

## North East Derbyshire District Council

### Capital Strategy 2019/20 – 2022/23

#### **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.

#### **Capital Expenditure and Financing**

- 1.2 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 assets costing below £10,000 are not capitalised and are charged to revenue in year.

In 2019/20, the Council is planning capital expenditure of £12.1m as summarised below:

**Table 1: Prudential Indicator: Estimates of Capital Expenditure**

	<b>2017/18 Actual £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Budget £m</b>	<b>2020/21 Budget £m</b>	<b>2021/22 Budget £m</b>	<b>2022/23 Budget £m</b>
General Fund services	1.1	2.6	2.0	3.2	3.2	1.2
Council housing (HRA)	14.0	14.4	10.1	9.5	9.5	9.5
Capital investments	0	0	0	0	0	0
<b>TOTAL</b>	<b>15.1</b>	<b>17.0</b>	<b>12.1</b>	<b>12.7</b>	<b>12.7</b>	<b>10.7</b>

- 1.3 The main General Fund capital projects include replacement vehicles, asset refurbishment, ICT replacement and disabled facilities grants.

- 1.4 The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately.
- 1.5 **Governance:** Projects are included in the capital programme as part of the annual budget review or through ad hoc approval during the year. The capital programme is refreshed each year and the new requirements are presented to Cabinet and Council each February. Full details of the Council's Capital Programme can be seen at **Appendix A** to this report.
- 1.6 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing and leasing). The planned financing of the above expenditure is as follows:

**Table 2: Financing of Capital Programme**

	<b>2017/18 Actual £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Budget £m</b>	<b>2020/21 Budget £m</b>	<b>2021/22 Budget £m</b>	<b>2022/23 Budget £m</b>
External sources	1.1	1.5	0.3	0.3	0.3	0.3
Own resources	10.8	12.2	10.2	10.1	10.1	10.1
Debt	3.2	3.3	1.6	2.3	2.3	0.2
<b>TOTAL</b>	<b>15.1</b>	<b>17.0</b>	<b>12.1</b>	<b>12.7</b>	<b>12.7</b>	<b>10.7</b>

- 1.7 Debt is only a temporary source of finance, since loans and leases 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: MRP and Use of Capital Receipts to Repay Existing Debt**

	<b>2017/18 Actual £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Budget £m</b>	<b>2020/21 Budget £m</b>	<b>2021/22 Budget £m</b>	<b>2022/23 Budget £m</b>
Own resources	2.8	1.7	1.9	2.1	2.1	2.1

The Council's full minimum revenue provision statement is **Appendix B** to this report.

- 1.8 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 £9.9m 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**

	<b>31/3/2018 Actual £m</b>	<b>31/3/2019 Forecast £m</b>	<b>31/3/2020 Budget £m</b>	<b>31/3/2021 Budget £m</b>	<b>31/3/2022 Budget £m</b>	<b>31/3/2023 Budget £m</b>
General Fund services	13.1	21.8	21.3	21.7	19.2	20.1
Council housing (HRA)	173.5	174.7	174.5	173.8	173.0	172.3
Capital investments	0	0	0	0	0	0
<b>TOTAL CFR</b>	<b>186.6</b>	<b>196.5</b>	<b>195.8</b>	<b>195.5</b>	<b>192.2</b>	<b>192.4</b>

- 1.9 **Asset management:** The Council's assets require regular maintenance to ensure they remain safe and fit for purpose. It is also important for income generation that assets remain in a good condition and so remain lettable. A planned approach yields savings in running costs and energy efficiency benefits over time as works are completed and asset conditions improve.
- 1.10 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £2.5m of capital receipts in the coming financial year as follows:

**Table 5: Capital receipts**

	<b>2017/18 Actual £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Budget £m</b>	<b>2020/21 Budget £m</b>	<b>2021/22 Budget £m</b>	<b>2022/23 Budget £m</b>
Asset sales	5.1	3.0	2.5	2.5	2.5	2.5
Loans repaid	0	0	0	0	0	0
<b>TOTAL</b>	<b>5.1</b>	<b>3.0</b>	<b>2.5</b>	<b>2.5</b>	<b>2.5</b>	<b>2.5</b>

### **Treasury Management**

- 1.11 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 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.

