Appendix A

Capital Strategy Report 2019/20

1. Introduction

1.1. This capital strategy is a new report for 2019/20, giving a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services, along with an overview of how associated risk is managed and the implications for future financial sustainability.

2. Capital Expenditure and Financing

2.1. Capital expenditure is where the Council spends money on assets, e.g. property/ 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, e.g. assets costing below £10,000 are not capitalised and are charged to revenue in the year.

2.2. The Council has incurred £24m capital expenditure in 2018/19 to date and may incur further capital expenditure by the end of the year. The Council has approved a Capital Programme for 2019/20 of £2.076 million all of which relates to general fund services. Officers are also currently working on Community Housing Schemes within the Borough and a report will be presented to the Hub Committee in the Summer regarding this. This is estimated to cost £4.7 million to deliver 30 residential units and would be funded in the short term by borrowing. A recommendation will be made to Council to approve the capital expenditure of £4.7m and it is included within the estimates below for modelling purposes and for completeness.

2.3 In September 2018 (Minute CM34) the Council approved an updated Commercial Property Strategy, which included multiple objectives: (a) to support regeneration and the economic activity of the Borough, the LEP area and the South West Peninsula (in that priority order) (b) to enhance economic benefit (c) to grow business rate income (d) to assist with the financial sustainability of the Council as an ancillary benefit and (e) to help continue deliver and/or improve frontline services in keeping with its adopted strategy and objectives.

2.4 Details of the Council's commercial property strategy can be found in the report taken to the Hub Committee on 11th September 2018 (and subsequently approved by Full Council on 25th September 2018 - minute Reference CM34 and HC26)

http://mg.swdevon.gov.uk/ieListDocuments.aspx?CId=221&MId=1206&Ver=4

2.5 This strategy, which is expected to be predominantly funded through prudential borrowing, has two strands. The first is development within the Borough, the second is commercial property acquisition either within the Borough, the LEP area or the South West Peninsula (in that priority order).

2.6 Also in September 2018 Council approved an overall Borrowing Limit (for all Council services) of £50 million. It is estimated that there is approximately £16million left of this overall limit that could potentially be spent on commercial investments in 2019/20. This has been included within the table below for modelling purposes and completeness also.

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ '000s

	2017/18 actual	**2018/19 forecast**	**2019/20 budget**	**2020/21 budget**	**2021/22 budget**
General Fund services	3,214	2,318	2,076	786	586
Community Housing (see 2.2 above)	0	0	4,700	0	0
Capital investments* (see 2.2 above)	0	21,452	16,000	0	0
TOTAL	**3,214**	**23,770**	**22,776**	**786**	**586**

*Capital investments relate to areas such as capital expenditure on investment properties.

2.7. A Commercial Development Financing Report was considered by the Hub Committee on 29th January 2019 which outlined the financing for three in-Borough developments. These were for a hotel development in Tavistock, a new leisure/hospitality/food retail unit in Okehampton (Okehampton Pod) and for new temporary accommodation provision in Tavistock.

http://mg.swdevon.gov.uk/documents/s20323/Commercial%20Development%20Financing.pdf

2.8 At the Council meeting on 12th February 2019, the Tavistock project and the Okehampton Pod were not approved (Council Minute CM 51). The new temporary accommodation provision in Tavistock was approved and is included within the 2019/20 Capital Programme within Table 1.

2.9 Also at the Council meeting on 12th February 2019, the Capital Programme Proposals (taken into account the changes in outlined in 2.8 above) was approved for £2.076 million. This is shown within Table 1 above.

2.10 In addition there will be a future recommendation to Council to fund £4.7m on Community Housing capital expenditure. Also in September 2018 Council approved an overall Borrowing Limit (for all Council services) of £50 million. It is estimated that there is approximately £16million left of this overall limit that could potentially be spent on commercial investments in 2019/20. This has been included within Table 1 for modelling purposes and completeness also.

2.11 The main General Fund capital project to which the Council is currently committed is Leisure Investment of £1.5m. The Council is being reimbursed by the leisure contractor for the borrowing of the Leisure Investment and the income has already been factored into the Medium Term Financial Strategy. In terms of slippage, £0.1m of capital expenditure approved for 2018/19 will be spent in 2019/20 (this is for all Council capital projects within the Capital Programme).

