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CAPITAL STRATEGY
2018-22

Introduction

This strategy sets out the County Councils approach to compiling the capital programme, its priorities, availability of funding and financial management.

The County Councils capital programme is derived primarily from the Strategic Plan. It aligns with departmental commissioning and service plans to ensure a prioritised, joined up use of resources to maximise outcomes for all Leicestershire service users, citizens and other stakeholders.

The Chartered Institute of Public Finance (CIPFA) have recently updated the requirements for a capital strategy which should be adopted from 2019/20. This strategy (and the Corporate Asset Investment Fund Strategy and Treasury Management Strategy) includes the main requirements but will be developed further over the next year to ensure that it fully complies with the new requirements from 2019/20.

The overall approach to developing the capital programme is based upon the following key principles;

- To invest in priority areas including schools, roads, and other essential infrastructure, economic growth and projects that generate positive financial returns.
- Passport central government capital grants received for key priorities for highways and education to those departments.
- Maximise other sources of income such bids to the LLEP, section106 housing developer contributions and other external funding agencies.
- Maximise the achievement of capital receipts.
- No or limited prudential borrowing (only if the returns exceed the borrowing costs).

Funding Sources

Due to the challenging financial environment the capital programme, where possible, will be funded without increasing the impact upon the County Council’s on-going revenue budget. One off revenue contributions will be used to support the capital programme resources when prioritisation cannot contained the demand.

In recent years the on-going revenue position has been successfully managed by funding the capital programme from a combination of central government grant allocations, other external grants, capital receipts, external contributions and one off revenue contributions. No new prudential borrowing is planned.

The approach to funding is:

<u>External Funding</u>
- Central Government Grants – passport grants to the relevant departments, even when not ring fenced.

- External Grants - maximise bids for funding from external sources including providing matched funding where appropriate to do so, subject to approval of fulfilment conditions and any contingent liabilities.
- External Contributions – maximise section 106 claims/ contributions to cover the full capital costs.

Discretionary Programme

- Capital Receipts – maximise individual receipts and use to fund the discretionary capital programme.
- Earmarked Capital Receipts – only to be used in situations where this is an unavoidable requirement of an external party, for example, there is a requirement to gain DfE approval for the disposal of education assets, with the related receipts to be earmarked to education assets. These will be reviewed on a case by case basis to ensure the requirement is met and to consider options for substitution of discretionary funding where appropriate.
- Revenue underspends and surplus earmarked funds – review opportunities as they arise to contribute to the discretionary capital programme.
- Prudential borrowing – only to be used after all other available funding and only then where the incremental costs are fully funded from savings from the new investment. Internal borrowing (from County Council cash balances) would be prioritised over external borrowing.
- Leasing – Due to the County Council's ability to access relatively inexpensive funding rental/ lease proposals need to be appraised to ensure additional benefits justify the financing cost.

Other

- Renewal Earmarked Funds – held to make an annual contribution reflecting the life and replacement cost of the asset. Use when the service is externally funded (commercial, partnerships, specific grants) or small scale asset owned by an individual service. Larger more significant assets will be funded through the discretionary capital programme.
- Building Maintenance – funded through the Central Maintenance (revenue) Fund (CMF). Significant lifecycle replacements to be funded through the discretionary capital programme.
- Tax Incremental Financing (TIF) – investment repaid from additional income generated, for example additional Business Rates.

Capital Requirements

Children's and Family Services

Demand	£	Funding
Meet demand for new school places.	High	Central Government grants Developer contributions (section 106)
Maintenance and renewal for: Maintained school estate Children's Centres	 High Low	 Central Government grants Discretionary Programme
Children's social care (minimal demand as commissioned service)	Low	Spend to save

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Adults and Communities

Demand	£	Funding
Disabled Facilities Grant	Mid	Central Government grants
Maintenance and renewal for: Libraries & Heritage Community Libraries	 Low Low	 Discretionary programme Support external funding bids
Adult Social Care* (minimal demand from commissioned service)	Low	Spend to save

* Supported Living accommodation for working age adults, shown under future developments

Public Health

Demand	£	Funding
Public Health (minimal demand from commissioned service)	Low	Spend to save

