# Nottingham City Council Capital & Investment Strategy

# Nottingham City Council Capital and Investment Strategy 2020/21 – 2024/25

## Contents

# Section One – Introduction

## Aims of the Capital and Investment Strategy and its links to the Council Plan

The Capital Strategy forms a key part of the City Council's overall Corporate Planning Framework by which capital and investment decisions will be made.

The overarching aim of the 2020/21 to 2024/25 Capital Strategy is to provide a framework within which the Council's capital investment and financing decisions can be aligned with the Council's corporate priorities and objectives over the medium term. The Strategy recognises uncertainties, especially in relation to funding in later years.

In order to reflect the Council's corporate priorities the Capital Strategy is driven by the Council Plan 2019-2023, which is founded on five key objectives:

- Build or buy 1,000 Council or social homes for rent
- Create 15,000 new jobs for Nottingham people
- Build a new Central Library, making it the best children's library in the UK
- Cut crime, and reduce anti-social behaviour by a quarter
- Ensure Nottingham is the cleanest big city in England and keep neighbourhoods as clean as the city centre

These objectives reflect an on-going commitment to the City Council's core aim to "put citizens at the heart of everything we do". This is central to the Council's priorities, decision making and service delivery.

Alongside the Council Plan the Council has also made a commitment to become the first carbon neutral city in the country, reaching this target by 2028, this has involved the creation of Nottingham's 2028 Carbon Neutral Charter.

Further details regarding how the Council Plan has influenced the capital projects include regeneration and transport priorities. Further details can be found in Section 2 (Council's Priority Areas for Capital Investment).

This strategy sets the framework for all aspects of the Council's capital and investment expenditure including planning, prioritisation, management, funding and monitoring. This strategy forms a key part of the Council's Medium Term Financial Strategy.

# Section Two – Capital Strategy Aims, Objectives, Principals and Priorities

## Aims & Objectives of the Capital and Investment Strategy

The Capital and Investment Strategy aims to:

- Provide a clear set of objectives and a framework, compliant with the CIPFA guidance and legislation, by which new projects are evaluated.

- Ensure projects meet the Council's priorities and are fully funded by means of whole life project costing.

- Prioritise projects that meet the following criteria:
    - Deliver Council Plan / Council Objectives
    - Invest to Save – assist the delivery of budget decisions
    - Commercialism – projects that generate a revenue surplus
    - Attract significant third party or match funding to the City
    - Deliver wider economic or service objectives e.g. regeneration / job growth

- Set out how the City Council identifies, programmes and prioritises funding requirements and proposals arising from a project gateway process. This involves a Full Financial Appraisal, Full Business Case and a review by the Project Assurance Group. The Council's capital prioritisation process is currently under review, due to limitations on available funding and in order to identify synergies within proposed schemes. Outcomes from the review and any recommendations will be reported as part of the capital monitoring presented to Executive Board.

- Aid decision making regarding use of funding, resource availability and how these might be maximised to deliver the Council's priorities.

- Ensure the capital programme maintains an overall balance of risk over the strategy period and provides insight into the funding envelopes and rates of return.

- Establish effective arrangements for the management of expenditure including the assessment of project spend, budget forecasting, contractual commitments, revenue impact (in year and projected over the Medium Term Financial Outlook (MTFO), value for money, opportunity cost and debt exposure.

## Capital Investment Principles and Priorities

### Principles

The Council's capital strategy ensures that all the projects are accounted for in the allocation of any available resources. The principles of the strategy are as follows:

- Current approved (or contractually committed) schemes will be supported and sufficient resources will be provided to enable them to proceed or complete up to the approved level of expenditure.

- Capital Project Sponsors and Managers must demonstrate that a rigorous process of options appraisal has been followed, requiring assessment of Council priorities, cost, risk, project deliverables and methods of financing. The Project Assurance Group has a clear role in ensuring all key questions have been asked prior to the scheme receiving formal approval.

- Any costs incurred on options not progressed will be abortive costs that do not meet the criteria for capitalisation.

- All capital investments are required to make reference to Council objectives and will only be considered for resource allocation once this has been demonstrated.

- There will be no ring-fencing of capital receipts to specific projects, with the exception of:
    - School Sites ring-fenced by the Secretary of State for education purposes
    - Sites identified as part of the Loxley House Acquisition
    - Property Trading Assets: Sites whose sale generates a revenue pressure will be assessed to identify how much the Council needs to reinvest to cover lost income

- The Council will consider the removal of ring-fencing from certain grant allocations to assist in the achievement of the Council's priorities and objectives. All uncommitted non ring-fenced capital funding will be reviewed.

  Non ring-fenced grants received in support of the three areas below will be earmarked to fund these initiatives.

    - Transport grant funding
    - Basic Needs Government funding, due to the current pressure on school places
    - Disabled Facilities Grant

- It is assumed that all resources that were not applied during the previous financial year remain fully committed and carried forward into the current year, as they are required to meet commitments within the Capital Programme.

- Future funding opportunities may arise for which the Council may wish to submit bids. The Council will respond in a manner it considers appropriate to bidding opportunities, ensuring that bids are submitted which align with its objectives and capital investment priorities. Match funding requirements are considered on a scheme-by-scheme basis with resourcing requirements prioritised accordingly.

- Business Cases and Financial Assessments (Section 3), adopt the prudent principle regarding the asset value at the end of the financial model, the normal assumption is the asset has £nil realisable value, although this will be considered on a case by case basis.