2.12. All items in Table 1 which are also in the Capital Programme for 2019/20 are based on budgeted estimates and will be subject to the normal project appraisal procedures as required under the Council's Assets Strategy.

2.13. Governance

2.13.1. The Head of Finance Practice invited bids for capital funding from all service areas, for a new capital programme during July 2018 on the strict proviso that all bids must go towards meeting a strategic priority. All capital bids received were ranked against a prescribed priority criteria set out in the bid process. The submitted capital bids have been assessed against the categories in each priority. Priority 1 categories include meeting strategic priorities and statutory obligations (e.g. Health and Safety, DDA etc.) and other capital works required to ensure the existing Council property assets remain open.

2.13.2. Priority 2 categories link to good asset management whereby the capital work proposed would either generate capital/revenue income or reduce revenue spending. A capital bid that will enable rationalised service delivery or improvement is also considered a Priority 2 category to meet the Council's aims and objectives.

2.14. Financing

2.14.1. All capital expenditure must be financed, either from (i) external sources (government grants and other contributions), (ii) the Council's own resources (revenue contribution, reserves and capital receipts) or (iii) debt (internal borrowing and borrowing from third party lenders such as the Public Work Loans Board). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ '000s

	2017/18 actual	**2018/19 forecast**	**2019/20 budget**	**2020/21 budget**	**2021/22 budget**
(i) External sources	331	629	938	597	536
(ii) Own resources	317	250	546	189	50
(iii) Debt	2,566*	22,891**	21,292	0	0
TOTAL	**3,214**	**23,770**	**22,776**	**786**	**586**

*Debt in 2017/18 relates to external PWLB borrowing for the waste vehicles - £2.65 million borrowed in March 2018.

** In 2018/19 the Council has undertaken capital expenditure (financed by prudential borrowing from the PWLB) of £22.9m. This was mainly to purchase four investment properties as part of the Council's Commercial Property Acquisition Strategy. A monitoring report was presented to the Audit Committee on 9th October 2018 and is available on the attached link:

http://mg.swdevon.gov.uk/ieListDocuments.aspx?CId=130&MId=1190&Ver=4

2.15. The projected debt for 2019/20 relates to borrowing for projects in Tavistock for a temporary accommodation development (which has been approved by Full Council in February 2019). In addition, an estimated maximum of £16m of further debt could be undertaken in relation to opportunities that may arise in 2019/20 for either further acquisitions of commercial property or further in Borough development opportunities. The £16m has been shown in Table 1 under the category of Commercial Investments.

2.16. Members have received briefings through the Members' Bulletin on potential community housing schemes within the Borough. A report on the schemes will be presented to the Hub Committee in the summer 2019, this will contain a recommendation to undertake capital expenditure of £4.7m to deliver the schemes.

2.17 Debt is only a temporary source of finance, since loans must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as Minimum Revenue Provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP and use of capital receipts are as follows:

Table 3: Replacement of debt finance in £ '000s

	2017/18 actual	**2018/19 forecast**	**2019/20 budget**	**2020/21 budget**	**2021/22 budget**
Own resources - MRP - Use of capital receipts	42	494	560	735	762 4,700

The Council's full MRP statement is shown below:

2.18. <u>Minimum revenue provision (MRP) policy statement</u>

2.18.1. Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2003 states that 'A local authority shall determine for the current financial year an amount of minimum revenue provision which it considers to be prudent'. The provision is made from revenue in respect of capital expenditure financed by borrowing or credit arrangements.

2.18.2. With all options MRP should normally commence in the financial year following the one in which expenditure was incurred. Regulation 28 does not define 'prudent'. However MRP guidance has been issued, which makes recommendations to authorities on the interpretation of that term. Authorities are legally obliged to 'have regard' to the guidance.

2.18.3. The first recommendation given by the guidance is to prepare, before the start of each financial year, an annual statement of the policy on making MRP in respect of that financial year and submit this to Full Council for approval.

2.18.4. The guidance aims to ensure that the provision for the repayment of borrowing which financed the acquisition of an asset should be made over a period bearing some relation to that over which the asset continues to provide a service.

