

ISLE OF ANGLESEY COUNTY COUNCIL

REPORT TO:	EXECUTIVE COMMITTEE
DATE:	30 OCTOBER 2017
SUBJECT:	CAPITAL STRATEGY 2018/19
PORTFOLIO HOLDER(S):	COUNCILLOR JOHN GRIFFITH
HEAD OF SERVICE:	MARC JONES – HEAD OF FUNCTION (RESOURCES)
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LOCAL MEMBERS:	n/a

A - Recommendation/s and reason/s

In order for the Council to determine which projects are included in the 2018/19 capital programme, guidance is sought from the Executive as to the level of funding that will be made available, bearing in mind the impact of the capital programme on the capital financing budget element of the Council's Revenue budget.

The Executive is requested to consider the points raised in the report, following which Officers can begin the work of preparing the 2018/19 capital programme.

B - What other options did you consider and why did you reject them and/or opt for this option?

N/A

C - Why is this decision for the Executive?

Responsibility for determining the Council's budget strategy is delegated to the Executive.

CH - Is this decision consistent with policy approved by the full Council?

Yes

D - Is this decision within the budget approved by the Council?

N/A

DD - Who did you consult?

What did they say?

	Who did you consult?	What did they say?
1	Chief Executive / Strategic Leadership Team (SLT) (mandatory)	
2	Finance / Section 151 (mandatory)	N/A – this is the Section 151 Officer's report
3	Legal / Monitoring Officer (mandatory)	TBC
4	Human Resources (HR)	
5	Property	
6	Information Communication Technology (ICT)	
7	Scrutiny	
8	Local Members	
9	Any external bodies / other/s	

E - Risks and any mitigation (if relevant)		
1	Economic	
2	Anti-poverty	
3	Crime and Disorder	
4	Environmental	
5	Equalities	
6	Outcome Agreements	
7	Other	
F - Appendices:		
Appendix 1 – Capital Strategy 2017/18		
FF - Background papers (please contact the author of the Report for any further information):		

1. INTRODUCTION

- 1.1. Part 1, Section 3 of the Local Government Finance Act 2003 requires that the Authority shall determine and keep under review how much it can afford to borrow. The Act is supported by the Prudential Framework for local authority capital investment and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Code).
- 1.2. The Code does not set out a maximum level of borrowing for an authority, but instead lays down principles for setting a level of affordable borrowing and how those levels must be monitored. The monitoring information (prudential indicators) are set out in the annual Treasury Management Strategy, mid-year review and end of year review which are reported to the Audit Committee, the Executive and the Full Council each year.
- 1.3. The following report identifies the potential future capital expenditure, assesses the impact on the capital financing element of the revenue account and determines the funding available to finance new capital schemes in 2018/19.

2. BACKGROUND INFORMATION

- 2.1. Capital expenditure is expenditure to acquire or create new assets or to maintain existing assets where the life of the asset is greater than one financial year. The assets can be tangible (buildings, vehicles, infrastructure) or intangible (software licences).
- 2.2. The capital programme is funded from the following sources:-
 - **General Capital Grant** – This is a sum of money which is provided by the Welsh Government as part of the annual settlement. The Council is free to use the capital grant on any capital project it wishes.
 - **Supported Borrowing** – The Council will borrow from the Public Works Loans Board (PWLB) to fund the expenditure. The revenue costs arising from the borrowing (Interest Costs and Minimum Revenue Provision) are funded by the Welsh Government through the annual revenue settlement, hence the term “Supported Borrowing”.
 - **Unsupported Borrowing** – Again, the Council borrows the funding from the PWLB but is required to finance the revenue costs from its own resources. Projects funded by means of unsupported borrowing tend to be projects which deliver revenue savings and it is these savings that are used to meet the additional revenue costs arising from the borrowing.
 - **Specific Capital Grants** – The Council will be awarded capital grants which partly or fully fund the cost of a project. Capital grants usually come with restrictions surrounding the expenditure which can be funded and by when the expenditure must be incurred.
 - **Revenue Contribution** – Services can make a contribution from their revenue budgets to fund projects. These contributions tend to be as a match funding to a project which is mainly funded from a specific capital grant.
 - **Capital Receipts** – The funds generated from the sale of assets can be used to contribute to the funding of the capital programme. These are usually generated from the sale of surplus assets (normally land or buildings).
 - **Reserves** – Funding held in reserve, e.g. unapplied capital receipts, can be used to support the capital programme.
- 2.3. The capital programme for 2017/18 was approved by the Full Council at its meeting on 28 February 2017 and is summarised in Table 1 below. A more detailed programme is attached as Appendix 2.

