



Draft Capital Strategy

2020-21 to 2029-30



1.0 INTRODUCTION

The Prudential Code for Capital Financing in Local Authorities (2017) placed a requirement on local authorities to determine a Capital Strategy, to be approved by full Council, which demonstrates that the authority takes capital expenditure and investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability. Local Authorities should have in place a Capital Strategy that sets out the long-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.

This Capital Strategy is the policy framework document that sets out the principles to be used to guide the allocation of capital investment across all the Council's services and informs decisions on capital spending priorities within the Council's 10 year Capital Programme. It also reports on the delivery, affordability and risks associated with this Strategy.

1.1 AIMS AND PRINCIPLES

The Capital Strategy is presented to Council as a Policy Framework document, and links with the Corporate Plan, Treasury Management Strategy (TMS), Medium Term Financial Strategy (MTFS) and the Council's Asset Management Plan (AMP). It sets out:

- what is capital expenditure/investment and why we incur it;
- the Council's overall capital objectives, priorities and plans;
- how the Council's capital expenditure/investment will be funded/resourced
- how the Council's capital expenditure/investment plans will be appraised;
- how capital plans will be approved, monitored and reported upon; and
- the skills and knowledge required to deliver the capital plans.

The Capital Strategy should be read in conjunction with the Council's TMS which covers the Council's Investment Strategy and Borrowing Strategy and the Minimum Revenue Provision (MRP) policy which is attached as Schedule A to this document. The Council's borrowing and MRP policy are directly impacted by capital plans.

The capital programme is a key element of the MTFS. The MTFS provides a set of clear principles which drive the budget and spending decisions of the Council. There are thirteen principles in total, but the following three refer specifically to the capital programme and Strategy:

10. Capital investment decisions are in alignment with the Council's Capital Strategy, and mitigate any statutory risks taking account of return on investment and sound option appraisals.
11. Prudential borrowing is only used to support the capital programme where it is affordable and sustainable within the Council's overall borrowing limits and the revenue budget over the long term.
12. Decisions on the treatment of surplus assets are based on an assessment of the potential contribution to the revenue budget and the capital programme.

The Capital Strategy sets out a number of guiding principles on the following:

PRINCIPLE 1 : Focus capital investment on delivery of the Council's Objectives and Priorities
<ul style="list-style-type: none"> • Ensuring that capital investment plans are driven by the Council's Corporate Plan • Ensuring decision-makers are clear on the positive contribution capital investment makes to our Wellbeing objectives • Appraising all investments in the context of objectives/priorities • Ensuring there is a corporate business planning process incorporating service transformation and the impact on property assets
PRINCIPLE 2 : Ensure strong governance over decision-making
<ul style="list-style-type: none"> • Ensuring that proposals demonstrate that a rigorous process of options appraisal has been followed, requiring evidence of need, cost, risk, outcomes and methods of financing • Schemes will only be added once an affordable business plan is in place and it demonstrates value for money • All major capital schemes have a lead Project Sponsor and follow project management principles • The approval process within the Financial Procedure Rules contained in the Constitution are strictly adhered to
PRINCIPLE 3 : Ensure capital plans are affordable, sustainable and prudent
<ul style="list-style-type: none"> • Promote capital investment which allows invest to save outcomes and which contribute to future MTFS savings • Make sure assets perform at an optimal level through effective ongoing asset management and are consistent with levels of investment • Review and challenge the Council's assets, including the need, cost and performance of the estate • Maximise the use of Internal Borrowing and maintain an under-borrowed position compared to its Capital Financing Requirement if feasible
PRINCIPLE 4 : Maximise and promote the best use of available funds
<ul style="list-style-type: none"> • Generate funding, where possible, from the rationalisation of existing assets with a strong Disposal Strategy • Minimise the use of ring-fencing capital receipts to ensure a One-Council approach • Bidding for external funds where appropriate and ensuring that there are effective working relationships with external funders • Have clear policies for the consumption of our reserves • Ensuring that there is effective pre- and-post project appraisal • Ensuring up to date property information relating to condition surveys, life cycle costs and maintenance back logs • An estates strategy which tracks lease covenant compliance

CAPITAL EXPENDITURE AND INVESTMENT

2.0 CAPITAL EXPENDITURE

Capital investment is technically described as:

“Expenditure on the acquisition, creation, or enhancement of ‘long term assets’”

This generally consists of land, property and plant which have a useful life of more than 1 year, but can also include funding passed on to other bodies in order for them to undertake capital works. Expenditure outside this definition will be, by definition, revenue expenditure.

Expenditure can be capitalised where it relates to the:

- Acquisition, reclamation, enhancement or laying out of land.
- Acquisition, construction, preparation, enhancement or replacement of roads, buildings and other structures.
- Acquisition, installation or replacement of movable or immovable plant, machinery, apparatus vehicles or vessels.

Enhancement of an existing fixed asset means:

- To lengthen the useful life of the asset; or
- To increase substantially the open market value of the asset; or
- To increase substantially the extent to which the asset can be used for the purposes of, or in connection with, the functions of the Council.

Within the Accounting Policies for the Council, expenditure on the acquisition, creation or enhancement of Property, Plant and Equipment is capitalised on an accruals basis, provided that it is probable that the future economic benefits or service potential associated with the item will flow to the Council and the cost of the item can be measured reliably. Expenditure that maintains but does not add to an asset’s potential to deliver future economic benefits or service potential (i.e. repairs and maintenance) is charged as an expense when it is incurred.

