CAPITAL AND INVESTMENT STRATEGY 2019/20 – 2023/24

1. INTRODUCTION

This strategy sets out Surrey County Council's approach to capital investment for the next 5 years. It forms a vital part of the Council's governance arrangements and provides a mechanism by which investment and financing plans can be prioritised, ensuring that capital decisions take account of stewardship, value for money, prudence, sustainability and affordability.

The Capital and Investment Strategy is an integral part of the Council's overall financial and asset management planning framework and should be read in conjunction with Financial Regulations and the Scheme of Delegation, the Financial Strategy 2019/24, the Treasury Management Strategy Statement (TMSS), the Minimum Revenue Provision (MRP) Policy (attached at Appendix 1), the Risk Management Strategy, the Investment Strategy, the Asset and Place Strategy for Surrey and the Highways Asset Management Plan.

The Council has regard to the Statutory Guidance on Local Government Investments issued by the Secretary of State and the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code, and has in place robust financial planning, option appraisal and governance arrangements as outlined in the Governance Section below.

2. OBJECTIVES

The Capital and Investment Strategy is a new report for 2019/20, providing a high level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services. It also provides an overview of risk management and the long term sustainability of capital investment plans.

This strategy will:

- ensure capital expenditure contributes to the achievement of the Council's organisational strategy
- set a capital programme which is affordable and sustainable
- maximise the use of the Council's assets
- provide a clear framework for decision making and prioritisation relating to capital expenditure
- establish a corporate approach to the review of asset utilisation

This Strategy covers the following distinct, but inter-related elements of capital and investment activity as follows:

Capital Expenditure (section 3); the Council incurs three distinct types of capital expenditure, (capital programme, strategic investment and commercial investment). This strategy covers each of these areas, setting out the Council's capital expenditure and financing plans over the medium term. It provides an overview of the governance arrangements for approval and monitoring of expenditure and, in relation to commercial investment activities, sets out the due diligence process and the Council's risk appetite in respect of these, including proportionality in respect of overall resources.

Capital financing and borrowing (Section 4); including a projection of the Council's capital financing requirement and how this will be funded and repaid. It links to the Council's borrowing strategy and sets out the Council's policy to meet its statutory duty to make an annual revenue provision for the repayment of debt (Appendix 1).

Prudential Indicators (Section 5); Local Authority borrowing is governed by CIPFA's Prudential Code, which requires local authorities to set indicators which ensure that the level of borrowing is affordable, prudent and sustainable. The Prudential Indicators are set in the Treasury Management Strategy Statement each year, and monitored throughout the year by the Audit & Governance Committee. This strategy highlights the key indicators relating to borrowing levels.

Treasury Management Investments (Section 7); provides an overview of the Council's approach to the management of investments and cash flows. Further details on this are contained in the Council's Treasury Management Strategy Statement.

Use of capital resources for revenue purposes (Section 8); provides a summary of the Council's plans to utilise the Governments flexibilities to use capital receipts to finance the costs of its transformation plans. These are further detailed in the Council's Flexible Use of Capital Receipts policy.

Knowledge & Skills (section 10); summarises the knowledge and skills available to the Council to support it in its decision making in these areas. Full details of processes and the roles and responsibilities of Budget Holders can be found in the 'Budget Holder Handbook – Capital.'

3. CAPITAL EXPENDITURE

Expenditure is classified as capital in nature when it results in the acquisition or construction of an asset (eg land, buildings, roads and bridges, vehicles, plant and equipment etc) that will:

- be held for use in the delivery of services, for rental to others or for administrative purposes; and
- be of continuing benefit to the Council for more than one financial year.

There are a number of other specific instances where expenditure is required to be classified as capital expenditure, including:

- where the Council does not directly benefit from, or control, the resulting asset but where if it did it would be required to classify the expenditure as capital expenditure.
- where statutory regulations require it.

This includes expenditure on the purchase of shares, assets owned by other bodies and loans or grants to other bodies or subsidiaries, enabling them to buy assets.

The Council incurs capital expenditure in three distinct areas:

- investment in new and existing operational assets to support the delivery of its services (**capital programme**),
- investment required to deliver the Council's new vision and transformation of its services (**transformation & strategic investment**),
- investment to balance the Council's existing commercial investment income portfolio, as set out in the Investment Strategy. This includes shareholdings and loans to third parties and subsidiaries (**commercial investment**).

There are currently reviews taking place of both the commercial investment and transformation & strategic investment areas. Conclusions from these reviews will be communicated in early 2019/20. Approval for any potential future expenditure will be sought via the appropriate governance arrangements.

