Appendix 1

Blackburn with Darwen Borough Council

Capital Strategy

2020/21 to 2022/23

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Appendix 1

Contents

1 Background

The Capital Strategy forms a key part of the Council's overall Corporate Budget Planning and provides a mechanism by which capital expenditure and investment decisions are aligned over the medium to long-term period.

The Council prepared a Capital Strategy for the first time in 2019/20, following the release of the updated *Prudential Code for Capital Finance in Local Authorities* by the Chartered Institute of Public Finance and Accountancy (CIPFA) in December 2017.

This Strategy sets out the framework for all aspects of the Council's capital and investment expenditure including prioritisation, governance, funding and monitoring and risk management, and maintains links to other key strategic documents, notably the Treasury Management Strategy and Medium Term Financial Strategy.

2 Aims of the Capital Strategy and its links to the Council's Corporate Plan

The aim of this Strategy is to ensure that the Council has overall long-term policy objectives in this area, resulting in the identification of capital strategy requirements, governance procedures and clarity in its risk appetite.

The capital strategy gives a high-level overview of how the Council's capital expenditure, capital financing and treasury management activity contribute to the provision of local public services, along with an overview of how associated risks are managed, and the implications for future financial sustainability.

Capital investment plans are driven by the Council's Corporate Plan. The Corporate Plan was agreed by elected members in March 2019 and is the Council's key strategic document. The Corporate Plan 2019-2023 sets out the Council's core priorities and ambitions for the next 4 years. The Council's plan has eight strategic priorities:

- **People:**
  - Supporting young people and raising aspirations
  - Safeguarding and supporting the most vulnerable people
  - Reducing health inequalities and improving health outcomes
- **Place:**
  - Connected communities
  - Safe and clean environment
- **Economy:**
  - Strong, growing economy to enable social mobility
  - Supporting our town centres and businesses
- **Council:**
  - Transparent and effective organisation

3 Capital spending priorities and governance

The key principles for the Council's 2020-2023 capital programme are summarised below:

- Capital investment decisions reflect the aspirations and priorities included within the Corporate Plan and supporting strategies.
- Schemes to be added to the capital programme will be evaluated and prioritised by senior management prior to Executive Board / Executive Member approval.
- The full cost of any capital scheme must be established at the outset, including any financing costs and future revenue operational costs.
- Commissioning and procuring of capital schemes will comply with the requirements set out in the Council's constitution and financial regulations/ contract procurement rules.

The Council prepares its capital programme on a 3 year rolling basis, which is approved annually by Finance Council. Quarterly monitoring and outturn reports are considered by Executive Board during the financial year.

The Council's capital investment priorities for 2020/21 include:

- Transforming our systems to offer digital solutions which improve customer satisfaction by ensuring all services where appropriate are able to be accessed digitally, and to allow the Council to operate as efficiently as possible.
- Delivering the growth plan priorities of Industry and Gateways; Town Centre; and Housing.
- Maintaining and improving our highways to support economic growth and improve the connectivity of transport networks.
- Developing commercial floor space and priority housing sites.

Local Plan 2018 to 2037

The Council is currently in the process of reviewing its Local Plan and expects the new plan, which will cover the period 2018 to 2037, to be submitted for consideration and approval in September 2021.

A number of studies have been conducted as part of this review, which highlighted some of the priority investment areas identified above:

- <u>Industry</u>

  The Council undertook an Employment Land Study Review in May 2019, looking at current business premises within the Borough, the projection of future need over the life of the Local Plan and the areas identified as potential sites to contribute towards fulfilling this identified need. This highlighted a requirement for additional industrial properties over the period, with the current demand being mainly for units sub-500sqm.

  The Council has a portfolio of industrial, retail and office properties, but will continue looking at opportunities for new developments to meet the future demand within the Borough.

- <u>Housing</u>

  In December 2018 the Council commissioned a Housing and Economic Need Assessment, which looked at the future development needs for housing and employment across the Borough. This identified a need for additional housing of differing size and tenure within the Borough over the period of the Local Plan, and also highlighted the fact that the forecast requirement exceeds the historic level of new houses delivered annually.