The MRP policy to be adopted is as below:-

Borrowing	**MRP Methodology**
Commercial Property acquisition (Total Council Borrowing of up to £50 million to include all Council services)	***Annuity Method (over the 50 years)*** Under this calculation, the revenue budget bears an equal annual charge (for principal and interest) over the life of the asset by taking into account the time value of money. Since MRP only relates to the 'principal' element, the amount of provision made annually gradually increases during the life of the asset. The interest rate used in annuity calculations will be referenced to prevailing average PWLB rates. In area Council developments on Council land may propose to repay MRP based on 50% on the annuity method over the 50 year life (the assets will be regularly maintained), and 50% will be paid on maturity of the loan from either sale of the asset (a capital receipt) or through refinancing of the debt. The position would be regularly monitored. If at any point in time the valuation of the asset falls below the open market value then the MRP policy will be revisited.
Waste Fleet, Leisure Investment and Kilworthy Park	**Asset Life Method** MRP is charged using the Asset Life method – based on the estimated life of the asset. This option provides for a reduction in the borrowing need over approximately the assets' life.

2.19. The Council's cumulative outstanding amount of debt finance is measured by the Capital Financing Requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £20.7m during 2019/20.

Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ '000s

	31.3.2018 actual	**31.3.2019 forecast**	**31.3.2020 budget**	**31.3.2021 budget**	**31.3.2022 budget**
General Fund services	4,240	5,366	5,638	5,313	4,971
Community Housing (2.2)	0	0	4,700	4,700	0
Capital investments	0	21,066	36,826	36,416	35,996
TOTAL CFR	**4,240**	**26,432**	**47,164**	**46,429**	**40,967**

2.20. Asset management

2.20.1. To ensure that capital assets continue to be of long-term use, the Council has an asset management strategy in place.

2.21. Asset disposals

2.21.1. 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. The Council is currently also permitted to spend capital receipts on service transformation projects until 2021/22. Repayments of capital grants, loans to third parties for capital expenditure and investments also generate capital receipts. The Council estimates to receive nil capital receipts in the coming financial year as follows:

Table 5: Capital receipts in £ '000s

	2017/18 actual	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget
Asset sales	31	100	0	0	0
Loans repaid	0	0	0	0	0
TOTAL	31	0	0	0	0

3. Treasury Management

3.1. 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. The Council is typically more 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.

3.2. At 31st March 2018, the Council had external borrowing of £4.75 million.

3.3. The Council currently has £10m treasury investments earning an average rate of around 0.70% which are expected to fall to £6.5m at 31/3/2019.

3.4. Borrowing strategy

3.4.1. The Council'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 Council therefore will seek 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 2.0 to 3.0%).

3.4.2. Projected levels of the Council's total outstanding debt which comprises borrowing is shown below, compared with the capital financing requirement (see above).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ '000s

	31.3.2018 actual	**31.3.2019 forecast**	**31.3.2020 budget**	**31.3.2021 budget**	**31.3.2022 budget**
Debt	4,750	24,200	46,850	46,234	40,904
Capital Financing Requirement	4,240	26,432	47,164	46,429	40,967

3.4.3. 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 Council expects to comply with this in the medium term. In 2017/18 the debt is slightly higher than the CFR by £0.51m but this is only a short term position as the gross debt will reduce in 2018/19.

3.5. Affordable borrowing limit

3.5.1. The Council is legally obliged to set an affordable borrowing limit (also termed the "Authorised Limit" for external debt) each year and to keep it under review. In line with statutory guidance, a lower "Operational Boundary" is also set as a warning level should debt approach the limit.

In view of the Council's commercial property strategy, the Council obtained independent external advice on the total amount of borrowing that would be acceptable for the Borough Council based on the Council's own financial status. The report on the advice is confidential, the advised maximum limit of £50 million is incorporated into the Prudential Indicator for the Authorised Limit. This limit takes into account the commercial property strategy and the other borrowing projections such as borrowing for community housing schemes.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £'000s

	2018/19 limit	**2019/20 limit**	**2020/21 limit**	**2021/22 limit**
Authorised limit – total external debt	**50,000**	**50,000**	**50,000**	**50,000**
Operational boundary – total external debt	**47,500**	**47,500**	**47,500**	**47,500**

3.5.2. Further details on borrowing are in the treasury management strategy (Appendix C).

3.6. Investment Strategy

3.6.1. 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.