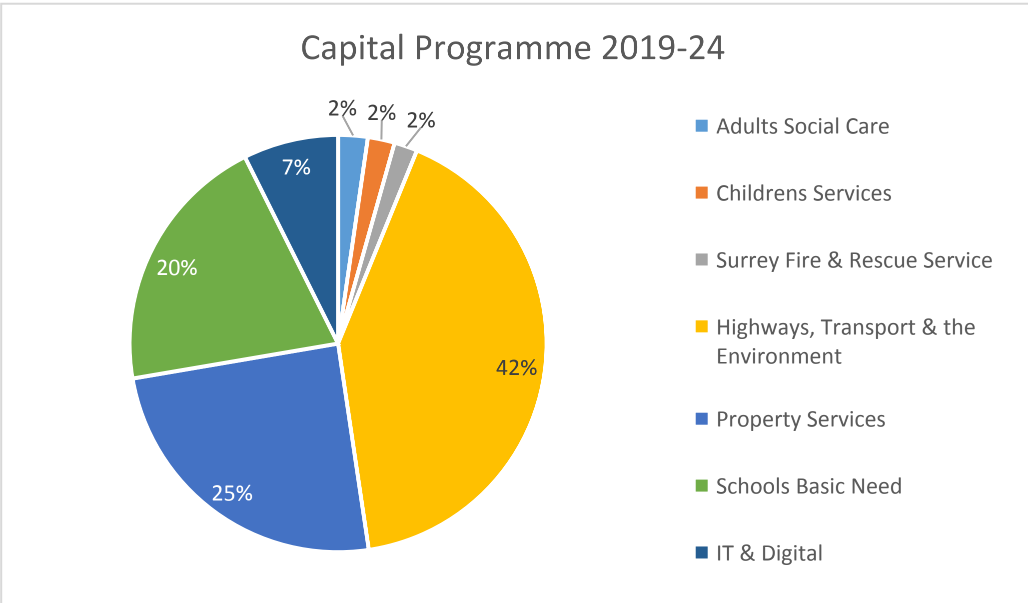
Capital Programme:

The capital programme represents the Council's commitment to continue to invest in its operational asset portfolio, specifically in the highways, operational property and in new pupil places. It is refreshed at least annually during budget planning and is approved by County Council as part of the revenue and capital budget setting process.

New capital schemes and projects will usually be added to the Capital Programme as part of the annual budget setting process, however, governance arrangements around managing the Capital Programme allow for new schemes and projects to be added in-year, subject to appropriate approval. All proposed new projects will assessed on a lifetime costing basis, making sure all revenue and maintenance costs are affordable.

The proposed capital programme includes £129.2m of investment in 2019-20, with an indicative programme for the subsequent four years of £283.6m.

Chart 1 shows a breakdown of the Capital Programme by main service type:



Governance: New capital schemes, projects and maintenance programmes are assessed and scrutinised in two stages prior to being included in the Capital Programme:

1) The Capital Programme Panel (CPP) an officer panel comprising a small team of Executive Directors and senior officers nominated by Executive Directors, and
2) The Asset Strategy Board (ASB), a member / officer board comprising Cabinet Members, the Executive Director of Economy, Growth & Commercial and the Executive Director of Finance.

All proposed schemes are based on a robust business case and subject to appropriate internal / external due diligence. In particular they must ensure:

- capital programme proposals are consistent with the Council's Organisational / Directorate Strategies;
- whole life costing is provided;
- financial and service risks are fully assessed and considered;
- proposed delivery timescales are realistic;
- all associated revenue implications are fully explained for the current and future years.

Only those schemes and projects that meet strategic priorities and have been supported via the two stages outlined above will be incorporated in the Capital Programme, which is approved by Council. Preference will be given to schemes and projects that are self-financing by generating additional income, reducing expenditure or realising a capital receipt. However, it is recognised that not all capital projects generate a return.

In addition, the Transformation Programme requires capital investment in assets, infrastructure and IT. The overall Transformation Programme will be supported by and delivered via individual business cases. Where these business cases have identified the need for capital funding, expenditure has been included in the capital programme, this relates mainly to the provision of IT equipment which is essential to the achievement of the agile workforce transformation project.

Budget monitoring - Budget managers must ensure capital expenditure does not exceed the allocated capital resources over the life of the project. Capital expenditure is monitored by CPP monthly, and reported to ASB, Corporate Leadership Team (CLT), Scrutiny Committee and Cabinet as part of the overall budget monitoring process. The monitoring report highlights any forecast variance in expenditure and the implications of changes, if any, to the expected timescales for delivery.

