APPENDIX B

Capital Strategy

2019/20 to 2023/24

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Contents

Section 1 - Introduction

This Capital Strategy details how the Council deploys and will subsequently manage its capital resources thereby explaining the Council's financial framework for capital investment in support of its strategic priorities.

This strategy covers all aspects of the Council's capital expenditure, resourced both directly by the Council and where resources have been attracted through external funding opportunities.

The strategy demonstrates that the Council takes capital expenditure and investment decisions in line with corporate and service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability. The strategy sets out the medium term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes.

The strategy reflects the aspirations and priorities identified in our Vision 2020 strategy. The Strategy considers external influences such as government policy changes and as well as internal influences.

The Council's capital programme consists of two elements:

- The General Investment Programme (GIP) with a budget for 2019-24 of £5.1 m
- The Housing Investment Programme (HIP) with a budget for 2019-24 of £62.1m

Both are accounted for separately, but the schemes making up the two programmes are subject to the same scrutiny and monitoring arrangements to ensure their effective delivery. General Investment Capital schemes are delivered through the Lincoln Project Management Model which evaluates the financial and service implications and potential risks that may arise from each scheme.

The Council has at 1 April 2018 a diverse asset portfolio including, 7,683 council dwellings, 2,863 car parking spaces, 2 sports and leisure centres, 1,131 acres of parks and recreation grounds, and 5 community centres. There is also a sizable commercial property portfolio including industrial units and shops.

The total value of assets held in the Council's Balance Sheet is shown in the following overleaf:

31/3/2017 £000		31/3/2018 £000
312,454	Property, Plant & Equipment	332,979
5,478	Heritage Assets	6,091
8,519	Investment Property	16,224
629	Intangible Assets	568
2,525	Assets held for sale	4,575
329,605	**Total assets**	**360,437**

Section 2 - Purpose and Objectives

The overall purpose of the Capital Strategy is to give a high level overview of how capital expenditure capital financing and treasury management activity contribute to the provision of services along with an overview of how associated risk is managed and the implications for future financial sustainability.

This Capital Strategy seeks to achieve a number of specific objectives:

- Ensure that the Capital Programme is realistic, affordable and well managed to avoid project over-runs and expensive claims beyond the budgeted scheme value

- Ensure that capital expenditure supports a defined priority of the council

- Ensure that any on-going revenue cost implications including Minimum Revenue Provisions (MRP) and debt costs are understood and accounted for without impacting on the existing financial savings target of the Council

- Wherever possible ensure capital investment activity is focussed on areas that yield on-going revenue savings for the Council or produce a contribution to revenue income.

- Use strategic procurement and new ways of procuring to drive up “value for money” and ‘get more for the same money’.

Section 3 - Policy and Financial Planning Framework

The capital programme for the council is a long term ambition with the obligation for maintaining and improving council and operational buildings stretching fat into the future, and as such should be considered accordingly in financial and asset management planning.

The Council’s capital programme and its subsequent revenue implications form part of the Medium Term Financial Strategy (MTFS) 19-24 and as such is one of a suite of plans and strategies that sit within the Council's Policy and Financial Planning Framework.

Longer term forecasts are not easily predicted and accuracy within them deteriorates the longer the period over which a plan is developed. Within longer term plans uncertainty and complexity in terms of for example economic, social and technological factors mean that long term planning becomes an iterative process which is adjusted for these changes in these and other factors. For major projects and investment, Western Growth Corridor for example, the funding and financial implications will need to be planned well in advance.

There is clearly a link between long term capital planning and treasury management with the council's debt portfolio containing loans which mature up to 2075/76. The profile of debt repayment needs to be managed alongside other long term capital expenditure and funding forecasts.

Linkages with other key strategies and plans are identified below:

Vision 2020

Our vision sets out what the city council wants to achieve for Lincoln and how we are going to achieve it.

The strategic priorities that support this vision are:

- Let's drive economic growth
- Let's reduce inequality
- Let's deliver quality housing
- Let's enhance our remarkable place

These are underpinned by a commitment to professional, high performing service delivery.

