

# **South Ribble Borough Council - Capital Strategy**

## **Introduction**

1. The Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code requires local authorities to provide a capital strategy to demonstrate that capital expenditure and investment decisions are taken in line with corporate objectives and take account of stewardship, value for money, prudence, sustainability and affordability.

## **Purpose**

2. The capital strategy sets out the long-term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward an impact on the achievement of corporate strategy priorities.
3. The capital strategy sets out a framework for the self-management of capital finance and examines the following areas:
  - Capital expenditure
  - Treasury Management
  - Commercial Activity
  - The future ambition of the council's capital programme
4. The capital strategy is to be approved annually by Full Council alongside the budget setting papers.

## **Changes to the Strategy**

5. The performance indicators included in the strategy are updated and included below with commentary.
6. The only other proposed updates to the strategy for the 2022/23 budget will be changes to the governance of new capital proposals, two changes have been identified:
  - Due to the restrictions now imposed regarding borrowing from PWLB, a new pro forma must be completed when a project requests funding through borrowing. This will be signed off by the S151 Officer and will ensure the council meets the requirements of the Government that council's do not borrow solely for yield.
  - A more thorough evaluation of business cases is being developed to ensure the council fully evaluates the rewards and risks of new investments. This was

a requirement of our external auditors. It will also ensure the correct procurement route is being followed, legal implications are correctly considered, and project milestones are identified.

## **Capital Expenditure**

7. The council's capital programme forms part of the council's overall financial strategy to deliver some of its key objectives contained in the Corporate Priorities. The capital programme must be affordable and based upon prudence. The current local government financial position and the need to make revenue savings will impact on the council's ability to finance further capital spending unless additional funding is secured from external sources. The capital programme is constructed based upon the following objectives.

## **Capital Programme Objectives**

The resources available will be targeted at areas that deliver corporate priorities as described in the annual Corporate Strategy

Borrowing will be managed to ensure the future impact on revenue is minimised

The council will consider the purchase and/or development of assets to generate a sustainable revenue stream to counteract against the risk of future reductions in grant funding and year to year fluctuations in locally sourced funding; however only where this investment supports the regeneration of the Borough.

Borrowing solely for the purpose of generating yield is no longer permissible.

The council will consider working with partners to assist them to meet both their objectives and the council's objectives; this must have no impact on revenue budgets. This support may include granting loans to organisations at a rate that generates a greater return to the council.

The council will continue to identify land to assist in delivering its affordable housing targets.

The council will look to maximise opportunities to attract external finance to sustain its programme of work.

## **Governance**

8. Democratic decision-making and scrutiny provide overall political direction and ensure accountability for investment in the capital programme. These processes include:
  - Full Council approves the Council's Corporate Strategy that is refreshed every year, this strategy features numerous capital projects that are then built into the council's budget setting process.
  - The Chief Finance Officer is responsible for ensuring that a capital programme is prepared on an annual basis for consideration by the executive before submission to the Full Council.
  - Full Council approves the capital programme as well as the Treasury Management and Investment Strategy. The revenue implications of these strategies are included in the annual budget and Medium-Term Financial Strategy, all of which is approved by Full Council.
  - Cabinet receives quarterly revenue and capital budget monitoring reports, approves variations (or recommends approvals to Full Council) and considers new bids for inclusion in the capital programme.
  - Portfolio holders are assigned projects in line with their responsibilities
  - Scrutiny can call in Cabinet reports, receive and scrutinise reports
  - All projects progressing to the capital programme follow the constitution and financial regulations, this includes adjustments to the projects as they progress
  - The capital programme is subject to review from internal and external audit.
9. The definition of 'capital' will be determined by the Chief Finance Officer, having regard to government regulations and accounting requirements.

## **New Capital Proposals**

10. A new proposed scheme must be assigned a project manager and a new project must focus on the benefits it can deliver through the measurable project outcomes, not just time and cost.
11. Where necessary, business cases are created and scrutinised by the finance team to ensure all financing, capital and revenue expenditure and income implications have been considered across the lifecycle of the investment with appropriate levels of sensitivity analysis surrounding key assumptions. If required, external expertise will be sought to provide specialist support such as VAT and governance advice. Outline risk registers are included and scrutinised by internal audit, finance and the service managers.
12. New proposals along with the business cases are reported to the Shared Senior Management Team (SMT) and Senior Leadership Team (SLT) to ensure schemes are compliant with the council's overall strategic objectives. The role of SLT is to ensure that new proposals are not considered in isolation but rather considered alongside existing schemes and other new proposals. In doing this SLT ensures the council's corporate priorities are driving future capital investment. For example, the council's Medium-term

Financial Strategy includes the ambition to create future efficiency savings, contract savings and income generation, as well as benefit residents and local communities. Projects that are brought forward to SLT must meet one or more of these objectives.

