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Corporate Capital Strategy (including the Capital Receipts Strategy)

Torbay Council

Contents

1 Introduction 3
2 Guiding Principles 4
2.1 Approach to Borrowing 4
2.2 Grants 4
2.3 Capital Receipts and Capital Contributions 5
Asset disposals 5
Asset disposals at nil consideration or below market value 5
Right-to-Buy Clawback 6
Section 106 contributions and Community Infrastructure Levy (CIL) 6
Repayment of loans for a capital purpose 6
2.4 Capital Receipts Strategy 6
2.5 Revenue and Reserves 7
2.6 Prioritisation and Approval 7
2.7 Alternative Funding and Delivery Opportunities 8
2.8 Investment Opportunities (including capital loans) 8
Appendix 1 – Definition of Capital Expenditure 9
Appendix 2 – Capital Scoring Matrix 10

1 Introduction

The Corporate Capital Strategy is the policy framework document that sets out the principles to be used to guide the allocation of capital investment across all of the Council's services and informs decisions on capital spending priorities within the Council's 4-year Capital Plan.

Capital investment is technically described as **"Expenditure on the acquisition, creation, or enhancement of 'non-current assets'"**. This is items of land, property and plant which have a useful life of more than one year. A fuller definition is attached at Appendix 1. Expenditure outside this definition will be, by definition, revenue expenditure.

Most non-current assets are properties that are used in service delivery. The Council's land, buildings and infrastructure asset base of some 3,700 properties has a current use Balance Sheet value of approx. £335 million. In addition the Council has an interest in assets held by Diocese and Foundation schools and assets of companies the Council has a financial interest in such as the Torbay Economic Development Company (TDA).

The changes in valuation for Highway Network Assets from a historic cost basis to a depreciated replacement cost basis is expected to increase the value of the Council's asset base by over £1.4 billion as at 31st March 2018.

Although this Strategy focuses on the Council's management of its own investment in assets, a wider view of capital investment throughout Torbay by both the public and private sectors will have a major influence on meeting Council aims and objectives.

The Capital Strategy is presented to Council as a Policy Framework document, and links with both the Treasury Management Strategy and the Corporate Asset Management Plan. Both documents are available from Council offices and on the Council's Website.

The Capital Strategy sets out the guiding principles on the following elements:

- Approach to Borrowing
- Grant Allocation
- Capital Receipts
- Capital Receipts Strategy
- Revenue and Reserves
- Prioritisation and Approval
- Alternative Funding and Delivery Options
- Investment Opportunities (including capital loans)

In considering the principles, the Council needs a balance between guidance and prescription to allow a flexible approach to be taken, but which is reflective of times of uncertainty. This Strategy focuses on the key policies for the allocation of capital resources to schemes in line with Council priorities and statutory responsibilities.

The management of the Capital Plan is also supported by the Council's approved Financial Regulations.

2 Guiding Principles

2.1 Approach to Borrowing

The Council is able to borrow money on the money market or from the Public Works Loans Board to fund capital schemes or, on a short term basis, use its own internal resources (i.e. cash flow). However for all schemes initially funded from borrowing, the Council will have to fund the repayment and interest costs as there is no longer any central government "supported borrowing" allocations and related revenue support.

The Council is only able to borrow for "unsupported borrowing" (also known as Prudential Borrowing) under the guidance contained in the CIPFA Prudential Code whereby, in summary, the Council is required to ensure that all borrowing is both prudent and affordable. All schemes funded from prudential borrowing are approved by full Council.

The Council's 2017/18 Treasury Management Strategy recognises the need to take up to £66m of borrowing to support a number of capital projects. Council approvals for expenditure funded from prudential borrowing such as £50m for an Investment Fund will significantly impact on treasury management strategies. Based on current economic forecasts a borrowing cost of 3% - 3.5% should be assumed for new borrowing in 2017/18.

The Council takes a prudent approach to new borrowing, paying particular regard to the robustness of the business case, to include forward predictions of affordability with the aim that projects should be self-funding (i.e. create a revenue stream so that the cost of borrowing is cost neutral). It is essential that any new proposals for a self funding or invest to save scheme supported by borrowing has a robust business case that is presented to senior members and officers prior to approval by Council.