Local Plan

The Central Lincolnshire Local Plan has been developed in collaboration with West Lindsey District Council, North Kesteven District Council and Lincolnshire County Council – for Lincoln it is a new city-wide planning and regeneration strategy running up to 2036.

The Local Plan:

- is underpinned by an aspiration for sustainable growth in homes, jobs, services and facilities;
- is aiming to deliver many new homes between now and 2036;

- is seeking to attract new businesses and jobs;
- sets out policies to ensure development is of high quality, sustainable and meets the needs of everyone;
- sets out policies to ensure all the infrastructure, such as play areas, roads, new schools and upgraded sewage disposal, are provided at the same time as the new homes;
- is complemented by a separate Policies Map, which sets out where development should take place.

Asset Management Plan

The Capital Strategy and the Asset Management Plan run alongside each other and have a number of key linkages. These include capital receipts and asset disposal programmes, maintaining, improving and deploying the Council's buildings to support delivery of services and potential loss of income from asset sales.

The MTFS includes capital receipts targets (capital monies received from the sale of council land and property) for both the General Investment Programme and the Housing Investment Programme. Currently the level of capital resources required to fund the capital programme is reliant upon the sale of assets surplus to requirements.

The capital receipts target, necessary to underpin the Capital Strategy, is included within the Asset Management Plan. The Property Services Team keeps under review the need for asset disposal and acquisition, which meet strategic priorities.

The Asset Management Group (AMG) whose membership consists of the Leader of the Council, the Deputy Leader of the Council and the Portfolio Holder for Economic Growth, in addition to Council officers from Financial Services, Property Management, Housing, Major Developments and Planning monitors progress on key aspects of the Capital Strategy and the Asset Management Plan. All proposed property disposals are reported to and agreed by the AMG.

The associated loss of any rental income from asset sales is built into the General Fund budget. The table below shows the current General Fund budget for the loss of revenue rental income.

	2019/20 £000	**2020/21 £000**	**2021/22 £000**	**2022/23 £000**	**2023/24 £000**
Loss of Revenue Rental Income	30	30	30	30	30

There is no budget provision set aside for the loss of revenue rental income in the Housing Revenue Account, however the rental income budget has been set allowing for an average level of right to buy sales spread throughout the financial year.

Risks associated with investing in property are considered on an individual basis and in line the Council's Investment Property Strategy, reports relating to the impact on the MTFS, sustainability of the council and affordability of individual schemes, including funding MRP and borrowing costs are subject to approval by the council's Executive prior to proceeding.

HRA Business Plan

The HRA Business Plan sets out how the Council will deliver its vision for the HRA including, investment in the housing stock, maintaining all homes to the Lincoln Homes Standard and the process of tenant consultation to agree priorities for investment in existing stock over and above the Decent Homes Standard. It also demonstrates that the proposed investment programme is financially viable by indicating that the underlying HRA debt is repayable within the 30 year period of the Business Plan, should the Council chose to do so. There is however, no obligation to repay debt and the MTFS does not assume this is the case. Further borrowing to fund HRA investment is now limited by prudence rather than the old system of an imposed borrowing cap – currently HRA borrowing stands at £58.113m.

The capital schemes contained within the Housing Investment Programme and the capital financing that underpins them feed from the HRA Business Plan and any updates to the plan. The key areas of capital spend identified within the HRA Business Plan and the Housing Investment Programme are based on the results of stock condition surveys of existing housing stock plus any proposed new build schemes. The main areas of expenditure cover:

- Lincoln Homes Programme
- Statutory Health and Safety Requirements
- Contingent Major Repairs Works
- Council House New Build Programme

Treasury Management Strategy

The Treasury Management Strategy is reviewed annually and forms part of the suite of documents which make up the Medium Term Financial Strategy approved by council each year. The Treasury Management Strategy deals with the borrowing and investments arising from all financial transactions of the council and is not limited to those arising from capital spending.

