EXECUTIVE – 3 FEBRUARY 2022

CAPITAL STRATEGY 2022-23

1.0 Introduction

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

1.2 Capital expenditure is focussed on the Council's priorities and is long term investment to secure long term improvements for the community. It is linked to the Council's long term strategies and vision in developing a sustainable future for the Borough. The Council's priorities areas are:

- Decent and Affordable Housing
- Economic Development
- The Environment; and
- Health and Wellbeing

1.3 Other important areas for capital investment are where there is a Health and Safety issue identified, or a need to make improvements to the Council's assets.

2.0 Capital Expenditure and Financing

2.1 Capital expenditure is where the Council spends money on assets, such as property or equipment, which will be used for more than one year. This includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy or develop assets.

2.2 Projects which involve capital expenditure are usually included in the Council's Investment Programme which is approved annually as part of the budget process. Financing costs in the General Fund and Housing Revenue Account budgets reflect the annual costs of implementing the Investment Programme.

2.3 It is possible that revenue (operational) budgets could be used for capital purposes however, there is not sufficient flexibility within service budgets to incur significant capital spend. The Council's Investment Programme includes both capital and revenue projects. Revenue projects such as feasibility studies are shown within the Investment Programme as they are one-off in nature. There is also often flexibility in timing as projects may be deferred if funding cannot be secured. Revenue budgets comprise operational costs and income which is expected to recur each year.

Investment Programme 2022/23

2.4 In 2022/23, the Council is planning Investment Programme expenditure of £231m as summarised below:

Table 1: Investment Programme February 2022

	2020/21 Actual £m	2021/22 Budget £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
General Fund	266	265	120	35	10	9
Housing (Including Council Housing)	77	105	111	114	63	81
TOTAL	344	370	231	150	73	90

2.5 The main General Fund capital projects in 2022/23 are:

- Victoria Arch and Integrated South Side Works (HIF bid) – highway improvements and replacement of Victoria Arch unlocking housing sites.
- Acquisition of Car Parks from Victoria Square Woking Ltd – providing sufficient parking for future town centre growth.
- Investment in Thameswey Central Milton Keynes
- Poole Road Energy Centre – creating a new energy centre to supply Victoria Square and other town centre properties.

2.6 There is a £3m budget for 'Opportunity Purchases' in 2022/23. The Opportunity Purchases budget enables the acquisition of small sites or properties which are of use to the Council if they become available. In some instances these assets will be disposed of if the use is only temporary. Opportunity purchases are reported during the year in the Council's monthly performance and financial monitoring (Green Book).

2.7 The Investment Programme includes annual provision for works to the Councils assets (The Asset Management Plan) and development/replacement of ICT systems.

2.8 The Housing Investment Programme (HIP) sets out the Council's housing related projects. Some of these are General Fund housing, for example relating to private sector housing provision or homelessness. Other expenditure is on the Council's own housing stock and is financed through the Housing Revenue Account (HRA). The HRA is a ring-fenced account separating the income and expenditure relating to council housing from other Council activities.

2.9 The main HIP projects in 2022/23 are:

- Provision of new homes by Thameswey Housing Ltd.
- Sheerwater Regeneration scheme – project which will improve the Sheerwater area with new housing and leisure facilities.
- Provision of new HRA properties using retained Right to Buy receipts.
- Improvement works to existing HRA properties.

2.10 Other areas of HIP spend include Disabled Facilities grants and provision of a new hostel.

<u>Investment Programme Governance</u>

2.11 Projects may be initiated by Service managers, Councillors, Corporate Leadership Team (CLT) or be the result of an external source or opportunity. A project manager is appointed and will prepare a short summary of the project for consideration by CLT. If CLT are supportive, the project manager will complete a more detailed workbook which covers the objectives of the project, the costs, funding and risks. If necessary a report will be presented to the Executive or Council to approve use of resources.