To support its revenue budget the Council will continue to evaluate any capital investment projects, either acting alone or with partners that will produce an ongoing revenue income stream for the Council. This is one of the scoring criteria now adopted by the Council when assessing competing capital projects.

There may be the need for borrowing that has no identifiable future revenue stream, for example, to repair or construct infrastructure assets. Here a broader view can be taken of the value of repairing the asset to the overall economy of Torbay. In these circumstances, the cost of such borrowing falls on the Council's revenue account, with the repayment of debt over a specified period of time. There may still be a need for such borrowing but each proposal should be reviewed on a case by case basis with the project evaluation clearly stating how the borrowing is to be afforded. Given the significant ongoing financial challenges facing this Council over the next few years it is likely that such schemes will be an "exception".

2.2 Grants

The Council receives capital grant funding from government and is able to bid for grant funding direct to particular government departments or from other grant awarding bodies. The funding from central government is typically un-ring fenced and without conditions, however this funding is now at levels significantly lower than in the last decade.

The Council now has greater flexibility in allocating capital grant funding which allows the Council to direct funding to local priorities which may not be in line with government allocations which are, to some extent, based on local need. Service intentions of the awarding government body should be taken into account in determining allocations, in particular if future funding allocations could be impacted.

Any un-ring fenced capital grants received, even if these are allocated with service intentions of the awarding government body, will be required to be approved by Council. Consequently once capital grants have been allocated to a specific service by Council, individual schemes within that allocation will be agreed in accordance with the Council's Constitution and Financial Regulations.

The Disabled Facilities Grant (now including the Social Care capital grant) is now included in the Health and Social Care "Better Care Fund", although outside the s75 pooled budget agreement with the Clinical Commissioning Group.

The Council continues to bid for additional external grant funding but restricts schemes to those which support corporate priorities or statutory service objectives and where it can be proved that the project is sustainable, and where requirements for match-funding and future revenue consequences have been considered and approved. All schemes are to be agreed by the Chief Executive in consultation with the Mayor/Executive Lead for Finance and the Head of Finance prior to submission and/or contractual commitment.

2.3 Capital Receipts and Capital Contributions

The Council receives capital receipts and capital contributions from:

- Asset disposals
- Right to Buy Clawback
- Section 106 and Community Infrastructure Levy (CIL)
- Repayment of loans for a capital purpose

Asset disposals

The current policy is to pool all receipts from the sale of all assets sold to support the Capital Plan in line with funding the Council's priorities with a capital receipts target set out in the Capital Plan. All capital receipts received should be allocated to support this target and not allocated to new schemes, subject to any potential use of capital receipts under the Capital Receipts Strategy (see para 2.4 below). An asset disposal will be deemed to occur when the Council transfers the freehold or a long lease (usually over 40 years)

The Council will consider exceptions to this policy where rationalisation of assets used for service delivery is undertaken and in respect of school sites where the Secretary of State has approved the disposal – such exceptions will require Council decision.

The Council will aim to maximise its capital receipts, where possible, by enhancing the land prior to disposal; e.g. by obtaining planning permission or providing a development plan. As appropriate the Council may dispose of assets by tender or by public auction.

Asset disposals at nil consideration or below market value

In considering asset disposals, the Council also needs to take into account the policy on Community Asset Transfers where the Council will consider, on a case by case basis, the potential transfer of assets to an alternative provider after a full assessment of the long term (full life) risks and rewards of the transfer, including the achievement of best value including potential market value, linked to the Council's aims and objectives.

The Localism Act 2011 introduced the “Community Right to Bid” and placed a duty upon local authorities in England to maintain a list of assets of community value. Once an asset is “Listed” any disposal will be under the Community Asset Transfer policy or for market value by tender/auction.

Where the Council proposes to dispose of, or grant a long lease, at nil consideration or at a value below market value this is required to be approved by Council. This will also apply where the disposal is for a community or service benefit.

There may be circumstances, such as the transfer of community school assets under the Academies Act, where assets will also be disposed of at nil consideration.