Section 4 - Financing the Capital Programmes

The resources necessary to fund the Council's Investment Programmes come from a variety of sources:

- Capital Receipts – from the sale of Council assets

- Use of Council's own resources – through depreciation charges, other contributions from revenue and use of reserves

- Capital Grants and Contributions – including contributions from developers and grants towards specific schemes

- Prudential Borrowing – the Prudential Code allows borrowing if the Council can demonstrate it is affordable, sustainable and prudent in its Prudential Indicators (detailed in the Treasury Management Strategy)

The General Investment Programme is reliant on the generation of capital receipts to fund the investment required to deliver its programme of spend. In the long term, this is not sustainable and other sources of funding are regularly sought to fund capital expenditure. However, many of the external grants and contributions, which are available, are designated for specific schemes, and whilst additional resources are clearly beneficial to local people, there is the danger that schemes funded may not be the Council's highest priorities.

The Capital Strategy must continue to identify both the priorities for these external funding regimes and pursue other innovative funding sources to improve its ability to deliver capital investment. Each project appraisal will consider all the internal and external resources available such as Lottery funding, Section 106 contributions and prudential borrowing.

The Council will actively pursue Invest to Save opportunities financed through prudential borrowing, where the revenue costs of borrowing are financed through additional income/reductions in expenditure as a direct result of the Invest to Save scheme. The cost effectiveness of borrowing as opposed to selling capital assets is reviewed regularly together with the affordability tests and impact on prudential indicators to check whether borrowing would provide more cost effective funding. It has been concluded that the use of prudential borrowing will now be a useful funding mechanism for some key projects.

Under the self-financing regime, the government retained the current arrangement for pooling of HRA capital receipts. All HRA capital receipts are pooled if they are not offset by the capital allowance (a capital allowance is permitted where the receipt is used to fund affordable housing, decent homes or regeneration schemes). It is the Council's strategy that 100% of non-Right to Buy (RTB) receipts will be offset by the capital allowance. However, 75% of all RTB capital receipts have to be pooled.

The Council's capital programme (expenditure and resources) is projected for a five-year period and is approved by full Council as part of the MTFS each year. It is monitored throughout the year by the Capital Programme Group and the Executive. Capital Programme Group and the Executive have varying levels of authority to approve changes to the programme during the year. A distinction is made between the General Fund schemes (GIP) and Housing Revenue Account schemes (HIP). It is Council policy that capital receipts from the sale of Council Houses and other Housing Revenue Account assets are used to fund the HIP, with capital receipts from the sale of General Fund assets used to fund the GIP.

The City Council's General Investment Programme and Housing Investment Programme for the period 2019/20 – 2023/24, are set out in the MTFS 2019-24.

Section 5 - Capital Prioritisation

In an environment of financial constraints and competing pressures on the Council it is important that the Council adheres to its methodology for prioritising potential projects and schemes. The methodology is based on both corporate and service based priorities. As well as considering capital costs and funding, attention is also focussed on the revenue implications of any capital expenditure to ensure the Council will not inherit a legacy of increased revenue costs. Therefore, only whole life costs are considered when evaluating potential capital projects.

The Vision 2020 Plan which was approved by Council in January 2017 focused on the following priorities:

- Let's drive economic growth
- Let's reduce inequality
- Let's deliver quality housing
- Let's enhance our remarkable place

These priorities will be underpinned by our commitment to:

- Professional, high performing service delivery

Inclusion of capital schemes within the strategic plan (currently Vision 2020) and future versions is dependent on a prioritisation process. Project Managers will be required to prepare bids for inclusion in the strategic plan. Project managers in preparing such bids will be required to effectively demonstrate how these will support the achievement of both their service area aims and the Council's strategic priorities.

The preparation of these project briefs must go through the five essential steps to initiate the project as defined in the Lincoln Model:

1. The project mandate – where the ideas for the project is first discussed between the project sponsor and the project manager. It provides an initial assessment of the project and provides a clear description of why the project is required and what it is intended to achieve in terms of benefits to the Council's corporate objectives.

