Capital Strategy

Havant Borough Council

2022/23 to 2026/27

Introduction

The Capital Investment Strategy is a key policy document for the Council and a key component of the Council's Medium Term Financial Strategy which itself forms part of the overall corporate planning framework. It provides the mechanism by which the Council's capital investment and financing decisions are aligned with the Council's overarching corporate priorities. The Capital Strategy follows guidance included in the Prudential Code (2021) and is required to be approved by Full Council.

The document sets the framework for all aspects of the Council's capital expenditure, including planning, funding, management, monitoring and reporting. The strategy links to the Council's Asset Management Plan and Procurement Strategy and incorporates the approaches to commercial investment and treasury management. Crucially, it links capital decisions to the medium-term impact on revenue budgets to ensure that the authority maintains good capital health and that investment plans are affordable both now and in the future.

Although primarily a financial document which seeks to secure long term sustainability and resilience, this Strategy also focusses on the delivery of the outcomes and projects set out in the Council's corporate plan. This will be achieved through the development of business cases which will set out success measures that meet corporate priorities, capture social, economic, and environmental well-being improvements alongside well-developed financial assessments.

Like all district councils, the revenue budget will in the medium term continue to experience significant pressure from anticipated funding reductions and demand pressures. Capital decisions impact on the revenue budget via the costs of capital financing in addition to ongoing revenue costs upon completion of capital schemes. It will be important that any such costs are recognised in the revenue budget and where possible set against income which is generated from the same schemes. Whilst schemes will be prioritised based upon an assessment of outcomes and costs, it will be necessary to ensure that the capital programme makes a positive overall financial contribution to the Council's medium term revenue position.

With the above in mind, the Strategy incorporates processes for the acquisition and subsequent management of commercial properties which should provide a net revenue income. Its is acknowledged that commercial investment is a riskier activity, and this strategy sets out how those risks will be managed, monitored and reported.

The Council's policy on capitalisation is included in the Accounting Policies of the

Statement of Accounts. The policy states that only assets with a value over £15,000 will be capitalised and therefore expenditure under these limits is deemed to be a revenue cost.

1. THE CAPITAL INVESTMENT STRATEGY

Aims of the Strategy:

1.1 To understand our capital health now and into the future

The strategy will provide a continuous assessment of the Council's capital health focussing on our borrowing, both in the context of gearing (our loans as a proportion of underpinning asset values) and of revenue costs, which includes loan interest and the setting aside of resources to repay loans (known as MRP). The strategy will set out a number of key measures which focus on strong and improving capital health with sector benchmarks.

1.2 Focus on Outcomes

Consolidation of existing portfolio as well as acquisition of commercial property investments which deliver a financial return to the Council both in terms of support to the revenue budget as well as capital appreciation.

Development of other corporate priorities; housing, regen, green technology etc all of which should have targeted yield rates.

Taking all of the above together, to develop a Capital Programme from 2022/23 to 2027/28 which both covers capital financing costs and sets out an agreed annual contribution to the revenue budget and a significant impact on the Council's revenue structural budget gap.

1.3 Focus on Processes

- The Capital Investment Strategy (section 1).
- The Financial Plan (section 2).
- Business Cases (section 3).
- Outcome Based Measures and Targets (section 4).
- Risk Management (Section 5).
- Prudential Framework and Investment Guidance (Section 6)
- Capacity Skills (Section 7).
- Governance arrangements (Section 8).
- Performance management arrangements (Section 9).

1.4 The Capital Strategy must both support and inform the Council's vision for the Havant Borough area and the strategic direction set out in the Corporate Strategy. This is to enable resources to be matched against the agreed priorities and any other supporting needs.

1.5 The Capital Strategy takes account of other Council Plans and Strategies of the Council, which have a potential impact on the use of resources by the Council. Particularly consideration is given to the following key strategies:

- The Medium Term Financial Strategy, which provides information on the proposed revenue budget and considerations that will impact on future budgets.
- The Treasury Management Strategy, Investment Strategy and Minimum Revenue Provision Strategy, which sets out the assumptions for financing requirements and interest rates and their effect on the revenue budget.
- Local Plan/Local Development Framework.
- There are also a number of other strategies, which set out policy direction for other key Council priorities.

