APPENDIX 2

Capital Strategy 2019/20

Introduction

This capital strategy provides a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of policing services along with an overview of how associated risk is managed and the implications for future financial sustainability.

Capital Expenditure and Financing

Capital expenditure is where the Police and Crime Commissioner (PCC) spends money on assets, such as property or vehicles, that will be used for more than one year. The PCC has some discretion on what counts as capital expenditure, for example assets costing less than £10k are not capitalised and are charged to revenue in year.

In 2019/20, the Force is proposing capital expenditure of £9.9m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2017/18 actual	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget
Estates	2.4	4.0	3.1	1.2	0.2
IT	3.0	3.7	3.9	1.6	
Fleet	1.0	1.4	1.0	1.0	1.0
ESN	-	-	-	3.5	
Corporate Projects	-	-	1.9	0.3	
TOTAL	**6.4**	**9.1**	**9.9**	**7.6**	**1.2**

The capital projects included in the expenditure above are summarised later in this report.

Governance: The Estates, IT and Transport Departmental Heads in conjunction with the business, bid annually during November for projects to be included in the Force's capital programme. Bids are collated by Corporate Finance who calculate the financing cost (which can be nil if the project is fully funded from other resources). The proposed capital programme has been reviewed by the Strategic Finance and Infrastructure Board and supported by the Executive Group at their meeting on the 20th December 2018. The capital programme is then presented to the Strategic Assurance Board in January.

All capital expenditure must be financed, either from external sources (government grants and other contributions), the PCC's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiative). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

	2017/18 actual	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget
External sources	1.9	0.9	1.2	1.1	0.7
Own resources	0.8	3.7	0.2	0.1	0.1
Debt	3.7	4.5	8.5	6.4	0.4
TOTAL	**6.4**	**9.1**	**9.9**	**7.6**	**1.2**

Where the commissioner finances capital expenditure through borrowing (debt) resources must be set aside to repay that debt from the revenue account. The amount charged to revenue account for the repayment of borrowing is known as the Minimum Revenue Provision (MRP). Planned MRP is as follows:

Table 3: Replacement of debt finance in £ millions

	2017/18 actual	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget
Own resources	1.5	1.9	1.7	2.5	3.5

The Statutory Guidance issued by the DCLG sets out the 4 options for calculating the MRP. The recommended MRP policy is:

- For capital expenditure incurred before the 1st April 2008 (which was supported capital expenditure) the policy will be based on 4% of the Capital Financing requirement

- From the 1st April 2008 for all unsupported borrowing the MRP policy will be the Asset Life Method (Equal instalment approach) – the MRP will be based on the estimated life of the assets.

The commissioner's policy is to finance shorter life assets from capital receipts, grants and revenue contributions with borrowing reserved generally for Land and Buildings with an expected life of 25 years and IT projects that cannot be financed from the PCC's own resources.

The PCC's cumulative outstanding 'debt finance' is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP repayments and capital receipts used to replace debt. The CFR is expected to increase by £6.8m during 2019/20. Based on the figures above for expenditure and financing, the PCC's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

	31.3.2018 actual	31.3.2019 forecast	31.3.2020 budget	31.3.2021 budget	31.3.2022 budget
TOTAL CFR	**23.2**	**25.8**	**32.6**	**36.5**	**33.4**

Asset disposals: When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. No capital receipts are expected to be received during 2019/20.

Treasury Management

Treasury management is concerned with keeping sufficient but not excessive cash available to meet the PCC's / Force'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. The PCC is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor 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.

Due to decisions taken in the past, the PCC currently has £12.9m borrowing at an average interest rate of 5.29% and £16.8m treasury investments at an average rate of 0.49%.

Borrowing strategy: The PCC'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 are often conflicting, and the PCC therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.75%) and long-term fixed rate loans where the future cost is known but higher (currently 1.75% to 3.0%).

Projected levels of the PCC's total outstanding debt (which comprises borrowing, PFI liabilities and leases) are shown below, compared with the capital financing requirement (see above).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	31.3.2018 actual	31.3.2019 forecast	31.3.2020 budget	31.3.2021 budget	31.3.2022 budget
Debt (incl. PFI & leases)	12.9	16.9	25.4	30.0	30.4
Capital Financing Requirement	23.2	25.8	32.6	36.5	33.4

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the PCC expects to comply with this in the medium term.