  Over recent years a number of new developments have started within the Borough, contributing towards fulfilling the need for residential housing in the area. The Council's Growth and Development team continue to work to identify potential sites for future developments, however the majority of this work does not fall within the Council's own capital programme.

  Currently around 5% of the total residential housing stock in the Borough is empty, with 13% of properites having stood empty for over 2 years. Empty properties in the borough can have negative environmental impact on neighbourhoods, in addition to being a wasted housing resource. Tackling empty properties supports the key priorities in the Council's Corporate Plan and the Empty Property Strategy. The Council currently has a Neighbourhood Intervention Project as part of the capital programme, which can be used to bring long-term empty properties back into use in cases where the owners have not done so themselves. This project will continue, and has the potential to grow, over the coming years.

Schools

As a result of new housing developments completed within the Borough, and those in the pipeline for the coming years, there is a need for additional school places in certain areas of Blackburn with Darwen, to meet the higher demand.

The Council has a Growth Education Board who meet regularly to review such matters and discuss potential sites for investment in creating new school places.

Pennine Gateways – Transport Infrastructure Growth Deal

The Pennine Gateways project, funded through the Lancashire Growth Deal, will deliver key transport infrastructure improvements at three of the main gateways into Blackburn with Darwen off the M65 motorway.

Investment at these adjoining gateways will extend the concept of the Hyndburn – Burnley – Pendle Growth Corridor to the M65 Growth Corridor and will release the potential of a number of adjacent strategic sites to attract and accelerate new development opportunities.

Major transport improvements will act as a catalyst for new housing and commercial development, contributing to the delivery of the Council's adopted Local Plan targets for new homes, businesses and jobs.

Continued Town Centre Development

There are a number of capital projects already ongoing within the town centre, which will continue to be supported into 2020/21 including:

- Cinema development
- Blakey Moor regeneration

There is a requirement for the continued funding of existing programmes of work on:

- Social Care (including an ongoing programme to provide aids and adaptations)
- Schools
- Environmental Services (Land Remediation Scheme)
- Growth and Development Projects (including Blakey Moor Renovation, LTP Corridors and Cinema Leisure Development)
- Development of the ICT Strategy
- Progression of the Corporate Accommodation Strategy

In addition to the projects referred to above, funding may be required in respect of further/new projects including:

- Low Carbon and Energy Efficiency Initiatives
- School Investment/ Pupil Places Pressures
- Housing Initiatives
- Transport and Highways
- Fleet Management

Further details of the Council's Capital Programme is included within the *Revenue Budget 2020/21, Medium Term Financial Strategy and Capital Programme 2020-2023 Report* which is on the agenda of this meeting.

4 Capital Expenditure

Capital expenditure is spending on assets such as property or vehicles that will be used for more than one year. In local government this includes spending by the Local Authority on assets owned by other bodies, and loans and grants made by the Local Authority to other bodies enabling them to buy assets. The Council has some limited discretion on what is deemed to be capital expenditure, for example assets costing below £10,000 are not capitalised and are instead charged to revenue in the year the expenditure is incurred.

For details of the Council's Capitalisation Policy, see **Appendix 2**.

In 2020/21, the Council is planning capital expenditure of £39.9 million, as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
Portfolio spending	20.4	28.9	33.9	9.4	8.7
Earmarked schemes	0	1.7	6.0	1.5	1.5
Contingent schemes	0	0	0	1.5	1.5
Total Capital Programme	**20.4**	**30.6**	**39.9**	**12.4**	**11.7**

Further analysis of planned capital expenditure by portfolio can be found in **Appendix 3.**

5 Capital Financing (Including MRP)

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, leasing and Private Finance Initiative). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
External sources	13.1	17.5	23.8	9.2	8.5
Own resources	0.7	1.3	0.3	0	0
Debt	6.6	11.8	15.8	3.2	3.2
Total capital financing	**20.4**	**30.6**	**39.9**	**12.4**	**11.7**