2 THE FINANCIAL PLAN

Investment Streams

Stream One – Commercial Property Investments – existing portfolio
Stream Two – Economic Regeneration Opportunities

Stream Three – Carbon Zero initiatives and schemes to deliver quantifiable priority social outcomes

Stream Four – Housing developments

Stream Five – New Commercial Property Investments – new acquisitions – only to be completed following satisfactory conclusion of scheme 1

It is important that the revenue implication of capital scheme is recognised. For example, average return must link to the capital outlay with revenue consequences. So for example if there was a planned £10m of expenditure, at 1% net return then the Council should able to recognise £100k in your revenue budget.

2.1 Commercial Activity

Whilst the Council does currently receive income from investment properties it is presently not actively seeking to generate additional revenue income through the purchase of new investment properties. Any investment will be subject to a full business case.

2.2 Financial Principals supporting the Capital Strategy

Capital expenditure is to be incurred in line with Financial Procedure Rules as follows:

- The Chief Finance Officer is responsible for ensuring that a capital programme is prepared for consideration by the Cabinet before submission to Full Council. New Capital projects should be identified by Heads of Service to the Chief Finance Officer, as part of the Budget Planning Process, for inclusion in the Capital Programme.
- Capital schemes may only be committed after:
- An assessment in the agreed standard format including an estimate of the associated revenue expenditure and income has been approved by the Cabinet; and
- Appropriate finance has been made available.

- Where it appears that any scheme in the capital programme will be overspent by a sum of £50,000 or more a report shall be made to the Cabinet. The Chief Finance Officer will advise the Cabinet whether or how requests for additional capital finance can be achieved within the overall capital programme. The Chief Finance Officer is authorised to approve virements within the capital programme as outlined in Standing Order 64.

The key principles to be applied to the Capital Strategy are set out below:

- Capital resources are held corporately and are allocated according to the priorities set out in the Corporate Strategy (i.e. there is no automatic ring-fencing of resources for specific purposes);
- Capital receipts will be allocated in accordance with Council priorities;
- The Council will seek to maximise the use of grants and external funding;
- The Council is committed to deliver capital investment with partners to maximise benefits where this fits with Council priorities;
- Redirection of capital resources from one project to another will be contained within existing budgets, unless increases can be justified through the budget process;
- Capital budgets are generally cash-limited i.e. no provision is made for inflation which effectively means that over time there is a real reduction in the value of resources allocated to specific capital projects;
- Review of capital financing decisions which will likely have a revenue

budget impact due to lack of capital resources (E.g. through reprofiling of capital receipts and borrowing);
- Revisit the Asset Management Plan to see if any asset can be sold;

In order to reduce the exposure of the council to a borrowing requirement the following steps should continue to be examined:

- Fundamental review of existing capital programme to ensure that schemes are still required and are accurate;
- Maximisation of the use of grants and contributions from external sources;
- Providing a recurring revenue contribution to the capital programme;
- Invest to save schemes that can repay the capital investment over a period of time.

3 BUSINESS CASES

All capital scheme proposals will be required to comply with the Council's business case protocol which follows the Treasury's green book methodology requiring all potential schemes to consider:

- **strategic fit** - how the project aligns with corporate priorities and what it is trying to achieve.
- **financial case** – what are the financial circumstances for the project, e.g. is funding readily available and is it affordable? The case should consider all capital costs and funding as well as ongoing revenue costs including financing costs. Reference should be made to the targets set out in the financial plan in section 3.
- **economic case** – a value for money assessment which identifies options for delivering the project and considers measurable outcomes arising from the project linking these to the corporate plan.
- **commercial case** – consideration of how the project will be delivered in terms of procurement.
- **management case** – project planning to ensure that resources are available to support completion of project in accordance with a set out timetable.

