Southampton City Council

CAPITAL STRATEGY

2024/25

Contents

	SECTION 1 – INTRODUCTION
1.1	**Background**
1.1.1	This capital strategy gives 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.
1.1.2	The Prudential Code requires the council to have in place a capital strategy that sets out the long-term context in which capital expenditure decisions are made in order to demonstrate that capital expenditure and investment decisions are taken in line with service objectives and properly take account of stewardship, value for money, prudence, sustainability and affordability.
1.1.3	Decisions made this year on capital and treasury management will have financial consequences for the Authority years into the future. They are therefore subject to both a national regulatory framework and to local policy framework, summarised within this strategy.
	SECTION 2 - CAPITAL EXPENDITURE AND FINANCING
2.1	**Estimates of Capital Expenditure**
2.1.1	Capital expenditure is where the council spends money on assets, such as property or vehicles, which will be operational 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 Authority has 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 2024/25 the council is planning capital expenditure of £156.97M, shown below:

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

Capital Expenditure and Financing	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28
	Actual	**Forecast**				
Children & Learning	12.78	9.88	18.47	9.84	26.22	0.71
Corporate Services	3.81	2.89	3.60	5.00	3.50	1.50
Place	42.61	60.26	65.64	26.11	5.65	4.20
Strategy & Performance	0.31	2.68	6.90	0.00	0.00	0.00
Wellbeing & Housing	3.44	3.21	3.63	3.35	0.55	0.00
Total General Fund	**62.94**	**78.93**	**98.24**	**44.30**	**35.93**	**6.41**
HRA	35.88	41.98	58.73	61.16	40.30	38.91
Total Expenditure	**98.82**	**120.91**	**156.97**	**105.46**	**76.23**	**45.32**
Capital Receipts	6.58	4.74	11.09	2.75	2.50	2.63
Capital Grants	34.92	46.70	65.06	16.70	2.05	0.00
Contributions	14.08	9.26	7.15	4.33	0.05	0.00
Major Repairs Allowance	20.76	21.49	22.35	22.84	23.40	23.79
Direct Revenue Financing	1.79	3.35	2.13	1.16	0.45	0.55
Council Resources - Borrowing	20.68	35.37	49.19	57.68	47.77	18.35
Total Financing	**98.82**	**120.91**	**156.97**	**105.46**	**76.23**	**45.32**

**This excludes any capitalisation direction*

Due to changes in the accounting requirements for ‘right to use’ leases, the Council will be implementing on 1 April 2024, the council is currently assessing what impact this will have on the Capital programme, Capital Financing Requirement (CFR) and MRP liability. It is unlikely to have a significant impact.

2.1.2 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 is in Table 1 above.

2.1.3 The main General Fund capital projects are summarised below, in Table 2, by portfolio. Following a change in the Prudential Code, the Authority no longer incurs capital expenditure on investments.

2.1.4 *Table 2: General Fund Major Projects by Programme*

Programme	Major Project	2023/ 2024 £M	2024/ 2025 £M	2025/ 2026 £M	2026/ 2027 £M	2027/ 2028 £M	2028/ 2029 £M
Children & Learning	Early Years Expansion	0.25	0.47	0.15	0.06	0.00	0.00
	School Capital Maintenance	2.72	6.78	0.31	0.34	0.00	0.00
	Secondary Review & Expansion	2.83	3.17	0.00	0.00	0.00	0.00
	SEND Review & Expansion	3.17	4.77	8.78	25.82	0.71	0.00
	Childrens Services - Residential/Assessment Unit	0.91	3.28	0.60	0.00	0.00	0.00
Corporate Services	Digital & IT	2.89	3.60	5.00	3.50	1.50	0.00
Place	Bridges Programme	1.53	4.35	0.15	0.00	0.00	0.00
	Highways Programme	11.98	4.72	3.25	0.00	0.00	0.00
	Integrated Transport	8.23	7.38	0.70	0.00	0.00	0.00
	Transforming Cities	21.52	14.36	0.00	0.00	0.00	0.00
	Future Transport Zone	5.36	7.13	0.44	0.00	0.00	0.00
	Outdoor Leisure	1.15	15.73	14.33	0.00	0.00	0.00
	Corporate Assets Decarbonisation Scheme (CADS)	1.48	2.54	0.71	0.00	0.00	0.00
	Materials Recycling Facility	0.00	0.00	3.45	0.00	0.00	0.00
	Fleet Investment	3.28	0.60	1.00	1.00	0.00	0.00
	Arts & Heritage	2.44	6.47	0.89	0.15	0.00	0.00
	River Itchen Flood Alleviation Scheme (RIFAS)	0.00	0.00	0.50	4.50	4.20	1.00
	Parks Development Works	1.80	1.42	0.00	0.00	0.00	0.00
	Play Area Improvements	0.03	0.70	0.35	0.00	0.00	0.00
	Coastal Erosion Measures	0.25	0.15	0.00	0.00	0.00	0.00
	Corporate Council Buildings	0.48	0.00	0.00	0.00	0.00	0.00
	Property Portfolio Enhancements	0.46	0.00	0.00	0.00	0.00	0.00

