CAPITAL STRATEGY

1st Draft September 2018

THREE RIVERS
DISTRICT COUNCIL

1. Introduction

1.1 The purpose of the capital strategy (the Strategy) is to tell a story that gives a clear and concise view of how the council determines it priorities for capital investment, decides how much it can afford to borrow and sets its risk appetite. It is intended to give a high level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services along with an overview of how associated risk is managed and the implications for future financial sustainability.

1.2 The framework the government uses to control how much councils can afford to spend on capital investment is known as the Prudential Framework. The objectives of the Prudential Code, which sets out how this framework is to be applied, are to ensure that local authorities' capital investment plans are:

- affordable, prudent and sustainable;
- that treasury management decisions are taken in accordance with good professional practice; and
- that local strategic planning, asset management planning and proper option appraisal are supported.

1.3 This capital strategy sets out how Three Rivers District Council will achieve the objectives set out above.

2. CAPITAL INVESTMENT PROGRAMME

Capital Investment Programme - Expenditure

2.1 Capital Investment is the term used to cover all expenditure by the council that can be classified as capital under legislation and proper accounting practice. This includes expenditure on:

- property, plant and equipment
- heritage assets, and
- investment properties.

2.2 Property plant and equipment includes assets that have physical substance and are held for use in the production or supply of goods and services, for rental to others, or for administrative purposes. They are expected to be used during more than one financial year. Expenditure on the acquisition, creation or enhancement of these assets is capitalised on an accruals basis, provided that the Council is likely to benefit from the future economic benefits or service potential and the cost of the item can be measured reliably. Expenditure on repairs and maintenance is charged to the revenue account when it is incurred.

2.3 Heritage Assets are held with the objective of increasing knowledge, understanding and the appreciation of the Council's history and local area.

2.4 Investment properties are those that are used solely to earn rentals and/or for increases in value. The definition is not met if the property is used in any way for the delivery of services or production of goods or is held for sale.

2.5 The Council is debt free so does not capitalise borrowing costs incurred whilst assets are under construction.

2.6 Detailed accounting policies in relation to assets and capital expenditure may be found in the annual statement of
accounts.

2.7 Appendix 1 shows the latest position on the agreed 2019/20 capital programme along with a forecast of expenditure to 2021/22.

2.5 The larger capital schemes include:

South Oxhey Initiative

The South Oxey initiative is a major development in partnership with Countrywide Properties for the development of the centre of South Oxey. The development costs and the funding for this project are shown separately at Appendix X. The progress of the scheme is monitored by the Property Investment Board (PIB) and reported to Members at Policy and Resources Committee or the South Oxhey Scrutiny Panel if Policy and Resources Committee is not available.

South Oxhey Leisure Facility

As part of re-procuring the Leisure Facility Management Contract (LFMC), the Council has agreed to replace the existing leisure facility at South Oxhey (known as 'The Centre') with a new building that new includes a swimming pool.

The new building will be constructed by the leisure contractor under a Design, Build, Operate and Maintain (DBOM) contract; however the Council has agreed to finance the build costs. These costs are contractually capped at £8.6 million with any project overspend to be met by the leisure contractor. The Council may need to borrow to fund this new capital investment, however, the financial analysis of the contractor's bid shows that in addition to the annual management fee (revenue) received there is a further element to cover the costs of the capital principal repayment and debt servicing over the life of the contract.

2.6 Proposals for new schemes require Project Initiation Documents (PIDs) to be prepared and presented to the relevant service Committee at the November/December meetings. The Council uses a scoring matrix (to be found at Appendix 2) to assess the contribution of projects to the councils objectives and need.

Property investment

2.11 In 2017/18, the Council set up its Property Investment Board (PIB) consisting of Senior Officers. The purpose of PIB is to approve the investment in property based assets primarily as capital expenditure. The primary aim of PIB is to alleviate some of the financial pressure on the Council's revenue account by acquiring or developing property assets that generate a significant revenue rental stream. The capital programme agreed by Council in February 2017 allowed the Council to invest up to £20 million into property based assets, with a targeted return on capital employed of 5%. The anticipated rental income had been factored into the Medium Term Financial Plan. Each individual acquisition must be subject to its own business case and the financial viability must be agreed by PIB before any Council funds are committed for expenditure.