3.1 All capital schemes are subject to a process as part of the capital programme process which requires business cases to be compiled and assessed. Briefly, the process is in the four stages:

Stage 1 - Scoping the Scheme and Preparing the Strategic Outline Case (SOC)

The purpose of this stage is to confirm the strategic context, and provide a robust case for change. This stage will consider the strategic, economic, procurement, financial and management cases and include a financial analysis taking account of the targets set out in the financial plan (section 3). Approval of the SOC will admit the project into the Capital Programme Development Pool and may release feasibility funding from reserves.

Stage 2 – Full business case (FBC)

The purpose of this this stage is to propose a viable project having taken account of any feasibility. The FBC will recommend the most economically advantageous offer, documenting the contractual arrangements, confirm funding and affordability and set out the detailed management arrangements and plans for successful delivery and post evaluation. The FBC will require approval by CSG prior to the scheme proceeding.

Stage 3 – Implementation

The business case should be used during the implementation stage as a reference point for monitoring implementation and for logging any material changes that the Council is required to make. The project will follow performance reporting protocols which will ensure that project progress, impact on outcomes and financial performance is measured throughout the project and following its completion.

Stage 4 - Evaluation

The business case and its supporting documentation should be used as the starting point for post implementation evaluation, both in terms of how well the project was delivered (project evaluation review) and whether it has delivered its projected benefits as planned (post implementation review) to the Council, in meeting strategic aims.

There will be separate arrangements for the consideration of Stream One investment proposals which require an assessment of financial yield, completion of a risk matrix and outcomes matrix.

3.2 Capital Investment Priorities

The Capital Strategy needs to ensure that any capital investment decisions are both affordable and achieve the priorities as set out in the Havant Corporate Strategy; any such investment in assets is likely to have implications on the revenue budget.

The Capital Strategy must therefore recognise the implications of capital investment decisions and ensure that they are in line with Council priorities and financing requirements are robustly evaluated and understood.

All business cases will be subject to the usual due diligence to ensure that they afford the best value for money for the Council, align with its core priorities and do not expose the Council to unnecessary risk that could put future delivery of services in jeopardy.

4 OUTCOMES BASED MEASURES AND TARGETS

4.1 An important element of the assessment of strategic fit in the business case process is the delivery of outcomes that meet corporate priorities. The Council takes a balanced scorecard approach to identification and measuring of outcomes which seeks to capture benefits in terms of economic, social, environmental and financial measures that have been identified in the Council's corporate plan.

Each capital scheme business case will be required to set out targeted benefits which reflect those measures set out in the corporate plan.

5 RISK MANAGEMENT

5.1 Effective risk management will allow the council to adapt rapidly to change and develop innovative responses to challenges and opportunities. The risk management cycle for capital projects incorporates risk identification, risk analysis, risk control and action planning and risk monitoring and review.

All significant capital projects will comply with the Councils project management process which follows good practice in the management of risk.

5.2 A full assessment of risk will be carried out individually for each commercial property acquisition proposal (scheme 1) before entering into any commitment and will include assessing the risk of loss. The risk assessment is an important part of the proposal process with separate consideration of each of the following factors:

- Portfolio Balance
- Location
- Tenant Covenant
- Building Quality
- Lease Term
- Tenants' Repairing Obligations
- Rent Review Mechanisms
- Occupational Demand
- Management Intensity
- Liquidity
- Tenure
- Environmental Impact
- Asset Management

The assessment and scoring of each of these risk factors will be set out in the investment proposal report and where necessary relevant external advice will be sought. A further due diligence review will be undertaken in respect of all of these risk factors for stream one investment proposals which are taken forward.

The portfolio as a whole will be risk managed through regular (quarterly) reviews of performance and annual valuations. Each asset is reviewed on an annual basis in order to review its performance, investment requirements and whether it should remain in the portfolio.

6 THE PRUDENTIAL FRAMEWORK AND INVESTMENT GUIDANCE

6.1 The Local Government Act 2003 (the Act) and supporting regulations requires the Council to 'have regard to' the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code, the CIPFA Treasury Management Code of Practice (the Code) and Investment Guidance (the Guidance) issued by The Ministry of Housing Communities and Local Government (MHCLG) to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

In February 2018 the Secretary of State issued new guidance on Local Government Investments (the Guidance), which widened the definition of an investment to include all the financial assets of a local authority as well as other non-financial assets held primarily or partially to generate a profit. This wider definition includes investment property portfolios as well as loans made to wholly owned companies or associates, joint ventures or third parties. The Guidance applies for financial years commencing on or after 1 April 2018.

