Committee report

Committee	**CORPORATE SCRUTINY COMMITTEE**
Date	**11 JULY 2023**
Topic	**CAPITAL PROGRAMME / CAPITAL STRATEGY**
Report of	**DIRECTOR OF FINANCE AND SECTION 151 OFFICER**

BACKGROUND

Overall Strategy

1. As described in the Medium-Term Financial Strategy (MTFS), the strategy is to maximise the capital resources available and then target the investment of those resources to areas that will enable the Council to meet its statutory responsibilities, stimulate the Island Economy and improve the Council's overall financial position.

2. The development of a Capital Strategy considers investments that will be made in the acquisition, creation, or enhancement of tangible or intangible fixed assets, in order to yield benefits to the council for a period of more than one year. It also considers how stewardship, value for money, prudence, sustainability and affordability will be secured. The Capital Strategy therefore has 3 core aims:

   Aim 1 - To support a Medium-Term Outlook
   - allocating known resources to future years for critical capital investment, ensuring that in years where capital resources are limited, critical investment can continue to be made;
   - aligning known resources and spending, ensuring that uncertain or forecast resources are not applied to current investment, thus leaving potentially unfunded obligations in the future; and
   - smoothing out any significant gaps between capital investment needs and capital resources available by utilising contributions from revenue.

   Aim 2 - To Maximise the Capital Resources available and the flexibility of their application
   - setting aside capital funding for "match funding" opportunities, where these are aligned with the Council's strategic objectives in order to take advantage of "free" funding;
   - reviewing contractually uncommitted schemes against newly emerging capital investment priorities;
   - avoiding ring-fencing of capital resources, except where such ring-fencing is statutory; and

- using prudential borrowing for "Invest to Save" schemes, or schemes which generate income.

Aim 3 - Targeted Capital Investment

- annual review of all contractually uncommitted capital schemes which rely on non-ring-fenced funding is undertaken to ensure that they remain a priority in the context of any newly emerging needs and aspirations;
- investment in programmes of a recurring nature that are essential to maintain operational effectiveness; and
- invest in specific schemes that:
    - have a significant catalytic potential to unlock the regeneration of the Island;
    - are significant in terms of the Council strategies that they serve;
    - are significantly income generating or efficiency generating; and
    - if not implemented would cause severe disruption to service delivery.

Prudential Borrowing

3. Prudential Borrowing is only available for a Council's "Primary Purpose for Investment" which must be "consistent with statutory provisions, proportionate to service and revenue budgets and consistent with effective treasury management practice".

4. The arrangements for Prudential Borrowing were strengthened in November 2020 and again in May 2022 and most recently in June 2023 following growing concerns over Local Government commercial property investments and taking on disproportionate levels of commercial debt to generate yield.

5. Borrowing for investments bought "primarily for financial return" (previously known as investment assets bought primarily for yield) is not permissible under the Prudential Code, as it does not constitute the primary purpose of investment and represents unnecessary risk to public funds.

6. Prudential Borrowing is available for "Invest to Save" schemes only where those savings must accrue directly to the Council on a sustained basis. Prudential Borrowing is governed by the Prudential Code and its associated tests of affordability, sustainability and prudence. Prudential borrowing is what is termed “unsupported borrowing” and means that the Government does not provide any revenue support through government grant for the repayment of that debt (neither principal nor interest).

7. The Affordability test dictates that the Council must be able to demonstrate that it can afford the debt repayments over the long term. Given the future forecast deficits of the Council, prudential borrowing is only available for Invest to Save schemes where there is a demonstrable case that the capital expenditure incurred will result in savings (i.e. cost reduction or additional income) that at least cover the cost of borrowing. Also, that those savings accrue directly to the Council and will be available on a sustained basis over the lifetime of any borrowing.

Responses to Specific Scrutiny Questions:

How are risk profiles analysed, recorded, and reported?/ Are there robust mechanisms in place to mitigate against risk?/ How is the capital programme managed?

8. Project managers within Directorates are assigned for each project. The Capital Programme progress is discussed at Directorate Service Boards where risks to delivery will be discussed and mitigating actions put in place. Risks relating to specific capital projects may form part of a Directorate's risk register.