Table 1 2017/18 Capital Programme	
Scheme	2017/18 Annual Budget £'000
Committed Schemes b/f from 2016/17	8,826
Disabled Facilities Grants	750
Investment in Existing Assets	1,551
Invest to Save Projects	186
Highway Maintenance	761
Strategic Infrastructure	7,524
Flood Alleviation	1,600
Social Services Care Schemes	1,250
Gypsy & Traveller Site	1,301
21 st Century Schools	6,865
HRA Schemes	9,889
TOTAL EXPENDITURE	40,503
Funded By:	
General Capital Grant	1,340
Specific Capital Grants	21,258
Capital Receipts	1,522
Supported Borrowing	3,472
Unsupported Borrowing	4,617
Reserves	8,294
TOTAL FUNDING	40,503

2.4. Although the Housing Revenue Account operates separately from the Council Fund, the Council operate a one pool approach in respect of borrowing, i.e. we do not borrow separately for Council Fund and HRA expenditure, all borrowing is combined into one pool and the costs apportioned to the two funds based on the level of expenditure funded from borrowing for the two funds.

3. PRINCIPLES OF THE CAPITAL STRATEGY

3.1. In October 2016, the Executive agreed to the following principles in respect of the capital strategy:-

- That the 21st Century Schools programme is considered separately from the remainder of the general Council capital programme.
- That a sum is allocated in the capital programme each year to fund the major repairs to or the replacement of existing I.T. equipment, vehicles and Council buildings.
- That a sum is allocated in the capital programme to meet the Council's statutory requirement to offer disabled facilities grants.

- Projects which are to be funded from unsupported borrowing will only be undertaken if the reduction in revenue costs or increased income generated is sufficient to meet the additional capital financing costs incurred.
- That a level of road surfacing work is funded from the capital programme each year. The sum allocated will be dependent on the funding required to achieve any minimum contract value guarantees, the level of funding available and an assessment of the state of repair of the Authority's roads.
- Projects that require a level of match funding to enable grant funding to be drawn down are assessed on a case by case basis by the Executive. The decision whether to commit funding will be dependent on the project, how it fits into the Council's corporate priorities and the ratio of Council funding to grant funding.

3.2. Members are requested to consider the above and whether they wish to reaffirm these principles as part of the capital strategy for 2018/19.

4. LIMITATIONS ON NEW FUNDING

4.1. As explained in paragraph 2.2, the capital programme is funded from various sources which impact on the Council's financial position in different ways:-

- Funding that is received in the form of grants (general or specific) does not have any impact on the long term financial position of the Council as any grant received is used to fund the capital expenditure. There may be timing differences which can lead to grants being unapplied and carried from one year to the next via the Council's balance sheet.
- Capital Receipts result in surplus assets being converted into cash which, in turn, results in the creation of a new asset. Again, this type of funding has little long term impact on the Council's financial position but there will come a point where all surplus assets have been disposed of and the level of funding available through capital receipts will fall.
- Use of the Housing Revenue Account uses the surplus on the HRA account (excess of rental income over expenditure) to fund capital expenditure. This is reflected in the HRA business plan and does not impact on the Council Fund.
- The use of revenue funding will reduce the value of funds held in reserves or the sum transferred to the general Council balances at the year end, i.e. it converts surplus cash into a new asset.
- Both supported and unsupported borrowing impacts on the Council's Capital Financing Requirement (CFR) which, in turn, has implications on the Revenue budget in the form of increased Minimum Revenue Provision (MRP) and annual interest payments.

4.2. The CFR measures the Council's underlying requirement to borrow to fund capital expenditure, i.e. the amount of capital spending that has not yet been financed by capital receipts, capital grants or contributions from revenue income. The level of gross external borrowing should not, except in the short term, exceed the capital financing requirement. The CFR is used to calculate the level of MRP charged to the Council's Revenue Account.