6.2 All capital schemes will follow the provisions of the Prudential Code and Stream One investments, and where applicable other capital schemes, will follow the MHCLG Investment Guidance. As a minimum the following will be kept under review:

- Transparency and democratic accountability – this investment strategy will be approved by Council each year at budget setting time and any material changes will be presented to Council prior to implementation.
- Contribution
- Proportionality
- Prudential Indicators
- Security
- Liquidity
- Borrowing in Advance of Need
- Capacity and Skills

A half yearly report on compliance with the prudential framework and investment guidance will be submitted for consideration by Council.

The Capital Strategy is an accompaniment to the Treasury Management Strategy. The latter sets out the required Prudential Indicators for Treasury Management and Capital Expenditure, and includes a Policy Statement for the Minimum Revenue Provision (MRP) for borrowing.

7. CAPACITY, SKILLS AND USE OF EXTERNAL ADVISORS

7.1 The Guidance requires that elected members and officers involved in the investment decision making process have appropriate capacity, skills and information to enable them to take informed decisions as to whether to enter into a specific investment.

The Council utilises the knowledge and skills of its internal officers when considering capital investment decisions and where necessary it also relies on the expert knowledge of specialist external advisors.

The Council employs professionally qualified legal, finance and property officers who are able to offer advice and guidance when considering any capital investment decisions.

The Council has a duty to ensure that advisors negotiating deals on its behalf are aware of the core principles of the prudential framework and the regulatory regime in which the Council operates. This will be achieved by ensuring an adequate and effective training programme, obtaining appropriate advice to inform the decision making process and by ensuring that procurement arrangements provide relevant information to potential advisers of the specific principles, regulations and governance relevant to the local authority sector.

The Council will appoint specialist advisors to provide training to ensure that relevant Officers and Members have the required skills to make informed decisions and assess the associated risks. This training will take place before any investment decisions associated with the Strategy are considered and on a regular basis to ensure that Officers are engaged in continual professional development in relation to property investment activity and that Members, as decision makers, have the skills, knowledge and relevant information to effectively assist the decision making process. This will include training for new Members of the Council.

The Council recognises that investing in land and properties to achieve business objectives and to generate returns is a specialist and potentially complex area. The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Where skills, or capacity are lacking, the Council will engage the services of professional property, legal and financial advisors, where appropriate, to access specialist skills and resources to inform the decision-making process associated with this Strategy. The Council measures the impact of investment decisions on borrowing and affordability through Investment Indicators to ensure that the overall risk exposure remains within acceptable levels.

8. GOVERNANCE ARRANGEMENTS

8.1 The Council has a Strategy Projects Board whose purpose is:

- To act as the Corporate Board for strategic/key corporate projects contributing to the delivery of the Corporate Strategy;
- To monitor the progress of the Council's strategic/key corporate projects; including governance arrangements;
- To review and consider resourcing issues on project.

8.2 The function of the board is to be accountable for the success of the key projects which contribute to the delivery of the Corporate Strategy. A "Strategic Project (also known as a "Key Corporate Project") is defined as – any project which Executive Board have deemed to require strategic oversight and is tracked on the "Strategic Project" list maintained by the Board.

8.3 Project Board will be responsible for 'live' projects. Any Corporate Project that requires approval will go through the usual mechanism of Executive Board – Cabinet – and/or Council. Once a Corporate Project is approved (including funds) then a decision will be made by Executive Board on whether the project should be managed through Project Board.

8.4 In line with Prince-2 management standards, the Strategic Project Board will:

- Consider recommendations from the projects and provide strategic oversight to ensure continued fit with the business strategy for the Council.
- Approve major plans and any major changes on key projects including invocation of Exception status where projects are not progressing to plan.
- Allocate corporate funding and resources to key projects.
- Ensure corporate-wide communication relating to key projects is relevant and timely.
- Ensure appropriate governance and project assurance is in place for key projects and risks are being appropriately monitored and escalated where necessary.