2.12 Project progress reports are prepared for the Executive and highlight any issues relating to the timescale or budget of a project as well as providing a high level update. Variations to project timescales or budgets are submitted to CLT to be considered. If necessary these will be reported to the Executive.

2.13 Some projects, due to their scale and importance to the Council, will have specific project governance assigned. For example there are Officer and Member working groups for the Sheerwater regeneration project, and a Member Oversight panel for the Victoria Square development.

2.14 Projects which have been subject to detailed consideration by the Executive or Council will also follow the project management mandate and workbook process which ensures that all the relevant information is considered.

2.15 Projects are consolidated into the Investment Programme on an annual basis and presented to the Executive/Council in budget papers. Where relevant the debt financing and repayment costs of the Investment Programme are incorporated into the General Fund and Housing Revenue Account budgets, and reflected in the Prudential Indicators approved by Council. New projects may be approved during the year subject to the impact on the revenue budget being assessed and affordable.

2.16 The Executive has authority to approve new projects up to a total of £10m in any one year, with any individual project no more than £5m. Any projects approved under this authority are reported in the Green Book during the year. Any new capital expenditure which exceeds these parameters must have full Council approval. The Council would also need to approve any changes in borrowing limits necessary to accommodate additional borrowing.

<u>Investment Programme Financing</u>

2.17 All projects within the Investment Programme are financed either from grants or contributions (external sources), reserves or capital receipts (internal sources) or borrowing (including leasing/Private Finance Initiative). Table 2 shows the financing of the February 2022 Investment Programme.

Table 2: Investment Programme Funding February 2022

	2020/21 Actual £m	2021/22 Budget £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
Borrowing	325	330	174	125	65	82
Grants & Contributions	18	30	49	17	2	2
Reserves & Capital Receipts	8	10	9	8	6	5
TOTAL	351	370	231	150	73	90

2.18 The Council must make provision for the repayment of any borrowing used to finance capital expenditure. This is normally through the annual charge to the revenue budget known as the 'minimum revenue provision' (MRP). The Council has a policy for the calculation of MRP which can be found at Appendix A.

2.19 Where borrowing has been used to advance loans, the loan repayments are set aside as MRP for the future repayment of the underlying borrowing. If borrowing has been used as a temporary funding source, capital receipts, developer contributions or grant may be applied to reduce the outstanding debt. For property acquisitions funded by borrowing, the MRP is charged on an annuity basis comparable to the principle repayments on an underlying annuity loan.

2.20 Planned set aside for the repayment of underlying Council borrowing (MRP) is shown in Table 3 below.

Table 3: MRP

	MRP (excluding loan repayments) £'000	Loan repayments set aside £'000	Total MRP £'000
2020/21 Actual	6,814	5,729	12,543
2021/22 Forecast	6,219	6,146	12,365
2022/23 Budget	7,348	9,508	16,856
2023/24 Budget	9,039	9,669	18,708
2024/25 Budget	9,414	10,013	19,427
2025/26 Budget	10,278	10,193	20,471

2.21 On the 30th November 2021 the Department for Levelling Up, Housing and Communities (DLUHC) issued a consultation on MRP. The consultation includes reviewing the approach of using capital receipts in lieu of MRP. The implications of this proposal are discussed in the General Fund budget report elsewhere on the agenda.

2.22 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 as funds are set aside to repay debt. The CFR is expected to increase by £165m during 2022/23. Based on the Council's Investment Programme the estimated CFR is as shown in Table 4 below:

Table 4: Estimate of Capital Financing Requirement (CFR)

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
General Fund Services	510	519	581	590	586	581
Council Housing (HRA)	146	153	156	158	160	161
Capital Investments	1,095	1,390	1,489	1,592	1,648	1,722
TOTAL CFR	1,751	2,062	2,227	2,341	2,394	2,464

2.23 Where opportunities arise, the Council will apply for government or other external funding to contribute towards planned Investment Programme projects. The award of grants is subject to the conditions of the grant awarding body and will often include a requirement for match funding by the Council and a repayment clause if funds are not applied in accordance with the grant terms.

