

# Capital Strategy 2019/20 to 2023/24

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## Introduction

This capital strategy provides a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local services and how associated risk is managed by the council.

## Our Strategic Aims & Objectives

A new Corporate Plan was approved on 23 January 2018 and runs until 31 March 2021. The priorities set out in the new plan represent the challenges and opportunities facing Chichester District Council over the new plan period.

Our priorities are to:

- Improve the provision of and access to suitable housing.
- Support our communities.
- Manage our built and natural environments to promote and maintain a positive sense of place
- Improve and support the local economy to enable appropriate local growth
- Manage the council's finances prudently and effectively

Each of these priorities is underpinned by several objectives, setting out what the Council aims to achieve. Below these objectives sit further, more specific, actions the council will undertake and, where appropriate, these are accompanied by specific, measurable targets

The council has a 5 year medium term financial strategy and a 5 year capital programme (with 5 year revenue implications) that links the estimated available resources directly to the corporate priorities. Annual reviews occur as part of the budget process and Council makes amendments in the light of revisions to the Corporate Plan and the Performance Plan following detailed consultation with the public and partners.

Beneath these overarching documents, the Capital Strategy and the Council's Asset Management Plan (AMP) provide the policy framework for the operational work of asset management, asset acquisition and disposal.

## Approval process

The Council approves a capital programme on recommendation from the Council's Cabinet. This programme consists of significant projects that qualify as capital expenditure and a planned programme of scheduled asset replacements (ie; the Asset Replacement Programme or ARP).

The Council follows the following key principles in determining its capital priorities:

1. All key decisions of the Council should relate back to the Corporate Plan
2. The revenue budget and capital programme must remain balanced and sustainable over a rolling 5 year period.
3. The Council will not use its reserves to fund ongoing services.
4. Savings in the revenue budget or external funding are identified before any new revenue expenditure, including capital expenditure that has revenue consequences, is approved.

Cabinet is responsible for the acquisition, management, maintenance and disposal or letting of all Council properties together with review and implementation of the Council's Asset Management plan and this Capital Strategy.

The Director of Corporate Services is responsible for providing professional advice to Cabinet and Council in the discharge of these functions, together with making arrangements for raising and repaying loans as necessary and overall treasury management of funds until they are needed.

## Our Assets

The Council's asset base at 31 March 2018 was



## Capital Programme

In 2018-19 the Council is planning to spend £14.0m on capital assets. This was part of an overall planned programme of £51.1m in the period 2018-19 to 2023-24, that includes the following major schemes

*Table 1: Capital programme and major schemes 2018-19 to 2023-24 £m*

Capital Expenditure	2018-19 Projected	2019-20	Later	Total
Total approved spend	14.0	8.9	28.2	51.1
<b>Major schemes</b>				
New Homes Bonus allocations	0.4	0.4	6.1	6.9
Disabled Facilities grants	1.5	1.3	3.7	6.5
Affordable and Community led Housing	1.4	1.4	5.4	8.2
St James's Industrial Estate	-	0.2	5.0	5.2
Southern Gateway Project	5.0	0.1	-	5.1
Infrastructure Business Plan: School Places	-	1.2	2.4	3.6
Infrastructure Business Plan: Sustainable Transport	-	0.5	0.4	0.9
Infrastructure Business Plan: Medical Centre West Chichester	-	1.3	-	1.3

## Affordability

The Council recognises that, due to its nature, the capital programme is constantly changing, so the resource position is regularly updated and monitored to ensure that the programme remains affordable. The Council's latest resource projection is shown below.

*Table 2: Resources available to finance our Capital programme (£m)*

Resources 2019-20 to 2023-24	Total
Expected available resources as at 1 April 2018(*)	23.9
New Resources expected in period	
- Capital receipts	9.4
- Revenue contributions	
o Asset replacements/Investment Opportunities Fund	8.6
o Interest receipts	2.0
- Other external income	
o Grants, contributions and CIL	26.9
o Other receipts	1.1
<b>Available Resources</b>	<b>71.9</b>

\* "Expected available resources" is Total Reserves less Reserves set aside for a specific purpose

As table 2 indicates, the Council currently expects capital resources of £71.9m to be available. The total expected capital expenditure over the same period is shown below.