2. Establishing Reporting Criteria – formal approval and subsequent monitoring will take place. Approval for all new project budgets and budget changes will follow Financial Procedure Rules.

3. Appraise Options for Delivery - in order to demonstrate that the project delivery selected is the most appropriate and the most cost-effective.

4. Develop the Project Brief, Financial Assessment and Impact Assessment - these three documents clearly document the scope of the project, its objectives, the potential resources required (including a full financial breakdown) to deliver it and its impact.

5. Obtain approval to submit the project - Formal approval to submit the project is agreed and signed-off between the Project Manager and the Project Sponsor.

Once prepared, the project brief is submitted to the Vision Theme Groups for approval ahead of consideration by the Corporate Management Team and Portfolio Holders to evaluate, including how well the proposal meets strategic priorities, including cross cutting strategies and budget priorities, and how it utilises partnership working and externally generated resources as well as its operational feasibility. They will also consider the robustness of each project brief against the corporate standards in relation to clarity of definition, establishment of measurable outcomes and overall deliverability and the robustness of each Financial Assessment and Impact Assessment, including cost data in relation to project costs (including any costs associated with borrowing), post implementation ongoing revenue costs and any consequential or related income.

This approach is an iterative process that involves and engages both Members and the public to produce a basket of schemes that meet recognised local needs. Once a programme of final projects is developed it is submitted to the Executive for approval and inclusion in the capital programmes.

Once projects are approved, the next stage is to develop the detailed Project Plan which will include a Communications Plan and public consultation where relevant. This is where the project is debated by the community, business and voluntary groups. The results of the consultation are reported back to Executive and Council and form part of the reporting process.

The entire process conforms to both the Council's project management methodology (The Lincoln Project Management Model) and also the Performance Management Framework adopted by the Council, which ensures schemes are not progressed for Member deliberation and support unless they are deliverable within the context of other competing pressures.

Once the Executive approve a scheme the budget is included in the capital programme.

Section 6 - Capital and Project Monitoring

The delivery of schemes supporting the delivery of Vision 2020 is monitored by the individual vision theme groups who report progress on an exceptions basis to the Executive and Performance Scrutiny on a quarterly basis. In addition the overall capital programmes are monitored by the Capital Programme Group, with financial performance reporting to the Executive and Performance Scrutiny on a quarterly basis.

The Capital Strategy and the capital programme are updated on a rolling basis and are reported annually to Executive and Council for approval alongside the MTFS. In addition, the Council's Executive is required to approve variations to the capital programme beyond the limit delegated to the Chief Finance Officer.

When a project is completed a Post Implementation Review (PIR) is carried out. However, some projects are recurring in nature such as the capital maintenance programme or the Decent Homes programme. These still require an annual PIR.
A PIR is a formal review of the project which aims to answer the question: "Did we achieve what we set out to do … and if not, what should be done?"

A PIR can provide valuable lessons and experience that can be used to improve and shape service delivery in the future. The Lincoln Project Model includes a robust post project review system, overseen and reviewed, to ensure relevant information is collected and communicated to all relevant parties to enable improvement in both procurement and service provision and will consider if the project:

- Met its stated aims and objectives
- Was delivered on time and within budget
- Was acceptable to the client/stakeholder and met all their specific requirements

Section 7 – Commercial Activity and Investment Property

The Chartered Institute of Public Finance and Accountancy (CIPFA) defines investment property as property held solely to earn rentals or for capital appreciation or both. Returns from property ownership can be both income driven (through the receipt of rent) and by way of appreciation of the underlying asset value (capital growth). The combination of these is a consideration in assessing the attractiveness of a property for acquisition.