Right-to-Buy Clawback

100% of these receipts are currently used to support the provision of the housing function, although this policy could be changed by Council to provide additional resources for projects in other service areas.

Section 106 contributions and Community Infrastructure Levy (CIL)

Section 106 (S106) monies come from developer contributions through the planning system. Unless there are service specific conditions on the use of the S106, the monies should be used to support existing Council priorities and commitments rather than be allocated to new schemes. Any S106 monies received without a service or scheme specific allocation within the planning agreement will be allocated in accordance with this Capital Strategy.

Any monies received for infrastructure from the Community Infrastructure Levy will not be allocated to a specific service but will be allocated under the CIL arrangements (“the Regulation 123 List”) in line with Council’s capital scheme priorities including any specific funding requirements such as the South Devon Highway.

The current policy is to pool all capital contributions to support the Capital Plan in line with funding the Council’s priorities. The current Capital Plan has a capital contributions target to support the approved Plan. All capital contributions received should, where possible, be allocated to support this target and not allocated to new schemes.

Repayment of loans for a capital purpose

Where the Council provides a loan for a capital purpose this will be approved and accounted for as capital expenditure. The repayment of a loan by the borrower will be treated as a capital receipt; however any receipts of this nature will be specifically applied to reduce the value of the outstanding loan.

2.4 Capital Receipts Strategy

The Department for Communities and Local Government (DCLG) have revised their statutory guidance in relation to the Local Government Act 2003 on the use of capital receipts for the period from April 2016 to March 2019. This now provides councils the flexibility to use capital receipts for “the revenue costs of service reform”. This flexibility is subject to a Strategy for the use of capital receipts being approved by Council. By approving this document Council will be approving this flexibility to be used as deemed appropriate by the Head of Finance with any use reported to Council as an amendment to the Council’s Capital Plan.

Potential uses for capital receipts (subject to the capital receipts being received and Council approval of changes to capital plan) would be to support any implementation costs for the Council's transformation programme. A number of transformation schemes were identified in the Council's Efficiency Plan approved by Council in September 2016.

DCLG, within their statutory guidance, have included a number of examples of the type of expenditure that would meet the definition of "revenue costs of service reform":

www.gov.uk/government/uploads/system/uploads/attachment_data/file/507170/Flexible_use_of_capital_receipts__updated_.pdf

2.5 Revenue and Reserves

The Council is able to use revenue funding and reserves for capital schemes. However, as a result of competing revenue budget pressures and the continued reduction in government support for revenue expenditure, the Council's policy is generally not to budget to use revenue or reserve funds to directly fund capital projects after the feasibility stage.

2.6 Prioritisation and Approval

It is always difficult to make choices between competing priorities within a top tier Council that delivers so many varied services. A Capital Reserve list is maintained. It will also be important to ensure sufficient flexibility to take advantage of any funding opportunities that may occur mid year or fill any gaps where slippage occurs.

The Council has approved a 'scoring matrix' to help inform its priority schemes and this can be used to evaluate competing projects on the Council's Capital Reserve List or new bids for capital funding as and when capital resources become available.

Scores are assigned to various capital projects using the matrix and are appended to the Capital Plan presented to Council in February each year. The scores are subjective in nature but provide a useful basis for comparing competing schemes.

The projects on the scored list include some schemes which are already part of the approved Capital Plan but which have not yet commenced, alongside schemes from the Capital Reserve List. There are also illustrative schemes from the Integrated Transport Block to indicate the types of projects included in this block funding. It should be noted that some projects are more fully 'worked up' than others and consequently the information available varies considerably and some assumptions have been necessary.

The scoring from the matrix is presented for information which can be used as a guide to informing future allocations of Council funding. In addition the Council is able, subject to any funding restrictions, to reverse previous allocations of funding to schemes that have not progressed and reallocate to other projects. The capital matrix again can help inform that process.

The capital matrix is an aid to evaluate priorities between often very disparate schemes; however allocation of funding to capital is ultimately a Council decision at the time funding becomes available.

The key stages in the Council's prioritisation and approval process are as follows:

1. If a specific scheme is requested to be approved/funded there will be a requirement for a detailed business plan or project outline. Business plans are to be submitted to the Chief Executive for review in consultation with the Mayor/Executive Lead for Finance and Head of

Finance. Decisions on whether to progress specific schemes will be made in accordance with the Council's Constitution and Financial Regulations.