Strategy & Performance	Other	0.26	0.09	0.35	0.00	0.00	0.00
	Transformation Programme	2.68	6.90	0.00	0.00	0.00	0.00
Wellbeing & Housing	Disabled Facilities Grants	0.45	0.55	0.55	0.55	0.00	0.00
	Adult Social Care Projects	0.21	0.16	0.12	0.00	0.00	0.00
	Community Safety	1.60	1.80	1.89	0.00	0.00	0.00
	Estate Improvements	0.96	1.12	0.79	0.00	0.00	0.00
	TOTAL	**78.93**	**98.24**	**44.30**	**35.93**	**6.41**	**1.00**

2.1.5 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 reported separately to Full Council and includes the building of new homes. The main programmes are below:

Table 3: HRA Major Projects by Programme

	2023/24 Forecast £M	2024/25 Budget £M	2025/26 Budget £M	2026/27 Budget £M	2027/28 Budget £M	2028/29 Budget £M	Total £M
Improving Quality of Homes	10.89	13.23	14.93	12.33	12.40	12.40	**76.17**
Improving Energy Efficiency	5.93	19.19	19.80	8.17	9.40	9.40	**71.90**
Impriving Safety of Homes	13.98	15.51	12.67	9.09	8.80	7.80	**67.85**
Regeneration	3.88	3.60	6.24	3.57	-	-	**17.29**
Supporting Communities	3.91	1.82	1.67	1.57	1.57	1.57	**12.11**
Supporting Independent Living	3.38	5.38	3.84	3.00	3.00	3.00	**21.60**
Inflation allowance			2.01	2.56	3.75	4.78	**13.09**
	41.98	**58.73**	**61.16**	**40.30**	**38.91**	**38.94**	**280.01**

2.2 Governance

2.2.1 Service managers have identified projects to be included in the council's capital programme. Projects are collated by corporate finance who calculate the financing cost (which can be zero if the project is fully externally financed). The Council Capital Board (CCB) appraises all projects based on a comparison of service priorities against financing costs and makes recommendations to Cabinet. The final capital programme is then presented to Cabinet and Council at budget and council tax setting each year.

This year has seen an increased focus on affordability, addressing health and safety concerns and opportunities for invest to save, given ongoing financial pressures and reducing resources. Capital construction costs have seen an unprecedented increase due to inflation and market volatility and the cost of borrowing to finance the programme has been affected by interest rates.

2.3 Methods of Funding

2.3.1 <u>Use of Leasing</u>

The council does have the option to lease assets using an operating lease arrangement, however with the flexibility afforded through Prudential Borrowing this source of financing has been less attractive. Going forward lease versus buy appraisal will be taken for each project, particularly fleet.