2.24 In July 2019 the Council was awarded £95m from the Homes England Housing Infrastructure Fund (HIF) towards the replacement of Victoria Arch and associated highways works. The full project is expected to cost £115m, with £10m contribution from Network Rail and £10m from the Council funded by development contributions (or interim borrowing if these contributions are not received at the time of financing the scheme).

Asset Management

2.25 To ensure that capital assets continue to be of long-term use, the Council includes an annual Asset Management Plan (AMP) allowance in the Investment Programme. This is used to improve the Council's existing assets. The planned use of the Asset Management Plan budget for 2022/23 is shown in an appendix to the Investment Programme.

2.26 If improvement works are required which cannot be met by the annual AMP budget a specific analysis will be prepared in order for the investment to be approved. Revenue budgets include allowance for day to day repairs and maintenance. Some works on commercial properties are the responsibility of the tenant. Other works may be recharged to tenants as part of the service charge either in-year or over a period of time.

2.27 The Council may invest in changes to commercial properties to secure a new tenancy or to relocate tenants to improve the offer, or diversity of services or employment space, within the Borough.

Asset Disposals

2.28 If an asset is not needed the Council may sell it generating a capital receipt. The capital receipt can be used for capital purposes such as to fund alternative capital investment, or to repay debt (MRP).

2.29 Repayments of capital grants, loans and investments also generate capital receipts. Where funded by borrowing the Council allocates these repayments as MRP for the repayment of the underlying debt.

2.30 When council houses are sold under the Right to Buy scheme the Council retains an element of the sale proceeds to be put towards replacement council housing. These receipts are held within the Council's capital receipts reserves but are separately identified due to the restrictions on use. If not spent within 5 years these receipts must be returned to the government with interest.

2.31 The Council is not actively holding assets for sale so a significant level of capital receipts is not expected to be available over the period of the Investment Programme. However, when opportunities arise, the Council will consider the disposal of assets if it is considered optimal to the vision for the Borough.

Table 5: Capital Receipts

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
Asset Sales	1.2	0.0	0.0	0.0	0.0	0.0
Right to Buy Sales	1.6	1.6	1.6	1.6	1.6	1.6
Loan Repayments	5.7	6.1	9.5	9.7	10.0	10.2
TOTAL	8.5	7.8	11.1	11.3	11.6	11.8

3.0 Treasury Management

3.1 The Council's Treasury Management Strategy sets out how the Council manages cash balances. Surplus cash may be invested until required, while a shortage of cash will be met by borrowing.

3.2 At the current time minimal cash balances will be held as the balances would earn little return due to current low interest rates. The Council's reserves will be used to reduce the overall borrowing drawn down which delays the Council incurring external financing costs for capital investment. Each year the annual budget assumes that the Council draws down the total level of borrowing required to fund the Investment Programme. Any under borrowing results in a saving against the interest cost budget.

3.3 During 2021/22 the Council has converted most of the short-term borrowing taken in the previous financial year to long term borrowing to take advantage of the low PWLB rates available.

3.4 Borrowing for long term assets is financed through long-term loans reflecting the long term life of the asset and mitigating the risk of rising interest rates. However flexibility is maintained to use short term borrowing to manage short term cash flows, to manage the timing of long term decisions and to generate in-year interest savings.

3.5 In November 2020 HM Treasury announced revised lending terms for the PWLB. The PWLB will no longer lend to any Local Authority which plans to buy investment assets primarily for yield (regardless of whether this purchase would be funded by PWLB borrowing or through other resources). The Treasury Management and Prudential Codes were updated in December 2021 confirming the principle that an authority must not borrow to invest primarily for financial return.

3.6 The Council's Capital Programme has been reviewed by the s151 Officer and a return has been provided to the PWLB and HM Treasury which confirms that Woking complies with these new rules and is able to access PWLB Borrowing.