Debt is only a temporary source of finance, since loans and leases must be repaid; these repayments must be financed over time, 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. The Council's planned MRP and use of capital receipts is as follows:

Table 3: Forecast MRP and Use of Capital Receipts To Repay Debt in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
Capital Receipts To Repay Debt	2.7	3.5	4.2	5.0	3.4
MRP	6.2	6.5	7.1	7.5	7.9

The Council's policy for setting a "prudent" level of Minimum Revenue Provision for the repayment of debt, must be consistent with the Council's Medium Term Financial Strategy, and can be found at **Appendix 4.**

The Council's cumulative outstanding amount of debt finance is measured by the Capital Financing Requirement (CFR):

- this increases as new debt-financed capital expenditure is incurred, and
- reduces as MRP increases and as capital receipts are used to replace debt.

The table below shows that the CFR is expected to increase by £7.9 million during 2020/21. 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 £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
General Fund services	212.3	214.6	223.0	214.3	206.6
Debt managed by LCC	15.6	15.3	15.0	14.6	14.3
PFI projects	69.7	69.5	69.3	69.1	68.9
Total CFR	**297.6**	**299.4**	**307.3**	**298.0**	**289.8**

The capital financing requirement for 2020/21 and subsequent years includes a £5.0 million increase due to a change in the accounting for leases. This is an estimate based on latest information and will be amended as more information becomes available.

6 Asset management

To ensure that capital assets continue to be of long-term use, the Council has an Asset Management Plan in place. This ensures that land and property assets support the aims and objectives of the Council and its key services. In particular, the plan aims to:

- Enable the Council to understand the scope of its property and land assets portfolio i.e. location, suitability, condition and value.
- Maximise the beneficial and efficient use of property and land assets.
- Encourage the regular review and challenge of the continued use and ownership of property and land assets to ensure they are still delivering a rate of return and are fit for purpose.
- Ensure that buildings are properly maintained.

Asset Management Plans are normally produced every 3 to 5 years; the plan produced in 2015/16 is now in the process of review and development and will be published during 2020/21.

The Council's Asset Management Group acts as a strategic steering group, which formulates and reviews the aims and objectives of the Asset Management Plan. The group works with the Corporate Finance team in overseeing the Capital Expenditure and Capital Receipts programmes.

In line with the Council's Corporate Plan and Growth Agenda, a Development Growth Board has been developed to run alongside and support the Asset Management Plan.

The Council's Highways Asset Management Strategy was revised in July 2019. This document describes the Council's strategy for the management of its highway assets, considering long-term needs as well as the short-term position to address maintenance requirements. The objectives of this strategy are:

- To direct investment in the highway related assets on the basis of 'prevention is better than cure', having consideration to the Council's priorities, risk and the current condition of the assets.
- To improve the overall condition and explore the most cost effective maintenance treatments, based on the whole life of the assets.
- To facilitate the development of cost-effective forward works programmes over a number of years based upon the principles of life cycle planning.
- To ensure the Council adheres to its duty of care under the Highways Act 1980.

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7 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 may be used to repay debt. At present the Council also has the authority to spend capital receipts on the revenue costs of service transformation projects until 2021/22, following a Government capitalisation direction giving all councils more flexibility in their use of capital receipts.

Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £4.2 million of capital receipts in the coming financial year as follows:

Table 5: Capital receipts in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	Future years budget
Asset sales	2.7	3.5	**4.2**	**5.0**	**33.3**
Loans repaid	0	0.0	0.0	0.0	0.0
Total Capital Receipts	**2.7**	**3.5**	**4.2**	**5.0**	**33.3**

The Council plans to continue to utilise all of the capital receipts generated from the disposal of land and property in support of the Minimum Revenue Provision i.e. to repay debt.

Further details of planned asset disposals, together with the Council's Flexible Use of Capital Receipts Policy are detailed in **Appendix 3.**

8 Treasury management

The Council produces a Treasury Management Strategy, which is approved annually by the Executive Board.

The Capital Strategy and Treasury Management Strategy are closely linked as the capital programme determines the borrowing need for the Council. This is part of the long term cash flow planning to ensure that the Council can meet its capital spending requirements.