- 4.3. The MRP is a minimal amount that must be charged to the revenue account in order to provide for the repayment of loans. The MRP charge does not result in loans actually being repaid at the same time or at the same rate as the MRP. Borrowing is repaid in accordance with the terms of the loan agreement and can be funded from new borrowing or by using surplus cash within the Authority.
- 4.4. The MRP charged to the Council Fund is calculated at 4% of the opening balance of the CFR for all projects apart from those projects funded through unsupported borrowing, where the MRP is based on the useful life of the asset. This policy is currently under review in order to determine whether the MRP charge can be reduced in the short to medium term.
- 4.5. In addition to the MRP, borrowing, whether supported or unsupported, will result in an interest charge which is charged to the Council's revenue account. As borrowing increases, the interest charge must also be funded and this interest charge, along with the MRP, is a restriction on the amount of borrowing which can be undertaken.
- 4.6. Within each settlement, the Welsh Government sets out the capital settlement for all local authorities and this, in turn, is shared out between the 22 local authorities, identifying how much will be funded in the form of the General Capital Grant and how much supported borrowing the Welsh Government will fund, i.e. the revenue settlement includes a sum which will cover the MRP relating to the supported borrowing plus the interest costs.
- 4.7. For 2017/18 and 2018/19, the settlement in respect of capital was as shown in Table 2 below:-

Table 2 Capital Settlement 2017/18 and 2018/19 (Provisional)			
	2017/18 £'m	2018/19 £'m	% Change
All Wales General Capital Funding	142,837	142,837	0%
Settlement Figures for Anglesey			
General Capital Grant (1)	1,340	1,334	-0.4%
Supported Borrowing (2)	2,203	2,192	-0.5%
General Capital Funding (1) + (2)	3,543	3,526	-0.5%
Revenue Settlement (Capital Element)			
Debt Repayment (3)	2,986	2,955	-1.0%
Interest Payments (4)	4,670	4,575	-2.0%
Total Capital Financing (3) + (4)	7,656	7,530	-1.6%

- 4.8. The provisional capital financing budget for 2018/19 is £8.511m, £0.98m higher than the funding allowed for in the settlement and this reflects the additional MRP and interest costs of the unsupported borrowing that has taken place over a number of years.
- 4.9. Therefore, it can be seen that there is scope to fund new projects in 2018/19 through the funding that is received as part of the Welsh Government's financial settlement. Unsupported borrowing is possible but, unless the projects generate revenue savings, then the additional MRP charge and interest costs will increase the revenue budget which must be funded by increased Council Tax or by making revenue savings elsewhere.

5. 21st CENTURY SCHOOLS

- 5.1. Members are aware that the Council has commenced an ambitious programme to modernise schools through the 21st Century schools programme. The programme, if it achieves all its planned objectives, will take over 10 years to complete at a total capital cost of around £120m. Work has already commenced on the programme with the completion of two new schools (Ysgol Cybi and Ysgol Y Llannau) and work commencing on a third new school (Ysgol Santes Dwynwen).
- 5.2. Band A of the 21st Century Schools programme is funded by 50% additional funding from the Welsh Government and 50% via unsupported borrowing. The Welsh Government funding is partly grant funding (67%) and partly supported borrowing (33%). The intervention rate by Welsh Government for band B has yet to be confirmed but it is anticipated to remain at 50% for the traditional funded schemes. Welsh Government have also introduced a mutual investment model for Band B (MIM) where the capital cost of the project is funded by the private sector and the Council then pays a rental fee to the investor for a prescribed period (expected to be 25 years). Welsh Government make a contribution to the rental fee each year (expected to be 70%).
- 5.3. The figures shown in Table 3 below are based on the Council's Strategic Outline Programme which was submitted to Welsh Government in July (approved by the Executive 17 July 2017).
- 5.4. The funding for the programme is summarised in Table 3 below:-