13. Once considered by SLT new proposals are taken to the Shared Senior Management Team (SMT), including the Chief Finance Officer, and if accepted they are taken to the administration for approval. In line with the requirements of the constitution, the new project may be taken to Cabinet or Full Council for final approval. Projects are monitored through the council's bespoke project management framework and toolkit (based on Prince 2 principles) to ensure responsible officers are identified, business cases are reviewed, risks managed, stakeholders suitably engaged, outputs achieved and benefits realised.

### **Affordability, Prudence and Sustainability**

14. The Prudential Code requires that the Authority shall ensure that all capital expenditure, investments and borrowing decisions are prudent and sustainable. In doing so it will take into account its arrangements for the repayment of debt and consideration of risk and the impact on the council's overall fiscal sustainability.
15. The Authority is required to make reasonable estimates of the total capital expenditure that it plans to incur in the forthcoming financial year and at least the following two financial years.
16. The capital programme outlined in Table 1; subject to approval at Full Council on 23 February 2022.

**Table 1: Capital Programme 2021/22 to 2024/25**

	<b>2021/22</b>	<b>2022/23</b>	<b>2023/24</b>	<b>2024/25</b>	<b>Total</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Good homes, green spaces and healthy places	8.894	20.769	25.739	0.874	<b>56.275</b>
A fair economy that works for everyone	2.606	4.587	1.000	0.000	<b>8.192</b>
Thriving communities	0.298	0.846	0.000	0.000	<b>1.144</b>
An exemplary council	1.942	2.991	1.038	0.000	<b>5.970</b>
<b>Total Capital Expenditure</b>	<b>13.739</b>	<b>29.192</b>	<b>27.776</b>	<b>0.874</b>	<b>71.582</b>
Developer Contributions (incl. s106 & CIL)	2.061	7.096	0.000	0.000	<b>9.157</b>
Grants	4.471	6.843	0.774	0.774	<b>12.862</b>
Capital Receipts	0.070	0.000	0.000	0.000	<b>0.070</b>
Reserves	3.889	4.153	0.000	0.000	<b>8.042</b>
Revenue Contribution	0.219	0.000	0.000	0.000	<b>0.219</b>
Prudential Borrowing	3.029	11.100	27.002	0.100	<b>41.232</b>
<b>Total Financing</b>	<b>13.739</b>	<b>29.192</b>	<b>27.776</b>	<b>0.874</b>	<b>71.582</b>

17. The Capital Expenditure Prudential Indicator (Table 1) is the platform from which most Prudential Indicators of the Council are formed; this Prudential Indicator (PI) is grounded in the Council's capital programme and is a stated affordability indicator within the Prudential Code.
18. The predominantly high value projects within any capital programme means capital expenditure is a significant source of risk for any Council; the nature of these projects means they are often subject to cost variations, slippage or changes in specification.
19. Having established through the governance process that the capital programme is affordable, the monitoring of agreed against actual is a key element of risk management which this PI is designed to assist with; quarterly monitoring, using this PI as it's cornerstone, will help sign-post where schemes are straying from expectation either in regard to cost or timeframe
20. A typical measure of affordability is to compare the council's capital financing costs (interest and MRP) to the net revenue stream (council tax, business rates, revenue support grant and new homes bonus income). An increasing percentage would mean a greater proportion of the council's funding being used to meet its debt.

**Table 2: Capital Financing / Net Revenue Stream**

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
<b>MRP and Interest</b>	<b>0.352</b>	<b>0.394</b>	<b>0.648</b>	<b>1.073</b>
Council Tax	(8.599)	(8.599)	(8.599)	(8.599)
Business Rates including grants for reliefs	(5.294)	(5.969)	(5.969)	(5.969)
Services Grant	(0.100)	(0.269)	0.000	0.000
New Homes Bonus	(0.363)	(0.802)	0.000	0.000
<b>Funding</b>	<b>(14.356)</b>	<b>(15.639)</b>	<b>(14.568)</b>	<b>(14.568)</b>
Net Income* - Tom Hansen site	(0.033)	(0.033)	(0.033)	(0.033)
Net Income* - McKenzie Arms site	0.000	0.000	(0.065)	(0.065)
<b>Net Income from Investment Assets</b>	<b>(0.033)</b>	<b>(0.033)</b>	<b>(0.098)</b>	<b>(0.098)</b>
<b>Adjusted Net Revenue Stream</b>	<b>(14.389)</b>	<b>(15.672)</b>	<b>(14.666)</b>	<b>(14.666)</b>
<b>Capital Financing/Net Revenue Stream</b>	<b>2.45%</b>	<b>2.51%</b>	<b>4.42%</b>	<b>7.32%</b>

\* Both projects do not include any borrowing

21. Table 2 gives a proposed performance indicator regarding the affordability of the council's capital strategy. It should be noted however that this indicator will increase due to

reductions in Government funding such as the elimination of New Homes Bonus and Services Grants.