The PIB investment budget had now been spent and the council is not expecting to make any further investments within this heading unless it is reinvesting capital receipts from existing assets in order to maintain the income stream and/or re-balance the investment portfolio or is self-financing.

Financial investments

2.12 At the meeting of Full Council on 17th July 2018, it was agreed to make loans available to housing associations and similar organisations working within the wider Three Rivers economic area to support growth within the area, particularly in respect of wider housing provision. The procedure for agreeing such investments mirrors the existing processes for investment. An initial £10.5M of investments was agreed.

Capital Investment Programme - Funding

2.12 The Capital Investment Programme can be funded from the following sources:

2.13 Government Grants & Other Contributions: These are grants for specific purposes which may be available from the Government, e.g. Disabled Facility Grants. The Council can also attract partnership funding from other local authorities and agencies e.g. Local Enterprise Partnership (LEP). The Council has also benefited in the past from other funding such as lottery grants.

2.14 Section 106 Contributions: These are contributions from developers to the public services and amenities required for the development. These have been in part replaced by the Community Infrastructure Levy.

2.15 Capital Receipts Reserve: Capital receipts are derived when selling assets such as land.

2.16 Revenue Contributions: Revenue balances from the General Fund may be used to support capital expenditure.

2.17 Future Capital Expenditure Reserve: The Council has a general reserve which it has put aside for future capital expenditure. It has the ability, should it wish, to re-designate this reserve for revenue use, however the current MTFP forecasts that this reserve will be fully utilised to support the capital programme.

2.18 New Homes Bonus Reserve: New Homes Bonus is a grant relating to the number of new homes delivered in a local authority area. There are no government restrictions on whether this is capital or revenue, nor is there any ringfence imposed. New Homes Bonus was expected to end as part of the Fair Funding Review, however, the Government has announced it will continue for another year.

2.19 Borrowing: The Council is allowed to borrow to support its capital expenditure as long as this is prudent, sustainable, and affordable.

2.20 The capital programme includes an assessment of likely available resources to finance capital expenditure and includes assumptions regarding capital receipts, which have been estimated at £2.5 million in 2020/21.

2.21 In addition, the Council is forecasted to generate:

- £0.500 million of Government Grants
- £0.110 million of New Homes Bonus allocated to capital over the medium term.

Future Investment

2.22 Future Investment Schemes will be assessed on the basis of a full business case which will include full resourcing for the project and an assessment of affordability. Priority areas for future capital investment are:

- Schemes that generate a financial surplus for the Council; and in particular those that increase the supply of housing locally (for example through the joint ventures with Watford Community Housing and Thrive).
- Schemes that generate revenue budget savings for the Council.
- Schemes that allow the Council to benefit from future economic regeneration potential within the local area; especially those that attract additional investment into the local area from regional or national agencies.
- Schemes that provide additional or improved services to the Council's residents, in line with the Council's Strategic Plan.

3. TREASURY MANAGEMENT

3.1 The Council is required to operate a balanced budget over the medium term which, after allowing for contributions to and from reserves, broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing the requisite liquidity before considering investment return.

3.2 The Treasury Management Policy Statement, details the policies, practices, objectives and approaches to risk management of its treasury management activities, which is to be monitored by the Audit Committee. The Council's investment strategy's primary objectives are safeguarding the repayment of the principal and interest of its investments on time, and then ensuring adequate liquidity, with the investment return being the final objective. The strategy allows the Director of Finance, in consultation with the Lead Member, the delegated authority to approve any variation to the Treasury Management Strategy during the year which may be brought about by investigating the opportunity to invest for greater than one year and also to invest in other investment instruments i.e Government bonds, Gilts and investment property with a view of maximising the Council's returns without significantly increasing risk.

The Council's Borrowing Need - The Capital Financing Requirement (CFR)

3.3 The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure, which has not immediately been paid for, will increase the CFR. An increase in the CFR does not necessarily mean that the council will borrow externally to fund the increase. The Council manages its cash balances as a whole and may choose to use internal cash (generated by holding reserves and through timing differences between income and expenditure).