Asset Disposal – The Council takes a strategic approach in identifying those assets that are surplus to requirements and considers a range of options for their future use including suitability for alternative use, e.g. Extra Care accommodation, the business case for commercial or residential development against the benefits to be gained from marketing for sale. The Council has recently entered into a joint venture arrangement with Places of People to undertake approved development schemes for a number of its vacant sites.

Asset Management – Highways and Transport - Surrey County Council provides essential services which benefit all of Surrey's residents, businesses and visitors. The infrastructure includes over 3,000 miles of roads, 3,262 miles of footway, 2,143 miles of footpaths, bridleways and byways, 2,300 hectares of countryside, 2,300 bridges and structures, 15 community recycling centres and 4 waste transfer stations. We promote road safety, regulate waste and minerals developments and work to ensure that new development across Surrey is sustainable.

Asset Management – Property - The Council owns approximately 5,800 registered assets both inside and outside Surrey. These cover a wide range of property types from farms and countryside through to the operational buildings such as schools, offices and fire stations. The total value of these assets amounts to circa £1.5 billion.

Strategic Investment

The Council is undergoing major transformation of the way it works and the way in which it delivers services to residents. Future services will be more about supporting people to make changes in their lives that will make them happier and healthier in their homes and communities and less about the buildings our staff are in. The asset management plan provides a guide for future property decisions and a link between the strategic consideration of assets and their role in the delivery of the Council's services.

Given the Council's ambitions and the financial challenges it faces, it is timely to review the contribution that property assets can make both to the transformation of Surrey County Council services and to the development of Surrey's wider economy. This will build on the Council's existing Investment Strategy and provide a wider approach to the development and utilisation of the Council's assets, enabling the development of housing and employment space and a contribution to the wider Surrey economy.

Work is underway to develop plans under the Asset and Place strategy and separate approval will be required to add these schemes to the capital programme.

Commercial Investment / Non-treasury Investment:

The Investment Strategy agreed by Cabinet in July 2013 was developed in response to the requirement for the Council to enhance its financial resilience in the longer term. The main principles of the strategy are to create a diversified and balanced portfolio of investments to facilitate future service provision, manage risk and secure an ongoing annual return to the Council.

Cabinet approved the business case for the creation of a Property Company and its associated subsidiaries in May 2014 to enable investment in property outside of the county and for the commercial income return. The property investment portfolio is therefore a combination of assets acquired or developed by the Council for future service need or economic development and those acquired or developed by Halsey Garton Property Group (HGP).

Governance

The governance for the Investment Strategy is provided by the Investment Board (IB), which is comprised of members of the Cabinet, who are supported by officers. The IB is responsible for making investment decisions in accordance with the framework established by the agreed Investment Strategy and for the strategic management of the overall portfolio consistent with the aims of the Investment Strategy. Officers, supported by independent specialist professional advisors, support the IB. These specialist advisors periodically evaluate the recommended portfolio of property investment, taking into account market conditions and achievable returns.

The Investment Board produces an Annual report for Cabinet and for the purposes of scrutiny which provides details about the investment portfolio governance, its processes and the responsible investment policy. A summary version of the report is also available to the public on the council's website. Capital expenditure and in-year financial performance is reported to the Cabinet monthly as part of the Financial Monitoring Report.

Further information about the Investment Strategy and the council's investment portfolio is shared in the Investment Board's Annual Report.

Financial Arrangements

Acquisitions by HGP are funded by the council from the provision of equity and debt finance. This finance is provided on market facing terms, on an 'arm's length' basis in order to be compliant with competition law and State Aid. The returns to the council from the provision of finance to HGP are received in the form of a net interest margin receivable by the council on the loans provided plus the annual dividend payment from the company.

In undertaking investment activity the council is required to take into account the new guidance that has been published by the Secretary of State and by CIPFA. In particular the new guidance in relation to "borrowing in advance of need". The Council does not borrow in advance of need purely in order to profit from the investment of the extra sums borrowed. The Council does however borrow to invest in order to fulfil its statutory duties and in doing so, will take into account the new guidance and the codes of practice. The Council has the power to invest legally and to provide financial support to its wholly owned property company, and in doing so will consider these regulations and will exercise its powers reasonably and in accordance with best value and fiduciary duties with regard to mitigation of risk and all due-diligence

Risk Management

The Investment Strategy means that the council is managing different financial risks. Investments will be subject to inherent economic and market risks which requires a balanced portfolio of investments to be built over time. The strategy notes a preference toward assets that are investment grade, are of good quality, in good or growth locations with a diversified portfolio a mix of geographical locations.