Table 3					
Estimated Funding for Remainder of Band A and Proposed Band B					
Band	Region	Unsupported Borrowing (net of capital receipt) £'m	Supported Borrowing £'m	WG Grant £'m	Total £'m
A	Ysgol Santes Dwynwen	2.18	69	69	3.56
A	Ysgol Bro Llangefni	1.04	1.87	1.86	4.77
	TOTAL BAND A	3.22	2.56	2.55	8.33
B	Ysgol Y Graig and Talwrn	3.71	1.27	2.58	7.56
B	Ysgol Syr Thomas Jones & associated primary schools	6.80	2.39	4.86	14.05
B	Lligwy Primary Schools	1.57	1.12	2.28	4.97
B	Seiriol Primary Schools	2.13	1.17	2.38	5.68
	TOTAL BAND B	14.21	5.95	12.10	32.26

- 5.5. Given the level of borrowing required, it is unlikely that the Council's own cash reserves (internal borrowing) could be used to any great extent. It is, therefore, assumed that all of the unsupported and supported borrowing would be undertaken through new PWLB loans over a length of time which matches the expected life of the asset (50 years).
- 5.6. As explained in paragraph 4.1, additional supported or unsupported borrowing will increase the Council's CFR which, in turn, will increase the annual MRP charge to the revenue account and will result in additional annual interest payments.

- 5.7.** The additional unsupported borrowing for Band B (based on a 50 year repayment period and annual interest at 2.5% would result in additional capital financing charges to the revenue budget of £639k. The Band B submission identifies that the proposed capital works would result in net savings of £272k for the Schools budget. This leaves a net shortfall of £368k per annum which has to be funded by the Council. This is equivalent to approximately an additional 1% in the level of Council Tax.
- 5.8.** It should be noted that the delivery of the Band B projects will eliminate the need to undertake backlog maintenance work at the various schools. For those schools which would close or be adapted under the Band B proposals, the estimated backlog maintenance amounts to approximately £5.5m. Currently the Council has not identified a budget to undertake this work and it would either have to be funded from either the General Capital Grant or Supported Borrowing or from unsupported borrowing. Using the General Capital Grant or Supported Borrowing would not increase the revenue costs but would leave little other funding for other projects and, given that the other commitments (noted in Table 5 below) utilises most of this funding this does not appear to be a viable option.
- 5.9.** It would, therefore be necessary to undertake unsupported borrowing to finance the costs although this would receive no contribution or support from the Welsh Government. The repayment period for any loan would have to be linked to the remaining useful life of the asset and this would be less than the 50 years used for new build. For the purposes of this report, a 30 year payback period is assumed. With an annual interest of 2.5%, the additional capital financing costs would be in the region of £320k per annum.
- 5.10.** Further additional revenue costs would be incurred as Band C and Band CH are delivered.

6. ESTIMATING THE FUNDING AVAILABLE FOR 2018/19

- 6.1.** As one of the main priorities for the Council is to reduce revenue expenditure in order to deliver a balanced budget whilst minimising the reduction in service budgets, it is reasonable for the Council to minimise the increase required to the capital financing budget. It will be necessary to provide additional capital funding but this should be maintained at a level that is funded through the settlement (general capital grant and supported borrowing) so that the increase in the capital financing costs is funded through capital receipts and any specific grants that are available.
- 6.2.** Unsupported borrowing (outside the 21st Century schools programme) should only be considered where the relevant service budget can be reduced by a sum greater than the MRP and interest costs.
- 6.3.** At this stage, the level of supported borrowing and general capital grant is not known but it is anticipated to be in line with the 2017/18 allocation i.e. £1.3m as a general capital grant and £2.2m as supported borrowing.
- 6.4.** In addition to this funding, there would be resources available to fund HRA projects through the Major Repair Allowance (£2.66m) and through any funding made available from the HRA's own reserves.
- 6.5.** Specific grants which have been approved, likely to be approved or that result from successful bids, will also be available to fund capital schemes. In some cases, it may be necessary for the Council to contribute a sum of its own capital funding as match funding to enable the grant funding to be drawn down. The grants which have been currently identified as sources of funding for 2018/19 include:-
- Llangefni Link Road – to enable the scheme to be completed;
 - Safer Route in the Community – 100% grant funding;
 - Beaumaris Flood Alleviation – around 85% funding;
 - Pentraeth Flood Alleviation – around 85% funding;

- Holyhead Market Hall – funding for Phase 2;
- Permanent Gypsy & Traveller Site – application not yet submitted;
- Llangefni Infrastructure – 99% of the funding is from grants;
- Holyhead Infrastructure – discussions are ongoing regarding the level of the Council's contribution.