3.7 Borrowing and treasury investments are reported in the Council's monthly performance and financial monitoring (Green Book).

3.8 Projected levels of the Council's total outstanding debt (which comprises borrowing, PFI liabilities and leases) are shown below, compared with the capital financing requirement. Statutory guidance is that debt should remain below the CFR except in the short term. This demonstrates that borrowing is only being taken to meet capital financing needs.

Table 6: Gross Debt & Capital Financing Requirement

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
Debt (including PFI & leases)	1,716	2,062	2,227	2,341	2,394	2,464
Capital Financing Requirement	1,751	2,062	2,227	2,341	2,394	2,464

Authorised and Operational borrowing limits

3.9 The Council is legally obliged to set an affordable borrowing limit known as the authorised limit each year. External debt must not exceed the authorised limit. A lower operational limit is also set which acts as a warning and requires a report to Council if breached.

3.10 The Authorised and Operational limits are set by full Council and reported on the Treasury pages of the Green Book each month so that actual borrowing can be assessed in the context of these limits.

3.11 The limits are calculated with reference to the planned Investment Programme, allowing scope for those projects funded by borrowing to proceed. When the Council approved the Victoria Square regeneration project the limits were increased to accommodate the full project cost from project commencement. This enabled flexibility to secure borrowing in at preferential rates, if available, in advance of cashflows.

3.12 The Treasury Management Strategy sets out the Authorised and Operational borrowing limits for 2022/23.

Treasury Management Strategy

3.13 Treasury Management is concerned with making investments of surplus cash and borrowing to manage delay in cash flows. Investments made for service reasons are not generally considered to be part of treasury management.

3.14 The Council's Treasury Management Strategy is to prioritise security and liquidity over yield for treasury management investments. Cash is invested securely with the Council's own bank, in diversified money market funds, or with other local authorities. The primary focus is on minimising risk rather than maximising returns.

3.15 Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Finance Director and finance team who follow the Treasury Management Strategy approved by the Executive. Treasury Management practices are in place which provide day to day guidance for treasury officers. The Green Book monthly monitoring report includes details of all investment and borrowing taken in the month and shows the overall position at the month end. A Treasury Management report is presented to the Executive after the end of the year detailing the activity for the year and the Overview and Scrutiny Committee receives a mid-year report.

4.0 Investments for Service Purposes

4.1 The Council uses different mechanisms and investment structures to secure capital developments for the Borough. This includes the use of its group companies through the Thameswey group, and joint ventures for example Victoria Square Woking Ltd, and enables the Council to take a longer term view than would otherwise be possible.

4.2 Investment in shares and loans to these entities is treated as capital investment and is financed within the Council's Investment Programme. Whilst these investments are made to secure service objectives, not for profit, the Council still plans to at least break even. The margins on loans made for service purposes have provided an additional income stream for the Council and have enabled services to continue despite reductions in government funding.

4.3 The Thameswey group continue to work to existing business plans. During 2022/23 there plans will be reviewed in detail to ensure they align with the adopted Council Corporate Strategy. Existing loan facilities are sufficient to progress the Thameswey group plans in 2022.

4.4 There is monthly reporting in the Green Book and a set of protocols which govern the practices of the group. Decision making for other loans and investments follows the processes for the Investment Programme.

4.5 The Council's capital programme does not include purchases for assets primarily for yield. Any commercial properties acquired are not bought purely for income but for future service opportunities or growth (for example for regeneration purposes). General Fund property purchases are treated as capital expenditure with the associated financing and capital repayment (MRP) costs included in the Council's budgets.

4.6 With the exception of lower value property acquired using the Council's opportunity purchases budget, new property acquisitions will be the subject of Executive or Council approval. The ongoing revenue impact of these purchases will be presented along with the strategic reason of the purpose including details of quality of tenancies, vacant space provided, and the future opportunities the acquisition of the property will provide for the Council. The revenue impact of strategic properties acquired since 2016/17 is reported monthly in the Green Book.

