital projects in 2019/20 include the Property Investment Strategy, £12.488m, Blackfriars housing development, £3.150m, and the site assembly costs for the redevelopment of the Bexhill Leisure Centre, £1.9m.

5. In terms of governance around new capital items, Services have two main opportunities to bid for projects to be included in the Council's Capital Programme, mid-year at the time of the Medium Term Financial Strategy Review and at year end when setting the following years' budgets. Depending on circumstances bids can come forward at other times of the year. The Strategic Management Team appraises all bids and now that the Capital Programme is not fully funded, will assess their relevant priority against other schemes and the affordability of any associated financing costs. This then forms part of the financial reporting to Cabinet for approval and recommendation to full Council.

6. All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and

Private Finance Initiative). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £'000

	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget	2023/24 budget
External sources	1,429	3,497			
Own resources	3,138	3,950	535	238	238
Debt	2,559	12,488	20,000		
TOTAL	**7,126**	**19,935**	**20,535**	**238**	**238**

7. Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as the minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP and use of capital receipts are as follows:

Table 3: Replacement of debt finance in £'000

	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget
MRP	0	156	291	515	527	540

8. The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to £15,982 during 2019/20. Based on the above figures for expenditure and financing, the Council's estimated CFR moves as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £'000

	31.3.19 forecast	31.3.20 budget	31.3.21 budget	31.3.22 budget	31.3.23 budget	31.3.24 budget
General Fund services#	1,138	1,136	1,134	1,132	1,130	1,128
Regen Investments	2,512	14,844	34,553	34,038	33,511	32,971
TOTAL	**3,650**	**15,980**	**35,687**	**35,170**	**34,641**	**34,099**

#including adjustment "A" £1.091m

Asset management

9. To ensure that capital assets continue to be of long-term use, the Council has an asset management strategy in place. This ensures that capital assets continue to be of long-term use, and the Council has an Asset Management Plan in place. This sets out the Council's strategy for acquisitions, disposals, and development to meet its corporate plan objectives and statutory requirements. It includes taking a proactive approach to acquisitions to invest in the local economy and generate income to the Council, in accordance with

the Council's Property Investment Strategy. It sets out the Council's approach to maintaining its assets in a useable state of repair, and towards the management of data. The Asset Management Plan also addresses issues relating to governance, risk management, performance management and monitoring.

Asset disposals

10. When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Council is currently also permitted (but no plans to do so) to spend capital receipts on service transformation projects until 2021/22. Repayments of capital grants, loans and investments also generate capital receipts. The Council has a number of small potential disposals in 2019/20. However, it is prudent not to rely on these until the sale is agreed.

Treasury Management

11. Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by short term borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing. The Council currently has £0.9m of borrowing at an average interest rate of 2.57% and £28.4m treasury investments at an average rate of 1.31%.

Borrowing strategy

12. The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.75%) and long-term fixed rate loans where the future cost is known but higher (currently 2.0 to 3.0%).

13. Projected levels of the Council's total outstanding debt is shown below, compared with the capital financing requirement (see above).

Table 5: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £'000

	31.3.19 forecast	**31.3.20 budget**	**31.3.21 budget**	**31.3.22 budget**	**31.3.23 budget**	**31.3.24 budget**
Gross Debt (incl. PFI & leases)	2,559	14,846	35,648	35,135	34,610	34,072
Capital Financing Requirement	3,650	15,982	36,782	36,267	35,740	35,200

14. Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from Table 6, the Council expects to comply with this in the medium term.

Affordable borrowing limit

15. The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 6: Prudential Indicators: Authorised limit and operational boundary for external debt in £'000

	2018/19 limit £'000	2019/20 limit £'000	2020/21 limit £'000	2021/22 limit £'000	2022/23 limit £'000	2023/24 limit £'000
Authorised limit – total external debt	21,000	35,000	56,000	55,000	55,000	55,000
Operational boundary – total external debt	16,000	30,000	51,000	50,000	50,000	50,000

16. Further details on the borrowing strategy is contained in the Councils treasury management strategy.

Other Liabilities

17. In addition to the debt detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £21.7m as at 31 March 2018). It has also set aside £0.7m to cover risks of business rate. The Council is also at risk of having to pay for a share of any unfunded liabilities of the Councils' former insurer Municipal Mutual Insurance Ltd (MMI) but has not put aside any money because the amount of any payment is uncertain. This is common to all local authorities insuring with MMI prior to 1993. Further details on liabilities and guarantees are shown in the 2017/18 statement of accounts.