- In accordance with CIPFA guidance the Council defines Capital Expenditure as:

  'Expenditure on the acquisition or enhancement of property, plant and equipment that has a long-term value to the Council. This includes grants or advances paid to third parties to assist them in acquiring or enhancing their own property, plant and equipment.'
  Nottingham City Council Statement of Accounts 2017/18

  Any expenditure that does not meet the above definition is charged directly to revenue, for example:
    - Routine repairs and maintenance of fixed assets
    - Feasibility and Development costs of options and schemes not progressed
    - Communications and Marketing
    - Expenditure not necessary to bring the asset into use

- Due to the level of risk contained within the Capital Programme approved projects are encouraged to value engineer / reduce costs where possible, especially when a reduction of costs can be achieved without significantly affected the project deliverables.

- The Council has established a Capital Risk Reserve from savings identified within the current capital programme. This Risk Reserve is to cover current risks within the capital programme, such as schemes with unsecured grants at the time of approval. Any savings or underspend within the Capital

Programme will be transferred to this reserve to offset an element of the Council's capital risk.

- All projects that are considered live projects but have not incurred any capital expenditure within the last two financial years will be automatically closed with any available funding transferred to the Capital Risk Reserve. Should late retention payment be required they can be funded from the Risk Reserve up to level of contribution.

- If the financial models for approved schemes move adversely during the pre-contract stage by the lower of £1.000m or 20% (either cash or NPV), further approval will be required including a revised business case.

- Due to the Council's current debt levels, the overall finance context and the level of risk to which the Council is exposed, the capital prioritisation process is being reviewed as detailed above. The outcome of this review may include the capping of future borrowing to enable the reduction of the Council's overall debt level.

**Prioritisation**
Under the current process each project or programme is subject to a gateway review / approval process that includes a full business case.

Projects / programmes that do not have a full funding package and require Council Resources (including schemes which have deficits in early years i.e. Medium Term Financial Plan (MTFP) Deficit), will be appraised using the following criteria should funding become available:

- Alignment to the Council Plan;
- Consequences of Exclusion (i.e. not providing Corporate Resource);
- Project Funding Package;
- Whether Project generates an income / reduces costs (including Invest to Save);
- Any pre-conditions;
- Impact on the environment and the Council's commitment to net zero;
- Effect on regeneration.

## Council's Priority Areas for Capital Investment

The Capital and Investment Strategy recognises the constraints imposed by a significant reduction in financial resources. Nottingham City Council must therefore rely on both internal and external capital resources and evaluate projects to ensure all investment decisions can be no less than financially self-sustaining whilst still meeting priorities.

As well as the Council prioritising projects individually, the Council also considers the

Capital Programme collectively in terms of how associated risk is managed, the cash flow implications and the impact of future financial sustainability.

The Corporate Asset Management Plan (CAMP) confirms the Council's commitment to provide good quality, sustainable and accessible accommodation for staff and citizens. However, the Council still owns Operational Assets that do not meet modern standards and the aim is to dispose of these sites, providing more effective accommodation for colleagues and an improved experience for citizens (i.e. Operational Property Rationalisation). To ensure resources are available for maintaining operational assets, all financial models will include whole life costing that is sufficent to fund future repair liabilities. The CAMP also provides the framework for which non-operational assets are managed.

As part of the Asset Rationalisation Programme (ARP) the Council is reviewing its Operational and Non-operational assets to identify assets for potential disposal. Any available capital receipt generated from the ARP will be used to offset the Council's current **£70.528m** commitment, further details can be found in section 4.

In addition to the ARP process, the Council is reviewing the resources set aside for fund maintenance of Council assets and IT infrastructure. With the aim to identify an affordable way to maintain its assets over the medium to long term.

The Council's capital investment priorities for the period 2019/20-2024/25 are covered below. These projects will be progressed subject to the availability of resources and the approval of a full business case.

**Existing Projects:**
There is a commitment to continued funding for the following priority areas:

- District Heating / Incinerator Works
- Nottingham Castle Transformation
- Southern Gateway Improvements
- Royal Centre Modernisation
- Council-wide IT Schemes
- Vehicle Replacement Programme
- Low Carbon and Energy Efficiency Initiatives
- Parks and Open Spaces Improvements
- City Regeneration Schemes
- Housing Initiatives
- Property Repairs and Investments
- Transport Repairs and Improvements
- School Condition Works
- Invest to Save or Commercialisation
- Property Rationalisation
- Delivery of key regeneration priorities

- Delivery of Local Transport Plan projects and infrastructure to support economic development
- Supporting Local Plan housing delivery
- Fit-out and operation of the new Central Library

**New and Emerging Projects (i.e. Planned and Potential Schemes)**
In addition to the projects specifically referred to above, the following is a list of priority projects that have not had the full business case approved:

- School Investment / Pupil Pressures
- Other Regeneration Schemes
- Further Southern Gateway Investments

## Non-Treasury Investments

Nottingham City Council invests in other financial assets (i.e. loans and investment properties), which are not part of treasury management activity. These other investments fall within two areas:

- **Service Investments** – investments held clearly and explicitly for the provision of operational services, including regeneration
- **Commercial Investment** – investments undertaken primarily for financial reasons

Appendix A contains service and commercial investments split between capital and revenue. The commercial investments are summarised in **Table 1**.

Non-Treasury investments are analysed periodically to ensure that the fair value / carrying value of each investment is appropriate as required under the relevant Accounting Standard (Service Investments – IFRS9, Commercial Investments – IAS40).