5.0 Liabilities

5.1 In addition to the borrowing considered in the sections above, and the Treasury Management Strategy, the Council is committed to making future payments to cover its pension fund deficit valued at £82m at 31 March 2021.

5.2 The Council has a Private Finance Initiative (PFI) scheme which provides 224 houses at social rents for 25 years. The liability associated with the repayment of the liability through the unitary charge was assessed as £25.6m at 31 March 2021.

5.3 Decisions on incurring new discretional liabilities are taken in the same way as other Council expenditure and will be the subject of Executive/Council decisions if not covered by approved budgets.

5.4 Further details on liabilities can be found in of the Council's statement of accounts published on the Council's website.

6.0 Revenue Budget Implications

6.1 Capital expenditure is not charged directly to the revenue budget, instead the financing and capital repayment (MRP) is charged in year. The costs net of investment income are shown as net financing costs in the table below. The table compares the net financing costs to the net revenue stream (amount funded by Council Tax, business rates and Government Funding).

6.2 This indicator has increased substantially over recent years due to two factors:

- Net financing costs do not include the income generated from assets acquired or developed, for example commercial property, car park provision.
- Net revenue stream has steadily reduced through government funding cuts to government funding and restrictions on Council Tax increases

Table 7: Proportion of Financing Costs to Net Revenue Stream

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
Financing Costs (£m)	14.5	14.5	17.0	20.2	19.7	19.7
Net Revenue Stream (£m)	12.5	12.6	13.2	12.2	12.1	11.9
Proportion of Net Revenue Stream	116%	116%	129%	165%	163%	165%

6.3 Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure and will extend up to 50 years into the future. The Council links the use of long term borrowing to capital expenditure where the benefits are also expected to extend into the long term. In particular spend on the transformation and regeneration of the town centre will have a long term impact and infrastructure works are hoped to attract further private investment into the Borough.

6.4 The Investment Programme was reduced in scope during 2020, with uncommitted projects funded by borrowing or reserves temporarily suspended while the Council assessed the financial position post Covid. These projects have been assessed and those which remain relevant included on a pipeline list which is not currently funded. The Finance Director is satisfied that the proposed capital programme is prudent, affordable and sustainable in 2022/23, and that the revenue impacts of the projects included have been recognised in the budget. Future years will need to be reviewed as the economic consequences of the recovery from the pandemic become clearer.

6.5 The Medium Term Financial Strategy (MTFS) sets out the impact and pressures on the Council over a four year period. The net cost of decisions, assessed individually, are consolidated into the next update of the MTFS.

6.6 The 2020/21 and 2021/22 budget forecast significant use of reserves covering the projected loss of income due to the Covid-19 pandemic. The Council has set a minimum level of reserves acceptable to enable sufficient resilience and scope for one-off spend. The MTFS determines the savings required to ensure this level of reserves is maintained.

7.0 Knowledge and Skills

7.1 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. The Finance Director, Financial Services Manager and senior members of the Finance team are qualified accountants with many years' experience. The Council has a Strategic Asset Manager and Estates Management team with experience in managing properties, and valuation. The Council also has an in-house legal team led by the Director of Democratic and Legal Services (Monitoring Officer).

7.2 External advisors and consultants are used where the Council does not have the technical knowledge, experience or skills required. They are also used to supplement the internal resource if Council staff do not have the capacity to manage the Council's requirements.

7.3 The Council supports training towards professional qualifications and for staff to attend relevant training courses for continued professional development. A management training programme is also being completed by senior members of staff. There is a Members' development programme and the Council has the Charter mark for Member Learning and Development. In October 2019 the Council was awarded the Investors in People Silver accreditation and the Health and Wellbeing Good Practice Award. Specific training and briefing sessions are organised on subjects or projects as needs are identified.