Treasury management is concerned with keeping sufficient but not excessive cash balances available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash is met through borrowing; this avoids excessive credit balances or overdrafts in the bank current account.

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 low-cost short-term loans and long-term fixed rate loans, where the future cost is known but is higher.

Projected levels of the Council's total outstanding debt (which comprises borrowing, PFI liabilities, and transfers from local government reorganisation) are shown below, compared with the capital financing requirement (see above).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
Debt (including PFI and LCC debt)	277.1	307.5	300.9	279.6	268.3

Capital Financing Requirement	297.6	299.4	307.3	298.0	289.8

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. The Council expects debt to be in excess of the capital financing requirement temporarily at the end of 2019/20, this is due to slippage on some capital schemes, and additional borrowing required for the advance payment of pension costs in April 2020. However, as can be seen from Table 6, the Council expects to comply with this guidance during 2020/21. The effects of the advance payment of pension costs will cease by the end of 2022/23, at which point debt is anticipated to return to normal levels, when compared to the capital financing requirement.

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 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £ millions

	2019/20 limit	2020/21 limit	2021/22 limit	2022/23 limit
Authorised limit - borrowing	250.8	286.0	265.5	244.0
Authorised limit – PFI and LCC debt	85.3	84.8	84.3	83.8
Authorised limit – total external debt	336.1	370.8	349.8	327.8
Operational boundary - borrowing	240.8	276.0	255.5	234.0
Operational boundary – PFI/LCC debt	85.3	84.8	84.3	83.8
Operational boundary – total external debt	326.1	360.8	339.8	317.8

The authorised limit and operational boundary are calculated based on the projected capital financing requirement of the Council and an allowance for other short-term borrowing needs.

The authorised limit and operational boundary for 2020/21 and subsequent years include a £5.0 million increase due to a change in the accounting for leases. This is an estimate based on latest information and will be amended once further information becomes available.

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

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 could be 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 if required.

Risk management: The effective management and control of risk are prime objectives of the Authority's treasury management activities. The treasury management strategy therefore sets out various indicators and limits to mitigate the risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.

Governance: Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Finance and Customer Services and staff within the Finance Team, who must act in line with the Treasury Management Strategy approved by Executive Board each year. A regular officer group (Treasury Management Group) also reviews treasury management activity and operational decisions. Quarterly reports on treasury management activity are presented to the Audit and Governance Committee, which is responsible for scrutinising treasury management decisions.

Further details of the Council's borrowing and treasury investments can be found in the Treasury Management Strategy which is to be presented to Executive Board for approval on 12 March 2020.

9 Other investment and long term liabilities

In addition to the treasury investments referred to in the section above, the Council may also make loans and investments for service purposes, and may purchase and maintain property for investment purposes. The Investment Strategy included at Appendix 6 focuses on these other, non-treasury investments.

Service investments

These investments, including loans and shareholdings, are made for their contribution toward service delivery objectives. For example, the Council could advance relatively small loans to local businesses and local residents for community and economic benefits. In light of the public service objective, the Council is willing to take more risk in making service investments than it is with treasury investments, however it still aims for such investments to contribute to its corporate priorities.

The Council has entered into joint ventures and partnerships previously, which have resulted in ownership of shares in the companies set up to deliver the objectives of these projects. These have included Building Schools for the Future – Private Finance Initiatives and joint ventures with development companies. These are held as long-term investments for the Council, but with the primary objective being their contribution towards service delivery.

Governance: Decisions on service investments are made by the Director of Finance and Customer Services / the Executive Member for Finance and Governance / the Executive Board, in line with the Council's constitution. Most loans and shares are capital expenditure and purchases will therefore be approved as part of the capital programme.

Commercial investments

Historically, the Council has invested in commercial property, largely for regeneration purposes, but has also received financial gain in the form of rental income.

