

## Appendix 3 – Capital Strategy

### Capital Strategy 2022-23 to 2026-27

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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.

This Capital strategy reflects the Council's capital investment and financing intentions in December 2021. Given the continuing economic uncertainties faced at present the position described within is very likely to evolve in line with the Council's ongoing pandemic response and development of its capital intentions.

## **Our Strategic Aims & Objectives**

The Council's Corporate Plan was approved on 23 January 2018 and runs until 31 March 2022. An updated corporate plan is presently being considered for adoption early in 2022 covering the period 2022/2025. Until this plan is formally adopted, the Council's priorities remain:

- Improving the provision of and access to suitable housing;
- Supporting our communities;
- Managing our built and natural environments to promote and maintain a positive sense of place;
- Improving and support the local economy to enable appropriate local growth; and,
- Managing 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.

## **Impact of COVID-19**

As part of the Council's response to the COVID-19 pandemic four groups were established to have oversight of the delivery of the recovery action plans:

- Housing and Community
- Economic Recovery Group
- Planning, Health and Environmental Protection Recovery Group
- Organisational Recovery Group

The Leader, Chief Executive and the Director of Corporate Services provides oversight of the four groups, monitored progress and co-ordinated resources.

The Recovery Groups were short-term groups focused on the delivery of the Covid Recovery Actions Plans approved by Council. These groups fulfilled their purpose and came to an end in 2021, although the Economic Recovery Group was replaced by an Economic Development Panel formed to continue to oversee the longer term economic recovery actions necessary.

## **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:

- All key decisions of the Council should relate back to the Corporate Plan
- The revenue budget and capital programme must remain balanced and sustainable over a rolling 5 year period.
- The Council will not use its reserves to fund ongoing services.
- Savings in the revenue budget or external funding are identified before any new revenue expenditure, including capital expenditure that has revenue consequences, or any reduction in planned income 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 Growth & Place has delegated authority to let, manage, repair and maintain properties.

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

## Supporting carbon reduction

Following the Declaration of a Climate Emergency in 2019, the Council has committed to working towards a carbon emissions reduction across the district of 10% year-on-year until 2025, supporting the national drive to deliver net zero carbon by 2050.

More about the Council's response to climate change can be found on the Council's website at <https://www.chichester.gov.uk/climatechange>

## Our Assets

The Council's asset base at 31 March 2021 was

Total Assets £290m			
Property, Plant & Equipment £128m	Investment Property £14m	Other Long Term Assets £61m	Current Assets £87m

## Capital Programme

The Council's present capital intentions are summarised in Table 1

*Table 1: Capital programme and major schemes 2021/22 to 2025/26*

Capital Expenditure (£m)	2021/22	2022/23	Later	Total
Total approved spend **	34.9	9.3	15.2	59.4
Major schemes – approval by year				
Projects and Schemes				
Disabled Facilities Grants	3.0	1.4	4.0	8.4
St. James Industrial Estate - Refurbishment and Replacement of Units	7.2	-	-	7.2
Southern Gateway Project	4.1	-	-	4.1
Westgate Leisure Centre: Decarbonisation	1.4	-	-	1.4
Freeland Close Redevelopment	2.5	-	-	2.5
Community led housing	0.7	0.4	-	1.1
Infrastructure Business Plan				
• School places	1.2	-	2.4	3.6
• Southern Gateway: 3G sports pitch	-	0.9	-	0.9
• Southern Gateway: road, pedestrian and public realm improvements	4.0	-	-	4.0

Capital Expenditure (£m)	2021/22	2022/23	Later	Total
• Westhampnett Waste transfer station and Household Waste recycling	0.3	2.2	-	2.5
• Early Years Places, Whitehouse Farm Development	-	-	2.1	2.1
Asset replacement programme				
• Vehicle Replacement	2.3	0.9	1.3	4.5
• Other asset replacements	3.2	0.3	2.6	6.1