3.4 The table below shows the estimate of the CFR for 2020/21 and 2021/22.

	2019/20 Outturn	2020/21 Estimate	2021/22 Estimate
	£M	£M	£M
Total Proposed Capex	17.7	5.4	3.3
Capital Financing			
Grants	0.5	0.5	0.5
Capital Receipts	0.5	1.0	2.3
Reserves	6.4	0.0	0.3
S.106 and CIL	0.1	1.5	0.0
Funding	7.5	3.0	3.1
Gap	10.2	2.3	0.2
Opening CFR	17.1	27.3	29.6
Closing CFR	27.3	29.6	29.9

External borrowing requires the Council to make minimum revenue payment to allow for the repayment of debt.

Minimum Revenue Provision (MRP) Strategy and Policy Statement

3.5 The Minimum Revenue Provision (MRP) is designed to pay off an element of the capital spend which has not already been financed from existing revenue or capital resources. The Council is required to make prudent provision, which means that the repayment of debt is enabled over a period that is reasonably commensurate with that over which the capital expenditure provides benefits.

3.6 The Council is also able to increase the rate it reduces its CFR by undertaking additional voluntary payments (voluntary revenue provision - VRP) in addition to any MRP; this is not currently the Council's policy.

3.7 Government Regulations require the Council to approve a MRP Statement in advance of each year. The following is Three Rivers MRP statement:

For all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- ***Asset life method** – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3)*

This option provides for a reduction in the borrowing need over the asset's estimated life.
Repayments of PFI or Finance Leases are allowable to use as a proxy for the above methods.

3.8 Three Rivers District Council's process is to produce for approval by the Director of Finance, in consultation with the Lead Member, a business case for each scheme intended to be unfunded from other resources. This will clearly show the level of MRP which is proposed to ensure that the repayment of any debt can be made in a period commensurate with the period over which the expenditure provides benefits or makes returns.

3.9 Although the South Oxhey Project results in a positive CFR it is recommended that MRP is not applied to this scheme as the project is short-dated and is expected to generate a receipt to cover any financing costs; it is mainly improving works, rather than a capital scheme which will depreciate over time; therefore the Council will not be making a Minimum Revenue Provision for this scheme.

Cash Flow

3.10 Appendix 4 contains the forecast cash flow**…(to be completed as part of the budget forecast)**

Revenue Cost of Borrowing

3.11 Should the council decide to borrow to fund capital expenditure the annual cost of borrowing would be.. (**to be completed as part of budget forecast)**

Prudential Indicators

3.12 There are two limits on external debt: the 'Operational Boundary' and the 'Authorised Limit'. Both are consistent with existing plans and the proposals in the budget report for capital expenditure and financing, and with approved treasury management policy statement and practices.

3.13 The first key control over the treasury activity is a Performance Indicator (PI) to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2018/19 and next two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

Treasury Management Indicator - The Operational Boundary

3.14 This is the limit beyond which external borrowing is not normally expected to exceed. In most cases this would link directly to the authority's plans for capital expenditure, its estimates for CFR and its estimate of cashflow requirements for the year for all purposes. The Council may need to borrow, this limit represents a contingency should the need arise.

Operational Boundary	**2019/20 Estimate**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**
Borrowing	£15M	£18M	£18M	£18M

Treasury Management Indicator - The Authorised Limit for External Borrowing

3.15 This PI, which is required to be set and revised by Members, controls the overall level of borrowing and represents the limit beyond which external long and short term borrowing is prohibited, and this limit needs to be set or revised by the Council. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (2) of the Local Government Act 2003.

Authorised Limit	**2019/20 Estimate**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**
Borrowing	£17M	£20M	£20M	£20M

4. Future Investments

4.1 The Council will continue to seek opportunities to work in partnership with others to promote economic development and the provision of housing within Three Rivers wider economic area. Current partners include Countrywide Properties for the South Oxey scheme, along with Watford Community Homes and Thrive Homes as the two major local registered social providers.

4.2 The council has established Three Rivers Commercial Services to allow it to work more closely with providers and exploit future commercial opportunities. The Council currently has two joint ventures with Watford Community Housing, Three Rivers Development LLP and Three Rivers Homes Ltd. The Council is currently in the process of setting up a similar structure with Thrive Homes to allow future joint schemes to be considered.

5. Skills and Knowledge and Professional Advice

5.1 The Council has a shared service with Watford Borough Council for the provision of the finance function allowing access to a greater range of professional skills than would otherwise be available if each council had a separate team. It also has in house property and legal teams. Where skills are not available in house, or in relation to material projects, the Council will draw on additional professional advisers as necessary. Anthony Collins Solicitors and Grant Thornton are currently providing advice on the proposed joint venture with Thrive Homes and Womble Bond Dickenson are advising on the loans to Watford Community Homes and Thrive Homes.