The investment portfolio is being delivered to ensure diversification of-

- **Asset Class**: a mix of office, retail, industrial and other investment classes (e.g. leisure, hotels etc.). The target mix of investments between classes is reviewed in detail bi-annually on the basis of an in-depth market report and recommendations from our strategic property investment advisors, CBRE.
- **Location:** a geographically diverse portfolio, focussed in good or growth locations for their asset class and for retail investments, a mix of high-street and out-of-town locations.
- **Tenants**: a mix of tenants across different sectors, including a diversified range of tenants within the retail sub-sector. Care is also taken to limit the number of lease breaks and lease expiry in any one-year.

The creation of a diversified portfolio of assets to mitigate risk will take some time to achieve. The investment portfolio, including future commitments, is currently over-weight in retail. To address this and achieve a balance closer to the benchmark would require further acquisitions of approximately £150m. We are currently undertaking a review of the Investment Strategy, and until this is complete, no further acquisitions are being actively pursued.

The purpose of the Investment Strategy is to deliver an annual income stream in support of the council's services and in doing so, the council is not assuming any gain from the value of the underlying assets. Instead a long-term view is taken, since the value of the assets may decrease as well as increase over time, and the costs of purchase – in particular stamp duty, are unlikely to be offset by increases in value in the much shorter term.

All investment assets are independently revalued each year as part of the year-end financial accounts process using a standard methodology of fair market value. This method takes into account the present value of the known income streams, the likelihood of future unknown income and the underlying site value of each asset. This means that generally, the shorter the lease the lower the asset value. The results of the year-end valuation are reported in the Annual Report provided by the Investment Board and are included in the Council's annual Statement of Accounts.

Values will therefore fluctuate but there are no financial implications unless or until the asset is sold and the timing of any sale is the decision of the Investment Board on behalf of the council. Investment grade assets are by their nature liquid since there is a well-developed market and as the council is not reliant upon the capital receipt investment, assets can be sold only when financially beneficial to do so.

Any revaluation loss does not impact upon the general fund of the council – there are no adverse implications for the tax-payer since financial adjustments of this nature are excluded from the calculation of the revenue requirements of the council by statute. Similarly this is the case if there is a revaluation gain. It is only realised profits (or losses) that have an impact upon the council.

Assets that are being developed will not produce an immediate income stream and there will be occasions when a tenant triggers their break clause or vacates at the end of the lease resulting in a potential letting void. In order to mitigate against these risks the council has a Revolving Investment and Infrastructure fund that meets the initial revenue costs of initiatives and can act, if required, as a method to smooth net income and offset the impact of voids, noting that one strand of the diversification approach is avoid potential void events occurring at the same time. The reserve has not been required to date, since the income delivered by acquisitions has offset development spend and voids in the portfolio.

Reliance and proportionality

The investment portfolio held by the council and its property company HGP was valued at £319m as at 31 March 2018, this is 16% of the Group's[1] land and buildings assets.

The returns from investment contribute to the funding of the council's services and is included in the MTFP at £4.0m in 2018/19 rising to the target return of £10.0m per annum

[1] Group consists of the Council and its wholly owned Local Authority Trading Companies (SE Business Services, Halsey Garton Property Ltd and Surrey Choices Ltd)

for 2019/20 onwards. The forecast income in 2018/19 is in excess of this target, at £5.2m. This compares to a total income, excluding grants, of £197m in the MTFP. Therefore the extent to which the delivery of the council's services is dependent upon the performance of its investments is significantly limited.

With financial return being the main objective, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk include property voids and fall in capital value. These risks are managed by ensuing that the portfolio is diversified across multiple property sectors and a range of geographical locations, and that reliance on a commercial return is in proportion to the Council's overall budget.

Specific tenant risk and voids are monitored by the Investment Board as part of in-depth quarterly reporting. Tenant voids as measured in terms of an estimate of the rent that would otherwise be receivable as a % of the total rent receivable are currently 3.7%. This is below industry benchmarks – which for an established diversified portfolio is currently c.7%.

The Council has established a Revolving Infrastructure and Investment Fund as a risk mitigation to smooth the investment income and mitigate against potential / inevitable voids. This fund will be called upon if target returns are not achieved and a shortfall results in an overall shortfall in the revenue budget. The fund will be replenished if actual income exceed targets and will be subject to approval by Cabinet.

Table 2 illustrates the proportion of investment income to gross service expenditure:

	2018/19 Forecast £m	**2019/20 Budget £m**	**2020/21 Budget £m**	**2021/22 Budget £m**	**2022/23 Budget £m**	**2022/23 Budget £m**
Net service expenditure	883.8	885.9	928.8	936.0	947.8	953.4
Investment income	5.2	10.0	10.0	10.0	10.0	10.0
Proportion	0.6%	1.1%	1.08%	1.07%	1.06%	1.05%

Purchase of shares/Provision of loans: The Council may make investments to assist local public services, including making loans to and buying shares in service providers, local businesses to promote economic growth and the Council's subsidiaries that provide services or which have been established for the purposes of trading. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to break even or generate a profit after all costs.