**Service Investments**
Service investments made by the Council are largely loans to third parties ranging from short-term to longer-term loans linked to assets or investments in group organisations. Following a detailed assessment, each loan will have an interest rate applied which reflects any appropriate legislation (e.g. State Aid). Scrutiny for Service Investments is undertaken by officers within the Council giving due regard to the relevant formal approval. This scrutiny will include a due diligence assessment to ensure that the Council has the appropriate level of:

- Security – due diligence is carried out on the loan counterparty to assess their credit strength and ability to make loan repayments. Security is also achieved by obtaining charges on assets, but could also include guarantees (e.g. Parent Company Guarantee)
- Liquidity – third party business cases to be critically assessed to identify financial performance including if the scheme has early year deficits
- Yield – reflecting market risk / return and the opportunity cost to the Council of not being able to use those funds elsewhere

**Commercial Investment**
Commercial Investments that the Council has undertaken to date are property investment acquisitions. **Table 1** below detail the Council's Commercial Investment at the 31st March 2019, how it was funded and the net effect on the General Fund:

| Table 1: Commercial Investments and contribution to Budget at 31st March 2019 |
|---|

| | £m |
|---|---|
| Gross Commercial Investment<br>Minimum Revenue Provision incurred | 251.488<br>(1.945) |
| **Net Commercial Investments** | **249.543** |
| Funding<br>Council Resources<br>Unsupported Borrowing (net of MRP paid to 31st March 2019) | <br>(5.736)<br>(243.807) |
| **Total Funding** | **(249.543)** |
| **Forecast Net income to the General Fund 2019/20 (*)** | **(6.140)** |

(*) Net of financing costs, operating costs and contribution to a sinking fund.

The average yield generated from the Commercial Investments included in **Table 1** is 2.52% (based on net income and unsupported borrowing net of MRP).

All Commercial Investments are reviewed on an on-going basis. These reviews support good estate management principles and ensure that the Council's risk and returns are appropriately managed. The investments are managed on an ongoing basis, reviewing the actual performance to the original financial model, paying particular attention to key events such as rent reviews.

The gross commercial investment made by the Council of £249.543m (excluding MRP payments to 31st March 19), leaves the Council open to the following risks:

- Voids due to economic downturn / tenant lease breaks
- Property Market downturn
- Inaccurate assumptions or changes in environment or management of asset causes lower final valuation or delays in disposal leading to unforeseen costs.

These risks have been mitigated by investing in a diverse property portfolio and the properties are transferred as a going concern by having a tenant with a strong covenant in occupation. A sinking fund is also set aside for the commercial investments based on rental level received. This reserve is available to smooth out void periods (in-year deficits) if they cannot be absorbed elsewhere within Property Services.

The Council continues to operate in a challenging financial environment of reduced levels of Government funding due to austerity policies. This level of commercial investment has been undertaken as part of the council's commercialisation policy, which seeks to address the funding gap and protect key services.

## Capitalisation Flexibilities

In December 2017 the Secretary of State announced that the capital receipt flexibility programme will be extended until 31st March 2022. This flexibility gives the Council the freedom to use non-Public Sector Housing capital receipts to fund the revenue costs of transformation projects and release savings.

As detailed within Section 3 the Council is not intending to use this flexibility due to all forecast receipts from property disposal (secured and unsecured) in the medium term being earmarked to fund the Council's ambitious capital programme. Receipts from principal loan repayments are earmarked to repayment of underlying debt.

# Section Three – Capital Programme Structure, Resourcing Strategy

## Capital Programme Structure

The Council's Capital Programme is split into three sections:

- Approved Projects – Projects that have been formally approved and have a funding package that is deemed affordable
- Planned Projects – Projects that have been agreed in principal and the Council is undergoing project feasibility and development to identify if the project's objectives can be achieved within an affordable funding envelope
- Potential Projects – Projects that are at the beginning of the scoping and development process and therefore are not included in the Council's borrowing forecasts

As projects progress through the above stages they will go through a gateway process to challenge the project team and provide assurance that the project is best use of public funds and will assist the Council in meeting its priorities.

Each of the three Capital Programme areas include a variety of capital projects, with each section divided into sub-sections as follows:

- Council Priorities / Service Delivery (including Regeneration Schemes)
- Asset Investments
- Third Party Loans
- Revenue Generating Investments (Invest to Save or Commercialism)
- Grants
- Revenue Expenditure Financed by Capital Under Statute (REFCUS)

**Capital Programme – General Fund**
**Table 2** below is a snapshot of the Capital Programme at 31st December 2019.

The funding is showing a balanced budget within **Table 2** assuming all forecast grants are received as expected and the pressure on the unsecured capital receipts as highlighted within **Table 5** is resolved.

| Table 2: General Fund - Capital Programme and Resources | | | | | | | |
|---|---|---|---|---|---|---|---|
| **2019/20 £m** | **Scheme** | **2020/21 £m** | **2021/22 £m** | **2022/23 £m** | **2023/24 £m** | **2024/25 £m** | **Total £m** |
| | **Approved Schemes** | | | | | | |
| 30.217 | Transport Schemes | 9.853 | 1.420 | 0.000 | 0.000 | 0.000 | **41.490** |
| 5.167 | Education | 3.092 | 0.000 | 0.000 | 0.000 | 0.000 | **8.259** |
| 143.979 | Other Services | 119.853 | 30.602 | 10.812 | 8.840 | 9.794 | **323.880** |
| 2.050 | **Category 2 - Planned Schemes** | 26.070 | 16.820 | 5.682 | 5.900 | 0.000 | **56.522** |
| **181.413** | **Total Programme** | **158.868** | **48.842** | **16.494** | **14.740** | **9.794** | **430.151** |
| | **Resources Available** | | | | | | |
| (99.757) | Prudential Borrowing | (98.227) | (36.339) | (7.845) | (6.377) | (7.398) | **(255.943)** |
| (68.201) | Grants & Contributions | (40.025) | (6.818) | (8.394) | (8.114) | (2.206) | **(133.758)** |
| (3.683) | Internal Funds / Revenue | (8.295) | (1.645) | (0.255) | (0.249) | (0.190) | **(14.317)** |
| (4.996) | Secured Capital Receipts | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 | **(4.996)** |
| (4.776) | Unsecured Capital Receipts | (12.321) | (4.040) | 0.000 | 0.000 | 0.000 | **(21.137)** |
| **(181.413)** | **Total Resources** | **(158.868)** | **(48.842)** | **(16.494)** | **(14.740)** | **(9.794)** | **(430.151)** |

