Agenda Item No: 4

BUSINESS PLANNING – CAPITAL STRATEGY

To:	**General Purposes Committee**
Meeting Date:	**1st July 2014**
From:	**Chief Finance Officer**
Electoral division(s):	**All**
Forward Plan ref:	**N/A** ***Key decision:*** **No**
Purpose:	**The Council's Capital Strategy details all aspects of the Council's capital expenditure programme: planning; prioritisation; management; and funding. The Strategy has been revised as part of the 2015-16 Business Planning Process, with respect to how the Council manages and scrutinises the Capital Programme as part of the Business Planning Process.**
Recommendation:	**General Purposes Committee is asked to recommend to Full Council the revisions to the Capital Strategy, to include:**

a) A recommended limit on the level of debt charges (and therefore prudential borrowing) that equates to the level of revenue debt charges as set out in the 2014-15 Business Plan over the next five years and capped at £45m from 2019-20 onwards.

b) That both the recommended limit on debt charges, and the associated level of borrowing this relates to, are reviewed annually by General Purposes Committee at the beginning of the Business Planning Process and are flexed if required.

c) That changes to the phasing of the recommended borrowing limit are allowed within any three-year block, to provide for flexibility of phasing.

d) That borrowing related to Invest to Save/Earn schemes is excluded from the recommended borrowing limit.

e) That prioritisation of schemes is undertaken using an improved version of the Investment Appraisal system.

f) That the process for determining the Children, Families and Adults Programme is highlighted more specifically within the Capital Strategy in order to bring the level of information in line with that for the rest of the Programme.

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1. BACKGROUND

1.1 The Council's Capital Strategy was significantly re-written as part of the 2014-15 Business Planning Process in order to ensure that it was fully comprehensive. It is recommended that some further amendments are made to the Business Planning Process for capital, particularly with respect to the determination of affordable levels ofrevenue financing costs. These amendments have been incorporated into the draft Capital Strategy in Appendix A.

1.2 Maintaining the current level of borrowing for the Council is unsustainable as the revenue impact of this (debt charges) will become an ever increasing percentage of the Council's budget. The Council's high borrowing levels were highlighted by the Local Government Association Peer Review, which recommended that the Council ensures the scale of its ambition is within the available financial resources. Determining the affordability of borrowing requires a long-term view of the revenue impact which the Business Planning Process has not focused on in recent years.

1.3 Under the committee system there is a risk that service committees will not align their spending plans with affordable borrowing levels since individual service committees do not have oversight of, and are not responsible for, the revenue impact of these decisions.

2. SETTING PRUDENTIAL BORROWING LEVELS

2.1 In its role of recommending the final budget to Full Council, General Purposes Committee (GPC) is responsible for ensuring that the level of borrowing arising from the capital programmes proposed by the Service Committees is prudential. Ultimately, if General Purposes Committeedoes not consider borrowing levels to be affordable and sustainable it has the option not to recommend the Business Plan to Council.

2.2 Due to the tight timescales of the Business Planning Process under the committee system this scenario provides little scope to produce a suitably iterated Capital Programme in time to meet the deadline for Full Council. To avoid this situation, this paper recommends that GPC agrees a recommended prudential borrowing limit annually, near the beginning of the Business Planning Process.

2.3 Determining an appropriate prudential borrowing limit must balance the need for capital investment against the ability to make revenue savings both now and in the future. As a rule of thumb, every £10m of capital borrowed means an additional £0.85m revenue savings are initially required for the next 25 years, falling to £0.4m by the end of the 25-year period. To put this in perspective, high levels of borrowing in recent years have led to a projected £10.6m increase in the annual budget for debt charges (savings required) by 2018-19.

2.4 The Council is now in its fourth year of austerity and it is becoming increasingly difficult for Services to make savings, as evidenced by the significant amount of unidentified savings in the current Business Plan. Against this backdrop, it would seem neither affordable nor sustainable to increase the level of debt charges in the current Business Plan any further.

2.5 It is suggested that GPC recommend the introduction of a limit on debt charges (and therefore prudential borrowing) that equates to the level of revenue debt charges as set out in the 2014-15 Business Plan over the next five years and capped at £45m from 2019-20 onwards.Due to the complex interactions between borrowing and debt charges, plus the impact of different phasing, a degree of tolerance around the debt charges limit (+/-£1m) is required in order to arrive at a stable prudential borrowing limit.

2.6 To afford a degree of flexibility from year to year, it is proposed to allow changes to the phasing of the prudential borrowing limits within any three-year block, so long as the recommended aggregate limit remains unchanged. Blocks refer to specific three-year periods, starting from 2015-16, rather than rolling three-year periods. For example, the aggregate prudential borrowing limit for the first block (2015-16 to 2017-18) is £138m, which could be divided either equally or unequally across the period.