*Table 3: Planned application of resources to capital projects (£m)*

	2018/19 Expected	2019/20 Budget	Later	Total
External sources				
- Grants and contributions	2.2	1.9	5.6	9.7
- LEP	4.5	-	-	4.5
- Section 106 contributions	1.1	0.2	0.1	1.4
- Community Led Housing Grant	0.3	0.5	0.6	1.4
Own resources				
- Revenue reserves and financing	4.3	2.6	8.2	15.1
- Capital receipts	1.2	1.4	2.0	4.6
- New Homes Bonus	0.4	0.4	6.1	6.9
Community Infrastructure Levy	-	1.8	5.7	7.5
Debt	0.0	0.0	0.0	0.0
<b>TOTAL</b>	<b>14.0</b>	<b>8.8</b>	<b>28.3</b>	<b>51.1</b>
Expected total external debt	0.0	0.0	0.0	0.0
Expected capital financing requirement	0.0	0.0	0.0	0.0

Tables 2 and 3, taken together demonstrate that the Council currently expects to be able to fully fund its approved capital and asset replacement programmes from existing and expected resources. Fully funding our capital programme and asset replacement programme from our own resources means that the Council also expects to remain debt free over this period.

The main risk managed by the Council is that the expected resources shown in the table above will not be received, or will be received significantly later than forecast.

The receipt of capital resources is closely monitored by the Council's finance and estates teams and the Commercial Programme Board and is regularly reported to the Portfolio holder for Corporate Services and to Cabinet. An annual statement on resource projections against capital needs is included with the Council's financial strategy that is presented each year to full Council for approval.

Guidance issued by the Government requires all Councils to be transparent where they plan to use capital receipts flexibility to part fund individual projects. As the Council currently makes significant revenue contributions to fund its capital programme, the Council presently does not intend to make use of this flexibility.

The Director of Corporate Services is satisfied that the proposed capital programme is prudent, affordable and sustainable and this is set out in more detail in the Council's 5 year financial strategy.

## **Other major future developments**

The capital strategy recognises the impact of future projects not presently included in the Council's capital programme, but which have a potentially significant impact on Council resources. One such project is the Southern Gateway, as described below.

### **Southern Gateway**

The Southern Gateway is the biggest regeneration project that the city has seen for decades. In November 2017 our councillors adopted the Southern Gateway Masterplan which sets out the basis on which the area can be comprehensively regenerated.

At the moment, the site includes several parcels of land:

- the bus station and depot
- Basin Road car park
- law courts
- part of the former Chichester Police Station playing field
- part of the former high school, and
- the Royal Mail depot buildings.

The project will involve transforming this mainly 30-acre brownfield area into a vibrant and attractive new southern quarter for the city of Chichester. It is the one of the biggest redevelopment projects undertaken in a generation within Chichester and the Council is working in partnership with West Sussex County Council and Homes England to bring this development forward.

The Council expects the opportunity will be taken to the market via an OJEU compliant process with a development partner being selected in 2019.

## **Managing our assets**

To ensure that capital assets continue to be of long-term use, the Council has an asset management Plan (AMP) which provides the policy framework for the operational work of asset management, asset acquisition and disposal.

### **Asset Replacement**

The Council recognises that it is not sufficient to simply provide for the initial purchase cost of capital assets. Investment in assets requires a long-term view to be taken of the cost of those assets across their entire lifespan.

The Council's revenue budget incorporates repairs and maintenance to council buildings, removing dependency on reserves to fund what is a recurring revenue cost. Commercial investments are let on fully repairing and insuring lease terms to protect the Council's assets.

Other lifecycle costs for all Council assets are forecast for 25 years and included in the Council's approved Asset Replacement Programme (ARP). An annual contribution from the Council's revenue budget to fund this programme is made equating to one 25<sup>th</sup> of the projected total ARP cost.

## **Treasury Management**

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 borrowing, to avoid excessive credit balances or overdrafts in the bank current account and where it is economical to borrow in advance of spend.

In addition its cash surplus balances, the Council has £7.5m of recently purchased property investments (at 30 September 2018) earning an average rate of return of 6.7%.

In managing these funds, the Council has adopted the following risk statement

“The Council's priority is the security and liquidity of its Treasury investments in accordance with the priorities set out in the CIPFA Code. Whilst fundamentally risk averse, the Council accepts some modest degree of risk within the limits and counterparty restrictions set out in its Treasury Management and Investment Strategy.”