All expenditure on Property, Plant and Equipment is recognised irrespective of value. Capital expenditure below £40,000 is considered non-enhancing and is immediately impaired unless cumulatively over more than one year the expenditure would amount to more than this value.

The Council currently does not make use of any capitalisation flexibilities nor capitalise any borrowing costs associated with the capital programme.

The Council’s capital expenditure plans are linked to the Corporate Plan, Asset Management Plan, priorities and service delivery plans with the inclusion of the ‘Future Property Needs’ within the business plan template.

The Council has acquired relatively few property assets over the last few years. Its focus has been on releasing or remodelling existing assets. From time to time it has acquired property required for service developments, for example purchasing land and buildings for school modernisation projects. It has also secured £1 million capital funding for commercial property investment, which has been partially spent on acquiring an income producing leased property.

To date the remainder is unspent as no suitable options which meet the Council's criteria have been forthcoming. It has also recently acquired third party interests in Salt Lake car park which has enabled it to take control of the regeneration and development of the site and generation of capital receipts.

In 2020-21, the Council is planning capital expenditure of £39.195 million as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
Council Fund services	27.614	37.653	39.195	23.941	25.308
Investment Properties		0.480			
TOTAL	27.614	38.133	39.195	23.941	25.308

2.1 CAPITAL FINANCING

The Council receives an annual 'General Capital Funding' allocation from Welsh Government, which comprises General Capital Grant and un-hypothecated Supported Borrowing. Revenue funding to repay the supporting borrowing is included within the Revenue Support Grant. Further details of funding sources are detailed in Schedule B.

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 net financing requirement (borrowing, leasing and Private Finance Initiative (PFI)). The planned financing of the expenditure outlined in Table 2 is as follows:

Table 2: Capital financing

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
External sources	12.407	17.383	13.822	9.492	18.158
Own resources	9.044	13.617	14.347	8.211	2.296
Net Financing Requirement	6.163	7.133	11.026	6.238	4.854
TOTAL	27.614	38.133	39.195	23.941	25.308

The net financing requirement or 'debt' is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as Minimum Revenue Provision, or MRP. As well as MRP, the Council makes additional voluntary revenue contributions to pay off Prudential or Unsupported Borrowing. The total of these are shown in Table 3 below:-

Table 3: Replacement of debt finance

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
Minimum Revenue Provision (MRP)	2.858	2.885	2.912	2.938	3.005
Additional Voluntary Revenue Provision	1.459	1.486	1.751	2.349	2.234
Total MRP & VRP	4.317	4.371	4.663	5.289	5.239
Other MRP on Long term Liabilities	0.641	0.690	0.743	0.801	0.863
Total Own Resources	4.958	5.061	5.406	6.088	6.102

The existing Capital Programme will be approved by Council before the start of the financial year 2020-21 as part of the MTFS.

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 by the MRP amount within the year. The CFR is expected to increase by £4.465 million during 2020-21. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
Capital Financing Requirement (CFR)					
Opening CFR adjusted excluding PFI & other liabilities	153.239	155.084	157.846	164.209	165.160
Opening PFI CFR	17.640	17.000	16.309	15.566	14.765
Total Opening CFR	170.879	172.084	174.155	179.775	179.925
Movement in CFR excluding PFI & other liabilities	1.845	2.761	6.363	0.951	(0.385)
Movement in PFI CFR	(0.640)	(0.690)	(0.743)	(0.801)	(0.863)
Total Movement in CFR	1.205	2.071	5.620	0.150	(1.248)
Closing CFR	172.084	174.155	179.775	179.925	178.677
Movement in CFR represented by :-					
Net Financing Need for Year (Table 2 Above)	6.163	7.133	11.026	6.238	4.854
Minimum and Voluntary Revenue Provisions	(4.317)	(4.371)	(4.663)	(5.287)	(5.239)
MRP on PFI and Other Long Term Leases (Table 3 above)	(0.641)	(0.690)	(0.743)	(0.801)	(0.863)
Total Movement	1.205	2.071	5.620	0.150	(1.248)

THE COUNCIL'S CAPITAL PLANS

3.0 CAPITAL PROGRAMME BY WELLBEING OBJECTIVE

Within the Corporate Plan, there are three Wellbeing Objectives namely:-

- Supporting a Successful Economy
- Helping People to be more Self-Reliant
- Smarter Use of Resources

In accordance with **PRINCIPLE 1** above, the majority of schemes within the existing Capital Programme link to the Council's Wellbeing Objectives, but there are also schemes that relate to Core Services and Statutory Functions.

Supporting a Successful Economy

The proposed capital programme includes a number of new and existing projects which will help to support a successful economy through regeneration and local development schemes. For example, the redevelopment of Maesteg Town Hall will provide improved community facilities to include the town library and performance spaces, as well as offering improved accessibility for visitors and creating jobs; and new Enterprise Hubs will create new business workspace. Regeneration work will continue to progress in Porthcawl following the acquisition of Salt Lake Car Park. There are also new allocations in respect of road safety improvements in a bid to improve access across the highway to residential and commercial areas. These supplement those existing schemes, such as the Cardiff Capital Region City Deal (CCRCD) investment, which will be targeted to focus on raising economic prosperity, increasing job prospects and improving digital and transport connectivity.

Helping People to be more Self-Reliant

In addition to the current programme of recommissioning adult home care and developing extra care there is continued investment in supporting people to be self-reliant through the Welsh Government funded disabled facilities grant scheme. Approximately £2 million of capital investment is made annually.