2.3.2	Tax Increment Financing (TIF) The Local Government Finance Act 2012 provided the legislative framework for the introduction of TIF, as an incentive to grow local economies and attract new businesses to areas. TIF allows councils to borrow against future increases in business rate revenues generated because of local developments and growth. By capturing predicted increases in income from business rates, it will create an income stream that can be used to borrow against, repay existing borrowing incurred under existing borrowing powers or to reimburse costs to a developer for the initial lay out of infrastructure work. This alternative financing for the infrastructure work is aimed at kick-starting regeneration and thereby supporting locally driven development and growth.
2.3.3	S106 Agreements S106 agreements are made with developers / landowners as part of the planning approval process to ensure that new development mitigates its own impact and provides the necessary site-specific infrastructure to support it. These contributions are site specific or can be 'pooled' for a maximum of five site specific projects. Any contributions received are 'ring-fenced' for the purpose as set out in the relevant S106 agreement and are applied to fund schemes within the relevant capital programme once an eligible scheme has been identified. S106 contribution agreements have covered all types of infrastructure including transport, affordable housing, play areas, open spaces, playing fields, public realm, and public art. However, since the council adopted CIL the planning obligations sought within S106 agreements have been scaled back to deal with only site-specific requirements, as required by the CIL Regulations. Pooled contributions previously sought for strategic transport, public realm and public open space related obligations are now dealt with by CIL. The S106 contributions are time limited in that if they are not spent within an agreed timescale, typically 5 – 10 years, dependent on what has been agreed in the S106 agreement and any funds not spent in line with the agreement would have to be repaid to the developer, which, may include interest.
2.3.4	Community Infrastructure Levy (CIL) CIL was adopted by the council in September 2013. CIL contributions are determined by set rates as detailed within the council's CIL Charging Schedule and based on the amount of floor space being created by the development. CIL can be used to fund a wide range of infrastructure that is needed because of new development but is not site specific, giving more flexibility in where the funding can be used in geographical terms. The CIL does not replace the requirement of S106 contributions. S106 contributions will still be relevant and will be sought alongside CIL. The Planning Act and subsequent Community Infrastructure Levy Regulations 2010 (as amended) says that authorities can only spend CIL on providing

	infrastructure to support the development of their areas. This includes flood defence, open space, recreation and sport, roads and transport facilities, education, and health facilities. However, it does not include affordable housing, which will continue to be funded by S106 obligations. In addition, SCC have opted to continue to seek S106 contributions for transport. All other S106s contributions are now agreed through CIL. The Localism Act also clarifies that CIL can be spent on the ongoing costs of providing infrastructure, including maintenance works. The funding could be used towards a substantial number of the council's current programmes i.e. School Expansion and the Roads Programme. The CIL funding can be used to fund existing schemes within the current General Fund capital programme that meet the definition of infrastructure. The previous agreed approach is to treat the CIL monies as a central pot of funding to be allocated as overall council resources to fund the capital programme. However, it should be noted that 15% (25% if a Neighbourhood Plan is in place) of receipts need to be applied to schemes in the ward that the receipt originated from, in consultation and agreement with the local community.
2.3.5	Private Finance Initiative (PFI) Although PFI schemes are not shown within the capital programme as they are not financed by capital resources, PFI is a means by which the council can facilitate major new infrastructure projects. PFI schemes involve partnerships between the public and private sector to fund public sector infrastructure projects with private capital. Under PFI, a private sector contractor agrees to accept the risks associated with the design, construction, and maintenance of the asset over the contract term, which is typically for a 25-year period. The public sector partner pays an annual fixed price during the contract term, part of which is subject to inflation. At the end of the term, the asset is wholly owned by the council. No additional PFI projects are anticipated. Any such proposals would be presented to the EMB for evaluation before presentation for Members approval.
2.4	**Gross Debt and the Capital Financing Requirement**
2.4.1	Debt is only a temporary source of finance, since loans and leases must be repaid, and this is 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.
2.4.2	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 £35.31M during 2024/25.
2.4.3	CFR is a key indicator of prudence. To ensure that over the medium-term debt will only be for a capital purpose, the council should ensure that debt does not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years. Based on the

above figures for expenditure and financing, the council's estimated CFR isdetailed in table 4 below.

2.4.4 *Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £M*

Capital Financing Requirement	**31-Mar-23 Actual**	**31-Mar-24 Forecast**	**31-Mar-25 Forecast**	**31-Mar-26 Forecast**	**31-Mar-27 Forecast**	**31-Mar-28 Forecast**
Balance Brought forward	339.15	342.57	350.62	355.88	363.38	384.59
New Capital Borrowing	14.53	20.40	19.13	21.69	34.97	6.41
MRP	(7.61)	(8.69)	(9.53)	(10.34)	(10.19)	(11.31)
Movement in Other Liabilities	(3.50)	(3.66)	(4.34)	(3.85)	(3.57)	(4.12)
Total General Fund Debt	**342.57**	**350.62**	**355.88**	**363.38**	**384.59**	**375.57**
HRA	174.88	189.85	219.90	255.89	268.69	280.63
Total CFR	**517.45**	**540.47**	**575.78**	**619.27**	**653.28**	**656.20**
Less Other Debt Liabilities*	(57.11)	(53.45)	(49.12)	(45.27)	(41.69)	(37.57)
Loans CFR	**460.34**	**487.02**	**526.66**	**574.00**	**611.59**	**618.63**