The decision to invest in shares or provide funding in the forms of loans is taken by Cabinet or in accordance with delegated decision-making, upon the basis of a business case which articulates the strategic rationale, the financial implications and associated risks for the council. The Shareholder Board safeguards the Council's interest and takes decisions in matters that require the approval of the Council as owner or a shareholder of a company. Shareholder control is exercised over all companies owned by the Council, and in relation to any shares held whether the purpose is trading, service provision or investment. Decisions in relation to the day to day operation of companies are taken by the directors of each company. The Shareholder Board produces a report on these shareholdings which is presented to Council annually.

Service investment (loans): Loans to local enterprises may be considered as part of a wider strategy for local economic growth. Such loans will be considered when all of the following criteria are satisfied:

- The loan is given towards expenditure which would, if incurred by the Council, be capital expenditure;
- The purpose for which the loan is given is consistent with the Council's corporate / strategic objectives and priorities;
- Due diligence is carried out that confirms the Council's legal powers to make the loan, and that assesses the risk of loss over the loan term;
- A formal loan agreement is put in place which stipulates the loan period, repayment terms and loan rate (which will be set at a level that seeks to mitigate any perceived risks of a loss being charged to the General Fund, and takes appropriate account of state aid rules) and any other terms that will protect the Council from loss;

Most loans are capital expenditure and proposals will therefore initially be presented to the CPP as part of the capital programme assessment, and all decisions on service investments and loans to third parties are subject to member approval.

Accounting standards require the Authority to set aside loss allowance for loans, reflecting the likelihood of non-payment. If applicable, the figures for loans in the Authority's statement of accounts from 2018/19 onwards will be shown net of this loss allowance. However, the Authority makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.

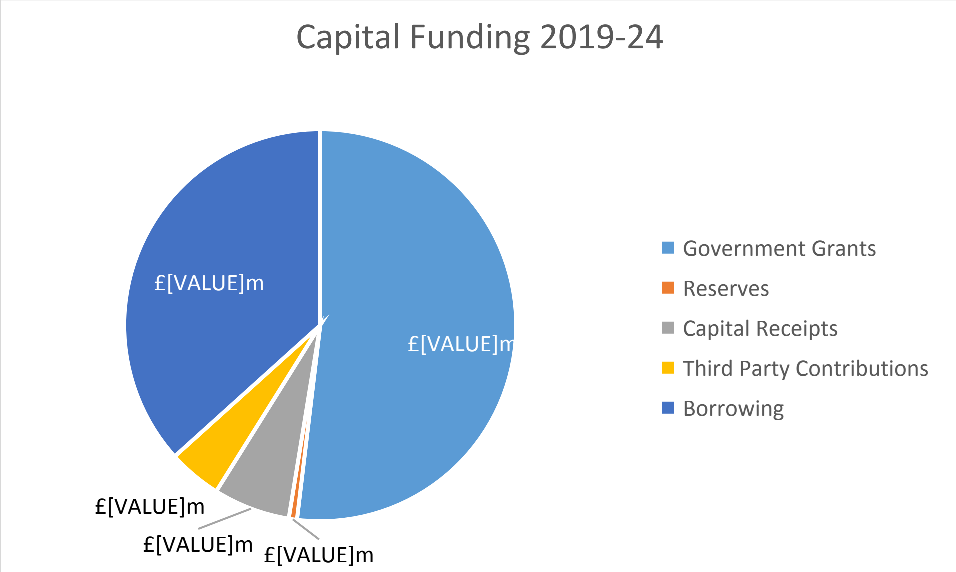
Non-specified Investments: Shares are the only investment type that the Authority has identified that meets the definition of a non-specified investment in the government guidance. The Authority has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

4. CAPITAL FINANCING & BORROWING

The Council's capital investments fall within "the Prudential Code for Capital Finance in Local Authorities" (the Code), and the Council complies with the Code. Under the Code, local authorities have discretion over the funding of capital expenditure and the freedom to determine the level of borrowing they wish to undertake to deliver the Capital Programme. There are a range of potential funding sources which can be generated locally, either by the Council itself or in partnership with others. The Council will fund the Capital Programme from the following sources:

- Government Grants
- Third Party Contributions (including section 106 agreements and Community Infrastructure Levy (CIL))
- Reserves and Capital Receipts
- Revenue Contributions to Capital
- Borrowing

Chart 2 below summarises the Council's estimated capital funding for the period 2019/24:



Government grants - Grants are allocated in relation to specific projects or schemes, and the Council will seek to maximise such allocations, developing projects and schemes which reflect government and partnership led initiatives, and at the same time address the Council's local priorities. The level of future government grants is uncertain, and the 2019/24 capital programme includes an estimate for each year. The Council reviews notification regularly, and the Capital Programme is adjusted accordingly and reported to Cabinet as part of the monthly budget monitoring.