3.6.2. The Council's policy on treasury investments is to prioritise security and liquidity over yield, i.e. to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely including in collective investment schemes (pooled funds whose underlying assets are company shares, bonds, property etc.) one example of which is the CCLA Local Authorities' Property Fund in which the Council is invested, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may 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 8: Treasury management investments in £'000s

	31.3.2018 actual	**31.3.2019 forecast**	**31.3.2020 budget**	**31.3.2021 budget**	**31.3.2022 budget**
Short-term investments	6,200	6,000	6,500	6,500	6,500
Longer-term investments	500	500	500	500	500
TOTAL	**6,700**	**6,500**	**7,000**	**7,000**	**7,000**

3.6.3. Further details on treasury investments can be found in the treasury management strategy (Appendix C).

3.7. Governance

3.7.1. Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Strategic Finance Lead (S151 Officer) and finance staff (where appropriate), who must act in line with the treasury management strategy approved by Council. Semi-annual reports on treasury management activity are presented to the Audit Committee which is responsible for scrutinising treasury management decisions.

4. Investments for Service Purposes

4.1. The Council has approved making a £50,000 investment in the South West Mutual Bank which takes the form of shareholding in the bank. Other than this, the Council does not currently have investments assisting local public services, such as making loans to local service providers or to local small businesses to promote economic growth or to subsidiaries that provide services. However, it may do so in the future if required. In light of the public service objective, the Council would thus be willing to take more risk than with treasury investments, however the objective would be for such investments to break even after all costs (Council Minute CM44).

4.2. Governance

4.2.1. Decisions on service investments are made by the relevant service manager in consultation with the Strategic Finance Lead (Section 151 Officer) and must meet pre-approved criteria and limits. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

5. Current and Proposed Commercial Activities

5.1. West Devon Borough Council owns a number of commercial units, industrial units, office accommodation, within the Borough, valued at £3 million at 31/3/2018.

5.2. The Council leases various parcels of land and buildings to external organisations. This reflects the historic policy of supporting small start-ups which has proved and continues to be successful.

5.3 Commercial activity generates net income each year after all costs, but it also exposes the Council to normal commercial risks. In 2018/19 rental income net of direct operating expenses is expected to be £195,000 as per the Quarter 3 Budget Monitoring report presented to the Hub Committee on 29th January 2019 .

5.4 The risks are managed by the Council's Senior Leadership Team and the Council's Assets team who engage specialist advisors where appropriate. The Council has a comprehensive due diligence check list which is completed before any commercial property acquisitions or commercial developments are made.

5.5. **The Council's Commercial Property Strategy**

5.5.1. With the withdrawal of Government funding, the Council recognises it will need to generate additional income (as an ancillary benefit) to be able to carry on delivering the current range of services.

5.5.2. In September 2018 (Minute CM34) the Council approved an updated Commercial Property Strategy, which included multiple objectives: (a) to support regeneration and the economic activity of the Borough, the LEP area and the South West Peninsula (in that priority order) (b) to enhance economic benefit (c) to grow business rate income (d) to assist with the financial sustainability of the Council as an ancillary benefit and (e) to help continue deliver and/or improve frontline services in keeping with its adopted strategy and objectives.

(Note the previous commercial property acquisition strategy was approved by Council on 27th March 2018. The new strategy approved in September 2018 included both commercial property acquisition as well as the funding of commercial development on Council land. This proposal is in line with the "Enterprise" corporate strategic aim of creating places for enterprise to thrive and business to grow.)

5.5.3. Details of this strategy can be found in the report taken to the Hub Committee on 11th September 2018 (and subsequently approved by Full Council on 25th September 2018 - minute Reference CM34 and HC26)

http://mg.swdevon.gov.uk/ieListDocuments.aspx?CId=221&MId=1206&Ver=4

5.5.4. This strategy, which is expected to be predominantly funded through prudential borrowing, has two strands. The first is development within the Borough, the second is commercial property acquisition either within the Borough, the LEP area or the South West Peninsula (in that priority order).