*(*) Traditionally the Local Transport Plan is set for three years, however due to the Spending Review outcome unknown, no Local Transport funding is programmed beyond 2020/21. Once the outcome of the spending review has been completed the Transport Programme will be reviewed to ensure it is able to respond to any new requirements or priorities.*

## Capital Programme – Public Sector Housing

**Table 3** is a snapshot of the Public Sector Housing Programme. The programme currently shows a resourcing shortfall due to additional capital projects being required following the Grenfell incident. If external grant cannot be identified, savings will need to be made elsewhere within the Public Sector Housing Programme to offset the forecast funding shortfall.

| Table 3: Public Sector Housing - Capital Programme and Resources | | | | | | | |
|---|---|---|---|---|---|---|---|
| **2019/20 £m** | **Scheme** | **2020/21 £m** | **2021/22 £m** | **2022/23 £m** | **2023/24 £m** | **2024/25 £m** | **Total £m** |
| 54.568 | Category 1 - Approved Schemes | 50.553 | 56.108 | 41.724 | 33.375 | 27.916 | **264.244** |
| 0.010 | Category 2 - Planned Schemes | 8.922 | 2.450 | 0.000 | 0.000 | 0.000 | **11.382** |
| **54.578** | **Total Programme** | **59.645** | **58.648** | **41.724** | **33.469** | **27.926** | **275.626** |
| | **Resources Available** | | | | | | |
| (12.415) | Prudential Borrowing | (18.444) | (15.309) | (9.682) | (3.572) | 0.000 | **(59.422)** |
| (3.694) | Grants & Contributions | (3.830) | (3.191) | 0.000 | 0.000 | 0.000 | **(10.715)** |
| (29.945) | Major Repairs Reserve | (29.415) | (31.746) | (24.955) | (25.335) | (24.839) | **(166.235)** |
| (8.524) | Secured Capital Receipts | (4.731) | (4.010) | (4.010) | (3.355) | 0.000 | **(24.630)** |
| 0.000 | Unsecured Capital Receipts | (3.055) | (4.302) | (3.077) | (1.113) | (3.077) | **(14.624)** |
| **(54.578)** | **Total Resources** | **(59.475)** | **(58.558)** | **(41.724)** | **(33.375)** | **(27.916)** | **(275.626)** |

## Capital Resourcing Approach

The Council's capital investment is governed by the 'Prudential Code for Capital Finance in Local Authorities' (Prudential Code). The Prudential Code provides the Council with a regulatory framework within which the Council has discretion over the funding of capital expenditure and the level of borrowing the Council wishes to undertake to deliver capital plans and programmes.

The strategy is intended to maximise the financial resources available for investment in service provision and improvement within the MTFO. At the same time it seeks to ensure that each business case has a robust self-sustainable financial model that delivers the Council's objectives.

The funding available to Nottingham City Council is split into five main categories:

1. Government grants and non-government grant and contributions
2. Unsupported borrowing
3. Capital Receipts
4. Internal Funds / Revenue
5. Leasing / Private Finance Initiatives (PFI)

**1. Government Grants and Non-Government Grant and Contributions**

These can be split into three sub categories:

- Ring-fenced grants and contributions (Reserved for a particular purpose and have a restricted use);
- Non-ring-fenced grants and contributions (Grant given with conditions which Projects are required to meet);
- Section 106 agreements (Planning obligations generally subject to conditions of use).

Where there is a requirement to make an application to an external body for funding and commit Council resources as match funding for any part of any bid, a business case and paper needs to be approved per the Council's current approval procedures (e.g. DDM, Leaders Key Decision, or Executive Board Report).

**2. Unsupported Borrowing (Prudential Borrowing)**

As detailed above the Council has the discretion to undertake borrowing on capital schemes (General Fund and Public Sector Housing) if the borrowing is deemed Value for Money and meets the following criteria as set out in the Prudential Code:

- **Affordable**
- **Sustainable**
- **Prudent**
- **Proportionate for the size of the authority**.

For any borrowing undertaken a full appraisal will take place to ensure that sufficient revenue returns are generated to cover the cost of borrowing, for example 'invest to save' or schemes which meet the Council's 'commercialisation agenda'.

To be deemed affordable, sustainable and prudent a full business case is carried out and schemes have to provide a surplus Net Present Value (NPV) to the Council over the life of the project.

Prudential Borrowing Loan repayments are spread over an asset's useful life, this means that for the longer term Capital Schemes (i.e. Land and Buildings) the borrowing term can be significant.

Where it is considered that prudential borrowing is the appropriate method of funding, the additional revenue costs related to debt repayment will be built into the service budget. When projects are approved, details of how any potential revenue impact will be managed must be included (e.g. early year deficits).

**Housing Revenue Account (HRA)**

The HRA has no statutory requirement to make Minimum Revenue Provision (MRP) contributions unlike unsupported borrowing within the General Fund. The Council uses the HRA 30 year business plan as a way of managing its debt position by making voluntary provisions / voluntary set aside as appropriate. Prudential Borrowing for Housing Revenue Account Projects is required to meet the same Prudential Code criteria as set out above (e.g. full financial appraisal, debt repaid over asset life, early year deficit impact).