This means that, when investing its surplus cash, the Council does not limit itself to making deposits only with the UK Government and local authorities, it can, and does, invest in other areas such as money market funds and tradable instruments such as corporate bonds and pooled funds. The duration of such investments is always carefully considered to limit that risk of them having to be sold (although they may be) prior to maturity, mitigating the risk of the capital sum being diminished through price movements.

Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Corporate Services and staff, who must act in line with the treasury management strategy approved by Council. Half yearly on treasury management activity are presented to the Corporate Governance and Audit Committee and Cabinet.

## **Investments**

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 business model for holding treasury investments is designated as 'hold to collect', in that that Council holds these financial assets to collect their contractual cash flows, rather than with a view to selling the assets to generate cash flows. However, there is no absolute

requirement that financial assets are always held until their maturity in all circumstances.

The Council prioritise security and liquidity over yield in holding Treasury investments. That is, it focusses on minimising risk rather than maximising returns.

Cash that is likely to be spent in the near term is invested securely 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 can 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 4: Forecast treasury management investments in £m (31 March)*

	2019	2020	2021	2022	2023
Near-term investments	25.9	24.0	24.0	23.4	23.4
Longer-term investments	18.0	18.0	18.0	18.0	18.0
<b>TOTAL</b>	<b>43.9</b>	<b>42.0</b>	<b>42.0</b>	<b>41.4</b>	<b>41.4</b>

*These figures do not account for any delays in timing of capital payments. Delays generally increase the available cash balances temporarily above forecast levels.*

## **Borrowing**

The Council is currently debt-free and has no borrowing other than that which might occur as part of routine working capital management. Under the Council’s current resource projections, there are no plans to borrow to finance new capital expenditure over the medium term but this remains an option.

The Capital Financing Requirement (CFR) is a measure of the Council’s underlying need to borrow to fund capital expenditure. The Council currently expects to have a zero CFR at 31 March 2019 and for this continue at zero throughout the period to 31 March 2023, although our projections below incorporate some potential for borrowing should the need arise.

The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each of the following three financial periods. In line with statutory guidance, a lower “operational boundary” is also set as a warning level should debt approach the limit.

*Table 5: Proposed Operational and authorised limits for borrowing (£M)*

	2019/20	2020/21	2021/22
Operational Boundary – borrowing	5	5	5
Operational Boundary– PFI and leases	2	2	2
Operational Boundary– total external debt	12	12	12
Authorised Limit – borrowing	20	20	20
Authorised Limit– PFI and leases	5	5	5
Authorised Limit– total external debt	25	25	25

Further details on borrowing are contained in the Council the treasury management strategy: <http://www.chichester.gov.uk/article/24169/Treasury-Management-Strategy>. The limits in this table are provisional until the 2019-20 strategy is approved by Full Council.

### **Liabilities**

Decisions on incurring new discretionary liabilities are taken by Divisional Managers in consultation with Director of Corporate Services and within the limits established by the Council’s Constitution and Treasury and Investment strategy. The risk of liabilities crystallising and requiring payment is monitored by financial services.

Further details on liabilities, contingent liabilities and guarantees are can be found in the Council’s statement of accounts:

<http://www.chichester.gov.uk/statementofaccounts>

### **Interest Rate Exposures**

The Council is not exposed to risk associated with the maturity structure of borrowing, but recognises that its Treasury investments are subject to risk from movements in interest rates. The Council manages this risk by ensuring an appropriate mix of short term fixed and variable rate investments and a portfolio of external investments in pooled funds.

### **Impact on Council tax**

Although capital expenditure is not charged directly to the revenue budget, a Minimum Revenue provision (MRP) is charged to revenue, offset by any investment income receivable. MRP charge is a set aside from council reserves to ensure that borrowing can be repaid when due and the overall 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.

As the Council is, and expects to remain, debt free, the Council is not required to make a charge to revenue to finance debt (minimum revenue provision).

Further details on the revenue implications of capital expenditure are published with the Council's revenue budget which is considered each year by Cabinet and Full Council.

### **Service investments**

The Council has made a very limited number of loans to assist local public services and residents, generally for housing renewal purposes. Some loans have been made to members of staff for transport purposes. Decisions on minor loans are made by the relevant service manager in consultation with the Director of Corporate Services.