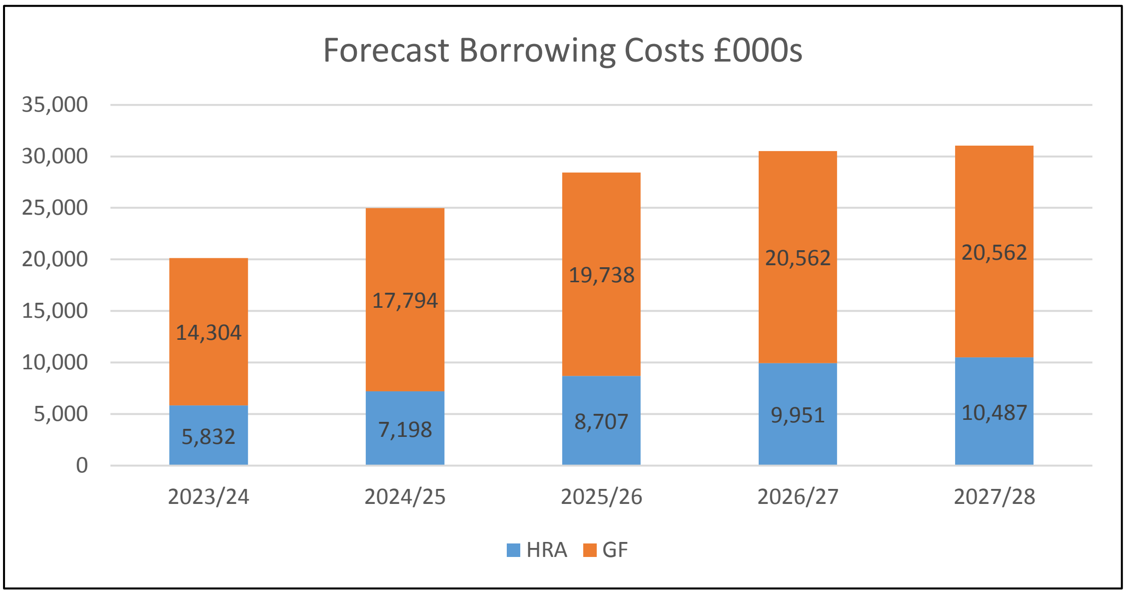
2.4.5 *Table 5 – Current and Estimated Movement in Gross Debt £M*

Gross Debt	**31-Mar-23 Actual**	**31-Mar-24 Forecast**	**31-Mar-25 Forecast**	**31-Mar-26 Forecast**	**31-Mar-27 Forecast**	**31-Mar-28 Forecast**
Borrowing (Long Term GF)	125.82	159.29	189.98	199.97	219.97	213.26
Borrowing (Long Term HRA)	172.37	188.01	218.02	254.02	258.49	270.40
Borrowing (Short Term)	5.00	20.00	0.00	0.00	0.00	0.00
Total Borrowing	**303.19**	**367.30**	**408.00**	**453.99**	**478.46**	**483.66**
Finance leases and Private Finance Initiatives	44.37	41.08	37.11	33.62	30.40	26.64
Transferred Debt	12.73	12.37	12.01	11.64	11.28	10.92
Total Other Debt	**57.10**	**53.45**	**49.12**	**45.26**	**41.68**	**37.56**
Total Debt	**360.29**	**420.75**	**457.12**	**499.25**	**520.14**	**521.22**

2.4.6 There is a significant difference between the gross external borrowing requirement and the net external borrowing requirement represented by the council's level of balances, reserves, provisions and working capital as the council's strategy has been to only borrow to the level of its net borrowing requirement. The reasons for this are to reduce credit risk, take pressure off the council's lending list and to avoid the cost of carry existing in the current interest rate environment.

2.4.7 Given the significant cuts to public expenditure and in particular to local government funding the council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short term to either use internal resources, or to borrow short-term instead.

2.4.8 By doing so, the council can reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal and short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the council with this 'cost of carry' and breakeven analysis.

