ARUN DISTRICT COUNCIL

CAPITAL STRATEGY - 2021/22 to 2023/24

1. INTRODUCTION

1.1 Overview

CIPFA’s Prudential Code requires Councils to have a capital strategy and a requirement for all local authorities from 1 April 2019. The Code states that “In order to demonstrate that the authority takes capital expenditure and investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability, authorities should have in place a capital strategy that sets out the long-term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes.

The aim of the capital strategy is to form a framework for capital investment decisions over the next three years which will inform the detailed annual capital budgets over this period.

1.2 Objectives

The purpose of the strategy as per the Code is that it is “intended to give a high level overview of how capital expenditure, capital financing and treasury management activity contributes to the provision of services, along with an overview of how associated risk is managed and what the implications might be for future financial sustainability.”

The Council must demonstrate that it takes capital expenditure and investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability giving due consideration to both risk and reward and the impact on outcomes.

The strategy aims to balance capital expenditure needs and expectations (e.g. replacement of business critical IT systems) with the scarcity of available resources to enable the identification and optimisation of all sources of capital funding and also be flexible enough in order to respond to emergencies and changes in priorities.

It is a collective document involving various departments within the organisation it is not purely a finance function, all the relevant officers should review this document from time to time and it be updated accordingly.

1.3 Scope

The capital strategy specifically focusses on the key areas of capital expenditure and treasury management.

Capital expenditure is strictly defined and is principally expenditure incurred in buying, constructing or improving assets such as land, buildings, vehicles, plant, machinery and intangibles (e.g. computer software). It also includes grant and advances to be used for capital purposes, such as Disabled Facility Grants.

The Council's policy on capitalisation in accordance with the Council's approved accounting policies and procedures, is that expenditure on land, buildings, vehicles, plant, machinery and intangibles over £25,000 will be capitalised, expenditure under these limits is deemed to be a revenue cost.

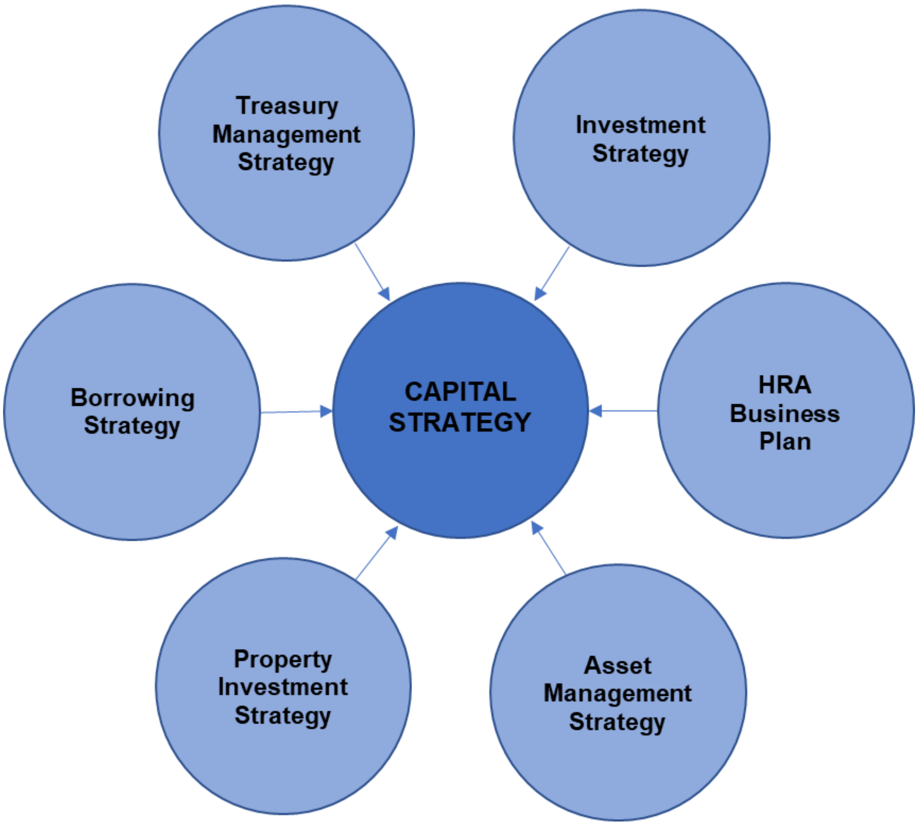
The Capital Expenditure & Financing forecast for the period 2021/22 to 2023/24 can be found in Appendix 1.