Investment strategy

18. Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

19. The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the Government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular

investments to buy and the Council may request its money back at short notice.

Table 7: Treasury management investments in £'000

	31.3.19 forecast	31.3.20 budget	31.3.21 budget	31.3.22 budget	31.3.23 budget	31.3.24 budget
Near-term investments	11,106	6,990	5,110	3,965	2,673	4,194
Longer-term investments	8,000	8,000	8,000	5,000	5,000	2,500
TOTAL	**19,106**	**14,990**	**13,110**	**8,965**	**7,673**	**6,694**

20. Further details on treasury investments are contained in the Council's Treasury Management Strategy.

21. In terms of governance around treasury activities, decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Executive Director and relevant staff, who must act in line with the treasury management strategy approved by Cabinet each year. Regular reports on treasury management activity are presented to the Audit and Standards Committee who scrutinise treasury management decisions.

Investment in Commercial Property

22. The Council invests in existing and developing new commercial property in its area. Due to the low net returns (in the region of 2% after all costs), the main driver for the activity is to support the areas economic sustainability by retaining employment space and delivering new employment opportunities. This activity is driven through the Council's Property Investment Strategy. This current activity is in addition to historic investments the Council has made to providing commercial work space in its area.

23. With this type of investment the Council accepts higher risk on commercial investment than with treasury investments. In relation to the reacquisition of the Beeching Road head leases the principal risk exposure relates to long term vacancies and the cost of any necessary improvements to the properties. Long term vacancies also feature as the main risk to the Council's finances with the remainder of the properties. These risks are actively managed by the Council. In order that commercial investments remain proportionate to the size of the authority, these are subject to an overall maximum investment limit of £35m and contingency plans are in place, which include disposing of assets and restructuring debt arrangements, should expected yields not materialise.

24. Decisions on commercial investments are made by the relevant Executive Director subject to the support of the Property Investment Panel. The Panel comprises 5 Members and 4 officers. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme.

Investments for Service Purposes

25. In the past, the Council has made on occasion investments through loans to assist local public services, such as the Hastings Furniture Service. In light of the public service objective, the Council can, if it wishes, take more risk than with treasury investments, however it still should ensure such investments break even after all costs. Decisions on service investments are made by Cabinet and Council. Most loans will be treated as capital expenditure and therefore will also be approved as part of the capital programme.

Revenue Budget Implications

26. Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

Table 8: Prudential Indicator: Proportion of financing costs to net revenue stream

	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget
Financing costs (£000)	64	376	1,163	1,380	1,379	1,379
Proportion of net revenue stream	0.5%	2.5%	8.6%	10.5%	10.4%	10.3%

27. Further details on the revenue implications of capital expenditure are contained in the 2019/20 revenue budget.

28. Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Section 151 Officer is satisfied that the proposed Capital Programme is prudent, affordable and sustainable because borrowing is linked to assets that will make a financial return sufficient to meet these costs.

Knowledge and Skills

29. The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Section 151 Officer is a qualified accountant with 29 years' post qualification experience and the Property Investment and Regeneration Manager is a qualified Chartered Surveyor with approximately 30 years post qualification experience, and is supported by a team which includes RICS and CIH qualified staff. The Council has access to specialist legal, valuation, surveying and procurement advice services. The Council pays for junior staff to study towards relevant professional qualifications including CIPFA, AAT, RICS and other relevant qualifications.

30. Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field.

The Council currently employs Link Asset Services as treasury management advisers and Savills. This approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

Conclusion

31. This strategy sets out the Councils approach to its Capital spending and its treasury activities including borrowing. It should be read in conjunction with the Council's revenue budget and the Treasury Management Strategy.