## Prudence

22. The Code also states that “In order to ensure that over the medium term net debt will only be for a capital purpose, the local authority should ensure that net debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.” This is a key indicator of prudence.

**Table 3: Capital Financing Requirement 2020/21 to 2023/24**

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
<b>Opening Capital Financing Requirement</b>	<b>2.500</b>	<b>5.259</b>	<b>16.058</b>	<b>42.754</b>
Increase in prudential borrowing	3.029	11.100	27.002	0.100
Provision made for debt repayments	(0.270)	(0.301)	(0.307)	(0.728)
<b>Closing Capital Financing Requirement</b>	<b>5.259</b>	<b>16.058</b>	<b>42.754</b>	<b>42.126</b>

23. As such there is a requirement to ensure that net debt (the sum of borrowing and other long-term liabilities, net of investments) in 2022/23 does not, except in the short term, exceed **£16.058m**.

## Income Generating Investments

24. The council owns over 130 units across numerous sites that generate a rental income to the council. There are currently five vacant units with strong demand for these units. Any temporary reduction in income from these sites will be met through a £150k reserve that has been created.

25. The council assets that generate net income are summarised below

**Table 4: Summary of Net Income from Investment in Capital Assets**

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
Income from Investment Properties	(1.105)	(1.120)	(1.120)	(1.120)
Income - Tom Hansen site	(0.033)	(0.033)	(0.033)	(0.033)
Income - McKenzie Arms site	0.000	0.000	(0.065)	(0.065)
<b>Total Net Income from Investments</b>	<b>(1.138)</b>	<b>(1.153)</b>	<b>(1.218)</b>	<b>(1.218)</b>
Gross Directorate Budgets South Ribble Council	15.171	15.694	15.307	15.582
<b>% Net Income to Gross Directorate Budgets</b>	<b>7.50%</b>	<b>7.35%</b>	<b>7.96%</b>	<b>7.82%</b>

26. The council's gross directorate budgets are funded by approximately 8% through the income generated by these assets. As the council invests in income generating assets throughout the MTFS period the percentage identified above will increase. As such it is important to monitor this performance indicator and analyse the risk associated with the income assumed in the budget.

## **Risk Appetite**

27. A key element of the capital strategy is to define the council's risk appetite. South Ribble Borough Council is exposed to a number of investment and commercial risks:

- **Financial risk** relating to the investment of cash, market volatility, currency markets, etc
- **Economic risk** relating to whether the local / national economy is growing or contracting
- **Counterparty risk** relating to investments, loans to third parties and business transactions
- **Operational risk** arising from transactions
- **Strategic risk** relating to the decisions taken by the council in pursuit of its corporate objectives, i.e. the purchase of major new assets.
- **Reputational risk** relating to the adverse impact of the council's dealings
- **Environmental and social risks** arising from the adverse impact of investments
- **Governance risk** relating to the transparency and accountability of decisions and decision-makers.

28. The council has no appetite for **reputational, governance and foreign currency risk**. Its approach to other risks is as follows:

- **Financial** – subject to full due diligence and appropriate external advice the council will have a moderate risk appetite for investment / expenditure on a range of asset classes, property and longer-term investments. Security and liquidity will be appropriate for the type of investment made. Income generation will prevail over capital appreciation. The council will have no appetite for volatile or emerging market sector investments.
- **Economic** – The council will have a high-risk appetite for appropriate investments / expenditure in the Borough, it has no risk appetite for investments outside the Borough. The council will have a low appetite for interest rate risk exposure. The key challenge for 2022/23 will be to restore economic activity in the wake of the ongoing Covid-19 pandemic.
- **Counterparty** – the council will have a high appetite for highly rated counterparties and financial institutions and a low appetite for unsecured non-investment debt. All investments will be subject to careful due diligence and an assessment of the council's corporate priorities and liquidity profile.