Smarter Use of Resources

One of the Council's Corporate Priorities is to ensure that we have Smarter Use of Resources and crucially this includes assets. The Council's AMP 2021 strategic aim is to have a lean sustainable estate that enables the authority to live within its means and support delivery of our wellbeing objectives. This is achieved through review and challenge on a geographic and service led basis and exploring how property assets can help enable innovative options for service transformation and maximising regeneration and growth. Examples of schemes within this priority include:-

- The Schools' Modernisation Programme and Strategic Review of Post-16 Education and Training - to provide sufficient school places in the right area and in new and improved schools by delivering 21st Century Schools, which will result in capital investment of around £49 million over the next 5 years.
- Parc Afon Ewenni - the Programme Board has reviewed its depot estate and is rationalising the number of depots it holds and investing in its existing larger depot sites at Waterton and Bryncethin.
- Porthcawl - the Council has substantial land holdings in Porthcawl which it is looking to bring forward to support regeneration of the area and to generate capital receipts.
- Community Asset Transfers – Review of assets and support services to enable the successful transfer of those most suitable to community groups and organisations.

3.1 OTHER KEY DRIVERS

As well as the Corporate Plan, there are other key drivers of the Council's capital plans. These are:

- Asset management requirements
- Health and Safety works

3.2 ASSET MANAGEMENT REQUIREMENTS

The Council's Asset Management Plan vision has been re-aligned with the Corporate Plan 2018-22 reviewed for 2019-20 "One Council Working Together to Improve Lives" as follows:

"To have a lean sustainable estate that enables BCBC to live within its means and support delivery of our wellbeing objectives"

The following clear principles drive the on-going challenge and management decisions relating to our assets:

1. The AMP 2021 supports and maintains alignment with the MTFs and the Corporate Plan, linking with other resource strategies.
2. Capital investment decisions support the Council's corporate priorities and mitigate any statutory risks taking account of return on investment and sound option appraisals.
3. Decisions on the treatment of surplus assets are based on an assessment of the potential contribution to the revenue budget and the capital programme.
4. A balance will be maintained within the non-operational portfolio between rental income, capital receipts, economic development/ community support.
5. Capital receipts generated will support the capital programme.

The Council also has a Highways Asset Management Plan (HAMP). The HAMP needs to take in account the following:

1. Much of the infrastructure serving the northern half of the county borough was originally constructed in the early 1900's and was not designed to cope with the current demands (economic, social and environmental) placed upon it.
2. The BCBC highway network is continuously growing with no sign of abatement. The Council has seen much in the way of development over the last decade, resulting in a significant increase in the amount of asset requiring management.
3. Highway Authorities have a statutory duty to maintain highways and ensure that they are available for safe use by all.

The HAMP is an essential document that sets out how the levels of service for the infrastructure network determined by the Council will be achieved. The HAMP is therefore a "living" document that will be subject to continual review and development.

3.3 HEALTH AND SAFETY WORKS

There is an earmarked reserve for Asset Management including funding for Condition Surveys. Up to date condition surveys for the whole estate are currently being procured, which will include planned preventative maintenance data. This will inform the Council's budget allocation for both revenue and capital repairs, maintenance and new build. Given the limited

capital and revenue funding and the currently known high level of maintenance backlog, a prioritisation matrix for budget allocation has been developed. The Matrix works to give highest priority to Health and safety works. Given the potential level of funding compared to the demand for repairs and maintenance, this may lead to the closure of buildings or the drive for further capital investment in new build projects. Once fully implemented the Corporate Landlord model will be able to effectively inform the capital funding planning and decision making as it relates to asset management.

For highway structures, the current basis for prioritisation is one of reactive safety repairs, where the asset is risk assessed using a standardised matrix. This risk assessment is then considered against the individual assets Bridge Condition Indices (BCI) rating. This allows the prioritisation of schemes and allocation of the available budget to ensure the best value is achieved. A similar approach is applied to carriageway and footway schemes, where combinations of technical survey, site inspections and member of public reports determine the basis for the prioritisation of works.

In 2019-20 a new Capital Asset Management Fund of £1.5m and a Highways Asset Management Fund of £1.2m were established. The intention of these is to fund those schemes that have been prioritised by the condition surveys as posing a Health and Safety risk either within buildings or within our Highways Infrastructure. The aim will be to replenish these reserves as funding allows. The monitoring of these reserves will be undertaken on a regular basis.

3.4 COMMERCIAL ACTIVITIES

The Council will consider, if the opportunities arise, the purchase of land and property as an investment – to both generate an ongoing income stream or to realise an increased capital value in the future. There are two ways that an authority can generate income from investment properties namely:-

- Direct purchase of investment property – through Capital Programme
- Investment in a Property Unit Trust – through Treasury Management

The first would see authorities investing in property by directly purchasing/developing properties with the intention of securing a revenue income from that investment. Investment in property leaves the Council open to all of the risks that would go with such a policy, such as devaluations, maintenance issues and potential tenant default, as well as the potential benefits such as a long term asset on the balance sheet and rental income. The second route would be to receive income from property by investing in an appropriate property unit trust. Returns from this fund are typically in the order of 5.5%-6% per annum though at a fee from the fund manager. It is an actively managed property fund, which means that fund managers have the potential for growth in the income as, over time, higher rents can be achieved by buying properties in areas where demand is growing, by adjusting the exposure to different areas of the market and by improving the quality of the properties as appropriate.