The Council is presently developing proposals to support the provision of temporary housing in the District. If approved this will allow funds of up to £2.1m to be used to support specific local groups.

The total value of loans made by the Council to external third parties is disclosed on the Council's annual statement of accounts. Further details on service investments are within the Council's investment strategy, which is published with the Council's Treasury management strategy:

<http://www.chichester.gov.uk/article/24169/Treasury-Management-Strategy>.

### **Commercial Activities**

The Council's existing property portfolio generates income of approximately £3 million per year for the General Fund revenue account.

This income comprises rents and licence fees principally from 49 industrial units, 72 commercial and industrial ground leases, 41 shops, 13 offices and other lettings to sports, community and voluntary organisations.

Capital investment is likely to take 3 main forms.

- Freehold or Long Leasehold Purchases
- Commercial development of property with the Council retaining ownership and receiving rental income.
- Partnerships where another party undertakes the development and the Council (as landowner) receives a proportion of the rental value.

Land and property acquisition and development is also a means of influencing regeneration and the economic development within the District. Therefore while one objective may be to increase the financial resources the Council has available, appropriate investment can also extend service delivery or provide community improvement generally.

For these reasons the Council gives priority to acquiring property in the Chichester District, albeit opportunities to acquire properties elsewhere are considered if a justifiable case exists for doing so.

The Council aims to acquire land and property for the longer term (10 years or more) to reap the benefit of sustained rental income and capital appreciation as land and property values recover from the effects of economic downturn in recent years.

There is a recognition that, in undertaking investments primarily for financial return, the Council needs to ensure that these decisions are subject to enhanced decision making and scrutiny as a result of the additional risk being taken on and the potential impact on the sustainability of the authority. The principal risk exposures in commercial property-based revenue strategy are:

- A downturn in the property market. This could lead to falling rents or higher vacancies, potentially meaning that the Council will need to find other sources of revenue, or reduce costs to balance its budgets. Its scenario could also lead to falling property values, with a risk that the asset would be worth less than the purchase price.
- Government intervention to set limits on commercial activities. This would force the Council to react, which may be against the Council's long term interests.
- Lack of expertise in specialist areas, leading to poor acquisition decisions.

To provide specific guidance on the enhanced scrutiny required, the Council has approved an investment opportunities protocol. The guidance includes requirements that:

- Acquisitions should be within the District Council's area, or sufficiently close by to be easily managed
- Priority is given to acquisitions which achieve a community or economic benefit and strengthen the local economy
- The acquisition provides an acceptable rate of return for the additional risk taken on, and will not increase the Council's ongoing revenue costs in the longer term
- Where necessary, Specialist advisers are to be employed to provide advice and act for the Council

Investment purchases are evaluated using a scoring matrix approach, with a minimum score required of least 100 out of a maximum score of 168 (60th percentile). The score reflects, amongst other things, tenancy strength, tenure, occupiers lease length and repairing terms.

Decisions on commercial investments are made by Cabinet in line with the criteria and process set out in the Council's investment opportunities protocol.

Further details on investment limits and risk management arrangements are contained in the Council's investment strategy and Treasury management strategy: <http://www.chichester.gov.uk/article/24169/Treasury-Management-Strategy>

## **Other long-term liabilities**

Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees do carry risks to the Council and as such, they are subject to separate risk mitigation procedures before they are entered into.

The only guarantees provided by the Council relate to possible pension liabilities associated with TUPE transfers of staff from public to private sector where staff have remained within the Local Government Pension Scheme.

In these circumstances the provision of a guarantee is a requirement of the Pension Fund. The financial risk of each guarantee is mitigated by a bond which is intended to cover all but the most extreme possible financial exposure.

Other than to cover mandatory requirement under the Local Government Pension Scheme, the Council does not expect to provide financial guarantees to, or on behalf of, any third party.

The Council expects to hold £5.3m in s.106 contributions at 31 March 2019. These sums are held to pay for planning obligations but are potentially repayable if projects do not proceed as expected.

## **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, both the Divisional Manager for Property & Growth and the Valuation & Estates Manager are chartered surveyors and registered valuers, with extensive professional experience.

The Council currently employs Arlingclose Limited as Treasury Management advisers, and individual property consultants for cases where specialist property advice is required such as major development schemes. It has also elected where possible to be treated as a professional investor under the requirements of the 2<sup>nd</sup> European Union Markets in Financial Instruments Directive.