Environment and Transport

Demand	£	Funding
Maintenance of the highway infrastructure (using asset management principles)	High	Central Government grants Discretionary programme
Improvement to the highway infrastructure Major schemes Minor Schemes Advanced Design	 Mid Mid Mid	External Funding Central Gov't grants (inc. LLEP, TIF) Central Government grants Discretionary programme
County Council vehicle replacement programme	Mid	Discretionary programme
Maintenance and renewal of waste management infrastructure	Mid	Discretionary programme

Chief Executives

Demand	£	Funding
Economic Development (e.g. Broadband)	Mid	Central Government and External grants Discretionary programme (inc. TIF)
Programme of small shire community grants	Low	Discretionary programme
Other Services	Low	Spend to save, Discretionary programme

Corporate Resources

Demand	£	Funding
ICT Infrastructure Renew and expand the current corporate estate Major ICT upgrades and replacements	Mid	 Discretionary programme Discretionary programme + Spend to save
Property Estate* Regulatory compliance Expansion and replacement	Mid	 Discretionary programme Spend to save
Commercial Services Replacement Expansion/Improvement	 Low	 Renewal reserve Spend to save
Transformation/change	Low	Spend to save

* maintenance of current properties funded from central maintenance fund (revenue budget)

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Corporate Programme

Demand	£	Funding
Corporate Asset Investment Fund	High	Spend to save
Deliver energy and water strategy	Mid	Spend to save

Future Developments Programme

Demand	£	Funding
Including: Collections and Records Hub, Health and Social Care Service User Accommodation, Melton Mowbray Distributer Road, Oracle Replacement, Workspace Strategy, Fire Safety.	High	One off revenue and earmarked fund contributions Reinvest returns Spend to save

External Funding

To ensure that funding is at the required level the following approach will be taken.

Children and Family Services
Maximise DfE capital grant through up to date capacity assessments and school place data. Submit bids, where appropriate to do so, for additional DfE capital funding when available. Take opportunities to lobby the DfE for additional funding.

Adults and Communities
Work with District Councils and other partners to ensure that the Disabled Facilities Grant is at an appropriate level and how it is spent to reduce the costs of adult social care. Take opportunities to lobby the Department of Health for Social Care infrastructure grants.

Environment and Transport
Attain Highways Infrastructure Asset Management Planning Level 3 by April 2018 and maintain. Invest in advance design and business case development work focused on government priorities to access capital grants (which are increasingly being channelled through bidding processes) and developer funding.

Section 106 Contributions
Maximise section 106 contributions through recovery of the total costs of required developments and regular review of key assumptions used (at least annually). Where funding of capital expenditure is required in advance of the receipt of section 106 income (usually paid on completion of trigger points) projects may require initial cash flow by the County Council or from rescheduling grant expenditure. This will be kept to a minimum, but where it is required, for instance highway infrastructure for new housing developments, to minimise risks developers will be engaged early in the process and by ensuring that section 106 agreements are robust.

Tax Incremental Financing
The County Council will work with District Councils on construction schemes that unlock infrastructure and housing growth and seek agreements to repay fund the work from linked Council Tax, Business Rates growth and additional New Homes Bonus Scheme grant.

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Summary
The 4 year capital programme 2018-22 totals £289m. External funding from capital grants, section 106 agreements and third party contributions totals £175m. Without this funding being available schemes of any significant size would not be affordable by the County Council.

Discretionary Funding

The discretionary capital programme totals £114m for the period 2018-22. Funding is from the sale of County Council capital assets (capital receipts), MTFS revenue contributions or surplus earmarked funds. Discretionary funding can also include prudential funding, which is unsupported by central government with the costs of financing borrowing undertaken falling on the County Councils revenue budget.

Capital receipts
Property Services are responsible for identifying additional capital receipts and maximising the sale value of surplus assets. Property Services will seek opportunities to maximise the value of surplus land, for instance by obtaining planning permission. The targets for new capital receipts to fund the 2018-22 capital programme, are:

2018/19	£13.1m
2019/20	£5.0m
2020/21	£1.5m
2021/22	£1.5m
Total	£21.1m

The estimates are higher in the earlier years reflecting the increased confidence in the sale of those assets. The targets will need adjusting to reflect shortfalls in previous years (if applicable) and any new spend to save or linked projects where funding for expenditure is advanced on the condition that future receipts are generated to fund the expenditure.