As well as the benefit of rental income from the direct purchase of an investment property, there might also be capital appreciation of the asset though this will only be realised once the asset is sold and a capital receipt is generated which could be then recycled to purchase replacement investment properties which would then not incur capital financing costs.

A strategy based on investment in properties does have the following risks:-

- Low liquidity and flexibility
- Physical/structural issues with buildings
- Greater exposure to economic, cultural and technological changes

- Void periods

But against this it has the potential benefits of:-

- Over a longer term a higher financial return and capital growth than other current investments
- A wider range and variety of investment tools

The Council does have an existing investment portfolio which is 100% based within the County Borough and primarily the office and industrial sectors. The income streams are generally spread between the single and multi-let office investments on Bridgend Science Park, the multi-let industrial estates and the freehold ground rent investments. The portfolio therefore does not accord with the risk balance in location and sectoral terms to the majority of investment portfolios and is also management intensive, with a large number of units relative to the overall income and value. The total value of Investment Properties was £4.635 million as at 31 March 2019. This would be expected to generate a rental income of £478,000 per annum excluding any vacant or rent-free periods.

There are limited opportunities within the existing investment portfolio to release / sell properties, as the current emphasis is to enhance income return (as opposed to capital value). The majority of the investments held are high yielding and an improved income stream is unlikely on any re-investment.

The majority of the Council's investment portfolio has grown organically. However, within the last 5 years, the Council approved £1 million within the capital programme and spent £520,000 on acquiring an office building, which generates a rental income of £56,000 per year or just over 9% return on the investment. There is a further £480,000 available but as yet no suitable options have been identified within the Bridgend area, which would produce a reasonable return and at acceptable levels of risk. The Council may in the future wish to consider expanding its property investment portfolio, in which case it would need to review the criteria and investment strategy and consider the investment taking into account the level of associated risk.

3.5 TREASURY MANAGEMENT STRATEGY (TMS)

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 Council 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.

3.6 BORROWING STRATEGY

The Council's major objectives when borrowing are:-

- to minimise the revenue costs of debt
- to manage the Council's debt maturity profile i.e. to leave no one future year with a high level of repayments that could cause problems in re-borrowing
- to effect funding in any one year at the cheapest cost commensurate with future risk
- to forecast average future interest rates and borrow accordingly

- to monitor and review the level of variable interest rate loans in order to take greater advantage of interest rate movement
- to reschedule debt if appropriate, in order to take advantage of potential savings as interest rates change
- to optimise the use of all capital resources including borrowing, both supported and unsupported, usable capital receipts, revenue contributions to capital and grants and contributions

3.7 LIMITS TO BORROWING ACTIVITY

The Council's long term borrowing at 31 December 2019 was £96.87 million. External borrowing can arise as a result of both capital and revenue expenditure and timing of cash flows. As the Council has an integrated TMS, there is no association between individual loans and particular types of expenditure. The Council makes use of internal borrowing and maintains an under-borrowed position in accordance with **PRINCIPLE 3** above. The capital borrowing need (Capital Financing Requirement) has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. Projected levels of the Council's total outstanding debt, which comprises borrowing, PFI and Other Long Term Liabilities, are shown below compared with the Capital Financing Requirement:-

Table 5: Prudential Indicator: Gross Debt and the Capital Financing Requirement

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
Debt (incl. PFI & leases)	117.891	116.991	130.758	135.709	143.283
Capital Financing Requirement	172.084	174.155	179.776	179.926	178.679

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen, the Council expects to comply with this in the medium term.

To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. Further details of the Liability Benchmark can be found within the Treasury Management Strategy 2020-21. It does show that an additional £19 million will need to be borrowed for the period 2020-21 to 2022-23 based on the assumptions within the Capital Programme and the use of Capital Receipts and Reserves. The actual amount will be monitored and assumptions challenged and borrowing will only be taken if there is no opportunity to use Internal Borrowing.

The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 6: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
Authorised limit – borrowing	145.000	145.000	170.000	170.000	175.000
Authorised limit – other long term liabilities	30.000	30.000	30.000	30.000	30.000
Authorised Limit Total	175.000	175.000	200.000	200.000	205.000
Operational boundary – borrowing	105.000	105.000	140.000	150.000	150.000
Operational boundary – other long term liabilities	25.000	25.000	20.000	20.000	20.000
Operational Boundary Limit Total	130.000	130.000	165.000	175.000	170.000
Total Borrowing and Long Term Liabilities	117.891	116.991	130.758	135.709	143.283

3.8 INVESTMENT STRATEGY

The Council's major objectives when investing are:-

- to maintain capital **security**
- to maintain **liquidity** so funds are available when expenditure is needed
- to achieve the **yield** on investments commensurate with the proper levels of security and liquidity

Cash that is likely to be spent in the near term is invested, 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 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 particular investments to buy and the Council may request its money back at short notice.

Table 7: Treasury management investments

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
Cash and Cash Equivalents	3.400	0.100	-	-	-
Short term Investments	20.000	31.650	27.033	9.686	7.000
Longer term Investments	4.000	12.000	3.000	3.000	3.000
TOTAL	27.400	43.750	30.033	12.686	10.000

Loans to Other Organisations

The Council can make investments to assist local public services, including making loans to small businesses to promote economic growth. The Council will assess these opportunities

and will only consider if such investments break even after all costs. Loans to such organisations will be approved as part of the capital programme.