8.5 The Strategic Project Board will link with the project management structures for each key project. The Business Solutions Unit will ensure appropriate and complementary project governance structures are in place, in line with Prince-2 management standards, to avoid confusion regarding roles and responsibilities. Prince 2-based templates for projects and programmes will be the standard reporting tools for all projects.

8.6 The Strategic Project Board will comprise of Senior Leaders within the organisation including Chief Executive, Director of Corporate Services (s151), Director of Regeneration & Place and Head of Programmes, Redesign & Quality.

8.7 In addition to this, Cabinet are the ultimate decision makers.

8.8 Overview and Scrutiny hold an important role to of scrutinise the capital process.

8.9 Full Council is responsible for agreeing the Capital Investment Strategy as part of the Budget Framework each year and will be required to approve any material changes in the strategy.

9. PERFORMANCE MANAGEMENT ARRANGEMENTS

9.1 The Investment Strategy is an important building block which provides the mechanisms for delivering the Council's corporate priority outcomes as well as contributing significantly to ensuring that the Council remains financially sustainable in the medium term. As such, the monitoring both of individual projects, particularly commercial investments, and the investment strategy as a whole will be essential to the achievement of the Council's strategic and financial objectives.

Performance monitoring will include:

- Monitoring of Capital Programme – as part of overall performance monitoring which incorporates financial, project and performance measures monitoring. Monitoring is quarterly to Cabinet and BP&P.

- Financial Monitoring of Investment Strategy – as the strategy is key to reducing the medium-term budget gap, regular monitoring of the progress of the strategy will take place. This will necessarily include the delivery of investments against budgets and the yield levels against target.

- Monitoring of Commercial Investments – it is acknowledged that there is risk of loss arising from commercial investment arising from possible impacts both on revenue income and on capital value. A regular (quarterly) report showing both the yield and income will be included in the financial monitoring to Cabinet and BP&P. The performance of individual acquisitions and the overall portfolio will be considered.

- Prudential indicators – a half yearly report on prudential indicators which aim to show that the capital programme remains prudent, affordable and sustainable will be considered by Council.

- Outcomes Delivery – progress against the measurable outcomes and measures set out in business cases which will provide a summary of the impact of the capital investment plan in delivering corporate priorities as well as achieving a more sustainable financial position.

9.2 Current Asset Portfolio

9.3 The Council holds assets split across three categories as detailed below:

- **Investment Property (Non-Operational)**
  These assets include Industrial Estates, land held for capital appreciation and rental income.

- **Property, Plant and Equipment**
  These are operational properties, land, vehicles, infrastructure and community assets that are used to deliver council services and include Council.

- **Assets Under Construction**
  These are assets that are in the course of construction but have not yet been completed.

9.4 The Council holds an investment portfolio that supports both its operational activities and non-operational activities from which it receives an element of rental income. For the year ended 31 March 2021 the value of portfolio assets held was as follows:

Asset Category	**Valuation 31/03/21 £000**
Investment Property	33,151
Property Plant and Equipment	64,104
Assets Under Construction	0
TOTAL	**97,255**

9.5 Capital Grants

The Council receives one primary capital grant from central Government to support its role in providing Disabled Facilities Grants; for 2022/23 the Council has been allocated £1.628 million. There have been changes to the way the grant is now distributed with the funding being provided to the County Council as the Better Care provider who then allocate funding to the District Councils. Future year’s allocations may therefore be subject to change as part of this change in procedure.

9.6 Revenue Contributions and Reserves

The capital programme can also be financed through the use of reserves (both capital and revenue) although revenue contributions will have an overall effect on the General Fund revenue budget.

9.7 Capital Recipes

Capital receipts arise principally from the sale of Council capital assets. The sales of assets are utilized to support the Capital programme in the Capital Strategy. The usable capital receipts reserve contained a balance of £10.320 million as at 31 March 2021.