Treasury Management is the management of the Council's borrowing, investments and cashflows and is essential in particular when accessing the affordability of a capital project, the Treasury Management Strategy includes:

- The incremental impact of capital investment on council tax and housing rent levels
- The borrowing strategy
- The authorised limit for external debt

1.4 How do existing strategies feed into the Capital Strategy

The strategy maintains a strong and current link to the council's priorities and to other key strategy documents as shown below:



1.5 Member approval and review

As local authorities become increasingly complex and diverse it is important that those charged with governance understand the long- term context in which investment decisions are made and the financial risks to which the Council is exposed. The strategy should therefore contain sufficient detail to allow Council members to understand how stewardship, value for money, prudence, sustainability and affordability will be achieved.

The Treasury Management Code allows authorities to delegate the detailed management of Treasury Management, including the Capital Strategy, to a sub-committee and this responsibility is delegated to the Audit and Governance Committee. This delegation will facilitate more active discussion of the Capital Strategy and its implementation though overall responsibility will at all times remain with the Full Council.

1.6 Strategic Direction of the Council

A key driver of the Capital Strategy is the Council's 2020 Vision programme "working together for a better future". This programme provides strategic direction to help the Council become more effective and sustainable and to enable it to meet the demands of the future. The strands of the Vision programme are:

- Offering a better customer experience
- Strengthening external relationships
- Providing more digital online services
- Becoming smaller and more effective

1.7 Capital Priorities

In common with other local authorities Arun is facing a challenging financial climate and it is therefore essential that systems are in place to ensure that scarce resources are allocated in the most effective possible way and therefore expenditure needs to be prioritised:

Priority	***Type of Projects***
Highest Priority	Unavoidable capital expenditure due to an emergency such as one affecting service continuity or business critcial infrastructure
	Projects that deliver strategic outcomes as per the Council's vision
	Projects necessary to deliver statutory, mandatory and legal/contractual obligations
	Projects that give rise to revenue savings or income generation. These can be developed as invest to save projects
	Projects attracting additional external funding
	Projects which improve and repair Council assets and reduce the need for revenue maintenance
Lowest Priority	Projects that are not for statutory or mandatory purposes, attract low external support, have little or no payback or result in increases in revenue costs

It is the responsibly of senior officers and members to consider and prioritise the competing demands for capital resources.

1.8 Capital Financing

The prudential code requires 'the local authority shall ensure that all of its capital and investment plans and borrowing are prudent and sustainable."

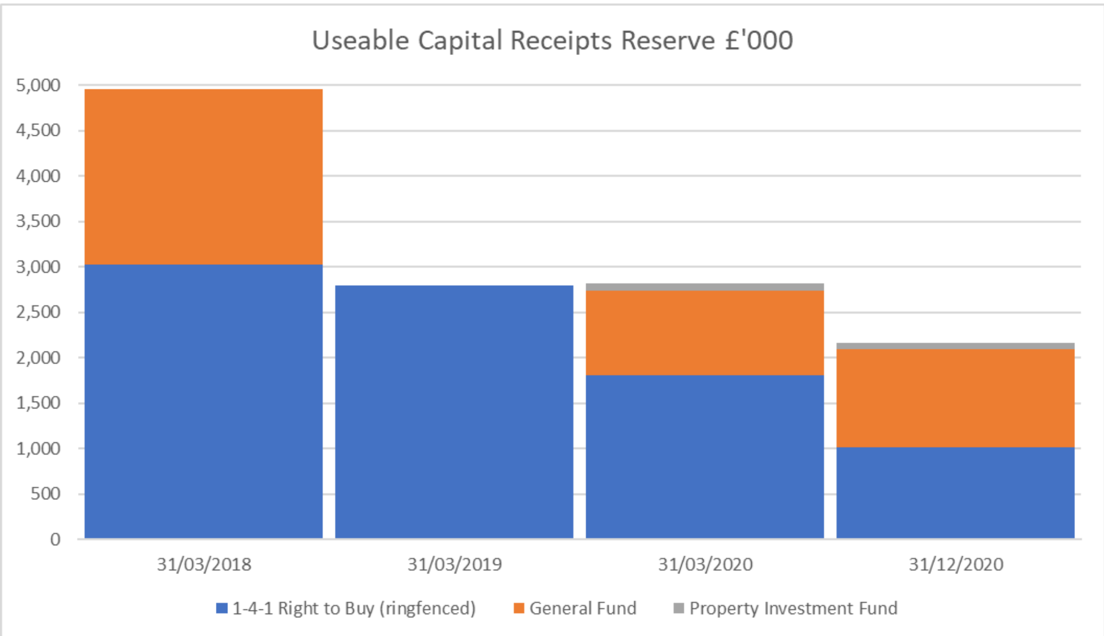
Capital expenditure can be funded in a variety of ways:

CAPITAL FINANCING				
Grants	Developer Contributions	Capital Receipts	Revenue Contributions	Borrowing

The funding of any capital project must be considered alongside any ongoing revenue budget requirements as part of the Council's financial planning.