3.9 OTHER LONG TERM LIABILITIES

Private Finance Initiative

The Council has a Private Finance Initiative (PFI) arrangement for the provision of a Secondary School in Maesteg. This forms a long-term liability for the Council (with fourteen years remaining on the term) which is £17.0 million at 31 March 2019 including the short term liability of £0.69 million included as current liabilities in the Council's balance sheet in the Statement of Accounts. This is a technical adjustment and is equivalent to the amount that is paid during 2020-21.

Pension Guarantees

The Council has entered into a number of long-term contracts for services that have been outsourced to service providers. These often involve the transfer of Council employees to the new service provider. Employee's rights are protected under the provision in Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE). However, pension rights are not fully covered within TUPE regulations. The Council have thus given a pension guarantee to Awen. This guarantee means that if an admitted body fails to pay its pension obligations then the Council will be responsible for taking on those obligations.

3.10 REVENUE BUDGET IMPLICATIONS

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as capital financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

Table 8: Prudential Indicator: Proportion of financing costs to net revenue stream

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Estimate £m	2021-22 Estimate £m	2022-23 Estimate £m
Capital Financing Central	6.451	6.509	7.049	7.264	6.650
Other Financing costs	3.406	3.451	3.698	4.296	4.181
TOTAL FINANCING COSTS	9.857	9.960	10.746	11.560	10.831
Proportion of net revenue stream	3.71%	3.68%	3.96%	4.24%	3.96%

From the table above it is evident that the proportion of the budget set aside to finance capital expenditure is due to increase over the life of the current programme, accelerating the pressure that capital expenditure, funded from debt, puts on the revenue budget.

Table 9: Central Capital Financing Revenue Budget 2020-21

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Budget £m
Interest Paid	4.534	5.447	5.346
Minimum Revenue Provision (MRP)	4.958	2.885	2.918
Other Financial Instruments	0.008	0.0089	0.008
Interest Received	(1.012)	(0.910)	(0.943)
Central Capital Financing Budget	8.488	7.430	7.329

The central revenue budget for capital financing for 2020-21 is £7.017 million as detailed above. The Projection for 2019-20 is lower than the actual spend 2018-19 because of the change in MRP Policy that Council approved in September 2018. The Interest Paid budget 2019-20 reflects the need to fund the increased costs of borrowing which is anticipated to rise over the period from 2019-20 to 2022-23 by £19 million.

There are also Financing Budgets within the Directorates for Prudential Borrowing and for the payment of the PFI School and other Lease Liabilities. These are detailed in Table 10 below:-

Table 10: Directorate Capital Financing Revenue Budget 2020-21

	2018-19 Actual £m	2019-20 Projection £m	2020-21 Budget £m
Additional Voluntary MRP	1.459	1.486	2.259
PFI & Lease Liability Payments	2.086	1.947	1.947
Directorate Capital Financing Budget	3.545	3.433	4.206

Table 11 shows how there will be increased revenue pressure on the capital financing budgets over the MTFS period:-

Table 11: Capital Financing Revenue Budget 2019-20 and Projected Costs

	2020-21 Projection £m	2021-22 Estimate £m	2022-23 Estimate £m
Central Capital Financing Budget (Table 9)	7.329	7.329	7.329
Directorate Capital Financing Budget (Table 10)	4.206	4.206	4.206
Total Capital Financing Budget	11.535	11.535	11.535
Total Financing Costs (Table 8)	10.746	11.560	10.831
Under/(Over) Spend	0.789	(0.025)	0.704

This would be the worst case scenario with unsupported borrowing being used for future schemes. The Council will endeavour to minimise the revenue pressure by maximising alternative capital resources such as earmarked reserves and capital receipts.

RESOURCING STRATEGY

4.0 FINANCIAL CONTEXT

Whilst the aims and priorities will shape decisions around capital expenditure, there is recognition that the financial resources available to meet priorities are constrained in the current economic and political climate. The context for capital expenditure decisions is as follows:

- The Council does have capital resources and expects to receive more resources in the future with an annual allocation from Welsh Government, potential s106 Monies or grant approvals.
- The Council does have a Disposal Strategy and has capital assets which it could sell and use receipts to reinvest
- The Council is currently servicing debt of £97 million with an average interest rate of 4.7%
- The Council's MTFS shows a funding gap so any additional capital expenditure which is not funded through capital resources will increase this gap unless that expenditure delivers revenue savings or income.

There had been a steady decline in the amount of general capital funding received from Welsh Government over several financial years. However, a letter from the First Minister in November 2019 identified an additional £100 million in capital funding across Wales over the period 2018-19 to 2020-21. From this for 2019-20 there is an additional £20 million across Wales, in addition to an additional £15 million across Wales to enable local authorities to respond to the urgent need to decarbonise. Bridgend has received an increase in general capital funding of £318,000 more than the amount received in 2019-20 but £761,000 more than was originally anticipated. In light of the above context, it is imperative that capital expenditure plans are affordable, prudent and sustainable.

4.1 PRINCIPLES FOR ALLOCATION OF CAPITAL ALLOCATION

The governing principles which underpin the allocation of capital resources are set out in the following diagram:

Nature of Capital Expenditure	Funding Source				
	General Capital Funding / Supported Borrowing	Capital Receipts / Uncommitted Reserves	Interest Free Loan	Unsupported Borrowing - Corporate Funding	Unsupported Borrowing - Directorate Funding
Mandatory					
Corporate Priority					
Investments which attracts Matched Funding					
Invest to Save / Income Generation - Commercial					

	Eligible for funding from this source
	Not eligible for funding from this source

In summary the main principles of capital allocation are:

General Capital Funding and Supported Borrowing from Welsh Government will be prioritised towards mandatory capital investments. This includes investment required to meet health and safety requirements. This principle also applies to uncommitted capital receipts and capital reserves.