**Forecast Borrowing General Fund and Housing Revenue Account**

The Council is forecasting to borrow **£315.365m** over the period 2019/20-2024/25, **Table 4** below breaks this forecast borrowing into financial years:

| **Table 4: Unsupported Borrowing Forecast Period 8** | | | | | | |
|---|---|---|---|---|---|---|
| **Area and Category** | **Forecast Borrowing Requirement** | | | | | |
| | **2019/20 £m** | **2020/21 £m** | **2021/22 £m** | **2022/23 £m** | **2023/24 £m** | **2024/25 £m** |
| **General Fund** | | | | | | |
| Category 1 - Approved Schemes | (97.166) | (76.067) | (21.224) | (7.845) | (6.377) | (7.398) |
| Category 2 - Planned Projects | (2.591) | (22.160) | (15.115) | 0.000 | 0.000 | 0.000 |
| **TOTAL General Fund** | **(99.757)** | **(98.227)** | **(36.339)** | **(7.845)** | **(6.377)** | **(7.398)** |
| **Public Sector Housing** | | | | | | |
| Category 1 - Approved Schemes | (12.405) | (9.842) | (15.309) | (9.682) | (3.572) | 0.000 |
| Category 2 - Planned Projects | (0.010) | (8.602) | 0.000 | 0.000 | 0.000 | 0.000 |
| **TOTAL Public Sector Housing** | **(12.415)** | **(18.444)** | **(15.309)** | **(9.682)** | **(3.572)** | **0.000** |
| **TOTAL Forecast Borrowing Requirement** | **(112.172)** | **(116.671)** | **(51.648)** | **(17.527)** | **(9.949)** | **(7.398)** |

The HRA considers projects on a programme approach, further details can be found within the Financial Appraisal section.

## 3. Capital Receipts

The Council's land and property estate is managed through the CAMP, which identifies the Council's property requirements. Where appropriate, properties are declared surplus to requirements and the Council will look to dispose of the asset.

Capital receipts generated from disposal of Council assets represent a finite funding source, therefore the Council is required to plan disposals to support its priorities.

Capital receipts will also be a key source of capital funding for projects that meet the Council's strategic aims / objectives but make insufficient financial return to cover the costs of borrowing.

Nottingham City Council has a strategy of not ring-fencing the use of specific Corporate Capital Receipts to fund specific schemes or service areas unless a suitable business case is created and approved.

All receipts are reviewed to see if there are any restrictions on the receipt (e.g. Secretary of State), or whether the asset had any clawback provision or debt outstanding as these have first call on the capital receipt. The remaining balance of general fund capital receipts is allocated between reinvestment in Property Income Generation and Corporate Capital Receipts:

The Council is establishing an Asset Rationalisation Programme, therefore at present the forecast receipts over the 2019/20-2024/25 period cannot be estimated until the Programme is in operation.

As detailed in **Table 2**, the General Fund Capital Programme is predicated on securing **£26.133m** receipts to March 2022. At Quarter 3 2020 the Council has committed to applying **£70.528m** of capital receipts. Further detail is shown in the table below:

**Table 5: General Fund Capital Receipt Commitment**

| | **Commitment £m** |
|---|---|
| General Fund Capital Programme | 26.133 |
| Past commitments from prior Capital Programme | 18.999 |
| Other commitments outside the Capital Programme (*) | 25.396 |
| **TOTAL Capital Receipt Commitment** | **70.528** |

*(*) Examples are sinking fund for Broadmarsh Shopping Centre and replenishment of Council SAM Resources*

**Housing Revenue Account (HRA) – Capital Receipts**
The HRA capital receipts are sub-categorised as follows:

- Non Right-to-Buy Receipts – The receipt is ring-fenced for reinvestment within the Capital Programme for Housing and Regeneration.
- Right-to-Buy (RTB) Receipts – Are accounted for as stipulated in the Local Government Act, with elements of the receipt net of transaction costs:
    - Repaid to Central Government
    - Capital spend for either allowable debt (i.e. Voluntary Set-aside) or to fund capital expenditure within the Capital Programme
    - Retained for reinvestment in Housing Stock (RTB Replacement Receipts), or returned to Central Government if unspent within timeframe

## 4. Internal Funds / Revenue

Capital Expenditure can be funded directly from revenue resources. The sources of revenue funding can be split into two clear categories:

- Funds and Reserves – specific reserves set aside for Capital purposes
- Direct Revenue Funding (DRF) – using revenue budget surpluses for capital purposes if it can be demonstrated that the funding is unfettered.

However, in the current economic climate and with increasing revenue pressure within Council finances, the extent to which this may be used to fund capital expenditure is significantly reduced.

**Housing Revenue Account (HRA)**
The HRA has a Major Repairs Reserve which is a specific reserve ring fenced for repairs and maintenance of the Council's housing stock.

## 5. Leasing / Private Finance Initiatives (PFI)

The Council does have the option to lease assets, however with the advent of Unsupported Borrowing this source of financing is becoming less attractive and the Council's Vehicle Replacement Scheme demonstrates this development. There may however be instances where leasing could offer value for money and it will remain a consideration when options are being appraised.

PFI schemes are not shown within the Capital Programme due to not being financed by capital resources.

However, the long-term affordability of the PFI schemes at the Council is being closely managed. The current situation is that one scheme is forecasting a temporary deficit in 2033/34, and there are certain schemes where the Council has an option to purchase at the end of the agreement but no monies have been set aside. Therefore, a business case will need to be established to identify whether or not acquiring the site at agreement termination is value for money.

When the Council identifies a service requirement all financing options are considered as part of the business case / feasibility. Where appropriate this will include the potential creation of a liability via a leasing or similar arrangement (e.g. PFI). Prior to entering into these agreements, a formal decision will need to follow the Council's standard approval process.

Leases and contracts entered into by the Council are periodically reviewed to identify all lease and embedded lease arrangements entered into that may create a potential liability for the Council.

## Resourcing Allocation Strategy and Procedures

### Resources Allocation Strategy

As detailed in Section Two, the Council is reviewing its prioritisation process which involves the Resource Allocation Strategy. The current proposal considers the following:

- Capital Receipts - no further capital receipt can be committed until the pressure identified in Table 5 has been resolved.
- Prudential Borrowing will be capped annually at a level under the Council's MRP budget, enabling the Council to reduce its debt position.

Once the current review is complete, potential schemes can be prioritised and any secured / available funding can be allocated as required.

