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Date: 26 January 2021

Notice of Extraordinary meeting

Overview and Scrutiny Committee

Date: Tuesday, 9 February 2021

Time: 6.00 pm

Place: Video conference call

To the members of the Overview and Scrutiny Committee

Councillors:

V.J. Leighton (Chairman)
O. Rybinski (Vice-Chairman)
C.L. Barratt
J.H.J. Doerfel
J.T.F. Doran
R.D. Dunn
T. Fidler
M. Gibson
A.C. Harman
I.T.E. Harvey
N. Islam
T. Lagden
D. Saliagopoulos
K.M. Grant

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AGENDA

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1. Apologies

To receive any apologies for non-attendance.

2. Disclosures of Interest

To receive any disclosures of interest from councillors in accordance with the Council's Code of Conduct for members.

3. Draft Capital Strategy **3 - 62**

The Overview and Scrutiny Committee is asked to:

1. Note the working draft of the Capital Strategy 2021.
2. Provide recommendations on how the Strategy could be improved and amended to Cabinet for them to consider prior to the report going to Cabinet on 24 February and Council on 25 February 2021.

4. Detailed Revenue Budget **To Follow**

To scrutinise the Detailed Revenue Budget for 2021/22 prior to it being considered by Cabinet on 24 February 2021.

Extraordinary Overview and Scrutiny

9 February 2021

	Draft Capital Strategy 2021
Purpose of the report	To make a recommendation to Cabinet
Report Author	Terry Collier, Deputy Chief Executive Heather Morgan, Group Head Regeneration and Growth
Cabinet Member	Cllr Boughtflower, Leader
Confidential	No
Corporate Priority	Housing Financial Sustainability
Recommendations	**Overview and Scrutiny is asked to:** • **Note the working draft of the Capital Strategy 2021** • **Provide recommendations on how the strategy could be improved and amended to Cabinet for them to consider prior to the report going to Cabinet on 24 February and Council on 25 February 2021**
Reason for Recommendation	**The Capital Strategy has to be produced on an annual basis** **It sets out in plain English the why, what, where, when and how of our capital investment decisions and how these dovetail into the Council's wider strategic aims – housing (with a focus on affordable), regeneration and green initiatives and climate change.** **Overview and Scrutiny are being asked to undertake pre-decision scrutiny of this key document to ensure it is robust and fit for purpose**

1. Key issues

1.1 Since April 2018 there has been a statutory requirement for every authority to have a Capital Strategy in place and it has to be formally adopted by Council.

All authorities are required to set out what need the Council has for capital financing, why it has this need and what the money will be spent on. In addition to that, there are more technical aspects which have to be included and the document should also outline our approach to risk management and how we are resourcing this side of our business.

1.2 The Council underwent a virtual financial Peer Review in November 2020. In its response the Peer Review team recognised that the ‘leadership team has ambitions to widen the current housing schemes and in delivering affordable housing for its residents’ and that ‘progress is already underway with a new corporate plan in development stages with a focus on 'Recovery (including Community Support), Affordable Housing and Climate Change'. This new focus has been reflected in the new Capital Strategy.

1.3 The 2021 Strategy is a very different document from those that have preceded it. There is a clear break from the past, and it puts ‘front and centre’ how the Council’s new priorities of:

- delivering affordable housing
- achieving the regeneration of our town centres
- ensuring a sustainable future in recognition of declaring a climate change emergency

are to be delivered through this Capital Strategy.

<u>Affordable housing (section 5)</u>

1.4 Over the past few years private housebuilders have failed to provide sufficient affordable housing to meet the growing needs of our residents. Over the past five years only 147 new build affordable rented units have been delivered (an average of 29 per year). This needs to be seen in the context of a widening gap between people’s income and the cost of housing (called affordability), the high use of emergency accommodation (we have 110 homeless households and the net cost of accommodating them is approximately £6,740 per household per annum), a year-on-year reduction in properties available for re-letting by 21% and an increase in the numbers of the housing register and in need (now in excess of 2,600)

1.5 The Capital Strategy sets out how the Council will actively reverse this trend by directly intervening in the direct delivery of additional housing, and in particular affordable homes (set at 80% of the full market rents). There is a commitment that Council developments will deliver at least 50% affordable provision on its schemes.

<u>Regeneration (section 6)</u>

1.6 Economic development and recovery from the economic impacts of the COVID-19 Pandemic is key and reflects the importance that the Council places on ensuring the overall prosperity of the Borough and its residents. The Council has significant landholdings in Staines-upon-Thames and has a pivotal role in using those assets to ensure a vibrant and sustainable town centre for this and future generations of residents.