Affordable borrowing limit: The PCC is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2018/19 limit	2019/20 limit	2020/21 limit	2021/22 limit
Authorised limit – borrowing	25.8	26.4	32.8	33.1
Authorised limit – Long Term Liabilities	1.0	0.5	0.5	0.5
Authorised limit – total external debt	**26.8**	**26.9**	**33.3**	**33.6**
Operational boundary – borrowing	24.8	25.4	31.8	32.1
Operational boundary – Long Term Liabilities	0.5	-	-	-
Operational boundary – total external debt	**25.3**	**25.4**	**31.8**	**32.1**

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 PCC's policy on treasury investments is to prioritise security and liquidity over yield. That is to focus on minimising risk rather than maximising returns. Surplus cash is invested securely, for example with the government, other local authorities, selected high-quality banks and pooled funds, to minimise the risk of loss.

Governance: Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Force's ACO (Resources) and staff, who must act in line with the treasury management strategy approved by the PCC. Quarterly reports on treasury management activity are presented to the Strategic Assurance Board.

Revenue Budget Implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax and core government grants.

Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream

	2017/18 actual	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget
Financing costs (£m)	2.2	2.5	2.4	3.4	4.4
Proportion of net revenue stream	1.27%	1.39%	1.25%	1.72%	2.19%

Sustainability: Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 25 years into the future. The estimate of the incremental impact of the capital investments proposed in this report for Band D Council Tax per week are:

2019/20	2020/21	2021/22
0p	6p	6p

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax levels. The incremental impact is the difference between the total revenue budget requirement of the current approved capital programme and the revenue budget requirement arising from the capital programme proposed.

Proposed Capital Programme

A summary of the proposed Capital Programme for 2019/20 is shown in the table below.

Proposed Capital Programme 2019/20

Expenditure	**£000**	**Funding**	**£000**
Property	3,119	Capital Grant (provisional)	700
Information Technology	3,851	Borrowing Requirement	8,515
Vehicle Fleet	950	Revenue Contributions	235
Corporate Projects	1,891	3rd Party Contributions	441
Emergency Services Network	55		
Operational equipment	25		
Total	**9,891**	Total	**9,891**

The 'Estates' programme is based on the approved Estates Strategy and includes the property store build, refurbishment of Keyham Lane, remodelling of FHQ accommodation to accommodate the new Forensic Investigator lab requirements, the purchase of land at Coalville to create the car park following the co-location with the Fire service and provision to increase the parking capacity at FHQ.

The IT programme includes:

- Investment in the data network and storage to ensure network performance and support new services such as enhanced CCTV for custody and site security.
- The Force has committed to the National Enabling Programme (NEP) Office 365 cloud service and 2019/20 is the second year of implementation.
- Significant investment (£1m) in the smartphone fleet to facilitate the on-going use of agile services.
- Provision for the on-going development of Pronto.
- Openscape 4000 project (CMD Telephony) to develop new methods of contact eg web chat, social media and video contact.
- Equipping Force Meeting rooms with audio visual and video conferencing facilities.

Provision is also made for the rolling programme of ANPR camera replacements (including vehicle fits), the Force wide security works, Custody CCTV replacement (both which were approved at the November 2018 Change Board), stage 2 of the CMD refurbishment (ergonomics) and the preparatory work in relation to the roll out of the Emergency Service Network.

Planned replacements for the existing vehicle fleet are also included.

Financing

The provisional 2019/20 capital grant is £0.7m, similar to the previous year. After the application of revenue contributions to capital schemes and the use of Section 106 funding, the 2019/20 borrowing requirement is **£8.515m**.

The Capital Programme assumes that the 19/20 borrowing requirement of £8.515m is financed through loans from the PWLB. Revenue resources are set a side over the life of the asset to repay the borrowing.

Knowledge and Skills

The PCC / Force employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions.

Where PCC / Force staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The PCC currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly, and ensures that the PCC / Force has access to knowledge and skills commensurate with its risk appetite.