# Internal Guidance / Business Case Considerations / Gateway Reviews

## Internal Guidance

### Project Management Handbook

The Project Management Handbook is a best practice document for project delivery. This section of the intranet also includes standardised templates that accompany the Project Management Handbook.

The link to the handbook is set out below:

http://intranet.nottinghamcity.gov.uk/major-projects/project-management/project-management-handbook/

### Accounting Handbook

The Accounting Handbook has a section regarding fixed assets and capital investment, this section includes information about:

- Fixed Assets
- Capital Expenditure Coding
- Capital Accruals
- Capital Funding
- Revenue Expenditure Funded from Capital Under Statute (REFCUS)
- Lease Accounting

As part of the capital monitoring process project managers are also sent guidance regarding expenditure capitalisation rules to assist them in their understanding of the revenue / capital split.

The link to the handbook is set out below:

http://intranet.nottinghamcity.gov.uk/finance/statutory-information/

## Gateway Review

The Council has introduced a Gateway Zero process which requires all new proposals for significant projects to go to the Corporate Leadership Team for sign-off prior to Council resources being committed.

Following a Gateway Zero, the business case and financial assessment are evaluated at a Project Assurance Group (PAG). The PAG is a panel who are not involved in the project's development and are tasked with reviewing and challenging the project and the decisions made.

**Business Case**

A business case is a formal document, which explains the case for the investment in a project or programme of work. The areas covered by a business case vary depending on whether it is an outline or full business case. An outline business case is used at the start of the planning process to obtain ‘approval in principle’ to proceed. A full business case is prepared after ‘approval in principle’ and is expected to cover the following areas:

1) The background to the business case - i.e. the reason for the project being put forward – in order to give context to the project;
2) Objectives
   a. The overall objectives of the project, and
   b. How the project will contribute to the achievement of corporate priorities, including the impact on the Council’s commitment to become the first carbon neutral city in the country, reaching this target by 2028;
3) Overview of options considered with a brief summary of why options were rejected;
4) Detailed explanation of the option accepted and why it was accepted;
5) Procurement details, including (but not limited to);
   a. details of tender process (when applicable)
   b. analysis of shortlisted tenders
   c. preferred supplier with explanation for decision
6) Financial appraisal of the scheme, including;
   a. profile of capital expenditure
   b. profile of funding broken down by funding source
   c. revenue implications (including the impact on the MTFO and any early year deficit)
7) Other advice required (as appropriate) per the standard approvals process;
   a. Legal
   b. Human Resources
   c. Procurement
   d. Property
8) Business Cases contain an inherent risk regarding the assumptions, in particular the likelihood of the revenue assumptions being achieved. This risk is amplified on the longer term business cases due to the uncertainty of predicting future cash flows / behaviours. This should be addressed through sensitivity and risk analysis.

## Financial Appraisal

The purpose of any financial appraisal is to evaluate the viability of a project by assessing the net cash flows that result from financial models, how it meets the requirements of the Prudential Code and provides an assessment of Value for Money.

All capital projects are required to undertake a financial appraisal if they have either:

- An element of borrowing within the project's funding envelope, or
- A revenue impact on service delivery

The Technical Accounting Team coordinates the financial appraisal.

Principles of the financial appraisal are:

- Full life project costing – For projects that are expected to create an asset with a long useful life the financial appraisal has an inherent risk due to uncertainty of cash flows in the longer term. A provision for a sinking fund to protect the Council from future liabilities should be included
- Revenue assumptions are required to have assumption owners who are either appropriately qualified Council officers or are specialist external advisors
- Revenue assumptions will be assessed to determine whether they should be subject to inflation at an appropriate rate
- Inclusion of a risk register including financial implications for both internal and external risks
- Optimism Bias is considered within all financial models by evaluating financial and service delivery inputs and including contingencies as appropriate, reducing the risk of over-optimistic assumptions locking the Council into undeliverable targets
- All financial models have the same prudent assumption that the residual value of assets at the end of the financial model is £nil, unless a strong case can be made for doing otherwise. The final decision would be made by the Strategic Director of Finance
- A Financial Assessment which will include:
    - Cash flow assessment - identifying any early years deficit and impact on the MTFO
    - Net Present Value (NPV) assessment - the cash flow being discounted using the rates recommended as a base in the Treasury Green Book plus additional percentage points for interest and project risk. The affordability requirement is that the project has to produce a surplus NPV
    - Payback Period - this is the year in which the project forecasts a cumulative surplus position

- Sensitivity Analysis - testing the key assumptions in the model to identify the financial impact if the approved base financial assumptions were not achieved
- Opportunity Cost - if the Council is using non ring-fenced grant / capital receipts or a revenue source of funding there is an opportunity cost to the Council of not being able to use those funds elsewhere.
- Tax Risk / Impact – management of Council's tax risk in accordance with the Council's Tax Strategy.

**Housing Revenue Account (HRA) – Financial Appraisal**

HRA schemes are typically subject to the following affordability criteria and minimum financial parameters required for the scheme to progress to construction contract:

- An overall surplus NPV within the financial models by the year the debt has been fully repaid that has undergone due diligence
- An assessment of the Early Year Deficit's both the schemes individually and across the wider Public Sector Housing Capital Programme, ensuring deficits are affordable and funded
- Model includes full lifecycle costs
- Financial model pays back within 40 years
- Right to Buys are assumed to be used to reduce the in-year Voluntary Revenue Provision (i.e. repayment of debt through revenue)

However, where schemes fall outside of the above criteria they need to be considered in the context of the overall affordability of the HRA, the need to provide additional social housing and the wider BABN programme. The HRA business plan will need to be refreshed following the approval of HRA schemes that have a revenue impact.

## Section Four – Monitoring and Measuring the Performance of the Council's Debt Position and the Capital Programme

### Monitoring and Measuring the Council's Debt Position

The Council will receive reports on its treasury management policies, practices and activities including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its Treasury Management Practices document (TMP).