9. The following risks relating to the council's overall capital programme are included in the Strategic Risk Register and are reported to the Audit Committee on a regular basis:
    a. Strategic Risk 1 – Lack of financial resource and the ability to deliver the council's in-year budget strategy; and
    b. Strategic Risk 2 – lack of financial resources and the ability to deliver the council's medium-term financial strategy

10. In addition, the performance of cumulative capital expenditure compared to the profiled budget is a measure reported to Cabinet within the quarterly performance management report (QPMR)

11. Finance staff will liaise with project managers to produce a monthly finance report for the whole capital programme which is presented to the Corporate Management Team and the Corporate Leadership Team

12. Quarterly Capital Reviews also take place with Finance to agree progress and any requirements to re-profile or address overspends.

13. There are also various Directorate Project Boards where specific capital projects e.g. ICT, Regeneration Boards are monitored and managed.

How are decisions on the capital programme agreed?/ What documentation is available to show a clear and detailed audit trail of all decisions related to the capital programme?

14. The proposed capital programme is developed using the aims of the capital strategy set out above as paragraph 2 and schemes are prioritised accordingly in order to make the best use of the modest resources available.

15. The approval of the capital programme is part of the annual Budget Report agreed by Cabinet and Full Council in February.

What criteria are used for allocating money to capital projects?/ Do such criteria link to corporate priorities?

16. See the aims of the capital strategy set out above at paragraph 2.

17. The main sources of capital funding are Government grants, other external grants, S106 funding, Corporate resources such as capital receipts and contributions from revenue budget both planned contributions and underspends transferred to the capital programme at year end and borrowing within the prudential framework.

18. If funding is via ring-fenced grants then this is allocated to the projects that meet the eligibility criteria e.g. Schools maintenance grants, Disabled Facilities Grants, Highways Grants.

19. Corporate resources are then applied to capital projects that are of the highest priority (see Aim 3 set out above at paragraph 2) i.e. that are essential to maintain operational effectiveness, have significant regeneration benefits, generate efficiencies and prevent severe disruption to service delivery such as health and safety schemes, ICT, and Fleet replacement.

20. Some government/external grants require match funding from the council which will be a call on Corporate resources, this is often prioritised as matched contributions can lever in significant amounts of external grant funding e.g. for coastal protection schemes.

Is there a long-term view of the Council's potential capital programme?

21. Please refer to the Capital Strategy as set out at paragraph 2 above.

22. The approved Capital Programme covers a 5 year forward view and will seek to allocate known resources to future years for critical capital investment ensuring that in all years where capital resources are limited, critical investment can continue to be made.

23. The rolling 5-year programme is reviewed annually to ensure that any contractually uncommitted schemes already in the programme are prioritised along with newly emerging capital investment priorities.

What slippage is there on the capital programme and what are the reasons for these?

24. Slippage in the Capital Programme does not mean that an underspend on a particular project has occurred, but that the budgeted spending forecast to take place in a particular financial year will now take place or extend into a subsequent year. The project will remain fully funded and the re-profiling of the budget will simply reflect that slippage has occurred and that spending will now take place at a later date than originally planned.

25. Slippage occurs for a variety of reasons often related to the contractors ability to deliver to the original timeframe due to a variety of factors including operational difficulties, weather and delay in obtaining permissions/licences required.

26. Slippage can also be a result of over-optimism in terms of project delivery planning.

How, are local Members informed of capital projects in their divisions?

27. Through the QPMR budget monitoring process which contains information across the full range projects within the capital programme.

28. Regeneration Place Plans for certain areas are in place which facilitates discussion about local capital projects and cabinet members also engage with local members about specific schemes in their areas.

What steps have been taken over the past 3 years to improve the management of the capital programme?

29. Improvement to the process of profiling expenditure over years. The spending profile is refreshed during the year following the quarterly review meetings with project managers and the revised current year programme is presented as part of the revised budget contained within the annual Budget Report to Cabinet & Full Council (although there still exists level of optimism bias in the delivery of capital schemes).

30. Additional focus is placed on inflationary cost pressures in the current economic environment.

BACKGROUND PAPERS

Budget & Council Tax Setting 2023/24 & Future Years Forecasts (moderngov.co.uk)
Capital Strategy 2023-24.pdf (moderngov.co.uk)

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