

CAPITAL STRATEGY 2019/20

1. Introduction

- 1.1 This capital strategy report forms a key part of the Council's overall Corporate Planning Framework. It provides a mechanism by which capital expenditure is aligned over a medium term (5 year) planning period.
- 1.2 This strategy sets the framework for all aspects of the Council's capital expenditure including prioritisation, planning outcomes, management, funding and monitoring, and is linked to the Council's Asset Management Plan, Investment Strategy and the Medium Term Financial Strategy.

2. Capital Expenditure

- 2.1 Capital expenditure is where the Council spends money on assets (such as property or vehicles) that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example at Derbyshire Dales District Council assets costing less than £10,000 are not capitalised and are charged to revenue in the year of purchase.
- 2.2 In 2019/20, the Council is planning capital expenditure of £3.9m. Expenditure is prioritised as identified in the corporate plan 2015-2019.
- 2.3 The Asset Management Plan identifies backlog maintenance issues across the District's property portfolio; improvement and transformation can progress within the resources that are available.

3. Sources of Capital Finance

- 3.1 Decisions on capital spending are made against the background of diminishing resources. The main sources of capital finance available to the Council are:

a) Capital Grants and Contributions

Grants are generally awarded to finance specific projects. Grants may be received from central government, the European Union (until 2019) or other organisations. Some grants come with the expectation of "match funding" from the Council.

The Council will continue to bid for capital grants when the opportunity arises

Developer contributions, usually derived from Section 106 agreements, are awarded to mitigate the impact of developments on communities. These contributions are usually earmarked for specific purposes in planning agreements and often relate to infrastructure projects or affordable housing schemes.

The Council will continue to seek section 106 contributions when appropriate.

Another type of developer contribution is the Community Infrastructure Levy. The Community Infrastructure Levy is a planning charge, introduced by the Planning Act 2008 as a tool for local authorities in England and Wales to help deliver infrastructure to support the development of their area. Development may be liable for a charge under the Community Infrastructure Levy (CIL), if the local planning authority has chosen to set a charge in its area. Derbyshire Dales District Council has suspended preparatory work on the Derbyshire Dales Community Infrastructure Levy. The financial viability of development across the plan area will be continually monitored and in the event that evidence suggests that the introduction of the Community Infrastructure Levy will not have an adverse effect upon economic viability, work will be re-commenced on the introduction of a Derbyshire Dales Community Infrastructure Levy.

Officers will monitor the financial viability of development across the District to determine whether to introduce a Community Infrastructure Levy. In the meantime, a Developer Contributions Supplementary Planning Document will be prepared.

The Council is committed to working with partners (e.g. housing associations) to provide assets. Various mechanisms provide opportunities to enhance the Council's investment potential with support and contributions from other organisations and partners. These may be through match funding, joint funding etc.

A report to Council in December 2018 pointed out that the funding environment is changing dramatically and new approaches need to be explored. Members agreed that proposals for the creation of a limited Liability Partnership to enable better management of its property portfolio with a view to generating additional income to support the council in becoming financially self-reliant.

The Council will continue to seek private sector investment. Should opportunities arise, officers will explore new approaches for capital contributions, such as joint ventures, and will prepare reports for Members' consideration.

b) Capital Receipts

Capital receipts are derived from the sales of assets. At Derbyshire Dales District Council this includes a share of receipts from the sale of former council houses, negotiated as part of the stock transfer in 2002, known as the Right to Buy Sharing Agreement. As the Council reviewed its assets some years ago, and disposed of surplus assets at that time,

the scope for future capital receipts, other than those under the Right to Buy Sharing Agreement, is limited.

Sometimes a third party will approach the Council with a request to purchase a particular asset, usually land. Each of these opportunities will be explored to identify whether it is in the Council's best interests to agree to a disposal, which would generate a capital receipt.