Within the report, the Council defines its treasury management activities as: "The management of the Council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

Nottingham City Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

The annual Treasury Management Strategy is approved by Full Council. This includes details regarding the Council's operational boundary and Prudential Indicators as prescribed by the CIPFA Treasury Management Code of Practice. These include a projection of external debt and use of internal borrowing to support capital expenditure and the council's overall borrowing requirement, which is known as the Capital Financing Requirement (CFR). The Prudential Indicators include the operational boundary and the authorised limit for external debt which is the statutory limit determined under Section 3(1) of the Local Government Act 2003: "A local authority shall determine and keep under review how much money it can afford to borrow".

An appendix to the Treasury Management Strategy is the Treasury Policy. This policy document sets out the parameters under which the Treasury function operates, including the key delegations. The Treasury Policy also stipulates that the Audit Committee is responsible for the scrutiny of the Treasury Management function.

The annual Treasury Management Strategy includes the policy for the repayment of debt known as Minimum Revenue Provision (MRP). The Council adopts the principle of making revenue provision for the repayment of debt over the life of the underlying debt by making reference to the useful life of the assets being created/purchased that were financed by borrowing.

**Annual Assessment of Non-Financial Investments**

As stipulated in CIPFA's Practitioners' Guide and International Financial Reporting Standards (IFRS), all investments that satisfy the non-financial investment criteria require an annual Fair Value assessment. Where the Fair Value of a non-financial investment is insufficient to provide the required security for the outstanding debt, then as part of the Capital Outturn Report a paper will be presented to Executive Board proposing mitigating actions to protect the capital invested and any revenue consequences.

## Monitoring the Capital Programme

Corporate Leadership Team are provided with a Capital Programme Report on a quarterly basis. This report breaks down the programme into the following areas:

- Approved Schemes (Split between General Fund, Local Transport Plan, Other Transport Schemes and Public Sector Housing)
- Planned Schemes
- Potential Schemes

Each scheme (or group of schemes) are then reported on the following basis:

- Full Project Cost
- Forecast Costs – current financial year plus 4 years
- Uncommitted Expenditure – current financial year plus 4 years
- Funding Breakdown
- Financing Costs
- Opportunity Cost
- Current Year Cash Impact
- MTFO Impact

### Detailed Programme

Project managers must provide an update for every live project detailing the following:

- Forecasting of expenditure (including overspend or slippage)
- Scheme status and whether it has reached completion
- Amount contractually committed

Any variance, change in funding or slippage will be reported to the Executive Board as part of the quarterly monitoring / capital outturn.

It is important to manage significant slippage against the planned Capital Programme as it may be possible to re-prioritise capital funding streams to the advantage of the Council. Advance notice of slippage also assists the Council's Treasury Management function by supporting improved cash flow management and funding decisions.

If an approved Capital Project underspends on its current approval, the funding is released back into the Capital Programme to fund other capital commitments. Should the Project Sponsor of an underspending project wish to change the project via either enhancement or amended specification, further approval is required.

The funding of Capital Projects is monitored to ensure that:

- Grants and contributions are received in a timely manner and any receipt is consistent with the approval
- Capital Receipts are monitored to ensure the Council has enough resources to fund the capital programme
- Revenue Funding / Resources are transferred to either capital reserves or drawn down direct to capital in-year

**Live / Completed Projects**

The actual financial performance of projects is monitored against the original and latest business case and material variance is reported to the CLT.

The Capital Programme is also measured by the Prudential Indicators, which are reported to Council as part of the Treasury Management Strategy, and by the post year-end review.

**Review and Evaluation**

Once a scheme is complete it is necessary to undertake an evaluation to compare the financial outturn against the approved financial appraisal and to assess the outcomes of the scheme against the deliverables in the full business case.

The extent of this evaluation process depends on the size and complexity of the project.

## Knowledge and Skills

The training needs of the Council's Capital and Treasury Management teams are assessed as part of the staff appraisal process. These staff periodically attend training courses, seminars and conferences provided by external advisors and CIPFA. Staff are also encouraged to study appropriate professional qualifications.

The CIPFA Code requires the responsible officer to ensure that councillors with responsibility for treasury management receive adequate training. This especially applies to Councillors responsible for scrutiny. Appropriate training is provided periodically to Councillors and other relevant staff that are charged with governance.

**External advisers**

As detailed within Section Three (Financial Model), external advisors are engaged where appropriate by the Council to support staff regarding the financial assumptions and modelling.

The Council uses Link Asset Services as treasury management advisers and receives specific advice on investment, debt and capital finance issues.

These Capital and Treasury external advisers are engaged so that the Council can access specialist skills and resources whilst the responsibility for every decision remains with the Council at all times, ensuring that undue reliance is not placed upon our external advisers.

**Register of Commercial and Service Investments** **Appendix A**

See exempt appendix A

See exempt appendix A

See exempt appendix A

**Capital Programme – Risk Register (independent of Project Risk Registers and Non Treasury Investments)** **Appendix B**

| Ref | Risk | Detail | Mitigation |
|---|---|---|---|
| **A) Approval & Expenditure** | | | |
| A1 | Expenditure classification | Revenue expenditure is incorrectly allocated to capital | Project managers are instructed to review transactions during the capital monitoring process<br>The Technical Team also periodically review items charged to capital and challenge project managers with transactions that are considered revenue |
| A2 | Project Overspend | Capital project spends more than its approval and there may be no additional funding forthcoming leading to a pressure within Capital resourcing | Project managers receive regular forecast information to enable budget management. Should a scheme overspend and no additional funding is identified, the Technical Team will close the project to mitigate the overspend pending further authorisation |
| **B) Funding** | | | |
| B1 | Proposed grants are not awarded | When capital projects are approved it can include an element of grant that is not yet approved, therefore within that approval there is a risk that the grant is not awarded | Project should not incur costs prior to grants being awarded. The project manager will then be required to amend the scheme accordingly |
| B2 | Awarded grant is less than anticipated | Risk of awarded grant being less than the approval | Where a funding shortfall is identified, the project manager is advised to find alternative funding or reduce the capital project accordingly |
| B3 | Interest Rates increase | A number of capital schemes contain assumptions around interest rates (current year and future years). If the interest rate increases unexpectedly this could affect scheme affordability | The interest rate used within financial models includes a risk element to protect the Council from rate increases<br>External advice is used to forecast potential increases and all projects being planned or |