1.12 Due to decisions taken in the past, the Council currently has £150.8m borrowing at an average interest rate of 3.52% and £24.5m treasury investments at an average rate of 0.51%.

1.13 **Borrowing strategy:** 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 seeks to strike a balance between cheap short-term loans (currently available at around 0.75%) and long-term fixed rate loans where the future cost is known but higher (currently 2-3%).

1.14 Projected levels of the Council's total outstanding debt is shown below, compared with the capital financing requirement:

**Table 6:** Prudential Indicator: Gross Debt and the Capital Financing Requirement

	31/3/2018 Actual £m	31/3/2019 Forecast £m	31/3/2020 Budget £m	31/3/2021 Budget £m	31/3/2022 Budget £m	31/3/2023 Budget £m
Debt	154.1	150.8	149.5	149.2	147.0	146.9
Capital Financing Requirement	186.6	196.5	195.8	195.5	192.2	192.4

1.15 Statutory guidance states 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.

1.16 **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing:

**Table 7:** Borrowing and the Liability Benchmark

	31/3/2018 Actual £m	31/3/2019 Forecast £m	31/3/2020 Budget £m	31/3/2021 Budget £m	31/3/2022 Budget £m	31/3/2023 Budget £m
Outstanding borrowing	154.1	150.8	149.5	149.2	147.0	146.9
Liability benchmark	150.4	150.3	149.5	149.3	147.0	147.0

1.17 The table above shows that the Council expects to remain borrowed above or at its liability benchmark. This is because cash outflows to date have been below the assumptions made when the loans were borrowed

1.18 **Affordable borrowing limit:** 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.

**Table 8:** Prudential Indicators: Authorised limit and operational boundary for external debt

	2018/19 limit £m	2019/20 limit £m	2020/21 limit £m	2021/22 limit £m	2022/23 limit £m
Authorised limit – total external debt	206.5	205.8	205.4	202.2	202.4
Operational boundary – total external debt	201.5	200.8	200.4	197.2	197.4

1.19 **Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

1.20 The Council’s policy on treasury investments is to prioritise security and liquidity over yield. That is 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 bonds, shares and property, 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 9:** Treasury management investments

	31/3/2018 Actual £m	31/3/2019 Forecast £m	31/3/2020 Budget £m	31/3/2021 Budget £m	31/3/2022 Budget £m	31/3/2023 Budget £m
Near-term investments	13.8	10.6	10.0	10.0	10.0	10.0
Longer-term investments	0	0	0	0	0	0
<b>TOTAL</b>	<b>13.8</b>	<b>10.6</b>	<b>10.0</b>	<b>10.0</b>	<b>10.0</b>	<b>10.0</b>

- 1.21 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Chief Finance Officer and staff, who must act in line with the treasury management strategy approved by Council. Quarterly reports on treasury management activity are presented to Cabinet. The Audit and Corporate Governance Scrutiny Committee is responsible for scrutinising treasury management decisions.

### **Investments for Service Purposes**

- 1.22 The Council can make investments to assist local public services, including making loans to local service providers and businesses to promote economic growth. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to at least break even after all costs. This includes loans to the Council's ALMO, Rykneld Homes Ltd to allow development of social housing. Rykneld homes Ltd is a wholly owned subsidiary of the Council, limited by guarantee.
- 1.23 **Governance:** Decisions on service investments are made by the relevant service manager and submitted to Cabinet then Council in consultation with the Chief Finance Officer and must meet the criteria and limits laid down in the Investment Strategy.