Beyond this, any consideration will be given to capital schemes which directly support the achievement of the Council's corporate objectives.

Unsupported (Prudential) Borrowing will be prioritised as follows:

- To mandatory capital expenditure, including health and safety requirements. This will be considered to be an inescapable budget pressure and will be included in future years' budgets as part of the annual budget setting process.
- To capital expenditure which directly supports the achievement of the Council's corporate priorities. Borrowing for such projects will be funded corporately through an increase in budget allocation, which must be approved by full Council. Such borrowing commits the Council to interest and repayments during the asset life, and therefore it must be recognised that as budgets are reduced, the financing costs must be met by budget cuts elsewhere.
- To capital expenditure which attracts a high level of matched funding. This is particularly important as the Council tries to maximise every £1 it spends on capital with schemes involving external grants or contributions from partners. The aim is for

the Council to ensure that it invests in its strategic buildings and town centre infrastructure as grant funding and inward investment opportunities become available by allocating uncommitted reserves, maximising interest free loans or unsupported borrowing.

- To capital expenditure which provides a good financial return. Borrowing for such projects must be funded by the directorate, and therefore the financial benefit accruing to the directorate will be net of financing costs. This approach aligns the directorate incentives with the corporate benefit of such projects. Advantage will be taken of interest free loans where available.

CAPITAL INVESTMENT APPRAISAL

5.0 CAPITAL EXPENDITURE BIDS

The Council will maintain a rolling ten year capital programme, to be updated on an annual basis (or more frequently as required) to take into account revised priorities, new schemes and changes in the availability of funding. The current year's programme is monitored on a quarterly basis by Cabinet and updated programmes approved by Council.

The Council's Capital Programme contains a number of recurrent Annual Allocations, which are the first call on its General Capital Funding. These allocations are reviewed annually with a view to determining whether they are still essential, relevant and achieving the outcomes expected, and amended accordingly.

Where capital resources allow as a result of additional general capital grant, earmarked reserves or capital receipts, as part of the MTFs process, Directorates will be requested from September each year to submit Expressions of Interest for new capital schemes, outlining:

- Proposed Project
- Timescale
- Potential Cost
- Potential Revenue Savings
- Link to Corporate Priorities
- Risk of not Undertaking

These will be ranked in order of fit to:

1. **Link to Wellbeing Objectives:**
2. **High level of Risk of not progressing, based on the following criteria**

High	High risk to BCBC in terms of service delivery and/or meeting MTFs Savings e.g. Urgent/ Essential Works to prevent imminent building failure and closure. Requirement to meet approved Bridgend Change Programme Project to deliver MTFs Savings
Medium	Medium risk to BCBC in terms of service delivery and/or meeting MTFs Savings e.g. identified works required over the next 2 to 5 years. Requirement to meet Proposed Bridgend Change Programme Project to deliver MTFs Savings
Low	Low risk to BCBC in terms of service delivery and/or meeting MTFs Savings e.g. identified works desirable , Requirement to meet yet to be identified Bridgend change Programme Project to deliver MTFs Savings

3. **Service is able to meet any additional revenue costs arising from the scheme e.g. increased Business Rates, running costs.**
4. **Ability to attract matched funding / high leverage ratio.**
5. **An appropriate return on investment where appropriate.**

5.1 EVALUATION APPROACH

As stated, the Council only has a limited amount of resources, and needs to have regard to the overall affordability of the capital programme in future years. Each scheme, therefore, needs to be evaluated to ensure it meets the Council's objectives and in accordance with **PRINCIPLE 1** above.

The business plan put forward for a capital project will be reviewed to ensure it takes account of stewardship, value for money, prudence, sustainability and affordability. Investment decisions will consider risk and reward and how the project contributes to the achievement of corporate objectives. The phasing of projects over more than one financial year will be assessed to ensure timetabling of plans and budgeting is realistic and funding is available over the life of the project.

The revenue implications for each capital bid are considered at the initial evaluation stage, covering both staffing /running costs associated with the bid and the financing costs over the lifetime of the asset created. One of the Chief Finance Officer's requirements when reviewing capital bids is to ensure that the revenue implications are realistic. The options appraisal exercise undertaken for larger projects seeks to ensure that the lifetime revenue implications of a capital project are fully considered and evaluated, are affordable and are included in the MTFs in accordance with **PRINCIPLE 2** above.

Successful projects will then be required to complete a full Business Case to be considered in more detail by Corporate Management Board and Cabinet for eventual inclusion in the Capital Programme to be incorporated in the MTFs, to be approved by Council.

The Council can also make Treasury investments including overnight deposits, fixed term investment, money market funds, property funds and government bonds. These investments are made in accordance with the TMS which is approved alongside the Capital Strategy.

In Year Approvals

Any bids for capital funding outside of the annual MTFs bidding round should be accompanied by a full business case and be supported by the appropriate Director, Section 151 Officer and Cabinet. All funding sources should be fully identified before the bid is taken forward for Council approval for inclusion in the capital programme.

In line with the Council's Financial Procedure Rules, schemes for which external funding has been approved (grants, S106 etc) will be added to the capital programme once the funding has been accepted and included in the next capital programme report to Council.