Appendix B

Capital Programme 2018/19 to 2023/24	2018/19 Forecast £ (000)	2019/20 Budget £ (000)	2020/21 Budget £ (000)	2021/22 Budget £ (000)	2022/23 Budget £ (000)	2023/24 Budget £ (000)	Total	Funded	Unfunded
Acquisitions, Transformation and Regeneration									
Community Grants	130	130	130	130	130	130	780	780	
East Parade - project A - Bexhill East Beach	8	0	360	327	0	0	695	295	400
East Parade - project B - Shelters and Heritage Hub	2	30	358	0	0	0	390	42	348
Colonnade Restaurant/units	333	0	0	0	0	0	333	333	
Cemetery Entrance	50	200	0	0	0	0	250	250	
Community Led Housing Schemes	300	350	0	0	0	0	650	650	
Blackfriars Housing Development	100	3,150	0	0	0	0	3,250	3,250	
Rother 2020 Programme									
Property Investment Strategy		12,238	20,000	0	0	0	32,238	32,238	
Acquisition 14 Terminus Road	887	0	0	0	0	0	887	887	
Acquisition 3 sites - Beeching Road	1,625	0	0	0	0	0	1,625	1,625	
Demolition		250	0	0	0	0	250	250	
Solar Panels	47	0	0	0	0	0	47	47	
Rother 20/20 ICT Investment	390	0	0	0	0	0	390	390	
Corporate Document Image Processing System	232	203	0	0	0	0	435	435	
Housing and Community Services									
De La Warr Pavilion - Capital Grant	52	53	0	0	0	0	105	105	
Fairlight Coastal Protection	29	47	0	0	0	0	76	76	
Sidley Sports and Recreation	0	300	0	0	0	0	300	300	
Land Swap re Former High School Site	1,085	0	0	0	0	0	1,085	1,085	
Bexhill Leisure Centre - site development (move to A,T,R)	260	1,930	11,810	0	0	0	14,000	2,190	11,810
Disabled Facilities Grant	1,300	797	0	0	0	0	2,097	2,097	
New bins	13	13	0	0	0	0	26	26	
Replacement/New bins - new contract	0	108	108	108	108	108	540	540	

	2018/19 Forecast £ (000)	2019/20 Budget £ (000)	2020/21 Budget £ (000)	2021/22 Budget £ (000)	2022/23 Budget £ (000)	2023/24 Budget £ (000)	Total	Funded	Unfunded
Camber Western Car park	120	120	120	0	0	0	360		360
Bexhill Promenade - Protective Barriers	0	50	0	0	0	0	50		50
Bexhill Promenade - Outflow pipe	0	100	0	0	0	0	100		100
Housing (purchases - temp accommodation)	0	1,000	1,000	0	0	0	2,000		2,000
Corporate Core including Executive Directors									
Delegate Conference System	50	0	0	0	0	0	50	50	
Accommodation Strategy		TBD					0		
Lift for Amherst Road Offices		100					100	100	
Resources									
Enterprise Resource Planning System upgrade	52	36	0	0	0	0	88	88	
Printing Services - Guillotine	15	0	0	0	0	0	15	15	
ICT Infrastructure - Ongoing Upgrade Programme	166	0	0	0	0	0	166	166	
Total Capital Programme	**7,246**	**21,205**	**33,886**	**565**	**238**	**238**	**63,378**	**48,310**	**15,068**

Funded By:	2018/19 Budget £ (000)	2019/20 Budget £ (000)	2020/21 Budget £ (000)	2021/22 Budget £ (000)	2022/23 Budget £ (000)	2023/24 Budget £ (000)	Total £ (000)
Capital Receipts	1,345	1,930	0	0	0	0	3,275
Grants and contributions	1,729	3,847		0	0	0	5,576
Borrowing	2,559	12,488	20,000	-	-	-	35,047
Capital Expenditure Charged to Revenue	1,493	1,670	535	238	238	238	4,412
Unfunded	120	1,270	13,351	327	0		15,068
Total Funding	**7,246**	**21,205**	**33,886**	**565**	**238**	**238**	**63,378**