### **Commercial Activities**

- 1.24 With central government financial support for local public services declining, the Council plans to invest in developing residential property through Northwood Group Ltd mainly for financial gain. An initial investment of £0.15m has been made into Northwood Group Ltd and further future investment of £8.7m is approved.
- 1.25 With financial return being the main objective, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include build cost estimates, sales values estimates and demand. These risks are mitigated by working with experienced builders and professionals who have knowledge of the local market. In order that commercial investments remain proportionate to the size of the Council, these are subject to an overall maximum investment limit of £8.7m and contingency plans are in place should expected yields not materialise.
- 1.26 **Governance:** Decisions on commercial investments are made by Council in line with the criteria and limits approved in the Investment Strategy.
- 1.27 The Council also has investment properties generating £0.4m in net income a year after all costs.

## **Liabilities**

- 1.28 In addition to debt of £154m detailed above, the Council is committed to making future payments to cover its net pension fund deficit (valued at £48m). It has also set aside £1.6m to cover risks of business rates appeals.
- 1.29 **Governance:** Decisions on incurring new discretionary liabilities are taken to Council for approval. The risk of liabilities occurring and requiring payment are monitored as part of the year-end process.

## **Revenue Budget Implications**

- 1.30 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 10: Prudential Indicator: Proportion of financing costs to net revenue stream**

	<b>2017/18 Actual £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Budget £m</b>	<b>2020/21 Budget £m</b>	<b>2021/22 Budget £m</b>	<b>2022/23 Budget £m</b>
Financing costs	1.1	1.1	1.0	0.8	0.8	0.9
Proportion of net revenue stream	8.24%	8.25%	7.2%	6.1%	6.3%	7.1%

- 1.31 **Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Chief Finance Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable.

## **Knowledge and Skills**

- 1.32 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Suitably qualified and experienced officers are employed throughout the Council to perform such functions.
- 1.33 Where Council officers do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers. 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.

- 1.34 Members receive individual training and development through the Member Development Programme and are periodically required to attend seminars held by the external treasury management advisors.

### **Treasury Management Operations**

- 1.35 As mentioned above the Council uses external treasury management advisors. The company provides a range of services which include:
- Technical support on treasury matters, capital finance issues and the drafting of Member reports;
  - Economic and interest rate analysis;
  - Debt services which includes advice on the timing of borrowing;
  - Debt rescheduling advice surrounding the existing portfolio;
  - Generic investment advice on interest rates, timing and investment instruments;
  - A number of places at training events offered on a regular basis.
  - Credit ratings/market information service comprising the three main credit rating agencies;
- 1.36 Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remains with the Council. This service is subject to regular review. It should be noted that the Council has Arlingclose Ltd as external treasury management advisors, for a period of 3 years commencing October 2016.

### **Banking Contract**

- 1.37 The contract with the Councils banking provider Lloyds Bank commenced on the 10<sup>th</sup> February 2015 for a period of 7 years.

### **Business Continuity Arrangements**

- 1.38 As part of the Councils business continuity arrangements officers have sought to set up and provide alternative banking arrangements for the Council should they be required at short notice. These arrangements effectively mean a separate bank account is in place with the required security controls and appropriate officer access to undertake transactions. This account is with Barclays Bank and will only be utilised should a business continuity need or similar issue arise. Officers will continue to review this arrangement.



