**APPENDIX 5**

# CAPITAL STRATEGY 2022/23 – 2024/25

1. Introduction

The Capital Strategy is intended to provide a high-level overview of how the Council's capital expenditure, capital financing and treasury management activity contribute to the provision of services to the residents of Broxtowe along with an overview of how associated risk is managed and the implications for future financial sustainability.

The Capital Strategy should be considered in conjunction with the Treasury Management Strategy Statement 2022/23 - 2024/25 (appendix 6) and Investments Strategy 2022/23 - 2024/25 (appendix 7).

Decisions made this year on capital and treasury management will have financial consequences for the Council for many years into the future. As such, they are subject to both a national regulatory framework and a local policy framework, summarised in this report.

2. Background

The Capital Strategy is intended to ensure that decisions about capital spending are taken in alignment with agreed corporate priorities and make the best use of scarce resources. It has been developed in conjunction with the Council's Corporate Plan, ICT Strategy, Asset Management Strategy and People Strategy and seeks links to other approved strategies and policies. The Council will have regard to the following in determining its capital expenditure plans:

- Corporate objectives (e.g. strategic planning)
- Stewardship of assets (e.g. asset management planning)
- Value for money (e.g. appraisal of options)
- Prudence and sustainability (e.g. implications for external borrowing and whole life costing)
- Affordability (e.g. implications for long–term resources and ultimately on the level of council tax)
- Practicality (e.g. the achievability of the Corporate Plan)

The production of the capital programme will be based upon the following eight core principles:

(i) All assets will be periodically reviewed to determine whether they remain fit for purpose.

(ii) Asset management systems will be used to increase the proportion of expenditure on planned as opposed to reactive maintenance and to determine appropriate levels of contingency in each planning period.

(iii) Capital expenditure, particularly in respect of investment in commercial assets, will be undertaken within the context of the Council's defined risk appetite and adopted priorities.

(iv) The decision to procure or build new assets will take into account the full revenue implications of the life cycle of the asset.

(v) Income from asset disposals will be retained centrally for the funding of future capital programmes.

(vi) Capital submissions produced by departments will be included in the third year of the three-year rolling capital programme unless they meet the specific criteria outlined above.

(vii) Capital submissions will be reviewed by the Council's Section 151 Officer in conjunction with General Management Team (GMT) using a pre-determined scoring matrix set out in the submission template.

(viii) Borrowing will only be pursued as an option for financing capital expenditure after all other potential financing options have been considered.

The capital programme is a three-year rolling programme with new submissions, based upon an agreed template, accepted only for year three unless they meet the following criteria:

- The project has health and safety implications which must be addressed as a priority or is a statutory requirement.
- The project generates more income over time than the investment required (an "invest to save" project).
- The project is required to match income from external sources that would otherwise be lost.

Unforeseen factors may arise will require schemes to be swiftly incorporated within the capital programme. These schemes will be subject to the same appraisal process set out above and will be funding will be assisted by the inclusion of suitable contingencies within the capital programme to avoid disrupting other planned capital schemes.

3. <u>Capital Expenditure and Financing</u>

Capital expenditure is where the Council spends money on assets (such as property, vehicles or equipment) that will be used for more than one year. In local government this includes expenditure on assets owned by other bodies and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion as to what to classify as capital expenditure and this is set out in its Accounting Policies.

Capital expenditure can be paid for immediately by applying capital resources, such as capital receipts or capital grants, or by using revenue resources. However, if these resources are insufficient then any residual expenditure will add to the Council's borrowing need.

The following table summarises the three-year capital programme as presented to the Finance and Resources Committee on 10 February 2022 along with the intended financing:

| | 2020/21 Actual £000 | 2021/22 Revised £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|---|---|---|---|---|---|
| **Capital Expenditure** | | | | | |
| General Fund | 10,358 | 10,051 | 8,415 | 12,807 | 2,592 |
| Housing Revenue Account | 6,367 | 13,678 | 11,035 | 13,949 | 9,817 |
| **Total** | **16,725** | **23,729** | **19,450** | **26,756** | **12,409** |
| | | | | | |
| **Financed by:** | | | | | |
| Borrowing – GF | 6,061 | 5,929 | 1,144 | 1,479 | 812 |
| Borrowing – HRA | 0 | 1,614 | 3,292 | 6,848 | 2,475 |
| Major Repairs Reserve | 4,227 | 4,211 | 4,211 | 4,211 | 4,073 |
| Capital Receipts – GF | 2,578 | 1,026 | 0 | 0 | 0 |
| Capital Receipts – HRA | 1,499 | 3,447 | 748 | 1,052 | 1,613 |
| Direct Revenue Financing GF | 15 | 15 | 0 | 0 | 0 |
| Direct Revenue Financing HRA | 365 | 3,852 | 1,786 | 1,650 | 1,656 |
| Better Care Fund | 784 | 1,401 | 798 | 798 | 798 |
| Section 106 Receipts | 540 | 346 | 0 | 188 | 0 |
| Department for Levelling-Up, Housing and Communities | 449 | 52 | 5,695* | 10,376* | 927* |
| D2N2 LEP | 207 | 0 | 0 | 0 | 0 |
| FCC (previously WREN) | 0 | 0 | 75 | 0 | 0 |
| Other Bodies | 0 | 753 | 998 | 0 | 0 |
| **Total** | **16,725** | **22,646** | **18,747** | **26,602** | **12,354** |
| | | | | | |
| Shortfall still to be funded | 0 | 1,083 | 703 | 154 | 55 |