Subject to Members' approval, the Council will dispose of surplus capital assets to generate capital receipts where there is a sound business case taking into account issues such as financial implications (revenue and capital) and service delivery.

c) Prudential Borrowing

The Council's capital investment falls within, and needs to comply with, the "Prudential Code for Capital Finance in Local Authorities" (The Code). Under the Code local authorities are allowed to set their own limits on the amount that may be borrowed to finance capital expenditure, provided that it is, and can be shown to be, prudent, affordable and sustainable. This method of financing capital expenditure is called "prudential borrowing".

In order for borrowing to be prudent, affordable and sustainable, there must be an identifiable, long-term source of revenue funding for the associated revenue (debt financing) costs. In some cases this will come from revenue savings or additional income arising directly from the capital scheme. For example, building a new car park could generate income through charges. In other cases, there will be no direct additional income or cost saving (but the scheme meets a corporate priority) so the Council will need to ensure that the cost of borrowing will be affordable to the Council's revenue account in the long term.

There could be circumstances where the Council will consider borrowing to then provide loans to other organisations, such as for economic development. This is treated as capital expenditure and funded through borrowing. Officers will explore such schemes and seek Council approval.

The Council is required to make provision for the principal repayment of borrowing; this is known as a Minimum Revenue Provision (MRP). The Council has to prepare an annual statement of its policy on making MRP, and this is reported to Council for approval (elsewhere on this agenda).

In future years, new borrowing could be a realistic way of funding capital expenditure. However, in order to meet the Prudential Code, the Council would have to identify sustainable income streams or re-examine its revenue spending priorities in order to generate sufficient revenue capacity to make new borrowing affordable.

Prudential borrowing will be considered as a method of capital financing provided that it is, and can be shown to be, prudent, affordable and sustainable.

d) Revenue Contributions to Strategic Reserves

The Council has, in previous years and in the 2019/20 budget, made contributions to strategic reserves to provide capital funding. Such reserves include the Capital Programme Reserve, the Vehicle Renewals Reserve and the ICT Reserve. Until recently, such transfers to reserves have generally taken place when a revenue account underspend has been identified, rather than as part of a planned financial strategy. The 2019/20 budget includes £150,000 transfer to the Vehicle Renewals Reserve to fund future vehicle replacements. The Medium Term Financial Plan assumes that this will continue.

In order to provide a source of capital finance, especially for the life cycle (replacement) costs of certain key assets that have a limited life expectancy (such as vehicles and play equipment), the Council's Medium Term Financial Strategy includes the following statements:

- I. the MTFP and future revenue budgets should include annual revenue contributions to capital reserves provided that they are affordable;
- II. Any under-spending on the revenue account will be transferred to strategic reserves used to finance the Capital Programme or "Invest To Save" Initiatives.

Strategic capital reserves will be used as a method of financing, subject to availability, and (for some reserves) the relevant purpose.

e) Leasing

Leases are currently classified in accounting terms as either finance or operating leases. This distinction is important because it dictates whether the lease must be classified as capital (finance leases) or revenue (operating leases), and different accounting treatment is required for each. However, changes in the classification of leases are due to be introduced in 2019/20. The impact if these changes will be assessed in due course.

At the present time, finance leases are not recommended as a source of capital funding unless there are exceptional circumstances. This is because other sources of finance usually offer greater benefits, especially in terms of cost.

Finance leases will not be considered as a method of capital financing unless there are exceptional circumstances and they can be shown to be cost effective (compared to other methods of finance that might be available), prudent, affordable and sustainable.

3.2 Capital Funding Strategy

The capital funding strategy is intended to set out the order that financing will be utilised. Financing will be allocated in the following order:

1. Capital grants and contributions that are linked directly to a specific capital project e.g. a HCA grant or Disabled Facilities Grants. These will be fully allocated to the relevant

project. Projects funded by external grants and contributions will not commence until such funding is definitely secured.