5.5.5 A Commercial Development Financing Report was considered by the Hub Committee on 29th January 2019 which outlined the financing for three in-Borough developments. These were for a hotel development in Tavistock, a new leisure/hospitality/food retail unit in Okehampton (Okehampton Pod) and for new temporary accommodation provision in Tavistock.

http://mg.swdevon.gov.uk/ieListDocuments.aspx?CId=221&MId=1209&Ver=4

5.5.6 At the Council meeting on 12th February 2019, the Tavistock project and the Okehampton Pod were not approved (Council Minute CM 51) . The new temporary accommodation provision in Tavistock was approved and is included within the 2019/20 Capital Programme within Table 1.

5.5.7. Due diligence and risk assessment will be undertaken and a business case produced for each development or acquisition opportunity, when identified. It will also be assessed on meeting the above objectives and on delivering one or more of the following outcomes: job creation or safeguarding; health and wellbeing; town centre regeneration; tourism / increased footfall; business rate growth; improved asset utilisation.

5.5.8. A minimum net yield return of 1% is being targeted. However, in some circumstances, e.g. where there is a community benefit, a lower return may be acceptable. The Council will put in place contingency plans should expected yields not materialise.

5.5.9. Other borrowing: Officers are also currently working on Community Housing Schemes within the Borough and a report will be presented to the Hub Committee in the Summer regarding this. This is estimated to cost £4.7 million to build out two schemes delivering 30 residential units and would be funded in the short term by borrowing. A recommendation will be made to Council to approve the capital expenditure of £4.7m and it is included within the capital expenditure estimates in Table 1 for modelling purposes and for completeness. This borrowing, in aggregate with other borrowing, will not exceed the Authorised Limit and Operational Boundary in Table 7.

5.6. Governance

5.6.1. Details of the Council's commercial property strategy can be found in the report taken to the Hub Committee on 11th September 2018 (and subsequently approved by Full Council on 25th September 2018 - minute Reference CM34 and HC26). The Governance arrangements are set out within Appendix A of the Strategy.

http://mg.swdevon.gov.uk/ieListDocuments.aspx?CId=221&MId=1206&Ver=4

5.6.2 The strategy has two strands. The first is development within the Borough, the second is commercial property acquisition either within the Borough, the LEP area or the South West Peninsula (in that priority order). Acquisitions and developments must conform to the adopted commercial property strategy.

5.6.3. Property and most other commercial investments are also capital expenditure; purchases and development will therefore also be approved as part of the capital programme.

5.7. Risk management

5.7.1. The Council accepts there is higher risk on commercial investment than with treasury investments. Financial risk will be weighed up against the social and economic benefits of the investment. The principal risk exposures include vacancies resulting in a disruption or fall in income streams, fall in capital value which is either site-specific or due to general market conditions, deterioration in the credit quality of the tenant. These risks will be managed, for example by having an appropriate tenant mix for small start-ups where the creditworthiness tends to be lower, targeting tenants with strong financial standing for larger units or, where there is single occupancy, having long unexpired leases on the date of acquisition.

Proportionality

5.7.2. The commercial property strategy considers the risks of investment and the Council has engaged Treasury Management advisors to analyse the level of debt proportionality to the Council's finances (e.g. levels of reserves, asset base and level of interest costs as a percentage of income). Commercial property acquisitions expand the Council's balance sheet and interest costs will form a higher percentage of locally derived income. It would absorb a high level of reserves if there are shortfalls in or disruption to the income stream required to meet the additional expenditure.

5.8 Sensitivity analysis on the level of debt interest against the Council's level of reserves was considered as part of the Medium Term Financial Strategy and as part of the budget proposals for 2019/20. In order that commercial investments remain proportionate to the size of this Council, borrowing for the Commercial Investment Property Strategy is subject to an overall maximum limit of £50m.

5.9 The Council set an upper limit on External Borrowing (for all Council services) as part of the Medium Term Financial Strategy of £50 million. Interest payments at 2.5% would equate to 28.4% of available reserves. At an interest rate of 3%, interest payments would equate to 34.1% of available reserves (Appendix H to the Budget Proposals report for 2019/20 – Council 12th February 2019).

6. Liabilities

6.1. In addition to the current debt of £24.2m detailed above, the Council is committed to making future payments to cover its pensions liability. The Pensions Reserve for the net defined benefit liability was £24.4m at 31/3/2018.