# Appendix A

## Capital Programme 2018-2023

Capital Expenditure	Revised Budget 2018/19 £	Original Budget 2019/20 £	Original Budget 2020/21 £	Original Budget 2021/22 £	Original Budget 2022/23 £
<b>Housing Revenue Account</b>					
HRA Capital Works	9,606,000	9,000,000	9,000,000	9,000,000	9,000,000
Demolition of Houses in Renishaw	30,000	0	0	0	0
EWI Scheme - Grassmoor	395,000	0	0	0	0
Pine View, Danesmoor	300,000	600,000	0	0	0
North Wingfield New Build Scheme	1,977,000	0	0	0	0
Stock Purchase Programme (1-4-1)	1,482,000	0	0	0	0
Acquisitions and Disposals (RHL)	560,000	500,000	500,000	500,000	500,000
Car Park Resurfacing - Holmesfield	40,000	0	0	0	0
Car Park Resurfacing - Pilsley	0	40,000	0	0	0
<b>HRA - Capital Expenditure</b>	<b>14,390,000</b>	<b>10,140,000</b>	<b>9,500,000</b>	<b>9,500,000</b>	<b>9,500,000</b>
<b>General Fund</b>					
Private Sector Housing Grants (DFG's)	689,487	393,000	393,000	393,000	393,000
ICT Schemes	109,000	159,508	45,500	24,800	100,000
Clay Cross Football Pitch	10,554	0	0	0	0
Asset Refurbishment - General	150,000	500,000	500,000	500,000	500,000
Roller Shutter Doors	82,000	0	0	0	0
Eckington Pool Roof Replacement	270,000	0	0	0	0
Eckington Pool Refurbishment	32,000	0	0	0	0
Leisure Centre Kit Replacement	106,243	0	0	0	0
Replacement of Vehicles	1,138,000	982,500	2,245,000	2,256,000	226,000
Contaminated Land	42,001	0	0	0	0
<b>General Fund Capital Expenditure</b>	<b>2,629,285</b>	<b>2,035,008</b>	<b>3,183,500</b>	<b>3,173,800</b>	<b>1,219,000</b>
<b>Total Capital Expenditure</b>	<b>17,019,285</b>	<b>12,175,008</b>	<b>12,683,500</b>	<b>12,673,800</b>	<b>10,719,000</b>
<b>Capital Financing</b>	<b>2018/19</b>	<b>2019/20</b>	<b>2020/21</b>	<b>2021/22</b>	<b>2022/23</b>
<b>Housing Revenue Account</b>					
Major Repairs Reserve	(9,536,000)	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)
Prudential Borrowing - HRA	(1,942,000)	(600,000)	0	0	0
External Grant - HCA	(730,000)	0	0	0	0
Development Reserve	(1,146,000)	(40,000)	0	0	0
Capital Receipts Reserve	(591,400)	(500,000)	(500,000)	(500,000)	(500,000)
1-4-1 Receipts	(444,600)	0	0	0	0
<b>HRA Capital Financing</b>	<b>(14,390,000)</b>	<b>(10,140,000)</b>	<b>(9,500,000)</b>	<b>(9,500,000)</b>	<b>(9,500,000)</b>
<b>General Fund</b>					
Disabled Facilities Grant	(669,487)	(373,000)	(373,000)	(373,000)	(373,000)
External Grant - Lottery Funded Schemes	(10,554)	0	0	0	0
External Grant - Contaminated Land	(42,001)	0	0	0	0
Prudential Borrowing - Vehicles	(1,138,000)	(982,500)	(2,245,000)	(2,256,000)	(226,000)
Prudential Borrowing - Eckington Pool Roof	(270,000)	0	0	0	0
RCCO - SPLC	(11,300)	0	0	0	0
RCCO - Roller Shutter Doors	(82,000)	0	0	0	0
RCCO - Vehicles	(61,220)	(35,739)	0	0	0
Useable Capital Receipts	(344,723)	(643,769)	(565,500)	(544,800)	(620,000)
<b>General Fund Capital Financing</b>	<b>(2,629,285)</b>	<b>(2,035,008)</b>	<b>(3,183,500)</b>	<b>(3,173,800)</b>	<b>(1,219,000)</b>
<b>HRA Development Reserve</b>					
Opening Balance	(1,480,718)	(1,264,302)	(1,986,105)	(2,854,051)	(4,012,726)
Amount due in year	(929,584)	(761,803)	(867,946)	(1,158,675)	(2,229,900)
Amount used in year	1,146,000	40,000	0	0	0
<b>Closing Balance</b>	<b>(1,264,302)</b>	<b>(1,986,105)</b>	<b>(2,854,051)</b>	<b>(4,012,726)</b>	<b>(6,242,626)</b>
<b>Major Repairs Reserve</b>					
Opening Balance	(825,921)	(219,921)	(219,921)	(219,921)	(219,921)
Amount due in year	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)	(9,000,000)
Amount used in year	9,606,000	9,000,000	9,000,000	9,000,000	9,000,000
<b>Closing Balance</b>	<b>(219,921)</b>	<b>(219,921)</b>	<b>(219,921)</b>	<b>(219,921)</b>	<b>(219,921)</b>
<b>Capital Receipts Reserve</b>					
Opening Balance	(1,970,251)	(1,134,128)	(1,490,359)	(1,924,859)	(2,380,059)
Income expected in year	(2,000,000)	(2,500,000)	(2,500,000)	(2,500,000)	(2,500,000)
Allowable Debt/Pooling Expenses	1,900,000	1,000,000	1,000,000	1,000,000	1,000,000
Amount used in year	936,123	1,143,769	1,065,500	1,044,800	1,120,000
<b>Closing Balance</b>	<b>(1,134,128)</b>	<b>(1,490,359)</b>	<b>(1,924,859)</b>	<b>(2,380,059)</b>	<b>(2,760,059)</b>
<b>Capital Receipts Reserve 1-4-1 receipts</b>					
Opening Balance	(2,870,660)	(3,426,060)	(3,426,060)	(3,426,060)	(3,426,060)
Income expected in year	(1,000,000)	0	0	0	0
Amount used in year	444,600	0	0	0	0
<b>Closing Balance</b>	<b>(3,426,060)</b>	<b>(3,426,060)</b>	<b>(3,426,060)</b>	<b>(3,426,060)</b>	<b>(3,426,060)</b>
<b>Total Capital Financing</b>	<b>(17,019,285)</b>	<b>(12,175,008)</b>	<b>(12,683,500)</b>	<b>(12,673,800)</b>	<b>(10,719,000)</b>