Revenue Funding
The capital programme 2018-22 includes a total of £85m in MTFS revenue funding of capital and surplus earmarked capital receipts.

On-going revenue - £2m is allocated in the MTFS.

One-off revenue - £83m is allocated in the MTFS. These have arisen from past:
- Opportunities from underspends – cannot be relied upon going forward.
- MTFS risk contingency
- Surplus earmarked funds no longer required

Other Earmarked Funds
These include earmarked capital receipts, surplus capital receipts from prior years and funds repaid under the Local Authority Mortgage Scheme (LAMS) and total £8m over the 2018-22 capital programme.

By using the funding available, the discretionary capital programme can be funded without any new borrowing.

If new unavoidable items or spend to save are identified during the MTFS, options to increase capital receipts and identify further revenue funding will be reviewed first. If these are not available then prudential borrowing will be considered, subject to the prudential indicators. In considering prudential borrowing using internal cash balances will be prioritised over raising new external loans. This has the advantage of avoiding debt interest payments which are expected to exceed current interest rates.

For invest to save schemes, a discount rate of 5% will be used (3.5% for energy projects) as part of the net present value assessment in the business case. Only projects that show a positive return using these rates will be considered for inclusion in the capital programme.

Affordability

The impact of the discretionary programme on the revenue budget, and forecast at the end of the MTFS is:

£m	2013/14	2014/15	2015/16	2016/17	2017/18	2021/22
Revenue	1.7	1.7	1.7	1.7	1.7	1.7
MRP	13.6	12.7	12.0	11.4	10.8	6.5
Interest	12.0	11.9	12.0	12.1	12.0	12.8
On-going revenue Total	**27.3**	**26.3**	**25.7**	**25.2**	**24.5**	**21.0**
% Revenue budget	7.7%	7.5%	7.4%	7.3%	7.0%	5.8%
Voluntary MRP	8.4	6.4	2.9	4.5	0.0	0.0
One-off revenue	17.0	8.4	6.1	8.8	16.1	0.0
One-off revenue	**25.4**	**14.8**	**9.0**	**13.3**	**16.1**	**0.0**
Total	**52.7**	**41.1**	**34.7**	**38.5**	**40.6**	**21.0**
% Revenue budget	14.8%	11.7%	9.9%	11.1%	11.7%	5.8%

To ensure the discretionary programme remains affordable the following approach is taken to manage the MRP and interest charges:

- No new borrowing to finance capital expenditure (last time was in 2012).
- Where new borrowing is needed to use temporary internal balances from the overall council cash balances in advance of their designated use.
- Review opportunities to repay debt.
- Re-profile MRP to be commensurate with the average age of assets funded from borrowing and delay the impact on the revenue budget. This is planned from 2020/21. It should be noted that this does not reduce the amount to be set aside but simply delays the period over which it is to be paid.

By 2021/22 by taking the above actions it is forecast to reduce the on-going revenue charge to £21.0m (5.8% of the revenue budget). By the end of the MTFS the annual cost will have been reduced by £6.3m, reducing the need for service reductions.

Capital Financing Requirement (Borrowing)

The Councils borrowing requirement is contained with the Capital Financing Requirement (CFR). The CFR is the measure of the Council's historic need to borrow for capital purposes. As at 31st March 2018 the CFR is forecast to be £257m compared with actual debt of £265m. The difference is a temporary 'over-borrowed' position pending future scheduled debt repayments and opportunities to repay debt early. The current cost of borrowing is £22.8m per annum in financing costs (external interest and MRP) which is met from the revenue budget. Where prudential borrowing is approved this would have the effect of increasing the CFR. As the CFR exceeds actual debt borrowed, if the Council was to undertake new prudential borrowing it would review options to use internal working cash balances instead of taking out new external borrowing. Over the period of the MTFS the over-borrowed position is forecast to increase to £39m. The Prudential Indicators show the CFR remaining at £257m over the next four years to allow provision to potentially use part of the over borrowed position to provide flexibility to raise prudential borrowing (funded from internal borrowing) to fund future capital developments and the Corporate Asset Investment Fund if needed.