Table 3 shows the grants expected for 2019/24.

Expected Government capital grants	**2019/20 £000**	**2020/21 £000**	**2021/22 £000**	**2022/23 £000**	**2023/24 £000**
School Basic Need*	27.1	17.6			
Schools condition allocation	9.8	9.8	9.8	9.8	9.8
Devolved Formula Capital (Schools)	1.2	1.2	1.2	1.2	1.2
Integrated transport block	4.8	4.8	4.8	4.8	4.8
Highways maintenance	13.4	13.4	13.4	13.4	13.4
Local Growth Fund	6.7				
Other capital grants	4.1	3.5	3.3	3.3	3.3
Total expected grant	**67.1**	**50.3**	**32.5**	**32.5**	**32.5**

* Includes some re-profiling of unspent grant from previous years

Third party contributions / Section 106 Agreement Contributions & Community Infrastructure Levy (CIL) – These are mainly generated from planning gain agreements under Section 106 or as community infrastructure levies (CIL) from developers. The 2019/24 Capital Programme relies on approximately £18m third party contributions. These contributions help to finance infrastructure, facilities and services, e.g. schools, highways and transport improvements. S106 is negotiated, CIL is levied, and collected by planning authorities in consultation and collaboration with the County Council. Planning authorities need to work closely with the County Council in setting priorities for how the s106 receipts and the levy will be spent, to ensure the required infrastructure is secured to support new development.

Reserves and Capital Receipts - These are amounts set aside from the revenue budget (revenue reserves) or from asset disposal (capital receipts) into a reserve for future capital expenditure. The Council plans to use approximately £29m of reserves and capital receipts to support the 2019/24 capital programme.

Revenue Contributions to Capital - Capital expenditure may be funded directly from revenue (REFCUS – Revenue Expenditure Funded from Capital Under Statute).

Borrowing - After the application of all other sources of capital funding, the Council will utilise Prudential Borrowing to finance the un-funded part of the Capital Programme.

The Council has a policy, that it will only finance a capital scheme from borrowing if it fulfils one, or more, of the following criteria:

- is a statutory requirement
- generates a revenue savings
- avoids a revenue costs
- produces a capital receipt

Over the five years of the 2019/24 capital programme, the Council expects to fund approximately £152m of capital expenditure in this way. In addition, any expenditure on commercial investments, loans to third parties or the purchase of shares will also be funded in this way.

The implications of financing capital expenditure from borrowing is that the expenditure is not funded immediately but charged to the revenue budget over a number of years. The Council may defer the timing of external borrowing on a short to medium term by using temporary cash resources held in reserves and balances. This practice, which is referred to as 'internal borrowing', does not reduce the magnitude of borrowing required or the level of funds held in reserves and balances; the funds are merely being utilised in the short term until they are required for their intended purpose. The timing of external borrowing and the balance of external / internal borrowing is determined by market conditions and the Council's cash flow position. Officers manage this position on a day to day basis in line with the overall TMSS, as approved by members of the Audit & Governance Committee.

Debt is only a temporary source of finance, loans must be repaid. The Council has a statutory duty to set aside an amount it considers to be prudent, in line with guidance, for the repayment of borrowing. This is known as the Minimum Revenue Provision (MRP). See Appendix A for this Councils MRP Policy for 2019/20. The Council's underlying debt liability will be repaid in line with the MRP Policy, amortised over the life of the assets creating the debt liability. Alternatively the Council can repay debt from selling capital assets (capital receipts).

Although capital expenditure is not charged directly to the revenue budget, interest payable and MRP are charged to revenue. This is offset by income and investment income. All treasury and non-treasury investments make a contribution to the Council's services, and in meeting the Council's strategic aims and objectives. Treasury investments follow the Security / Liquidity / Yield criteria, but the Council also makes a range of investments with the intention of making a return that will be spent on local public services. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from local taxation and general government grants.

Table 4 below provides the Prudential Indicator for proportion of financing cost to net revenue stream:

	2018/19 forecast	**2019/20 projection**	**2020/21 projection**	**2021/22 projection**	**2022/23 projection**	**2023/24 projection**
Financing costs (£m)	£17.9m	£13.7m	£16.2m	£17.7m	£19.1m	£19.7m
Proportion of net revenue stream	2.02%	1.55%	1.75%	1.89%	2.02%	2.02%

Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Section 151 Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable due to the robust assessment process and the close links between the Medium Term Financial Plan, the capital programme and revenue budget and the TMSS.