6.6. The level of capital receipts is dependent on which assets become available to sell. The receipts from the sale of some assets are linked to projects which have already commenced, e.g. sales of former school sites are linked to the 21st Century Schools programme. As a result, not all capital receipts received in 2018/19 can be allocated to fund new capital projects. It is estimated that £500k will be available from capital receipts to fund capital projects.

6.7. As stated previously, any unsupported borrowing must generate additional income / revenue expenditure savings to fund the additional capital financing costs (MRP and interest charges) which will be charged to the revenue account. Any proposed schemes funded by unsupported borrowing will be assessed on a scheme by scheme basis.

6.8. In summary, the funding for new capital projects in 2018/19 should be limited to the level of general capital grant (estimate £1.34m), supported borrowing (estimate £2.2m), and any unallocated capital receipts generated in the year (estimated at £0.5m). This would give a total budget available in the region of £4.04m (final figure is dependent on the Welsh Government settlement) excluding grants, 21st Century Schools funding and HRA funding.

7. POTENTIAL COMMITMENTS FOR 2018/19

7.1. As part of the planning process, future commitments for the following two years are also identified, although there is no guarantee that the funding will actually be released for the specific project. The potential commitments for 2018/19, along with the potential source of funding, is shown in Table 4 below:-

Scheme	2018/19 Cost £'000	Funded By				
		Slippage from 2017/18 £'000	Grants / External Funding £'000	General Capital Grant £'000	Unallocated Capital Receipts £'000	Supported / Unsupported Borrowing £'000
Holy Island Visitor Gateway	353		323		30	
Lôn Newydd Wylfa	12,000		12,000			
Llangefni Link Road	2,975		2,677		298	
Holyhead Strategic Infrastructure	1,370	35	1,335			
Llangefni Strategic Infrastructure	3,357	35	3,322			
Flood Alleviation Schemes	400		340			60
Gypsy and Traveller Sites	1,858	970	450			438
Holyhead Market Hall	1,086		1,086			
TOTAL	23,399	1,040	21,533	0	328	498

7.2. If the principles agreed in 2016/17, which are set out in paragraph 3.1 in respect of existing assets are followed and the level of funding is in line with 2017/18 (after allowing for inflation), the additional commitments for 2018/19 would be as shown in Table 5 below:-

Table 5 Potential Funding to Maintain Existing Assets					
Scheme	Potential Budget Requirement £'000	Funding Source			Total Funding £'000
		General Capital Grant £'000	Supported Borrowing £'000	Unallocated Capital Receipts £'000	
Disabled Facilities Grant	0.750	0.750			0.750
Disabled Access - Education	0.300	0.300			0.300
Vehicles	0.150	0.150			0.150
IT Infrastructure	0.418		0.418		0.418
School Refurbishment	0.500		0.500		0.500
Non School Refurbishment	0.400		0.400		0.400
Highway Resurfacing	0.699	0.140	0.387	0.172	0.699
TOTAL	3.217	1.340	1.705	0.172	3.217

7.3. In addition to the above allocations, there are a number of potential schemes which may also require to be funded. These include:-

- New Gritters – the existing gritters are coming to the end of their useful life and will require replacing. It is estimated that 3 new gritters will be required, each costing between £120k and £150k.
- In the 2017/18 capital budget, a sum of £200k was allocated to smaller Invest to Save projects. These projects do not score well against the larger projects but they are of benefit to the Council because they bring revenue savings e.g. boiler and lighting replacements.
- Improvements and refurbishments to elderly residential homes. £100k was requested last year but the bid was unsuccessful and changes may be required to kitchen storage to enable a potential proposed revenue saving to be achieved.
- The current telephone system is nearing the end of its useful life and may require replacement. Estimated cost £250k.
- Leisure Services submitted two bids last year for a new 3G football pitch in Llangefni and to upgrade the leisure fitness equipment in Holyhead Leisure Centre. Both of these schemes could be funded from unsupported borrowing if the additional revenue income is sufficient to meet the capital financing costs.