The detailed approach to this is covered in the Treasury Management Strategy, approved by the County Council annually in February.

Financial Management of the Capital Programme

Prioritising the Programme

The approach to compiling the capital programme is through a combination of service requirements developed by each relevant department, statutory requirements and asset management planning.

For land and building assets, Strategic Property, in conjunction with service areas, develops all the estate strategies, asset management plans and property elements of the corporate capital and revenue programmes. They seek to ensure that the County Council is making full use of all assets, and any under-performing or surplus assets are identified and dealt with by either their disposal or investment to improve their usage. Outcomes from condition survey information together with on-going reviews of the property portfolio feed into the capital programme and revenue budget. The Corporate Asset Management Plan, which promotes the rationalisation of property assets, reducing running costs and cost effective procurement of property and property services is reported annually to the Cabinet.

The County Council operates the Corporate Asset Investment Fund (CAIF) which invests in assets to achieve both economic development and investment returns. The CAIF operates through the Corporate Asset Investment Fund Strategy with a view to:

- Ensuring that there is a diverse range of properties available to meet the aims of economic development.
- Increasing the size of the portfolio.
- Improving the quality of land and property available.
- Ensuring the sustainability of the County Farms and Industrial portfolio by replacing land sold to generate capital receipts, and
- Providing a revenue income stream that can be used to support ongoing service delivery.

The fund has a notional target of achieving a holding of £200m. It is expected that this will be achieved within the next 5 years. Appraisal includes external due diligence performed before each purchase.

For highways and associated infrastructure needs, the Council's key transport policy document is the Local Transport Plan. This provides the long term strategy within which the Council manages and maintains its network. In light of the continuing financial challenge the Council's priority is only to add to the highway network where this will help to enable new housing and jobs. Furthermore, additions will normally be considered only in circumstances where specific external funding can be secured to achieve this.

Further improvements to the highway network will require continued pursuit of external resources such as Government grants and developer funding. Government grants include bids to funds including Growth Fund (through the LLEP), the Growth and Housing Fund, the National Productivity Investment Fund, Local Authorities Majors Fund and the Housing Investment Fund. In order to maximise the impact of funding that can be secured for improvements, the County Council is doing more to define the roles of the various elements of the road network so that it is able to target investment where it will be of most benefit, particularly in terms of supporting economic prosperity and growth.

Bids for funding from the discretionary programme require the completion of a capital appraisal form for each project. The forms collate detailed information on the proposed project including justification against strategic outcomes, service objectives, statutory requirements and/or asset management planning, timelines, detailed costings including revenue consequences of the capital investment, and risks to delivery. All bids for land and building projects are also supplemented by a Strategic Property scoping and assessment form. Bids are then prioritised and assessed against the discretionary funding available. The revenue costs and savings associated with approved capital projects are included in the revenue budget.

Where schemes have not yet been fully developed these are included as future developments in the capital programme. As schemes are developed they are assessed against the available resources and included in the capital programme as appropriate.

<u>Financial Management of Delivery</u>

The key risks to the delivery of the capital programme are overspending against the approved budget for a scheme, project/programme slippage where the project is not delivered in accordance within the planned timescales thereby delaying approval of the expected benefits, and delays in or non-receipt of external contributions towards the cost of the scheme.

To ensure that capital spending and the delivery of this strategy is effectively managed:

- Programmes being reviewed in light of the most up to date information around funding available and latest priorities.
- All schemes within the programme being monitored regularly, usually monthly.
- Financial progress being reported on a regular basis throughout the year and at year end to the Cabinet and Scrutiny Commission to update them on progress and any significant variations in costs.
- Projects part or wholly funded by external contributions being separately monitored to ensure compliance with any funding conditions applicable.
- All projects are assigned a project manager appropriate to the scale of the scheme.
- The procurement of projects within the capital programme following the Councils approved contract procedure rules and where applicable the Public Contract's Regulations 2015.