5.2 The Council contracts with Link Asset Services for the provision of Treasury advice. Link Asset Services provide non-regulated advice on the management of the council's cash flows, investments and borrowings and a markets information service. The Councils VAT advisers are PSTax.

6. Risk

6.1 Financial risks are closely monitored as a separately identifiable part of the corporate risk management framework. The Council currently has a low risk appetite as a debt free authority that has limited its commercial activity to the investment of surplus cash. The structure of the South Oxhey joint venture was designed to transfer risk to the private sector partner.

6.2 Moving forward the Council is borrowing to finance its capital investment activities and to make loans available to Watford Community homes and Thrive. In respect of these loans they are part of a wider partnership with the local registered social providers and the Council will take security from the proposed developments against the loan values.

6.3 The council currently has an income target of £1.0M pa from its commercial investment activities. This is equivalent to 4.2% of its total gross income (excluding housing benefit reimbursements from government) of £24.0M in 2018/19. The Council does not receive RSG and is entirely dependent upon locally raised taxes and locally generated income to fund services. The general fund balance as at 31st March 2018 was £4.3M.

6.4 Whilst recognising the importance of generating income to support services, the Council will ensure that such activity remains prudent in relation to the future financial sustainability of the council. In this respect it will continue to seek to balance income from its commercial investment activities against its overall level of risk and the amount of reserves available to mitigate this risk.

6.5 In assessing the risk of its commercial investments the Council will consider the level of risk inherent in the income stream, the security held, its ability to realise assets or other security should the need arise and the level of income received from commercial investments compared to the total income of the council.

APPENDIX 1

Medium Term Capital Investment Programme (to be updated at budget setting, currently Q1 monitoring)

Summary - Capital Programme 2018-2021	Forecast Outturn 2019/20 £	Forecast 2020/21 £	Forecast 2021/22 £
Leisure, Environment & Community			
Community Safety & Partnership	44,290	26,000	26,000
Leisure	1,298,584	177,000	221,000
Environmental Services	2,515,116	680,000	1,142,000
Total	**3,857,990**	**883,000**	**1,389,000**
Infrastructure Housing & Economic Development			
Economic Development	747,349	689,140	291,500
Housing	549,339	510,000	510,000
Total	**1,296,688**	**1,199,140**	**801,500**
Policy & Resources			
Resources & Shared Services	2,055,007	962,850	929,850
Total before Major projects	**7,209,685**	**3,044,990**	**3,120,350**
Major Projects			
Leisure Facility - South Oxhey	6,029,328	1,527,943	226,823
South Oxhey Initiative	1,986,876	0	0
Property Investment Board	769,333	0	0
Temporary Accommodation	1,706,116	800,000	0
Total	**10,491,653**	**2,327,943**	**226,823**
TOTAL	**17,701,338**	**5,372,933**	**3,347,173**

APPENDIX 2

SCHEME FOR PRIORITISING CAPITAL BIDS

Criteria	Capital Bids	
	Score	Description
Measure of Quality of Service	3	Maintaining Current Service
	6	Improved Internal Service
	9	Improved External Service
Customer Impact / Quantity of Service	3	Affects < 10% of residents
	6	Affects < 50% of residents
	9	Affects all residents
Links to Strategic Plan	2	Contributes to General Theme
	4	Contributes to General Aim
	6	Contributes to Specific Objective
Impact on Partners (as defined in the Community Strategy)	1	No impact on partner agencies or joint priorities
	2	Impacts on 1 partner agency / priority
	3	Impacts several partners / priorities
Partnership Funding	1	No Partnership Funding
	2	Partly Funded by Partners
	3	Fully Funded by Partners
Equalities	1	No impact on vulnerable groups
	2	Impacts on one vulnerable group
	3	Impacts on several vulnerable groups
Asset Management	1	Not related to asset maintenance
	2	Allowing asset to continue in use
	3	Expenditure required to bring asset up to standard enabling service to continue (i.e. an element of 'backlog' repair exists)
Statutory/Discretionary Service	1	Entirely Discretionary
	2	Partly Statutory
	3	Entirely Statutory
Contractually Committed	1	No Commitment
	2	Moral Obligation (e.g. SLA)
	3	Contractually Committed
Financial Implications	1	Revenue Cost
	2	Revenue Neutral
	3	Revenue Saving
Invest to Save Will the original capital investment be repaid?	6	Return on Investment in 1 Yr
	4	Return on Investment in 3 Yr
	2	Return on Investment in 5 Yr