7.4. In addition to the sources of funding noted above, the Council holds a capital funding reserve, which was built up from unspent revenue budgets some time ago. The current uncommitted balance stands at £0.5m. This fund is mainly used to fund schemes that arise during the year, not included in the original budget, where a small contribution from the Council allows access to grant funding or where emergency works arise during the year e.g. boiler replacement. Maintaining a balance is necessary and useful but £0.25m could be released in 2018/19 to fund some of the additional pressures detailed in 7.3 above.

8. INITIAL DRAFT CAPITAL PROGRAMME COUNCIL FUND 2018/19

8.1. Based on paragraphs 6 and 7, a draft capital programme for the Council Fund for 2018/19 would be as shown in Table 6 below. The HRA capital programme will be funded from borrowing or from the fund reserves and the schemes which will be included in the capital programme will be initially determined by the Housing Services Board.

Table 6 Outline Capital Programme 2018/19		
2018/19 Outline Capital Programme (excluding 21st Century Schools, HRA and grant funded projects)		
Funding	£'m	Comment
General Capital Grant	1.340	This is the 2017/18 allocation
Supported Borrowing	2.203	This is the 2017/18 allocation
Capital Receipts	0.500	Estimate
TOTAL FUNDING	4.043	
2018/19 Projects to be Funded		
Ongoing Commitments from 2017/18	0.826	Table 4
Maintaining Existing Assets	3.217	Table 5
TOTAL COSTS	4.043	

9. RECOMMENDATIONS

9.1. The Executive is asked to approve the following recommendations as part of the capital strategy:-

1. To reaffirm the capital strategy principles set out in paragraph 3.
2. To consider how to fund the net additional capital financing costs of 21st Century Schools Band B as set out in paragraph 5.
3. To confirm that the 2018/19 capital programme funding will be limited to the total of the general capital grant and supported borrowing (as determined by Welsh Government) and the estimated value of any capital receipts that will be received.
4. That the existing project commitments (Table 5) and the funding for the renewal / upgrade of existing assets for 2018/19 is as set out in Table 6.

**Breakdown of Table 1
2017/18 Capital Programme**

Scheme	2017/18 Annual Budget £'000
CCIS Implementation	65
Compulsory Purchase Order	200
Holy Island Visitor Gateway	1,050
Lôn Wylfa Newydd	4,097
Llangefni Link Road	3,414
Disabled Facilities Grants	750
Education Disabled Access Vehicles	300
	150
ICT Core Infrastructure	150
ICT Desktop Refresh	100
ICT Legacy System Migration	50
ICT MS Licensing	101
Refurbishing Existing Assets - Schools	500
Refurbishing Existing Assets - Non School	200
Invest to Save Traeth Coch	75
Invest to Save Energy Efficiencies Leisure Centres	111
Highway Maintenance	761
Holyhead Strategic Infrastructure	5,001
Llangefni Strategic Infrastructure	2,523
Beaumaris Flood Alleviation	800
Pentraeth Flood Alleviation	800
Social Services Care Schemes - Seiriol	1,000
Social Services Care Schemes - Garreglwyd	250
Gypsy & Traveller Site	1,301
21 st Century Schools – Ysgol Cybi	502
21 st Century Schools – Ysgol Rhyd y Llan	1,545
21 st Century Schools – Ysgol Brynsiencyn	217
21 st Century Schools – Ysgol Parc y Bont	169
21 st Century Schools – Ysgol Santes Dwynwen	3,591
21 st Century Schools – Llangefni	675
21 st Century Schools – Seiriol	166
HRA – Development of Additional Council Dwellings	2,800
HRA – Planned Refurbishment	6,585
HRA – HMU Vehicles	144
HRA – Premises	110
HRA – Remodelling Llawr y Dref	250
TOTAL EXPENDITURE	40,503
Funded By:-	
General Capital Grant	1,340
Specific Capital Grants	21,258
Capital Receipts	1,522
Supported Borrowing	3,472
Unsupported Borrowing	4,617
Reserves	8,294
TOTAL FUNDING	40,503