| | | | |
|---|---|---|---|
| | | | proposed have the interest rate updated as per external advice |
| B4 | Revenue resources shortfall | Due to increasing revenue pressures resources are not available when required to fund the Capital Programme | When new approvals are identified as per section A3, all revenue funds are immediately committed / drawn down to ensure resources are available for the Capital Programme as detailed in the approvals |
| B5 | Capital receipt shortfall | Unsecured capital receipts may be realised at a value less than anticipated, or in year receipts may slip into following financial years, leading to a capital funding shortfall.<br><br>As detailed in Table 5 the Council has committed to applying a significant amount of Capital Receipts **(£70.528m)**. If assets are not realised in line with the Council's requirements this will lead to increased or continuation of revenue pressures. | Unsecured capital receipts are closely monitored by Finance and Property Services and Finance have representation on the Asset Rationalisation project team.<br><br>All forecast receipts are subject to a risk factor which discounts the forecast receipt, this discount is to mitigate against slippage and receipt shortfall.<br><br>If during the monitoring cycle a capital receipt shortfall is anticipated at year end then alternative temporary funding options are considered to enable the programme to be fully funded. |
| **C) Project Specific** | | | |
| C1 | Revenue assumptions not achieved | Capital projects include revenue assumptions for the construction period and as an operational asset. There are financial implications if the revenue assumptions may not be achieved | Financial models include assumptions which are prudent and agreed by Senior Officers. The projects are regularly monitored and if a revenue pressure is generated the Project Sponsor and Budget Manager are required to manage any pressure within the budget process. |
| C2 | Project dependencies do not progress as desired | The Capital Programme consists of a number of projects that have interdependencies, the | Where a specific project has key interdependencies the approval of that project |

| | | | |
|---|---|---|---|
| | | financial implications of the chain breaking require identification | should detail the links and make the approver aware of the financial and non-financial impact should the chain break. This may include an alternative financing option. |
| C3 | Project manager not engaged in Capital monitoring | Project manager does not engage in capital monitoring therefore lack of visibility / project oversight | If a project manager does not respond to consecutive capital monitoring they are contacted by Technical Finance to identify the reason for lack of engagement and if Technical Finance can further support the project manager. |
| C4 | Capital / Final asset valuation not achieved | If assets are realised at a value less than the anticipated value or it takes longer to dispose of the assets then the Council has the following risks:<br>• Negative equity<br>• Pressure generated within the capital programme<br>Holding costs of surplus assets | Business cases need to consider:<br>• That costs incurred by the Council will generate an asset of equivalent or greater value<br>• Models include whole life costing<br>During the disposal process, the asset will be closely monitored to ensure holding costs are kept to a minimum and the asset is disposed in a timely manner. |

# Glossary of Financial Terms

**Appendix C**

**Capital Expenditure**
Expenditure on the acquisition or enhancement of property, plant and equipment that has a long-term value to the Council. This includes grants or advances paid to third parties to assist them in acquiring or enhancing their own property, plant and equipment.

**Capital Receipt**
Money received from the disposal of land and other **assets**, and from the repayment of capital grants and loans made by the Council.

**Corporate Asset Management Plan (CAMP)**
Is a plan that ensures that the land and buildings, or the asset base of the Council is optimally structured.

**Debt Exposure**
The cost of the debt and interest on the project / programme.

**Embedded Leases**
An embedded lease exists if there is an explicit or implicit identified asset within a contract and the recipient obtains control of the assets via the contracted terms.

**Fair Value**
The fair value of an asset is the price at which assets or liabilities could be exchanged between market participants at the measurement date under current market conditions.

**Housing Revenue Account (HRA)**
Sets out the expenditure and income arising from the provision of social housing by the local authority as landlord.

**Medium Term Financial Outlook (MTFO)**
A plan detailing projected expenditure and available resources over a period of more than one year. The Council's MTFO currently covers three years.

**Minimum Revenue Provision (MRP)**
The minimum amount that the Council must charge to the income and expenditure account to provide for the repayment of debt.

**Operational Assets**
Assets held by the Council for the purpose of the direct delivery of services for which the Council has either a statutory or a discretionary responsibility.

**Optimism Bias**
Officers involved in appraising projects have a tendency to be over optimistic. Which may lead to assumptions (both financial and non-financial) proving to be unachievable.

**Private Finance Initiative (PFI)**

A long-term contractual public private partnership under which the private sector takes on the risks associated with the delivery of public services in exchange for payments tied to standards of performance.

**Project Assurance Group (PAG)**
A group of senior officers at the Council (larger projects can include external representatives), who are tasked with reviewing and challenging the project and the decisions made.

**Prudential Code**
The Prudential Code ensures, within a clear framework, that the capital investment plans of the Council are affordable, prudent and sustainable.

**Revenue Expenditure Financed by Capital Under Statute (REFCUS)**
This is expenditure that legislation allows to be funded from capital resources that does not result in an asset to the Council (e.g. Housing improvement grants). This expenditure is written off to the Income and Expenditure Account in the year it is incurred.

**State Aid**
An advantage granted by public authorities through state resources on a selective basis to any organisation that could distort competition and trade.