Leasing – Assets such as vehicles and IT equipment may be leased rather than purchased where there is a financial benefit in doing so, subject to a robust options appraisal. The financing of expenditure by lease needs to take into account:

- Value of expenditure
- Residual value
- Life span of equipment matches the funding proposed

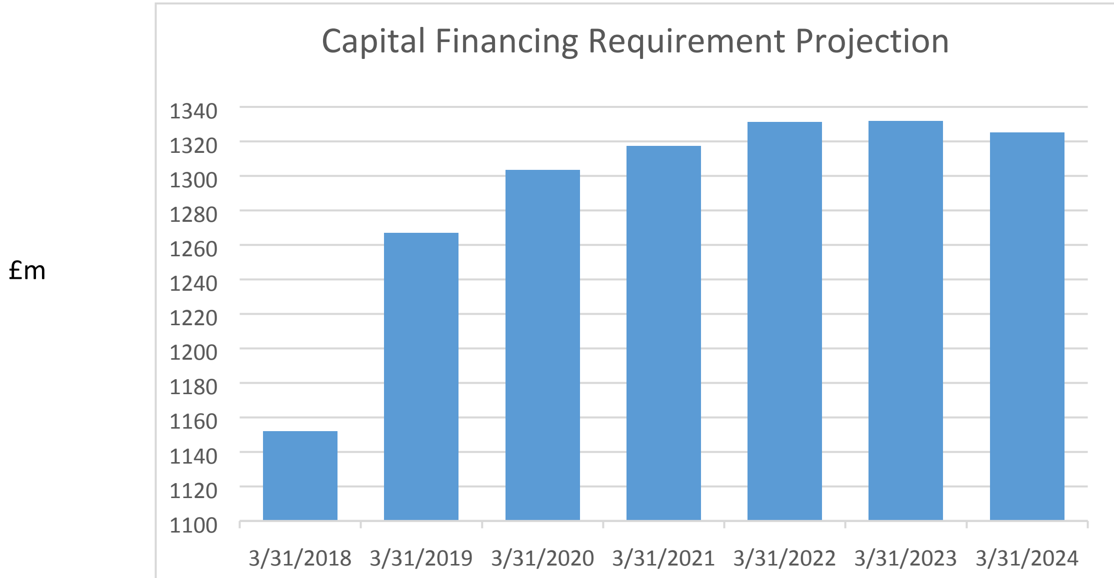
Leasing is considered to be a type of credit arrangement and therefore forms part of the Council's Capital Financing Requirement, as if it were borrowing.

5. PRUDENTIAL INDICATORS

Local Authority borrowing is governed by CIPFA's Prudential Code, which requires local authorities to set indicators which ensure that the level of borrowing is affordable, prudent and sustainable. The Prudential Indicators are set in the TMSS each year, and monitored throughout the year by the Audit & Governance Committee.

The Capital Financing Requirement provides a measure of the amount of capital expenditure that the Council has already spent but not yet funded. The CFR is the measure of the Council's debt liability; i.e. the need to borrow for capital financing purposes. Credit arrangements are included in the CFR calculation as such arrangements are a form of borrowing. Examples of credit arrangements include Private Finance Initiative (PFI) schemes and finance leases.

The Authority's CFR projections are shown in ***Table 5*** below:



CFR movements are caused by:

- the Council incurring further capital expenditure which is not funded from existing capital resources, (the CFR **increases)**
- the Council makes a statutory provision for the repayment of debt through MRP, (the CFR **decreases)**.

Projected levels of the Council's total outstanding debt (which comprises borrowing, PFI liabilities and leases) are shown below, compared with the capital financing requirement (see above). ***Table 6*** shows the gross debt compared to the CFR:

	2017/18 actual £m	2018/19 forecast £m	2019/20 projection £m	2020/21 projection £m	2021/22 projection £m	2022/23 projection £m	2023/24 projection £m
Gross Borrowing (incl. PFI & Leases)	590	689	716	732	759	743	736
CFR	1,152	1,267	1,303	1,317	1,337	1,332	1,325

Affordable borrowing limits: 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 7*** sets out the Council's Authorised Limit and Operational Boundary for external debt, and full details can be found in the TMSS.