A commercial property investment strategy document is under development which will identify the criteria against which decisions are taken. The council invests in property to provide a positive surplus/financial return after the payment of borrowing costs but to also as a direct way if influencing regeneration and the economic development of the City. This enables the council to invest the surplus in the provision of services to local people. The council may fund the purchase of property through borrowing (through the PWLB or as part of cash flow borrowing). Under new guidance issued by CIPFA, borrowing solely to invest in revenue generating investments is considered to be borrowing in advance of need – whilst this is not prohibited councils are required to make disclosures to the effect that this borrowing is taking place, their dependence on commercial income to deliver statutory services and the amount of borrowing committed to generate that income. Further details are listed in this section.

Historically the council's property investments have provided strong returns in terms of capital growth and generation of stable income. Property investments are not without risk as property values are subject to many national and other external factors which are outside the control of the council. Where possible investments of this type will also have a 'fall back' position in addition to their expected commercial arrangement e.g. the council has purchased the freehold of a car park which it leases to a large, national company however should the company surrender the lease or not meet the lease payments the council could operate the car park themselves or seek an alternative tenant.

The strategy continues to be that the council will invest prudently on a commercial basis and take advantage of opportunities as they may arise which meet our strategic objectives and provide a revenue surplus, supported by our robust governance arrangements.

At 1/4/2018 the council has £17.044m of investment properties on the balance sheet with further investment of £19m planned within the current General Investment Programme for 2018/19. The income from investment properties is predominantly derived from ground rent and land leases. Further details relating to investment properties are given below:

Total value of investment properties	£17,043,500
Value of properties held for rental income	£16,218,000
Value of properties earning rental income	£15,601,000
Potential income from all investment properties held for rental income	£866,271
Potential yield from all properties held for rental income	5.34%
Income from properties earning rental income	£780,671

Yield from properties earning rental income	3.80%
Value of properties held for capital appreciation or where the freehold has a market value*	£825,500

*The council has arrangements where the freehold on land is retained, generally subject to a long lease but which produces no rental income, however the freehold land does have a market value.

For the year 2018/19 the anticipated income from investment properties represents less than 1% of the council's gross expenditure.

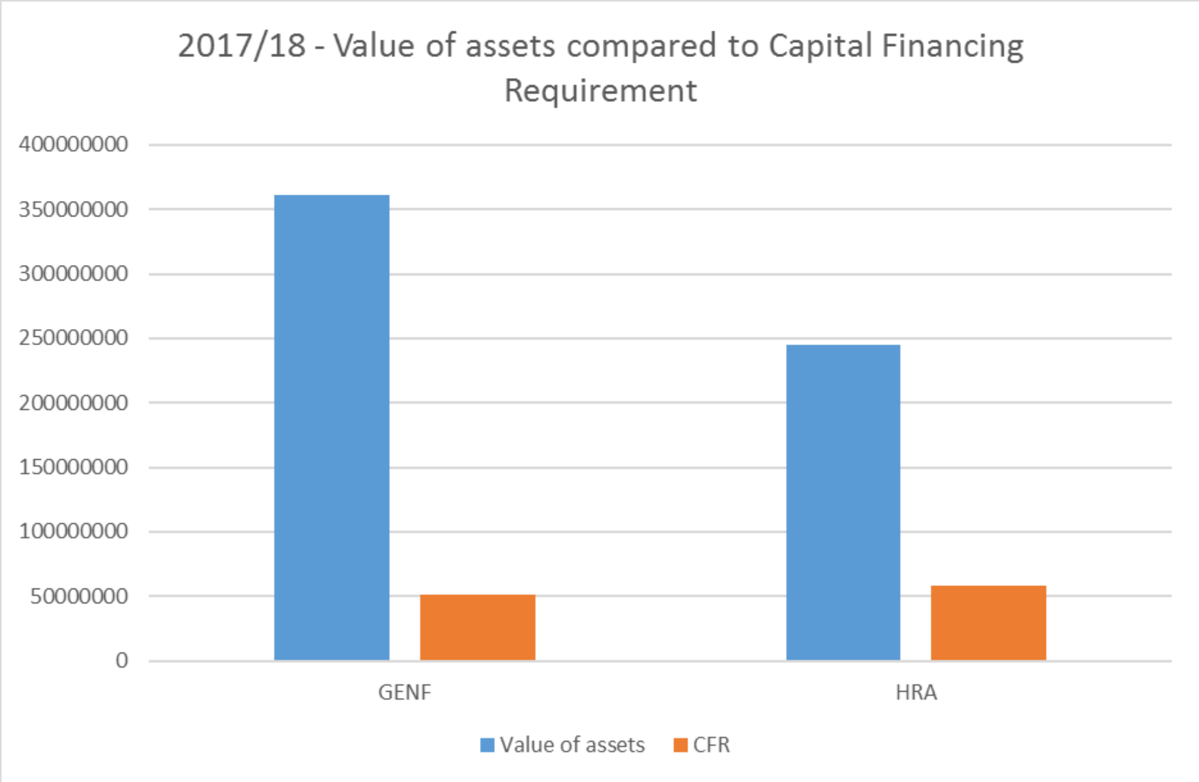
Many of the council's investment properties have been council assets for a number of years. More recently the council has borrowed to fund the purchase of assets. The financial impact of this is shown in the table below.