In addition, any urgent expenditure not included in any budget approval, which needs to be agreed prior to the next meeting of Council, may only be incurred with the approval of the Chief Finance Officer, subject to a maximum value of £100,000. Any such decision requires approval by either the Chief Executive Officer (or can be sub-delegated to the Section 151 Officer) under the Scheme of Delegation, Scheme B1 paragraph 2.2.

GOVERNANCE AND RISK MANAGEMENT

6.0 STRATEGY

It is important given the risks surrounding Capital Projects that the appropriate Governance framework is in place. This is highlighted in **PRINCIPLE 2** above.

The Prudential Code sets out a clear governance procedure for the setting and revising of a capital strategy and prudential indicators i.e. this should be done by the same body that takes the decisions for the local authority's budget – i.e. Full Council.

The Chief Finance Officer will prepare a Capital Programme for consideration by Corporate Management Board (CMB) and Cabinet. It must be approved by Council in accordance with the Financial Procedure Rules of the Council's Constitution.

Variations to the capital programme, other than those permitted under Rules 3.4.7 and 3.4.9 of these Rules, shall require the approval of the Council following a report of the Chief Finance Officer after taking into consideration the recommendations of the Cabinet.

6.1 CAPITAL EXPENDITURE/INVESTMENT DECISION

A monitoring process is in place which:

- Reports on variances in expenditure and slippage on schemes and seeks explanations from project managers to report back to CMB and Cabinet to inform future planning decisions
- Quarterly capital monitoring reports will be prepared for Cabinet which should include details of any virements between projects as well as projections of likely year end spend.

A post project appraisal of all projects in accordance with the Project Management Toolkit must be completed to demonstrate how objectives have been met, how final costs compared to budget and what revenue costs / savings materialised. This information will be reported back to feed future appraisal exercises.

6.2 RISK MANAGEMENT

Major capital projects require careful management to mitigate the potential risks which can arise. The effective monitoring, management and mitigation of these risks is a key part of managing the capital strategy.

General risks are those which are faced as a consequence of the nature of the major projects being undertaken. Most of these risks are outside of the Council's control but mitigations have been developed as part of the business planning and governance process.

The effective management and control of risk are also prime objectives of the Authority'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.

7.0 KNOWLEDGE AND SKILLS

Within Finance, the Capital Programme and TMS are managed by professionally qualified accountants or staff with extensive Local Government finance experience. They all follow a Continuous Professional Development Plan (CPD) and attend courses on an ongoing basis to keep abreast of new developments and skills. The Council subscribes to the CIPFA Financial Advisory Network (FAN) and as a result has access to courses and documentation on developments within the capital and treasury management fields. The Council's Section 151 Officer is the officer with overall responsibility for Capital and Treasury activities and is a professionally qualified accountant and follows an ongoing CPD programme. All Treasury Management Practices (TMPs) are reviewed and updated as necessary.

Where Authority staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Authority currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly and ensures that the Authority has access to knowledge and skills commensurate with its risk appetite.

All the Council's commercial projects have project teams from all the professional disciplines from across the Council and when required external professional advice is also taken. Project management tools are used and there is a strong project management ethos within the Council. Throughout the Council is a good mix of professional qualified staff and staff with both commercial and local authority experience. There is a Corporate Landlord team consisting of skilled and professional staff covering design and management, estates and valuation, statutory compliance, strategic asset management planning, facilities management, management and commissioning of repairs and maintenance and energy management to introduce new energy efficiency measures such as upgraded heating, lighting, insulation and investigating new technological solutions that will enable staff to be fully agile and provide a better service, while an online portal is being developed that will provide information, process customer requests and enable staff to log jobs and track progress. The Regeneration Team within the Communities Directorate has been successful in applying for monies from various sources such as Welsh Government, Heritage Lottery and European monies.

Schedule A**ANNUAL MINIMUM REVENUE PROVISION STATEMENT 2020-21**

The Annual Minimum Revenue Provision Statement needs to be approved by Council before the start of each financial year. The MRP charges for 2020-21 will be on the following bases:-

- i. Capital expenditure incurred before 1 April 2008 and any capital expenditure after 1 April 2008 that is government supported expenditure and does not result in a significant asset will be based on the Capital Financing Requirement after accounting adjustments on a straight line basis over 45 years
- ii. Supported capital expenditure that results in a significant asset (based on an internal assessment) incurred on or after 1 April 2008 and all unsupported capital expenditure, exercised under the Prudential Code, the MRP charge will be based on the Asset Life Method. The minimum revenue provision will be at equal annual instalments over the life of the asset. The first charge can be delayed until the year after the asset is operational but this will be at the discretion of the Section 151 Officer
- iii. for assets reclassified as finance leases under International Financial Reporting Standards (IFRS) or resulting from a Private Finance Initiative, the MRP charge will be regarded as met by a charge equal to the element of the rent/charge that goes to write down the balance sheet liability for the year
- iv. Where loans are made to other bodies for their capital expenditure with an obligation for the bodies to repay, no MRP will be charged. The capital receipts generated by the annual repayments on those loans will be put aside to repay debt instead
- v. MRP may be waived on expenditure recoverable within a prudent period of time through capital receipts (e.g. land purchases) or deferred to when the benefits from investment are scheduled to begin or when confirmed external grant payments towards that expenditure are expected.