2.4.9	Constant monitoring of rates also allows the Council to take advantage when long-term rates fall. In 2023/24, long term PWLB loans were taken when rates fell and were able to secure a rate lower than budgeted and lower than short term.
2.4.10	Any change to the strategy would require approval by full Council and additional Treasury Training would be provided to assist members in understanding the risks and implications of any change to the current strategy.
	Revenue Impact of the Capital Programme
2.4.10	In terms of the impact on the revenue budget of the council the forecast for borrowing costs (for capital financing) in 2024/25 is £25.19M, of which £7.20M relates to the HRA. This is made up of interest on borrowing of £15.11M and other costs of £10.08M. This is expected to rise to £33.05M (£10.49M HRA) by 2027/28 to accommodate the capital programme, utilisation of reserves and refinancing of borrowing. However, this will be subject to movement as the need for further borrowing becomes more certain. The impact is also shown in the chart below: 
2.5	**Asset Management**
2.5.1	To ensure that capital assets continue to be of long-term use, the council has engaged a specialist to assist with the production of a comprehensive corporate asset management strategy. This strategy allows the council to plan effectively for its property needs now and, in the future, focusing on: • what property assets the council owns and uses, • how property is used by the council, • how the council's property needs might change and evolve over time, and • ensuring where possible that the council always has the right property fit for purpose.
2.5.2	When determining the capital programme and allocating resources the Council will also have regard to: • The preparation of the statutory Local Transport Plan, and Highways Asset Management Strategy,

	• The preparation of the Asset Management Plan for Schools and Council Buildings to ensure health and safety issues are dealt with appropriately, and • The council's obligation to finance adaptations to the homes of disabled residents. Funding is passported directly to the Better Care Fund along with the Adults Personal Social Services grant. It has been agreed with the CCG that these monies will be retained by the council, as part of the S75 pooling arrangement.
2.6	**Asset Disposals**
2.6.1	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. The council is currently permitted to spend capital receipts "flexibly" on service transformation projects until 2025/26. Repayments of capital grants, loans and investments also generate capital receipts.
2.6.2	The Asset Development & Disposal Programme (ADDP) was initiated in 2023/24 with the vision to drive Southampton's growth through the retention, development, or disposal of SCC's corporate, operational and investment portfolio. It is a capital transformation programme, with capital receipts secured from the disposal of assets funding future transformation activity across the council, including ADDP resources. Along with the securing of capital receipts, ADDP is seeking to achieve wider financial benefits through development and disposal activity. This includes achieving additional council tax revenue and business rates, as well as other revenue savings through reductions in utilities and maintenance costs. One of the early activities within the ADD programme is reviewing corporate and operational assets to assess whether they should be retained, disposed, or redeveloped in the future.
2.6.3	Assets to be disposed of are still being assessed as part of ADDP as noted above with the intention of generating a minimum of £15M capital receipts per year. *Table 6: GF Capital receipts receivable (£M)*

	2022/23 Actual	2023/24 Forecast	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
Asset sales	0.21	12.79	15.00	15.00	15.35
Loans repaid*	0.12	0.22	0.10	0.10	0.10
TOTAL	**0.33**	**13.01**	**15.10**	**15.10**	**15.10**

*It is difficult to predict future receipts, as based on recipient moving property which is outside the Authority's control. So, this is a prudent estimate based on previous years actuals.

Expected capital receipts are reported as part of the quarterly financial monitoring.

2.6.4	The current strategy for the use of capital receipts is to:

- Consider funding transformational projects on a case-by-case basis,
- Consider funding potential capitalisation directions, and
- Consider forgoing the immediate capital receipt for longer term and sustainable income stream through development of sites within the city.

2.6.5 <u>Flexible use of Capital Receipts</u>

The 2015 Comprehensive Spend Review (CSR) announced that local authorities will be allowed to spend up to 100% of capital receipts (excluding Right to Buy receipts) on the revenue costs of reform projects between 1st April 2016 to 31st March 2019, this was then extended until March 2022.