6.2. As at 31st March 2018 the Council had no contingent liabilities.

Governance

6.3 Decisions on incurring new discretional liabilities are taken by Heads of Practice in consultation with the Strategic Finance Lead (S.151 Officer). The risk of liabilities crystallising and requiring payment is monitored as part of budget monitoring and reported quarterly.

7. Revenue Budget Implications

7.1. 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, business rates and general 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)	81,140	1,033,877	1,756,601	1,898,601	1,784,542
Proportion of net revenue stream	1.1%	14.1%	24.8%	26.1%	26.1%

Further details on the revenue implications of capital expenditure are included in the 2019/20 Revenue Budget.

7.2. Statement on Sustainability

7.2.1. 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 50 years into the future.

7.2.2. With £4.75m external debt at 31st March 2018, the Council is starting from a low base when comparing interest costs with income and reserves. It is anticipated that debt funded acquisitions will generate additional revenue above the capital funding costs. Based on reserves of £4.4m (£1.2m unearmarked and £3.2m earmarked), as shown in Appendix H of the Budget Proposals 2019/20 report to Council, an increase in debt to £50m will result in debt interest costs being equivalent to 28.4% of reserves (assuming an interest rate of 2.5%). Should average the average rate rise to 3%, then debt costs will be 34.1% of reserves. These costs do not include MRP which will also need to be considered.

7.2.3. The Strategic Finance Lead (S151 Officer) is satisfied that the proposed capital programme is prudent, affordable and sustainable and it is fully integrated with the Council's 2019/20 Medium Term Financial Strategy, Treasury Management Strategy and Investment Strategy and other strategic plans. The Capital Strategy is compiled in line with the requirements of the 2017 CIPFA Prudential Code and 2017 Treasury Management Code. The risks associated with the Commercial Property Strategy are covered within the Investment Strategy.

7.2.4. The delivery of the individual capital schemes on the plan is directly linked to the original approval of the capital project supported by each project having a project lead who is responsible for the delivery of the project (appropriate skills, contracting, planning etc.) and the subsequent achievement of the objectives of that project.

7.2.5 Members, via the Hub Committee meetings receive quarterly budget monitoring reports on the Council's Capital Programme. Through these updates, which are driven by the requirement of financial reporting, Members can review and challenge the delivery of projects and any changes to both the timing and expenditure of the capital project.

7.2.6 If subsequent to the capital project being completed there are variations to the income expected to be generated from that asset, this will be reported as a variance in the quarterly budget monitoring reporting and if ongoing will be included in the following year's revenue budget proposals.

7.2.7 The Council's Senior Leadership Team has oversight for the delivery of and challenge to the Capital Strategy and Capital Programme.

Affordability

7.2.8 Affordability is critical in applying the capital strategy and approving projects for inclusion in the capital programme. This is either demonstrated by a report on the project being presented to Hub/Council for approval supported by a business case identifying the expenditure and funding, appraisal of alternative options and the risks and rewards for the approval of the scheme, or by delegated procedures set out within the commercial property strategy (containing this information).

7.2.9 All projects need to have a clear funding source. If external funding such as an external grant is to be used, there needs to be a clear funding commitment.

7.2.10 Affordability of each project needs to be clear, not only for the funding of the capital spend, but also to cover any ongoing costs of the operation and funding of that capital spend.

7.2.11 Where borrowing is to be used the affordability is of greater importance and the affordability has to include the interest costs of that borrowing and the provision for the repayment of the borrowing (MRP). This repayment is matched to a prudent asset life and any income streams estimated to fund this asset must be sustainable. The rules around the governance of this borrowing are outlined in the Prudential Code (as summarised above).

7.2.12 At no stage should the asset value be lower than the value of outstanding debt unless there is a clear plan to mitigate that shortfall or to sell that asset.

Risks

7.3.1. The risks associated with a significant Capital Programme and a significant level of borrowing can be mitigated through all capital projects being supported by a business case, having adequate project management and/or project boards, suitable skills for the delivery of the project, tax planning, cash flow, clear operational plan for the use of the asset, security and due diligence on loans and purchases, use of external advice where appropriate, project contingencies, full tender process and regular and transparent reporting to Members.