It should be noted that the Council has extremely limited resources for the funding of capital expenditure. Other than right to buy receipts (as discussed in 2.1) there are very little opportunities for capital receipts, asset disposals are infrequent and although there are a few assets which have been identified as possible disposals this can take years.

The graph below shows how the levels of useable capital receipts have reduced over the last few years as a result of being applied to fund capital expenditure:



With the exception of the PWLB loan taken out on the inception of self-financing of the HRA at the end of the previous subsidy system, the Council currently has no external debt. The expenditure on HRA stock development not funded from 1-4-1 receipts will require external borrowing. It should be noted that due to the cost of borrowing the Council will only consider it as a last resort after all other sources of financing have been exhausted.

1.9 Invest to save

Invest to save is the investment now to transform and reshape services to reduce running costs/generate efficiency savings or earn income to payback the initial outlay. Priority should be given to these projects providing that they are supported by a sound business case and financial appraisal. A good example would be investment in new beach huts, as there is a demand for beach huts (supported by a waiting list), the initial outlay to build new huts would be recovered over a period of years through the rental these would generate.

1.10 Scheme evaluation and risk

Any new proposed capital scheme should be supported by a sound business case/options appraisal and should include a full evaluation of risk, having regard to the whole life costing methodology.

Whole life costing can be defined as "the systematic consideration of all relevant costs and revenues associated with the acquisition and ownership of an asset." In practical terms this means that any appraisal of a proposed capital project will need to consider not just the initial capital outlay but all costs and income streams associated with the project that are likely to occur in future years, including possible replacement or disposal costs. This is vital to ensure that the Council is not committing itself to future liabilities that are unsustainable.

Depending on the type of expenditure consideration should be given to the cost/benefit for instance of leasing a piece of equipment over an outright purchase (for instance the costs of repairs and maintenance that may be covered by leasing it).

1.11 Monitoring of approved capital schemes

It is the responsibility of the relevant budget holder and their team to manage costs and to provide explanations for any variations from the approved budget. Budget monitoring statements are presented to Corporate Management Team on a monthly basis and to Cabinet quarterly.

1.12 Post project evaluation

A post project evaluation is required to be undertaken to measure delivery against required project outcomes, not just time and cost. It is again the responsibility of the budget holder to undertake this review. This will help Council for the future as lessons learned can be transferred to new projects and help with such things as benchmarking.

1.13 Separate capital programmes for the HRA and the General Fund

The Housing Revenue Account (HRA) is a statutorily ring-fenced account covering income and expenditure relating to the Council's rented stock and the General Fund covers all other Council services. This ring-fence means that the HRA and the General Fund are completely separate entities, each having their own budget and financial model. For these reasons the HRA and General Fund capital programmes are considered separately, see below.

2. HOUSING REVENUE ACCOUNT (HRA) PROGRAMME

2.1 Stock Development

The HRA capital programme for 2021/22 to 2023/24 will be driven by the updated HRA Business Plan, will be approved in February 2021. One of the key priorities of this plan is the provision of 250 new dwellings over the 10 year life of the plan, the acquisition/building of these dwellings funded from a mix of “1 for 1” Right to Buy receipts and borrowing. Right to buy receipts are retained by agreement with the Government subject to them being used for the provision of new social housing within three years of receipt. These can be used to fund up to 30% of the cost of acquisition/new build schemes, whilst the Council has to fund the remaining 70%. A number of acquisition/new build schemes have already been delivered with new schemes currently progressing.

The initial £15m budget in 2018/19 was supplemented in 2020/21 with an additional £9m. This expenditure is funded from a combination of 1-4-1 right to buy receipts and borrowing. £100k pa is set aside to cover any revenue expenditure such as feasibilities which cannot be capitalised.

2.2 Housing Repairs & Improvements

The updated HRA Business Plan reflects a substantial increase in the levels of investment required in the existing housing stock including statutory compliance which is heavily regulated.

This expenditure is a combination of revenue and capital. The capital includes boiler, kitchen and bathroom replacement programmes as well as reroofing and rewiring.

2.3 Other Expenditure

There are plans to redevelop the sheltered housing stock and therefore additional capital expenditure will be required from 2022/23 onwards, this is subject to a full feasibility has been undertaken.