In February 2021, the Government announced that it would be extending the scheme for a further 3 years until March 2025 with the following conditions:

- The key criteria to use when deciding whether expenditure can be funded by the capital receipts flexibility is that it is forecast to generate ongoing savings to the authority’s net service expenditure and is expenditure on a project where incurring up-front costs will generate ongoing savings; and
- Individual authorities demonstrate the highest standards of accountability and transparency. The guidance recommends that each authority should prepare a strategy that includes separate disclosure of the individual projects that will be funded, or part funded through capital receipts flexibility and that the strategy is approved by full Council or the equivalent.
- Examples of qualifying expenditure include the sharing of back office and administrative services; investment in service reform feasibility work; collaboration between central and local government to free up land for economic use; funding the cost of service reconfiguration or restructuring leading to ongoing efficiencies; sharing Chief Executives; driving a digital approach; aggregating procurement on common goods; improving systems and processes to tackle fraud; setting up commercial or alternative delivery models to deliver services more efficiently or increase revenue income; and integrating public facing services across two or more public sector bodies.

The council has chosen to implement this policy and has prepared a Flexible Use of Capital Receipts Strategy 2024/25.

It should be noted that the Secretary of State announced on 18 December 2023 consultation on further flexibilities for capital receipts including:

- Capitalising general cost pressures.
- Extending flexible use of capital receipts to allow councils to borrow for revenue costs.
- New flexibilities for the use of proceeds of selling investment assets used for rent or capital appreciation only.

2.6.6 <u>HRA Right to Buy Receipts</u>

In most cases there will be no ring fencing of capital receipts to specific projects. One exception to this is the retained Right to Buy (RTB) receipts held by the council under the agreement signed in June 2012 and amended in June 2013.

Under this agreement any retained RTB receipts, which are not used for the specific purpose of providing replacement affordable housing, must be returned to DLUHC.

SECTION 3 - TREASURY MANAGEMENT

3.1 **Background**

3.1.1 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 Authority 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.

3.2 **Borrowing strategy**

3.2.1 The Authority'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 Authority therefore seeks to strike a balance between cheap short-term loans and long-term fixed rate loans where the future cost is known but higher.

The Authority does not borrow to invest for the primary purpose of financial return and therefore retains full access to the Public Works Loans Board.

Projected levels of the council's total outstanding debt (which comprises borrowing, PFI liabilities, leases and transferred debt) are shown below in Table 6, compared with the capital financing requirement (see Table 4 above).

Statutory guidance is 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.

3.3 **Liability benchmark**

3.3.1 To compare the council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that cash and investment balances are kept to a minimum level of £20M at each year-end. This benchmark is currently £303.20M and is forecast to rise to £454.05M over the next three years.

Table 7: Liability Benchmark in £M

	31-Mar-23 Actual	31-Mar-24 Forecast	31-Mar-25 Forecast	31-Mar-26 Forecast	31-Mar-27 Forecast	31-Mar-28 Forecast
Loans CFR	**460.34**	**487.02**	**526.66**	**574.01**	**611.60**	**618.64**
Less Balance sheet Resources	(157.14)	(165.78)	(166.59)	(167.96)	(172.70)	(172.70)
Plus Minimum Investments		48.00	48.00	48.00	48.00	48.00
Liability Benchmark	**303.20**	**369.24**	**408.07**	**454.05**	**486.90**	**493.94**
Less Committed External Borrowing	(303.20)	(312.60)	(282.00)	(271.40)	(260.80)	(250.20)
Minimum Borrowing Need	**0.00**	**56.64**	**126.07**	**182.65**	**226.10**	**243.74**

3.4 **Affordable Borrowing Limit**

3.4.1 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.

The council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise because of all the financial transactions of the council and not just those arising from capital spending reflected in the CFR.

3.4.2 The ***Authorised Limit*** sets the maximum level of external borrowing on a gross basis (i.e. excluding investments) for the council. It is measured daily against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long-term liabilities). This Prudential Indicator separately identifies borrowing from other long-term liabilities such as finance leases.

The Authorised Limit, shown in table 8, has been set on the estimate of the prudent but not worst-case scenario with sufficient headroom to allow for unusual cash movements, for example a complete debt restructure requiring monies to be borrowed in advance of repayment of existing debt.

3.4.3 *Table 8 – Authorised Limit for External Debt £M*

	2023/24	2024/25	2025/26	2026/27
Borrowing	710	750	840	930
Other Long-term Liabilities	60	60	50	50
Total	**770**	**810**	**890**	**980**

3.4.4 The ***Operational Boundary*** is linked directly to the council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the prudent but not worst-case scenario but without the additional headroom included within the Authorised Limit which allows for a full debt restructure if a favourable opportunity arose.