7.3.2 There are clear links from the capital strategy to both the treasury management strategy, prudential indicators, authorised borrowing limits and the revenue budget. These are also subject to review and oversight by Members at the Audit Committee and Council. For any new borrowing, and this is a greater risk as the value of borrowing increases, this does increase the Council's overall liabilities that will need to be repaid in the future.

7.3.3. In addition, this increases the Council's level of fixed interest and repayment costs that it will incur each year. This is currently increasing by 2022 and could be up to a borrowing liability of £40.9m (see Table 6) and ongoing financing costs of the borrowing of approx. £1.89m by 2021/22. This is a clear risk that all Members need to be aware of.

7.3.4. However this risk for assets is mitigated by a robust business case and a MRP that will repay the borrowing costs over a (prudent) asset life. Any variations from this are set out in the MRP Policy (See section 2.18.4). Any variation in expected income is an issue, however given the wide range of operational assets and different income streams this helps to mitigate this risk.

7.3.5 As outlined above in the position statement, investment properties are a different type and level of risk. Risk arises from both variations in income streams (tenant non-renewal etc.) and from asset values (impact economic conditions and retail trends etc.). The Council has established a clear strategy, criteria and a governance route for these purchases which has included member training, second opinion on asset values, due diligence, site visits, surveys etc.

7.3.6 There are risks (and rewards) associated with the purchase of this type of assets, therefore all Members need to have sight of and understand the risks and rewards inherent in these commercial investments(development opportunities).

Knowledge and Skills

8.1 The Council employs professionally qualified and experienced staff in senior positions with responsibility for recommending capital expenditure, borrowing and investment decisions to Members.

8.2 The Group Manager of Business Development is a qualified Project Manager and Accounting Technician, with a RICS (Royal Institute of Chartered Surveyors) Accredited degree in Estates Management, incorporating Investment and Development. In addition, the Group Manager for Business Development also has 15 years of banking/lending experience, having worked on multi-million pound asset investment, disposal and development projects.

8.3 The Chief Executive has a MSc in Leadership of Public Services (2009) from UWE (Bristol Business School) and an IoD (Institute of Directors) Certificate of Directorship in 2016. In addition, the Chief Executive has been involved in the oversight of the Councils' interests (as shareholder) in its wholly owned companies when working as a Director for a Unitary Council.

8.4 The Strategic Finance Lead (S.151 Officer) is a Chartered Accountant (ICAEW) with 15 years of experience of being a S151 Officer (Chief Finance Officer). In addition, the Strategic Finance Lead holds a BSc in Mathematics and has previously worked in the private sector for accountancy firms.

8.5 The Head of Assets Practice is a Chartered Civic Engineer with sixteen years of experience. In addition, the Head of Assets holds a MSc in Construction Law.

8.6 The Estates Specialist is a Chartered Surveyor, qualified for over 13 years, with an Estate Surveying degree. In addition they are a Registered Valuer.

8.7 Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The appropriate expertise is always resourced in relation to any financial, legal and asset related due diligence required. A list is below:-

- Savills - Property agents
- CCD Properties Limited - Development specialists
- Arcadis – Building Surveyors and Engineers
- Womble Bond Dickinson - Solicitors
- Link Services – Treasury Management advice
- Arlingclose – Treasury Management advice

8.8 This approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

8.9 In 2018 some external training from a LGIU (Local Government Information Unit) Associate on Local Government Finance (including commercialism) was arranged for all Members aswell as some internal training events facilitated by the S151 Officer and the Group Manager for Business Development on the Council's Medium Term Financial Strategy which included an update on commercial property investment. The Council's Members' Services are consulted when organising all training in order to maintain training and development plans for Councillors.

8.10 A comprehensive Members' Induction Programme, following the District Elections in May 2019 has been organised, this includes specific financial and treasury management training which will be undertaken as part of the induction. External treasury management training will be offered to all Members in June 2019 to ensure Members have up to date skills to continue to make capital and treasury management decisions.

8.11 The purpose of this training is to ensure elected Members involved in the investments decision making process have appropriate capacity, skills and information to enable them to: 1. take informed decisions as to whether to enter into a specific investment; 2. to assess individual assessments in the context of the strategic objectives and risk profile of the local authority; and 3. to enable them to understand how the quantum of these decisions have changed the overall risk exposure of the local authority.