As there are financial and wider economic returns, the Council accepts higher risk on commercial investment than on treasury investments. The principal risk exposures include: vacancies, rent arrears and a fall in capital value. These risks are managed by the Council's Asset Management Group as part of their regular review of the continued ownership of property and land assets to ensure they are still delivering a rate of return and are fit for purpose.

Governance: Decisions on commercial investments are made by the Director of Growth and Development / the Executive Member for Finance and Governance / the Executive Board in line with the Council's constitution. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme.

Further details on service and commercial investments are included in the Investment Strategy in **Appendix 6.**

Liabilities

In addition to the debt detailed in Table 6 above, the Council is committed to making future payments to cover its pension fund deficit (valued at £269.165 million at 31st March 2019), and other liabilities arising from the Council's PFI contracts under the Building Schools for the Future programme (£65.130 million at 31st March 2019). It has also set aside £3.052 million to cover risks in relation to:

- Backdated appeals against the rateable value of business ratepayers (£1.673 million)
- Injury and damage compensation claims (£0.979 million)
- The aftercare costs for closed landfill sites (£0.400 million)

The Council is also at risk of having to settle additional insurance claims, not provided for in the list above, in relation to the "Scheme of Arrangement" between local authorities and the administrators of Municipal Mutual Insurance. The Council has not put aside any funds for this purpose because the potential liability is less certain and the amount cannot be measured reliably. It does, however, disclose this item as a “contingent liability” in the Statement of Accounts.

Governance: Decisions on incurring new discretional liabilities are taken by service managers in consultation with the Director of Finance and Customer Services. The risk of liabilities crystallising and requiring payment is monitored by the Finance Team together with budget holders, and significant potential liabilities are reported quarterly to Executive Board within the quarterly Corporate Budget Monitoring reports.

10 Revenue budget implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP repayments are charged to revenue, offset by any investment income receivable. The net annual charge is known as the Financing Cost; within the Prudential Indicators, this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

Table 8: Prudential Indicator: Proportion of financing costs to net revenue stream

	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
Main Programme capital financing costs as a proportion of Net Revenue Stream	9.15%	9.30%	9.56%	9.77%
BSF PFI capital financing costs as a proportion of Net Revenue Stream	4.61%	4.38%	4.32%	4.28%
Prudential Indicator for ratio of financing costs to Net Revenue Stream	**13.76%**	**13.68%**	**13.88%**	**14.05%**

Further details on the revenue implications of capital expenditure can be found within the *Revenue Budget 2020/21, Medium Term financial Strategy and Capital Programme 2020-2023* report which is on the agenda of this meeting

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 Director of Finance and Customer Services is satisfied that the proposed capital programme is prudent, affordable and sustainable as set out in the *Robustness of the 2020/21 Budget and the Recommended Level of Reserves* report which is on the agenda of this meeting.

11 Knowledge and skills

The Council's approach to ensuring that the requisite knowledge and skills are held and demonstrated when making capital expenditure, borrowing and investment decisions, includes:

- Employment of professionally qualified and experienced staff in senior positions with responsibility for making decisions.
- Training for council members to aid informed decision making and effective scrutiny.
- Engagement of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers, and other appropriate advisors as required.

The intention is that by building a solid knowledge base for both Officers and Members, they are fully informed when taking decisions to realise corporate objectives. Specialist support from external advisors strengthens the decision making process and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

12 Prudential indicators

The Prudential Code provides a framework to ensure that the capital investment plans of the Council are affordable, prudent and sustainable. The Prudential Indicators required by the Prudential Code are designed to support and record local decision making in a manner that is publicly accountable. They are not designed to be comparative performance indicators, and should be considered in parallel with the Treasury Management Indicators required by the CIPFA *Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes*.

In setting or revising its Prudential Indicators, the Council must have regard to the following matters:

- service objectives – alignment with the Council's strategic plan
- stewardship of assets – asset management planning
- value for money – option appraisal
- prudence and sustainability – risk and implications for external debt and whole life costing
- affordability – the amount of money the Council can afford to borrow and the impact on revenue budgets

Although a number of Prudential Indicators have been referred to already in the body of this report, the full list of indicators is detailed in **Appendix 5**.