The MRP Charge 2020-21 based on the estimated capital financing requirement is detailed below:-

	Options	Estimated Capital Financing Requirement 31/03/20 £m	2020/21 Estimated MRP £m
Capital expenditure before 01/02/2008 and any after 01/04/2008 that does not result in a significant asset (Supported)	(i)	125.184	2.780
Supported capital expenditure that results in a significant asset, incurred on or after 1 April 2008 (Supported)	(ii)	3.157	0.132
Unsupported capital expenditure, exercised under the Prudential Code (Unsupported)		29.505	1.751
PFI, Finance Leases and other arrangements – PFI School	(iii)	16.309	0.743
TOTAL		174.155	5.406

Sources of Capital Investment

Borrowing

The Council is able to borrow money on the money market or from the Public Works Loan Board (PWLB) 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 and any on-going related revenue support. With the exception of the Welsh Government's allocation of Supported Borrowing, all other borrowing is unsupported i.e. where associated interest and debt repayment costs must be met from existing revenue budgets, Council Tax, savings or additional income generation.

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, and in accordance with MTFS **PRINCIPLE 11** must be affordable and sustainable, with payback met from Directorate or Council revenue budgets over a period no longer than the life of the asset. Projects requiring funding through prudential borrowing should submit a robust 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 on Council Tax).

The potential for Prudential Borrowing is not unlimited and must be considered within the Council's overall borrowing limits. Whenever Prudential Borrowing is under consideration, the means of payment must be clearly identified. Typically this can be from:

- Income or savings generated by the investment;
- Budget reductions made elsewhere in the Directorate to compensate;
- Additional recurrent funding approved by Council as part of the budget setting process.

There may be the need for borrowing where there is no identifiable future revenue stream, for example, to repair or construct infrastructure assets. This may be to support Corporate Priorities. The cost of such borrowing falls on the council tax payer through payments of debt interest on the Council's revenue account and repayment of debt over a specified period of time. This is known as the Minimum Revenue Provision (MRP). 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, it is likely that such schemes will be an "exception".

External Grants

The Council receives annual capital grant funding from Welsh Government and is able to bid for grant funding directly to other government departments or from other grant awarding bodies.

The annual funding from Welsh Government is not ring-fenced so the Council has flexibility in how it allocates this funding. It is proposed that this is earmarked in the first instance to works deemed to be of a mandatory nature e.g. health and safety, or towards Wellbeing Objectives.

Any additional capital grant funding received from external sources must be managed in line with the Council's Grants Policy. Delegated authority is required to bid for and accept any external funding, and external funding applications should be supported by a strong business

case which demonstrates how the project meets the Council's Corporate Priorities and how any future revenue costs will be met.

Capital Receipts from Asset Disposals

The Council generates capital receipts from the sale of surplus assets. Maximisation of these receipts will increase the amount that can be spent on capital investment. Capital receipts cannot be spent on revenue items.

The Council has a statutory obligation to deliver best consideration under S123 of the Local Government Act 1972 and will seek to obtain market value in its disposals. However, there are exceptions and there will sometimes be a balance to strike where disposals can achieve social, economic or environmental policy objectives which contribute towards the Corporate Plan. In such instances, consideration will be given to the Value for Money that this represents.

The Council has also introduced a Community Asset Transfer (CAT) Strategy, where it considers the transfer of assets to third party groups at less than best consideration to support its objectives. 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. Where the Council proposes to dispose of or grant a long lease at nil consideration, or at a value below market value, a valuation will be undertaken to ensure that the Council is fully aware of the receipt that it is foregoing as a result of the Community Asset Transfer.

A key principle of the Council's Capital Strategy, **PRINCIPLE 4**, is that, unless specifically agreed by Cabinet for exceptional circumstances, all capital receipts will be treated as general capital funding and allocated according to determined priorities. This supports the "One Council" approach. However, this does not negate the need for Council to approve any proposed schemes from that receipt. One example of where the Council has departed from the principle is with regards to school disposals and the ring fencing of those capital receipts to fund the School Modernisation Band A Programme. There may potentially be other schemes where the Council decides to set aside receipts in this way and these will be approved within the reporting of the Capital Programme.

The Council will aim to maximise its capital receipts, where possible, by enhancing the land prior to disposal. In relation to development sites it will produce a technical pack which will include site investigations, planning briefs, utilities and drainage information, as relevant. The Council will consider the most appropriate method of disposal by way of private treaty, tender or by public auction. Generally it will dispose of assets on the open market, in order to robustly demonstrate that it has delivered best consideration. However, there will be occasions when it will sell off market to a single bidder. In these instances it will seek an independent valuation to assess the capital receipt and to affirm that best consideration has been delivered.

S106 contributions

Section 106 (S106) Agreements are legal agreements between Local Authorities and developers; these are linked to planning permissions and can also be known as planning obligations. A section 106 agreement is designed to make a development possible that would otherwise not be possible, by obtaining concessions and financial contributions from the developer. Any contributions received from the developer are 'ring-fenced' for the purpose as set out in the relevant S106 agreement and are applied to fund schemes within the capital programme once an eligible scheme has been identified. S106 contribution agreements can be used, for example, for the provision of educational facilities, highways infrastructure, affordable housing, play areas and open spaces, in line with the Council's adopted policy on the use of section 106 agreements. Consideration of available S106 funding should be taken

when agreeing the capital programme for future years to maximise the use of the available funding and reduce the reliance on other sources of funding. Contributions can be 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, any funds not spent in line with the agreement would have to be repaid to the developer.

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 funding for revenue expenditure, the Council's policy is generally not to budget to use revenue or reserves to directly fund capital projects, unless funding has already been set aside.