2.4 Affordability, borrowing and the abolition of the HRA debt cap

The HRA capital programme will need to be constantly reviewed to assess affordability. In particular, consideration will need to be given to the loan servicing costs of any new borrowing to ensure that these costs, together with the costs associated with existing (self-financing) debt can be sustained. This is particularly important in the light of the significant reduction in the number of right to buy disposals. The “1 for 1” Right to Buy receipts being used to part-fund current acquisition/new build schemes are not being replaced by new receipts and there will therefore be insufficient receipts to support future schemes. The Council will thus be required to fund up to 100%, rather than just 70%, of these future schemes resulting in additional loan servicing charges.

3. GENERAL FUND PROGRAMME

3.1 Core & enhanced programme

The Council has a core annual programme comprising:

- Asset Management – the repairs and maintenance of all non HRA land and property assets, generally revenue in nature and therefore mainly funded by revenue contributions.

- Disabled Facilities Grants (DFG's) – these grants pay for essential adaptations to help people with disabilities stay in their own homes. The DFG programme is entirely funded by a Better Care Fund Government Grant.

In addition, the Council also has an enhanced programme of expenditure which is based on the additional requirements for the year, expenditure will likely be more of a capital nature. The expenditure comprises of such things as:

- Asset management – a programme of larger one-off projects, more likely to be capital expenditure, for instance a schedule of public convenience refurbishments over the next 3 years.

- Play areas – a programme of play area replacements for the next five years, most expenditure is capital and is funded from a combination of external funding, capital receipts, developers' contributions and revenue.

- ICT – the replacement of business-critical systems over a period of 5 years which is normally the useful life of a piece of software.

- Other one offs – for instance replacement of life expired pieces of equipment, regeneration projects.

The key issue with the enhanced programme is the uncertainty with regard to future funding levels. The Council's Medium-Term Financial Strategy (MTFS) recognises that capital investment needs to be carefully prioritised due to limited amount of Council resources.

3.2 Asset Management Strategy

The asset management strategy establishes the priorities for this programme having regard to asset condition and their respective priorities in terms of delivering Council services or generating rental income.

The core asset management programme is supplemented with additional budget as a result of a review in 2019 of the condition of the Council's General Fund assets. This revealed that after years of under investment that significant funding would be required to ensure that they are maintained at an acceptable standard to allow the Council to continue to delivery its services.

3.3 Property Investment Strategy

This strategy sets out the policies relating to the Property Investment Fund which aims to generate a return for the Council through property acquisitions. These are funded by earmarking a proportion of the Council's capital receipts from land and property disposals. Acquisitions can only be made once a full business case has been completed and the risks fully understood and evaluated. Further details are set out in the Arun District Council Property Investment Strategy 2017–2022 as amended by Cabinet 13 January 2020.

3.4 Affordability and available resources

In addition to considering the merits of individual schemes the Council will need to assess the overall affordability of any new programme, having regard to the availability of resources, existing financial commitments and the projected level of balances forecast in the medium term financial strategy.

3.5 Specific resource issues

Grants and Section 106 contributions are generally used to fund specific capital schemes linked to the conditions imposed by the relevant grant or section 106 contribution. There is little, if any, latitude in the way grant funding can be applied.

Capital receipts are derived from the sale of the Council's assets, including council houses sold under the Right to Buy. It is the Council's policy to use these receipts (with the exception of "1 for 1" Right to Buy receipts which can only be used for the provision of new social housing) to support the General Fund capital programme. A specified proportion of these receipts will be earmarked for the Property Investment Fund (see 3.3 above).

Revenue contributions are a flexible source of funding, but they put an immediate strain on the General Fund balance and can therefore only be used to a limited extent.

Borrowing spreads the cost over a number of years but loan servicing costs and the overall level of debt exposure both need to be considered and clearly flagged in a business case.

Appendix A

Capital Expenditure & Financing 2021/22 to 2023/24

			2021/22 Forecast £'000	2022/23 Forecast £'000	2023/24 Forecast £'000
Expenditure	General Fund	Asset Management	1,582	1,233	1,499
		Disabled Facilities	1,400	1,400	1,400
		Play Areas	100	255	100
		ICT	120	315	200
		Chipper	26	0	0
			3,228	3,203	3,199
	HRA	Repairs	4,632	4,524	4,524
		Stock Development	100	100	100
		Sheltered Accommodation*	0	2,000	2,000
			4,732	6,624	6,624
	Total Expenditure		***7,960***	***9,827***	***9,823***
Financing	General Fund	Revenue	1,711	1,603	1,699
		Capital Receipts	117	200	100
		Improvement Grants	1,400	1,400	1,400
			3,228	3,203	3,199
	HRA	MRR	4,602	4,494	4,494
		Revenue	130	380	380
		Borrowing	0	1,750	1,750
			4,732	6,624	6,624
	Total Financing		***7,960***	***9,827***	***9,823***

* Subject to full feasibility/options appraisal