*\*\* 2021-25 programme - Autumn 2021*

## 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 resource projection at mid-November 2021 is shown below.

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

Resources 2021/22 to 2025/26	Total
Reserves at April 2021	66.9
New Resources expected in period	
- Capital receipts	-
- Interest on Leases	1.1
- Interest on Investments	1.5
- Revenue contributions	7.5
- External income, including CIL	30.8
- New Hones Bonus 2021/22	1.5
- Lower tier support grant	0.1
Total Resources	109.4
Less commitments	
- Earmarked revenue funding	-26.4
- Minimum Reserves Provision	-4.0
- LEP Grant	-5.0
- COVID 19 Recovery	-8.0
- Other	-0.3
	-
Capital Programme	
- Approved capital projects	-48.8
- Current Asset replacements	-10.6
Available Uncommitted Resources	6.3

Tables 1 and 2, 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.

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. To mitigate this risk, in the above analysis the Council has not anticipated any income from capital receipts.

The receipt of capital resources is closely monitored by the Council's Finance and Estates teams and is regularly reported to the Portfolio holder 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.

An assessment is made by the Council's Financial Services Division of the best financing method for all major capital investments at the earliest stage of the proposal's development. Whilst the present intention is to remain debt free through this period, the Council will assess on a case by case basis what financing options exist and which represents the best value for money.

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 and 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.

## **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 approximately 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 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 is 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 3: Forecast treasury management investments in £m (31 March)*

	2022	2023	2024	2025	2025
Near-term investments	41	29	30	28	30
Longer-term investments	37	37	37	37	37
<b>TOTAL</b>	<b>78</b>	<b>66</b>	<b>67</b>	<b>65</b>	<b>67</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.

Although our projections below incorporate some headroom for potential for borrowing should the need arise, funding options for major projects are assessed on a case by case basis by the Council's Financial Services Division. If any future projects are to be funded by borrowing, the project approval process will include the necessary actions to approve any necessary increase to these limits.

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

	2022/23	2023/24	2024/25	2025/26
Operational Boundary – borrowing	10	10	10	10
Operational Boundary– PFI and leases	2	3	3	3
Operational Boundary– total				



external debt	12	13	13	13
Authorised Limit – borrowing	20	20	20	20
Authorised Limit– PFI and leases	5	5	5	5
Authorised Limit– total external debt	25	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 2022/23 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, the majority 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 total value of loans made by the Council to external third parties is disclosed on the Council's annual statement of accounts, although some loans have been treated as capital expenditure in accordance with the Local Authorities (Capital Finance and Accounting) (England) Regulations.

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 £3m million per year for the General Fund revenue account.

The majority of this income comes from properties held primarily to support the provision of local services, not to make a profit or for any appreciation in value. Examples of these activities include rents from industrial units, commercial ground leases, shops, offices and other lettings to sports, community and voluntary organisations.

Only a small proportion of the Council's built assets are held because rental income and/ or capital appreciation were substantial factors in the decision to acquire or hold them. These are classified as 'investment properties' and disclosed in the Council's statement of accounts. These assets generate around £1m per annum in income which is used to support front line services.

General capital investment in commercial property is likely to take three 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 and promoting 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.

The Council has an approved investment opportunities protocol that 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 protocol also provides specific guidance on the enhanced scrutiny required, including:

- 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

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 anticipated capital appreciation.

There is a recognition that, in undertaking investments primarily for financial return, the Council needs to ensure that these decisions are subject to robust 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. This scenario could also lead to falling property values, with a potential 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.

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.

For 2022/23 the Council has followed the recommendations of the Department for Levelling Up, Housing and Communities and included an indicator for the ratio of commercial income to net service expenditure in its investment strategy.

Further details on this and general 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 has disclosed total long term liabilities of £10.3m in its last statement of accounts. The majority of this figure (£5.9m) relates to section 106 contributions which are fees paid by applicants seeking planning permission for the mitigation of the impact of new homes on the local community and infrastructure.

## **Knowledge and Skills**

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions and recommendations. The Divisional Manager for Property & Growth and the Valuation & Estates Manager are both chartered surveyors and registered valuers and who have significant post qualification experience

The Council currently employs Arlingclose Limited as Treasury Management advisors, 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 relevant financial regulations.