- **Operational** – the council will have a low risk appetite for all operational risk arising from factors such as: price errors, administrative errors, IT security, etc. Specific business risks are identified at business unit level and business continuity plans identify and mitigate as appropriate. There is no appetite for fraud, regulatory breaches and exceeding approved limits.
- **Strategic** – The council will have a high appetite for investments which further its corporate priorities, increase revenue streams and / or facilitate the efficient and effective delivery of core service objectives,
- **Environmental and social** – the council will have no appetite for environmental and social risk

## Future Capital Investment Ambition

29. The council's ambition to invest within the borough stretches beyond the time scales of its approved capital programme. The council will invest to deliver efficiency savings, generate additional income to be reinvested in services and invest to support local residents and communities.

## Income Generating investment

30. The council is committed to investing within the borough to bring forward sites that will further enhance local employment as well as generating a revenue stream for the council. The council's local plan is undergoing a review to be concluded within the MTFS period. Employment sites identified from this review will be considered for development whether controlled by the council or in partnership with other developers.

31. The council will identify external funding wherever possible to deliver its investment ambitions. The council has already successfully bid for and received £750k to purchase sites in Leyland town centre and has received a further £160k to create a Leyland town investment plan. The council has successfully bid for a £25m **Town Fund** grant with proposed match funding of £8m. This will deliver transformational change to areas of Leyland including new housing and employment opportunities. It is expected that this will also deliver a net income stream to the council helping it to manage future budget deficits.

32. **Worden Hall** – the council is investing £3m in the refurbishment of the hall enhancing the visitor experience whilst also generating an increase in income to the council through hire of community spaces, additional events and improved café facilities. This is forecast to generate additional income of £65k from the site which will fund additional staff in the museums and events teams.



## Housing

33. The council already has included in the capital programme several large scale projects to bring forward affordable housing in the borough. The council will continue to implement these projects bringing forward the development of better quality of homes in South Ribble.
34. The council will develop over 70 self-contained **extra care** units embracing the principles of the lifetime homes standard that ensures the homes will be accessible and adaptable. It is forecast this development will generate a net income to the council in 2025/26 onwards.
35. The council will continue to bid for and utilise external funds to complete housing projects including One Public Estate, funding from Homes England and Commuted (s106) sums.

## Investing to Generate Efficiency Savings

36. The council's Medium-Term Financial Strategy identifies, as a minimum, a further £732k revenue budget efficiency savings to be realised by 2024/25. These savings will come through reduced revenue budgets and additional income generation. The council's Corporate Strategy recognises the need to invest in services to deliver these savings.
37. The council has approved a capital budget of £0.970m for investment in its **ICT infrastructure**. Capital investment is necessary to keep pace with the changing demands in technology and enable delivery of the councils Shared Digital Strategy and Workplace Strategy. The investment will replace outdated CCTV infrastructure and expand internet connectivity to improve the security of the council's buildings.
38. The council is committed to reducing its impact on the environment with the aim of being carbon neutral by 2030. A £5m bid to **decarbonise** its assets has been made to Government. If approved, this grant will enable the council to significantly reduce its use of fossil fuels to power its leisure centres, vehicle depot and office buildings. As well as reducing the council's carbon footprint, it is also expected that such investment will reduce the ongoing revenue costs of operating its buildings with estimate savings of approximately £600k over an 8 year period, as per the report to Council on 21 July 2021.

## Knowledge and Skills

39. The council has professionally qualified staff across a range of disciplines including finance, legal and property that follow continuous professional development (CPD) and attend courses on an ongoing basis to keep abreast of new developments and skills. The council establishes project teams from all the professional disciplines from across the council as and when required. External professional advice is taken where required and will always be sought in consideration of any major commercial property investment decision.

40. Internal and external training is offered to members to ensure they have up to date knowledge and expertise to understand and challenge capital and treasury decisions taken by the strategic director of finance and governance.

## Recommendations

41. It is recommended that the prudential indicators outlined in Table 5 are approved as part of the 2022/23 budget.
42. It should be noted that these performance indicators are specific to South Ribble Borough Council due both to its composition of funding and its unique level of commercial activity. As such these cannot be benchmarked effectively against other council's indicators. The indicators can however be monitored over time. As such it is proposed that these performance indicators will be monitored, reported and, where necessary adjusted, every six months. They will be reported to Governance Committee and Full Council.

**Table 5 – Prudential Indicators 2020/21 to 2023/24**

Indicator	2021/22	2022/23	2023/24	2024/25
Estimated Capital Expenditure (Table 1)	£13.739m	£29.192m	£27.776m	£0.874m
Capital Financing / Net Revenue Stream (Table 2)	2.45%	2.51%	4.42%	7.32%
Estimated Capital Financing Requirement (Table 3)	£5.259m	£16.058m	£42.753m	£42.125m
% Net Income to Gross Directorate Budgets (Table 4)	7.50%	7.35%	7.96%	7.82%