2. Capital receipts that are linked directly to a specific capital project e.g. the proceeds from the sale of an asset that will be used as financing for its replacement. Projects funded by capital receipts will not commence until such funding is definitely secured.
3. Capital grants and contributions that are not linked to a particular project but are for a particular purpose e.g. Section 106 agreements for affordable housing - these will be used as funding for projects that meet the specified purpose ahead of other funding sources. Schemes funded by external grants and contributions will not commence until such funding is definitely secured.
4. Transfers from strategic reserves – these will be used to fund capital expenditure subject to availability, and (for some reserves) the relevant purpose.
5. Capital receipts not directly linked to a particular project, where expenditure is within rules set down by the Government. Schemes funded by capital receipts will not commence until such funding is definitely secured.
6. Self-funded borrowing - where the capital investment itself will produce revenue savings or additional income, which is sufficient to cover the cost of borrowing to fund the investment.
7. Prudential Borrowing will be used to fund capital investment if the cost of the borrowing is affordable within the overall General Fund revenue projections. This will be funding source of last resort.

4. Governance of the Programme

- 4.1 The Council's Capital Programme is prepared annually in March by the Head of Resources in consultation with the Corporate Leadership Team, and reported to full Council for approval. The programme sets out the capital projects that will take place in the forthcoming financial year and the projects that are forecast for the following four financial years. The capital programme is updated in May (to reflect the outturn of the previous financial year and any slippage, as well as adding any new bids) and in October/November (reflecting progress on projects and adding any new bids).
- 4.2 Where expenditure is required or anticipated which has not been included in the Capital Programme, then a revision to the Capital Programme is required before that spending can proceed. Revisions to the Capital Programme must be approved firstly by the Corporate Leadership Team, then by Council. For projects over £25,000, or those of a political nature, a report is required to the relevant policy committee before the project is reported to Council. Revisions to the Capital Programme will generally be taken to Council only in June and October/November each year, unless there are exceptional circumstances.
- 4.3 All projects within the programme will be financed in accordance with the funding strategy set out above. Within the available resources, bids for new capital projects are evaluated and prioritised by the Corporate Leadership Team prior to seeking Committee / Council approval.
- 4.4 Bids for inclusion are supported by business cases, which must demonstrate that the project provides an effective and value for money solution, and that all possible sources of external funding have been sought. The business cases also identify any implications for the revenue account, such as increased or reduced expenditure or increased income.

- 4.5 Once approved by Council, a project manager is identified to be responsible for the effective control and monitoring of each project, including financial monitoring. Any projects that might exceed the agreed budget must be reported to the Head of Resources. If appropriate corrective action cannot be taken to bring the project back within budget, the additional costs will be reflected in the next update of the capital programme. Changes which result in an increase in the amount of an accepted tender or estimate by 10% or £50,000, whichever is the lower, will be reported to the relevant Policy Committee as soon as possible with an estimate of the probable new cost, and subsequently to full Council for approval of any additional expenditure.
- 4.6 To assist with medium term financial planning, a list of potential future liabilities is reported regularly to Council. This shows possible future capital projects that have not yet been included in the capital programme.

5. Risk Management

- 5.1 Significant risks associated with individual capital projects are identified in the business case and in the policy committee report associated with the bid, as well as in departmental risk registers.

The most significant risks to the achievement of the overall capital programme are:

- Forecast capital receipts may not be achieved;
- The danger of overspending on capital schemes with no available finance to meet the overspending;
- Budgets for individual projects may be insufficient when tenders are received;
- Availability of funding for future capital projects (though the current programme is fully financed) means that the Council's future ability to finance mandatory Capital expenditure, such as Disabled Facility Grants, will need to be kept under review and the amount available might be insufficient to deal with unforeseen capital expenditure, for example, if there was a requirement similar to the costs of addressing structural damage at the Memorial Gardens Toilets.

6. Capital Prudential Indicators

The Local Government Act 2003 requires the Authority to have regard to the Chartered Institute of Public Finance and Accountancy's *Prudential Code for Capital Finance in Local Authorities* (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Authority has fulfilled these objectives, the Prudential Code sets out the indicators that must be set and monitored each year. These prudential indicators are set out in The Capital and Treasury Monitoring report (elsewhere on the agenda).