## Appendix B

### Annual Minimum Revenue Provision Statement 2019/20

Where the Council finances General Fund capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Authority to have regard to the Ministry for Housing, Communities and Local Government's *Guidance on Minimum Revenue Provision* (the MHCLG Guidance) most recently issued in 2018.

The broad aim of the MHCLG Guidance is to ensure that capital expenditure is financed over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government, Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The MHCLG Guidance requires the Council, to approve an Annual MRP Statement each year, and includes recommendations for calculating a prudent amount of MRP. In line with this guidance the Council has adopted the following:

- For capital expenditure incurred before 1<sup>st</sup> April 2008 MRP will be determined in accordance with the former regulations. A sum of £0.2m is set aside each year.
- For capital expenditure incurred after 31<sup>st</sup> March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments, starting in the year after the asset becomes operational.

Capital expenditure incurred during 2019/20 will not be subject to a MRP charge until 2020/21 and so on.

Based on the Council's latest estimate of its Capital Financing Requirement on 31<sup>st</sup> March 2019, the budget for MRP has been set as follows:

	<b>31/03/19 Estimated CFR £m</b>	<b>2019/20 Estimated MRP £m</b>
Capital expenditure before 01.04.2008	2.1	0.2
Supported capital expenditure after 31.03.2008	0	0
Unsupported capital expenditure after 31.03.2008	19.7	1.0
<b>Total General Fund</b>	<b>21.8</b>	<b>1.2</b>
Assets in the Housing Revenue Account	47.6	0
HRA subsidy reform payment	127.1	0
<b>Total Housing Revenue Account</b>	<b>174.7</b>	<b>0</b>
<b>Total</b>	<b>196.5</b>	<b>1.2</b>

#### Housing Revenue Account (HRA)

Following the budget on 30 October 2018, the legislation that capped the amount of HRA debt a local housing authority could hold was revoked with immediate effect. The capital financing requirements relating to the HRA will remain the same so there will still be no requirement for an MRP and levels of debt will be managed through prudential borrowing limits controlled by the Treasury Management Strategy.

Removing the debt cap and not having a statutory requirement to make a provision to repay debt presents a significant risk to the HRA. Very careful treasury management is needed to ensure that the Council's HRA borrowing remains affordable, prudent and reasonable and that the HRA remains sustainable over the long term. Provision is being made within the HRA to set aside amounts that will repay the loans borrowed as part of the 2012 Self Financing Settlement as resources allow.