2.7 However, other factors such as levels of external funding may impact on the level of debt charges that GPC is willing to commit to.Therefore, the level recommended by GPC should be reviewed each year to ensure it is still relevant.

2.8 In addition, other factors such as interest rates have an impact on the amount of borrowing that it is possible to undertake whilst remaining within a given level of debt charges. Therefore the debt charges resulting from a specified level of borrowing may increase or decrease, depending on the movement in interest rates. As such, the cap on borrowing resulting from a recommended limit on debt charges also needs to be reconsidered each year to ensure that the debt charges remain in line with the agreed prudential level.

2.9 Acknowledging the Council’s strategic role in stimulating economic growth across the County, e.g. through infrastructure investment, it is recommended that any new, or changes to existing, capital proposals are able to reliably demonstrate revenue income / savings at least equal to the debt charges generated by the scheme’s borrowing requirement be excluded from contributing towards the recommended limit.However GPCwill still need to review the timing of the repayment, in conjunction with the overall total level of debt charges when determining affordability.

3. PRIORITSATION OF THE PROGRAMME

3.1 Recommending a limit on prudential borrowing has the potential to act as a constraint on capital spending and gives rise to the need for a method to identify schemes of greatest priority to the Council. To maximise the value of this finite resource the prioritisation process should allow comparison of schemes both across and within Services / committees.

3.2 For the majority of schemes an investment appraisal approach is the most useful and expedient method of prioritising capital proposals. This was trialled during the 2014-15 Business Planning Process, and it is proposed to build on this, incorporating lessons learned from last year.It is not currently particularly suited to help prioritise the schools’ Capital Programme; as such, the process will be adapted so that it can also act as a useful tool for Children, Families and Adults (CFA) to review their programme and present it to committees by better taking into account factors that affect CFA schemes.

3.3 The process was also of limited value in scrutinising the schools' Capital Programme due to the statutory requirements giving rise to these proposals. Whilst acknowledging the high priority this statutory requirement correctly affords schools' capital proposals, the scrutiny of the costs of delivering these schemes is still valid as for any other proposals.The Department for Education's Basic Need scorecard published earlier this year indicates Cambridgeshire's average cost per primary school place is in the highest quintile for both permanent expanded schools and new schools. Whilst acknowledging there may be specific reasons that contribute towards this situation, these figures still suggest that there is considerable range in the cost of building schools. This indicates that the Council has a degree of influence over their costs and that delivery policies should therefore be regularly re-evaluated in light of financial constraints.

3.4 To help achieve this, the Capital Strategy has been revised to highlight the influencing factors and the Council's current policies for delivering school places, as these are not currently specified within the Business Planning documentation and would help provide increased clarity to Members. Within the Capital Strategy currently, there is a lot of information regarding both working in partnership and asset management, which helps to provide context for how the programmes for both Economy, Transport and Environment and Corporate and Managed Services are shaped. However, this context does not currently exist within the Strategy for schools.

4. ALIGNMENT WITH CORPORATE PRIORITIES

4.1 Developing the local economy for the benefit of all

The following bullet points set out details of implications identified by officers:

- Recommending a limit on the level of borrowing will inevitably have an impact on the Council's ability to drive forward investment in the local economy. However, to limit the impact it is recommended that any capital proposals that are able to reliably demonstrate revenue income / savings at least equal to the debt charges generated by the scheme's borrowing requirement are excluded from contributing towards this limit.

- In addition, the Council is looking to stimulate economic growth through capital investment via other mechanisms, such as the Local Enterprise Partnership and the City Deal.

4.2 Helping people live healthy and independent lives

There are no significant implications for this priority.

4.3 Supporting and protecting vulnerable people

There are no significant implications for this priority.

5. SIGNIFICANT IMPLICATIONS

5.1 Resource Implications

The following bullet points set out details of significant implications identified by officers:

- This report provides detail about a change in the process of planning for capital schemes, which has a direct impact on both capital and revenue (through financing costs).Improvements to the process will ensure that resources are targeted efficiently, effectively and equitably, and will provide Value for Money.

5.2 Statutory, Risk and Legal Implications

The following bullet points set out details of significant implications identified by officers:

- The suggested process will ensure that statutory obligations will be met and will help to minimise the risk of borrowing in an unaffordable and unsustainable manner.

5.3 Equality and Diversity Implications

The following bullet points set out details of significant implications identified by officers:

- The suggested process to improve control of borrowing will reduce the intergenerational inequality currently building up through high levels of unsustainable borrowing.

5.4 Engagement and Consultation Implications

There are no significant implications within this category.

5.5 Localism and Local Member Involvement

There are no significant implications within this category.

5.6 Public Health Implications

There are no significant implications within this category.

Source Documents	**Location**
Draft Capital Strategy 2015-16	Room 301 Shire Hall Cambridge
Business Plan 2014-15	http://www.cambridgeshire.gov.uk/info/20043/finance_and_budget/90/business_plan_2014_to_2015