Appendix 3

Capital Funding 2018-2021

CAPITAL INVESTMENT PROGRAMME 2019-2022 - FUNDING			
	2019/20	2020/21	2021/22
Capital Programme - Services	**Outturn Forecast at P6**	**Forecast**	**Forecast**
	£	£	£
Balance Brought Forward			
Govt Grants: Disabled Facility Grants	(239,088)	(421,908)	(421,908)
Other Contributions: Other external Sources		0	0
Section 106 Contributions	(2,974,426)	(2,920,146)	(1,420,146)
Capital Receipts Reserve	0	(642,260)	(2,097,270)
Future Capital Expenditure Reserve	(2,610,155)	(864,216)	(864,216)
New Homes Bonus Reserve	(4,592,778)	(241,843)	(352,683)
Total Funding Brought Forward	**(10,416,447)**	**(5,090,373)**	**(5,156,223)**
Generated in the Year			
Govt Grants: Disabled Facility Grants	(722,160)	(500,000)	(500,000)
Other Contributions: Other external Sources	0	0	0
Section 106 Contributions	0	0	0
Capital Receipts Reserve	(1,100,000)	(2,500,000)	(1,000,000)
Future Capital Expenditure Reserve	0	0	0
New Homes Bonus Reserve	(317,680)	(110,840)	(110,840)
Total Generated	**(2,139,840)**	**(3,110,840)**	**(1,610,840)**
Use of Funding			
Govt Grants: Disabled Facility Grants	539,340	500,000	500,000
Other Contributions: Other external Sources	0	0	0
Section 106 Contributions	54,280	1,500,000	0
Capital Receipts Reserve	457,740	1,044,990	2,308,650
Future Capital Expenditure Reserve	1,745,939	0	311,700
New Homes Bonus Reserve	4,668,615	0	0
Total Use of Funding	**7,465,914**	**3,044,990**	**3,120,350**
Balance Carried Forward			
Govt Grants: Disabled Facility Grants	(421,908)	(421,908)	(421,908)
Other Contributions: Other external Sources	0	0	0
Section 106 Contributions	(2,920,146)	(1,420,146)	(1,420,146)
Capital Receipts Reserve	(642,260)	(2,097,270)	(788,620)
Future Capital Expenditure Reserve	(864,216)	(864,216)	(552,516)
New Homes Bonus Reserve	(241,843)	(352,683)	(463,523)
Total Funding Carried Forward	**(5,090,373)**	**(5,156,223)**	**(3,646,713)**
South Oxhey Initiative			
Balance Brought Forward	**0**	**0**	**0**
Generated in the Year (Land Receipts)	(3,332,575)	(6,502,792)	(6,502,792)
Generated in the Year (LEP Funding)	0	0	0
Use of Funding (Spend)	1,986,876	0	0
Borrowing	1,345,699	6,502,792	6,502,792
Total	**0**	**0**	**0**
South Oxhey Leisure Facility			
Balance Brought Forward	**0**	**0**	**0**
Use of Funding (Spend)	6,029,328	1,527,943	226,823
Contractor Funded Borrowing	(6,029,328)	(1,527,943)	(226,823)
Total	**0**	**0**	**0**
Property Investment			
Balance Brought Forward	**0**	**0**	**0**
Generated in the Year	0	0	0
Use of Funding (Spend)	769,333	0	0
Capital Receipt	0	0	0
Borrowing	(769,333)	0	0
Total	**0**	**0**	**0**
Temporary Accommodation			
Balance Brought Forward	**0**	**0**	**0**
Generated in the Year	0	0	0
Use of Funding (Spend)	1,449,887	800,000	0
Borrowing	(1,449,887)	(800,000)	0
Total	**0**	**0**	**0**
Total Expenditure Capital Investment Programme	**17,701,338**	**5,372,933**	**3,347,173**

Appendix 4

Cash Flow Forecast

…(to be completed as part of the budget forecast)