Operational Boundary	**2018/19**	**2019/20**	**2020/21**	**2021/22**	**2022/23**	**2023/24**
	Agreed	**← ---------------------**		**Estimated**		**--------------------- →**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Borrowing	702	966	1131	1179	1173	1166
Other long term liabilities	170	143	124	106	87	68
Total	**872**	**1108**	**1256**	**1285**	**1260**	**1234**
Estimated external debt	689	716	732	759	743	736

Authorised Limit	**2018/19**	**2019/20**	**2020/21**	**2021/22**	**2022/23**	**2023/24**
	Agreed	**← ---------------------**		**Estimated**		**--------------------- →**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Borrowing	1,092	1,553	1,717	1,757	1,762	1,755
Other long term liabilities	182	143	124	106	87	68
Total	**1274**	**1696**	**1841**	**1863**	**1849**	**1823**
Estimated external debt	689	716	732	759	743	736

6. BALANCED PORTFOLIO APPROACH

The Council will assess its overall approach to capital expenditure and investment, and will aim to avoid over-exposure to specific markets, sectors or activity. This will reflect investments made to deliver Council services and to those service designed for wider economic benefit.

All projects will reflect full development costs including purchase, fees to cover due diligence, site surveys, legal and transactional costs. The overall business case will include full lifetime maintenance and management costs as well as projected income. Where necessary, external specialist advice and support will be sought, and internal / external due diligence will be undertaken.

The portfolio will comprise an acceptable balance of risk and return, based on market conditions and the level of secured / unsecured investments. Appropriate risk management tools will be applied, tailored to individual schemes and projects.

The Capital and Investment Strategy covers a range of capital investments, and the balanced portfolio approach will ensure an overall average net return reflecting that some projects will yield a higher return than others, and that some schemes are not delivered purely to generate a return.

7. TREASURY MANAGEMENT INVESTMENTS

The Council's investment activities are undertaken in compliance with statutory regulation, the CIPFA Treasury Management in the Public Services: Code of Practice and Cross-

Sectoral Guidance Notes (referred to as the Treasury Management Code). The Treasury Management Code and statutory regulations require the Council to prepare an annual strategy that explains how the Council will invest its funds. In accordance with regulatory requirements, the primary objectives when investing funds for treasury management purposes are **Security**, **Liquidity**; and **Yield**, in that order of importance, often referred to as the **SLY** criteria. The Council's current policy is to maximise the use of reserves and balances for the purpose of internal borrowing, and thereby keeping investment balances to a minimum. This policy reduces the cost of external borrowing and also reduces the market risk of investments.

Day to day decisions on investment and borrowing are delegated to the Section 151 Officer and the Finance Team, who act in line with the TMSS, which is approved by the Audit and Governance Committee before the start of each financial year. Effective scrutiny of the TMSS is undertaken by the Corporate Overview Standards Committee.

8. FLEXIBLE USE OF CAPITAL RECIEPTS

In the Spending Review 2015, the Chancellor of the Exchequer announced that to support local authorities to deliver more efficient and sustainable services, the government will allow local authorities to spend up to 100% of their capital receipts from the sale of non-housing assets on revenue costs incurred to generate ongoing revenue savings, to reduce costs and / or transform service delivery in a way that reduces costs or demand for services in future years. This flexibility relates to expenditure which is properly incurred for the financial years that begin on 1 April from 2016 to 2021.

Local authorities are only able to use capital receipts in the years in which this flexibility is offered. In using the flexibility, the Council will have due regard to the requirements of the Prudential Code, the CIPFA Local Authority Accounting Code of Practice and the current edition of the Treasury Management in Public Services Code of Practice. A flexible use of capital receipts policy will be presented to Council before the start of each financial year for which the flexibilities are proposed to be utilised.

9. RISK MANAGEMENT

Internal and external financial and service related risks are assessed in line with the Council's Risk Management Strategy. Future costs are estimated using interest rate forecasts and projections provided by the Council's treasury management advisers and other financial advisers, and lessons learned from completed schemes and projects are reported to CPP. Operational risks are identified and mitigating controls are applied wherever possible. Residual risks are managed by Budget Managers and reported to CPP monthly.

10. KNOWLEDGE AND SKILLS

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. The Council pays for officers to study towards relevant professional qualifications including CIPFA.

All officers involved in the treasury and investment management function have access to relevant technical guidance and training to enable them to acquire and maintain the appropriate level of expertise, knowledge and skills to undertake the duties and responsibilities allocated to them. The Council currently employs treasury management advisers, and seeks external legal and property related advice and due diligence as required. The Council's commercial investment strategy is supported by advice from CBRE.

Those charged with governance (Members of the Audit and Governance Committee and the Corporate Overview Select Committee) recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively. The Section 151 Officer will ensure that elected members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and responsibilities.

The Orbis partnership enables the creation and development of specialist resources. Centres of Expertise have been established for key areas of finance and property, and central teams of pooled expertise have been created to provide robust services which are resilient to meet the changing service needs of partners.

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