**Stapleford Towns Fund*

Note: This table does not include any capital amendments being considered elsewhere as part of this agenda. These will be added accordingly once approved. The overall impact is not considered to be significant.

One of the key risks to the capital expenditure plans above is the level of resources available within the Housing Revenue Account (HRA) to support capital expenditure. The current version of the HRA Business Plan model demonstrated that this should not be a major risk over the three-year period, particularly in view of the availability of capital receipts from right to buy sales and the greater freedom to borrow following the abolition of the 'debt cap'.

The three-year capital programme from 2021/22 includes £1,400,000 per annum for the purchase of former right to buy and other properties by the HRA as set out in the Housing Delivery Plan. Each acquisition will be subject to an appraisal process before a decision to purchase is made to ensure that the acquisition meets the Council's needs and provides value for money. It is anticipated that the rental income from the properties acquired will meet the accompanying ongoing borrowing costs.

Similarly, a risk to General Fund capital expenditure plans is that some of the estimates for other sources of funding may also be subject to change over this timescale. The table above, for example, assumes there are limited capital receipts available to finance General Fund capital expenditure.

No assumptions have been made with regards to either the value or timing of any further capital receipts that may subsequently be received.

The Council's land and property holdings will continue to be reviewed in line with a new Asset Management Strategy to be produced that will, among other things, seek to identify opportunities to bring forward recommendations to dispose of or make alternative use of surplus assets.

It is anticipated that borrowing of £1,144,000 will be undertaken to finance General Fund capital expenditure in 2022/23 with further borrowing of £1,479,000 in 2023/24 and £812,000 in 2024/25. HRA borrowing is expected to increase substantially when compared to recent year due to the extensive house building programme that is planned. HRA borrowing in 2022/23 is forecast at £3,292,000 with additional borrowing of £6,848,000 anticipated in 2023/24 and £2,475,000 in 2024/25.

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 may sometimes be conflicting and the Council therefore seeks to strike a balance between cheap short-term loans (currently available between 0.10% and 1.00%) and long-term fixed rate loans where the future cost is known but slightly higher (currently 1.60% to 2.00%).

The tight revenue situation is such that it has been assumed that the capital programme from 2022/23 will be revisited and re-aligned as far as possible to tie into available capital resources in order to minimise the level of prudential borrowing required.

4. The Capital Financing Requirement

The Capital Financing Requirement (CFR) represents the Council's underlying need to borrow for capital purposes. It is the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. The CFR will change each year in accordance with the value of the approved capital programme and the financing available. The capital expenditure above which has not been financed from available internal resources or from grants or third party contributions will increase the CFR.

| | 2021/22 Revised £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|---|---|---|---|---|
| **Capital Financing Requirement** | | | | |
| CFR – General Fund | 29,660 | 29,480 | 29,539 | 28,743 |
| CFR – HRA | 82,881 | 86,174 | 93,022 | 95,497 |
| **Total CFR – 31 March** | **112,541** | **115,654** | **122,561** | **124,240** |
| | | | | |
| Movement in CFR represented by: | | | | |
| Borrowing need for the year | 7,543 | 4,437 | 8,327 | 3,287 |
| MRP/VRP/other financing movements | (1,125) | (1,324) | (1,420) | (1,608) |
| **Movement in CFR** | **6,418** | **3,113** | **6,907** | **1,679** |

As debt is only a temporary source of finance, since loans and leases must be repaid, this is therefore repaid over time by other financing, usually from revenue which is known as the Minimum Revenue Provision (MRP).

5. Treasury Management

Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's needs whilst managing the risks involved. Surplus cash is invested until required whilst an anticipated shortage of cash is met by borrowing in order to avoid an overdraft in the Council's bank current account.

The Council usually has surplus cash available in the short-term as revenue income is normally received before it is spent but can have a cash deficit 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.

i) Borrowing Strategy

The Council's main objectives when borrowing are to achieve a low but certain cost of finance whilst retaining flexibility should plans change in the future. These objectives are often conflicting and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at 0.10% to 1.00%) and long-term fixed rate loans where the future cost is known but higher (currently 1.60% to 2.0%).