Asset type	Value	Annual income	Yield on value of assets	Borrowing costs	Annual surplus
Car Parks	£6,580,000	£316,161	4.81%	£192,180*	£123,981

*assumed in business case

Within the General Fund Investment Programme a further £19m purchase of investment property will take place during 2018/19, funded by borrowing. Net income expected from this purchase is budgeted to be £288k per annum – a further update will be provided once the properties has been valued at 31 March 2019.

A graph illustrating the value of the council's assets compared to the capital financing requirement (the underlying need to borrow to fund capital investment) at 31 March 2018 is given below:



The table below indicates the interest cost of borrowing within the general fund and the housing revenue accounts compared to overall gross expenditure. The limits indicated are set locally and are not imposed by central government or advisory levels provided by CIPFA.

Current budgeted cost of borrowing

	19/20	20/21	21/22	22/23	23/24
GENF borrowing cost as a % of gross revenue expenditure	8.76%	8.82%	8.75%	8.58%	8.49%
Limit of GENF borrowing cost as a % of gross revenue expenditure	12%	12%	12%	12%	12%
HRA borrowing cost as a % of gross revenue expenditure	10.57%	10.47%	10.26%	10.05%	10.00%
Limit of HRA borrowing cost as a % of gross revenue expenditure	14%	14%	14%	14%	14%

Section 8 – Loans and investments in local businesses and organisations

The council has the discretion to make loans and investments in local organisations for a number of reasons, primarily for economic growth; these loans are treated as capital expenditure.

In making these arrangements the council exposes itself to the risk that the borrower defaults on repayments. The council must therefore ensure that it has fully considered the risk implications with regard to both the individual loan and that the value of them individually and collectively is proportionate and prudent within the overall exposure to the council to risk of default.

To ensure that the risk is managed a full due diligence exercise is undertaken, with a business case that identifies the benefits and risks and considers whether adequate security is in place. Loans and investments will be agreed by Executive and will be subject to close regular monitoring.

Section 9 – Knowledge and Skills

The Council's Capital Strategy is reviewed annually and compiled by the Chief Finance Officer, an experienced and qualified accountant. External advice is available from the Council's Treasury Management advisors (Link Asset Services) who offer a range of services in relation to borrowing advice, leasing and capital investment options. The council is also a subscriber to the CIPFA Finance Advisory Network which provides advice on technical accounting matters. Additional specialist tax advice in respect of tax implications for property transactions is available from an external supplier of this service (PS Tax). The council has an in-house legal team and additional legal specialist support is available from external sources. The council has an in-house property services section headed by a RICS qualified surveyor and additional specialist support in respect of property matters is available through the district valuer and other external sources.

Section 10 - Conclusion

The Council's Capital Strategy is a 'live' document, which provides a framework for the deployment and management of capital resources across the organisation in accordance with corporate priorities. It is therefore the framework for capital investment across the Council. The Strategy will be reviewed annually, to ensure it is kept up to date and is relevant and effective and reflects best practice.