2. Proposals for invest to save or self financing schemes, (usually financed from prudential borrowing), will also require a detailed business case to be submitted to the Chief Executive for review in consultation with the Mayor/Executive Lead for Finance and Head of Finance. If the scheme is supported it will be recommended to Council for approval, in accordance with the Constitution and Financial Regulations.

3. The Capital Plan will be updated and any recommendations for schemes to be approved by Council included in the next quarterly Capital Plan Update Report.

4. Other schemes that do not require financial support but include the use of Council assets as a Council contribution to a scheme will also be subject to the Council's approval process.

5. Where there is a proposal to transfer capital resources from a previously approved scheme to a new scheme and there is a change of "policy", the new scheme will be approved by Council.

2.7 Alternative Funding and Delivery Opportunities

As Council capital funding is reduced the Council will continue to consider alternative methods of supporting capital expenditure within Torbay, using alternative funding, such as social investment, private sector finance and third sector funding or by other bodies delivering capital schemes instead of the Council.

The Council can use its assets to support schemes or aim to maximise funding from any source possible, such as European or Local Enterprise Partnership funding.

The Council continues to bid for additional external funding, work with other bodies to secure capital investment or consider use of its own assets in a development. It restricts schemes to those which support corporate priorities or statutory service objectives and where it can be proved that the project is sustainable. It will also consider the requirements for match-funding and future revenue consequences along with an assessment of the opportunity costs of alternative options. All schemes are to be agreed by the Chief Executive in consultation with the Mayor/Executive Lead for Finance and the Head of Finance prior to submission and/or contractual commitment.

2.8 Investment Opportunities (including capital loans)

Linked to its approach to borrowing and its Treasury Management Strategy the Council will consider, if the opportunities arise, the purchase of land and property as an investment – to both generate an ongoing income stream and to realise an increased capital value in the future. This could include the purchase of land or property or the purchase of "shares" in a property fund. Depending on the capital funding proposed the appropriate approvals will be requested including approval within the Treasury Management Strategy.

Loans for a capital purpose can also be approved subject to a business case and due diligence on the borrower including, as appropriate, guarantees and bonds to secure the repayment of the loan.

The Council at its meeting in September 2016 approved an increase in a capital investment fund from £10m to £50m to seek investment opportunities.

Appendix 1 – Definition of Capital Expenditure

Capital investment is simply described as:

> *Expenditure on the acquisition, creation or enhancement of "non-current assets"*
>
> *(non-current assets are items of land and property which have a useful life of more than 1 year)*

This definition of capital expenditure that the Council has to comply with for the classification and, therefore, the funding of capital expenditure in linked to International Financial Reporting Standards. "Qualifying Capital Expenditure" under s25 of Local Government Act 2003 is defined when:

> "The expenditure results in the acquisition, construction or enhancement of fixed assets (tangible and intangible) in accordance with "proper practices""

"Proper Practice" (from 1 April 2010) is under International Financial Reporting Standards (IFRS) rules. The relevant standard is IAS16 which has the following definition of capital expenditure:

> "Expenses that are directly attributable to bringing an asset to the location and condition necessary for it to be capable of operating in the manner intended by management".

"Directly attributable" means that, for examples, if building a school, it is the costs linked to the actual construction of the building, not temporary accommodation, moving people around etc.

Subsequent Capital Expenditure on an asset is defined as:

> "Expenses that make it probable that future economic benefits will flow to the authority and whose cost can be measured reliably" subject to "if the expenditure is to replace a component, the old component must be written out of the balance sheet".

Future economic benefits means that it is not necessary for the expenditure to improve the condition of the asset beyond its previously assessed standard of performance. The measurement is against the actual standard of performance at the date of expenditure; e.g. if service potential or asset life is increased.