3.4.5 *Table 9 – Operational Boundary for External Debt £M*

	2023/24	2024/25	2025/26	2026/27
Borrowing	610	630	660	710
Other Long-term Liabilities	60	60	50	50
Total	**670**	**690**	**710**	**760**

3.4.6 The Executive Director Corporate Services & S151 Officer has delegated authority, within the above limits for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Council will be notified of any use of this delegated authority.

3.5 **Treasury Investment Strategy**

3.5.1	Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not considered to be part of treasury management and are therefore dealt with in the Non-Treasury Strategy.
3.5.2	The Authority's policy on treasury investments is to prioritise security and liquidity over yield, which is to focus on minimising risk rather than maximising returns. Cash that is likely to be required 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 investments to buy, and the Authority may request its money back at short notice. Further details on treasury investments are in the Treasury Management Strategy.
3.6	**Risk Management**
3.6.1	The effective management and control of risk are prime objectives of the council's treasury management activities. The Treasury Management Strategy therefore sets out various indicators and limits to constrain the risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.
3.6.2	The treasury management prudential indicators are considered by the Governance Committee on 4 March 2024.
3.7	**Governance**
3.7.1	Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Executive Director Corporate Services & S151 Officer and staff, who must act in line with the Treasury Management Strategy to be approved by Governance Committee on 4th March 2024. Quarterly financial monitoring reports to Cabinet include treasury management activity. The Governance Committee is responsible for scrutinising treasury management decisions.
	<u>SECTION 4 - INVESTMENTS FOR SERVICE PURPOSES</u>
4.1	**Background**
4.1.1	The council may make investments to assist local public services, including making loans to and buying shares in local service providers and businesses to promote economic growth. Considering the public service objective, the council is willing to take more risk than with treasury investments, however it still plans for such investments to break-even after all costs. Currently the council does not have any investments for service purposes, the criteria for potential investments in the future is set out in the Non-Treasury Investment Strategy 2024/25.

4.2	**Governance**
4.2.1	Decisions on service investments are made by the relevant service director following consultation with the Executive Director Corporate Services & S151 Officer and must meet the criteria and limits laid down in the Investment Strategy. Most loans and shares are capital expenditure and will be approved as part of the capital programme. The relevant service director is responsible for ensuring adequate due diligence before investment is made, including engaging independent and expert advice where necessary. Further details on service investments are included in the Non-Treasury Investment Strategy 2024/25.
	<u>SECTION 5 - COMMERCIAL ACTIVITIES</u>
5.1	**Background**
5.1.1	With central government financial support for local public services declining, the council had previously invested in commercial property for financial gain. Total commercial investments are valued at £23.8M, as of 31 March 2022, consisting of three properties providing a net return after all costs of 1.84%. With financial return being the main objective, the council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include reduced income due to rent voids or rent reductions and fall in capital value due to market conditions/demands. These risks are managed by performing credit checks on potential tenants, having a provision for bad debts and budget for maintenance costs, and regular monitoring to identify potential risks as early as possible. There are no plans for future commercial investments and current investments will be in scope of the ADDP.
5.2	**Governance**
5.2.1	Decisions on commercial investments are made by the Head of Property and Executive Director Corporate Services & S151 Officer, in consultation with the Cabinet Member for Finance & Change and the Leader of the Council in line with the criteria and limits in the Property Investment Strategy approved by Council. Property and most other commercial investments are also capital expenditure and will be approved as part of the capital programme. The relevant service director is responsible for ensuring adequate due diligence before investment is made, including engaging independent and expert advice where necessary. Further details on commercial investments and limits on their use are detailed in the Non-Treasury Investment Strategy 2024/25.
5.2.2	**Net Income from Commercial Investment to Net Revenue Stream (NRS)** The council's income from commercial investments as a proportion of its net revenue stream has been and is forecast, in Table 10 below. This shows that the council is not over dependent on income from investments.

5.2.3 *Table 10 - Net Income from Commercial Investment to NRS £M to %*

Ratio of Net Income from Commercial Investment to NRS	2022/23 Actual	2023/24 Forecast	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast	2027/28 Forecast
Total net income from commercial investments	6.48	7.40	7.03	7.28	7.28	7.28
Net Revenue Stream GF	193.17	221.58	239.17	290.03	305.84	317.76
Proportion of NRS	3.36%	3.34%	2.94%	2.51%	2.38%	2.29%

SECTION 6 – OTHER LIABILITIES

6.1 Background

6.1.1 In addition to debt detailed above, the council has set aside an earmarked insurance reserve of £0.13M to cover risks of a potential liability created by Municipal Mutual Insurance (MMI) levy and other uninsured losses which might occur in the future. As of 31 March 2023, the council's outstanding potential liability stood at £1.390M (2021/22 £1.390M), less the £0.347M payment already made under the Scheme of Arrangement with MMI.