Projected levels of the Council's total borrowing when compared with the capital financing requirement are shown in the table below.

| | 2021/22 Revised £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|---|---|---|---|---|
| Gross Borrowing | | | | |
| - PWLB and Market | 98,896 | 108,896 | 112,096 | 122,161 |
| - Bramcote Crematorium | 500 | 400 | 400 | 400 |
| **Net Borrowing – 31 March** | **99,396** | **109,296** | **112,496** | **122,561** |
| | | | | |
| Capital Financing Requirement | | | | |
| CFR – General Fund | 29,660 | 29,480 | 29,539 | 28,743 |
| CFR – HRA | 82,881 | 86,174 | 93,022 | 95,497 |
| **Total CFR – 31 March** | **112,541** | **115,654** | **122,561** | **124,240** |

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

ii) Affordable Borrowing Limit

The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit) each year. In line with statutory guidance, a lower 'operational boundary' is also set as a warning level should borrowing approach this limit.

| | 2021/22 Revised £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|---|---|---|---|---|
| Authorised Limit for Borrowing | 126,500 | 138,900 | 142,400 | 155,500 |
| Operational Boundary for External Debt | 101,200 | 111,100 | 113,900 | 124,400 |

The authorised limit and operational boundary as set out above assume that the Council will not be entering into any private finance initiatives or leases over the period shown. The Council presently has no plans to enter into such arrangements.

iii) Treasury Investment Strategy

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.

The Council's policy on treasury investments is to prioritise security and liquidity over yield. In other words, the objective is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the short-term is invested securely with, for example, the government, other local authorities or selected high-quality banks to minimise the risk of loss. Money that will be held for the long-term is invested more widely to balance the risk of loss against the risk of receiving returns below inflation. Both short-term and long-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.

The table below highlights the expected change in investment balances.

| | 2021/22 Revised £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|---|---|---|---|---|
| Investments at 1 April | 18,842 | 10,533 | 12,000 | 10,000 |
| Expected Change in Investments | (8,309) | 1,467 | (2,000) | 0 |
| Investments at 31 March | 10,533 | 12,000 | 10,000 | 10,000 |

iv) Risk Management

The effective management and control of risk are prime objectives of the Council's treasury management activities. The Treasury Management Strategy therefore sets out various indicators and limits to constrain the risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.

v) Governance

Decisions on treasury management investment and borrowing are made daily and are delegated to the Deputy Chief Executive and Section 151 Officer and colleagues who must act in accordance with the Treasury Management Strategy approved by Finance and Resources Committee. Reports on treasury management activity are also presented to the Finance and Resources Committee (or equivalent) whose members are responsible for scrutinising treasury management decisions.

6. Revenue Budget Implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and minimum revenue provision (MRP) are charged to revenue albeit offset by investment income receivable. The net annual charge is known as financing costs and is compared to the net revenue stream (i.e. the amount funded from council tax, business rates and general government grants).

| | 2021/22 Revised | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|
| General Fund | 13.4% | 15.1% | 15.8% | 17.3% |
| HRA | 14.8% | 14.9% | 15.2% | 16.2% |

The estimates of financing costs reflect current commitments and the proposals in the revenue and capital budget reports elsewhere on the agenda.

The indicators for the General Fund rise significantly from 2022/23 to reflect the increase in MRP following the additional borrowing to finance capital expenditure, particularly the Beeston town centre redevelopment. HRA indicators show a large increase between 2023/24 and 2024/25 due to significant planned borrowing to finance the house building programme.

The Council intends to undertake a prudent level of borrowing to support the capital programme during the period covered by its medium term financial plans.

7. Knowledge and Skills

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the following individuals all hold the Chartered Institute of Public Finance and Accountancy (CIPFA) or other CCAB (Consultative Committee of Accountancy Bodies) professional accountancy qualifications:

- Deputy Chief Executive and Section 151 Officer (CPFA)
- Head of Finance Services (CPFA)
- Chief Accountant (CPFA)
- Chief Audit and Control Officer
- Principal Accountant

The Council also pays for staff to study towards CIPFA and other relevant qualifications such the Association of Accounting Technicians (AAT).

Where Council staff do not have the knowledge and skills required, use is made of external advisors and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisors. The contract with Arlingclose has, in recent years, been extended on a 12 month rolling basis and is currently due to expire on 31 March 2022. An exercise is to be undertaken to establish the service provider from 1 April 2022.

The services currently provided by Arlingclose include:

- technical support on treasury matters and capital finance issues
- economic and interest rate analysis
- debt services (including advice on the timing of borrowing)
- debt rescheduling advice surrounding the existing portfolio
- generic investment advice on interest rates etc.
- credit ratings/market information service comprising the three main credit rating agencies.

Whilst the treasury advisors provide support to the internal treasury function, the current market rules and the CIPFA Treasury Management Code confirms that the final decision on treasury management matters rests with the Council.