Appendix 2 – Capital Scoring Matrix

Capital Projects Assessment Criteria

Possible Weightings

1 **Statutory Status: includes support of a statutory Service requirement**

3 points	Meets a specific immediate or forthcoming statutory requirement	factor = x	**3**
2 points	Meets an underlying statutory duty	Max score	**9**
1 point	Meets a discretionary requirement		
0 points	no indication of status		

2 **Corporate Plan Priorities**

3 points	Specifically identified in Corporate Plan	factor = x	**2**
2 points	Identified as a key Project/Activity in the Corporate Plan or directly supports a number of specific outcomes	Max score	**6**
1 point	Generally supports specific Actions or outcomes		
0 points	Will not deliver any identified outcomes		

3 **Mayoral Promises (per Manifesto)**

3 points	Identified as a specific Action or directly supports a number of specific outcomes	factor = x	**1**
2 points	Generally supports specific Actions or outcomes	Max score	**3**
1 point	Broadly related to achieving outcomes		
0 points	Will not deliver any identified outcomes		

4 **Equality , Diversity & Deprivation Issues**

3 points	Will achieve improvement in 3 issues	factor = x	**1**
2 points	Will achieve improvement in at least 1 issue	Max score	**3**
1 point	Possibility of improvement in at least 1 issue		
0 points	No demonstrated improvement in any issues		

5 **Condition, Health and Safety risk and Strategic Importance of Asset Issues**

3 points	Expenditure on asset will reduce impact of 3 issues	factor = x	**1**
2 points	Expenditure on asset will reduce impact of at least 1 issue	Max score	**3**
1 point	Expenditure will have a possibility of reduced impact in at least 1 issue		
0 points	No demonstrated impact on any issues		

6 Outcomes, Added Value, Cross-service benefit

3 points	Good - Large number of beneficiaries / target groups (>25,000)	factor = x	**1**
2 points	Satisfactory - Significant number of beneficiaries / target groups (10,000-25,000)	Max score	**3**
1 point	Fair - Reasonable number of beneficiaries / target groups (1,000-10,000)		
0 points	Poor - Few beneficiaries / target groups (<1,000)		

7 Risk to Community of NOT doing (i.e. identified in Risk Register)

3 points	High Risk (9-16)	factor = x	**2**
2 points	Medium Risk (5-8)	Max score	**6**
1 point	Low Risk (1-4)		
0 points	no Risk identified		

8 Risk of Doing (Can project be delivered?) - achievability, timescale, resources required

3 points	Low Risk (1-4)	factor = x	**2**
2 points	Medium Risk (5-8)	Max score	**6**
1 point	High Risk (9-16) with Mitigation		
0 points	High Risk (9-16) with no Mitigation		

9 Quality of Business Plan

3 points	Option proposed demonstrates a strong case based on full assessment of the options	factor = x	**2**
2 points	Reseasonable case with some assessment of the options	Max score	**6**
1 point	Basic case presented		
0 points	Weak case with no comparison of options		

10 Potential to generate future investment return

3 points	Considerable additional net revenue income stream meets both £100k pa and > 25% of project cost)	factor = x	**5**
2 points	Moderate additional net revenue income stream (meets both £50k - £100k pa and 10-25% of project cost)	Max score	**15**
1 point	Small additional net revenue income stream (meets both <£50k pa and < 10% of project cost)		
0 points	No potential net revenue income		

11 Ongoing revenue costs over the life of the asset

2 points	Revenue saving or income exceeds borrowing and running costs	factor = x	**2**
1 points	Revenue saving or income exceeds running costs	Max score	**4**
0 points	Additional costs can be met solely from within existing resources		
-2 points	Additional on going resources required over existing budgets		

12 Specific External resources to support scheme (including Regional funding)

3 points	Specific (ring fenced) funding requires no additional Council funds	factor = x	**4**
2 points	Specific (ring fenced) funding and requires Council funds of both 10% match funding or up to £250k	Max score	**12**
1 point	Specific (ring fenced) funding and requires Council funds of both 50% match funding or between £250-500k		
0 points	Specific (ring fenced) funding but requires Council funds of both 75% match funding or > £500k		

13 Deprivation Critical Factor

1 points	Project is able to reduce the level of deprivation within Bay	factor = x	**5**
0 points	Project does not impact or has minimal impact on reducing the level of deprivation within Bay	Max score	**5**
		Max score	**81**