6.2 Governance

6.2.1 Decisions on incurring new discretional liabilities are taken by service managers in consultation with the Executive Director Corporate Services & S151 Officer. The risk of liabilities crystallising and requiring payment is monitored by corporate finance and reported to the appropriate committee. New liabilities exceeding £2M are reported to full Council for approval/notification as appropriate.

Further details on liabilities and guarantees are on page 103 of the 2022/23 statement of accounts.

SECTION 7- REVENUE BUDGET IMPLICATIONS

7.1 Background

7.1.1 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans, MRP and loans fund repayments are charged to revenue. 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.

7.2 Ratio of financing costs to net revenue stream

7.2.1 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs. The upper limit for this ratio is currently set at 15% overall and 11% for General Fund only. The table below shows the likely position based on the proposed capital programme.

7.2.2	*Table 11: Prudential Indicator: Ratio of financing costs to net revenue stream %*

Ratio of Financing Costs to Net Revenue Stream	2022/23 Actual	2023/24 Forecast	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast	2027/28 Forecast
General Fund	9.58	9.50	10.41	8.92	8.47	8.74
HRA	6.81	7.87	8.57	9.99	11.02	11.26
Total	**8.79**	**9.09**	**9.92**	**9.17**	**9.06**	**9.32**

7.2.3 An application has been made to Government seeking Exceptional Financial Support to help balance the budget for 2024/25.

The exceptional support is in the form of a ‘capitalisation direction.’ It is important to note that this is not additional funding or any form of ‘bailout.’ Capitalisation is how the government permits local authorities to treat revenue costs as capital expenditure. It is a relaxation of the rules that require revenue costs to be met from revenue resources only and that councils should not “borrow” to fund revenue expenditure. Obviously, a local authority does not have to borrow to fund the capitalised expenditure as it can legitimately use capital receipts to do.

It offers only a ‘window’ to take some pressure off the General Fund revenue budget by using capital as a funding source thereby providing a time-limited opportunity to review spending plans and to re-balance revenue budgets taking a longer-term view. The capitalisation direction does not have to be used, but it provides the option to council to supplement funding using the capitalisation direction.

Any use of exceptional support must be agreed by the government, and there are no guarantees their agreement will be forthcoming. But if granted, it comes at the cost of generating capital receipts to create the necessary funding, or at a cost of new borrowing, which also must be financed, adding to financial pressure. If sufficient asset sales cannot be generated within the necessary timescales to meet requirements, future years’ revenue budgets will need to be increased to reflect the extra borrowing costs.

Any new borrowing taken under this arrangement does not qualify for the PWLB certainty rate and incurs a premium of 1%, so any borrowing taken will be 1.2% above the certainty rate, an additional £0.12M interest for each £10M taken. Current forecast for the 20-year PWLB maturity borrowing is around 5%, so including the additional 1.2%, additional revenue interest costs will be £0.62M for every £10M borrowing taken. This will impact on the figures in table 10 and the limit for the GF would need to increase above the current 11%.

7.2.4 This indicator is not so relevant for the HRA, especially since the introduction of self-financing, as financing costs have been built into their 40-year business plan, including the voluntary payment of MRP. There are no issues with affordability but if difficulties were to arise then the HRA would have the option not to make principal repayments in the early years, which it has currently opted to do.

7.3 **Sustainability**

7.3.1 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 40 years into the future. The Executive Director for Corporate Services & S151 Officer is satisfied that the proposed capital programme is prudent, affordable, and sustainable.
	<u>SECTION 8 - CAPACITY AND SKILLS</u>
8.1	**Background**
8.1.1	The Authority employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Executive Director Corporate Services & S151 Officer is a qualified accountant with extensive years' experience within local government at a senior level. The Council pays for junior staff to study towards relevant professional qualifications including CIPFA, ACCA, AAT, ACT (treasury), ATT (tax). Where council staff 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.