1.7 The Council’s landholdings within the town centre (including our strategic acquisitions) provide a clear opportunity to bring forward at least 1,420 units in the next 10 years. As a result, we are in a position to ensure the delivery of

22% of the Borough's assessed 5-year land supply requirement in the Local Plan (738 units to be delivered by the Council out of a required 3,343. This is key plank in protecting our green belt from being put at risk through the submission of unacceptable applications on the premise that we as a Council cannot deliver our housing need numbers.

Climate change and green initiatives

1.8 The Council has joined a growing number of domestic and international authorities in declaring a climate emergency and adopting a carbon-neutral target. A Climate Change Task Group has been set up and the Council is at an early stage of fully assessing and identifying our own carbon footprint along with developing a carbon trajectory to reach carbon neutrality. This work will help to inform where investment will be required to meet our targets.

1.9 Focus areas for capital investment in green measures will include the transition of our fleet of vehicles to low carbon alternatives and the decarbonisation of Council owned buildings. Best practice environmental design will be built into our developments. An example of this are the plans are underway to redevelop Spelthorne Leisure Centre to be the first fully compliant Passivhaus Leisure Centre in the Country demonstrating the Council's commitment to tackling climate change.

1.10 There is also a capital sum for the Lower River Thames scheme. This will reduce flood risk to people living and working near the Thames, contribute to a vibrant local economy and maximise the social and environmental value of the river. The Scheme is expected to cost (including contingencies) £640m. To date Spelthorne has committed £49k per year in revenue costs. In early discussions partners agreed a contribution to the capital costs and this was identified as £1.3m for Spelthorne. With the scheme progressing it is expected this spend would take place between 2023 and 2025.

2. Options analysis and proposal

2.1 There is a statutory requirement for a Council to have a Capital Strategy and for this to be adopted on an annual basis before the end of the financial year (in much the same way as we are required to do with our Treasury Management Strategy). This Strategy needs to be formally agreed by Council and needs to be agreed by Cabinet before that can take place. Overview and Scrutiny are being asked to feed into this decision making process with their views and recommendations.

3. Financial implications

3.1 The Capital Strategy sets out a number of financial matters around sources of funding, what we spend annually on services, the range of options available to us for borrowing, and how we undertake effective treasury management of our funds. It also sets out the Councils proposed development programme for future years (which is focused on delivering affordable housing and regeneration activity).

3.2 One particularly important matter is the capital requirement to deliver the proposed housing activity (with its significant focus on affordable housing). The funding for the developments identified in the Capital Strategy were considered at the Extraordinary Council Meeting on 21 January 2021. That meeting agreed that budgetary provision should be made. These budget estimates/costs will be reflected in the Capital Programme which is going to Council on 25 February 2021 as part of the budget setting process

3.3 It should be noted that the Council has already set (as required by the Prudential Code), borrowing limits for its total capital expenditure (Operational Boundary and Authorised Limit). These limits have been agreed for the current financial year and the following three financial years to fund all the schemes in the current Capital Programme.

3.4 The Council at its February 2021 meeting will be refreshing the Capital Programme (alongside the Capital Strategy) by rolling forward the period covered by the Programme by one year to cover the period of 2021-22 to 2024-25 and will be updating its Borrowing Limits for that period. Currently the Operational Boundary borrowing limit is as follows:

2020-21 £1,250m

2021-22 £1,250m

2022-22 £1,300m

2023-241,350m

and the Authorised Limit (which is a worst-case limit and allows for unforeseen cashflow events) is as follows:

2020-21 £1,350m

2021-22 £1,350m

2022-23 £1,400m

2023-24 £1,450m

3.5 These limits include borrowing already undertaken by the Council. As a result of the initial work by officers on the draft Capital Programme for 2021-22 to 2024-25 (with some general contingency provisions being removed), it is anticipated that the total Capital Spend over the next four years will reduce. Initial modelling suggests a reduction from £326m for the current 4-year period to approximately £250m for the new 4 year period (a reduction of £76m). Current borrowing limits are likely to be more than sufficient for the next four years and indeed may be reduced slightly. Council are therefore not required to extend the borrowing limit.

3.6 The strategy needs to be read alongside and in conjunction with the annual Treasury Management Strategy and the budget for 2021/22.

4. Other considerations

4.1 Risk management, skills, and performance management are all covered in the Capital Strategy itself and do not require repeating here.

4.2 An Executive Summary will be provided to give the headline information in an easily digestible format. A series of appendices provide the supporting and technical detail. As a whole the strategy has again been kept short, informative and readable. There are no specific equality and diversity matters to be taken into account when developing the Capital Strategy.

4.3 One of the challenges that the Peer Review identified that needs to be addressed is the need to ‘ensure that effective programme and project management is further developed and embedded across the organisation for both capital and revenue spend reflecting internal controls and proportionate risk management'. Appendix 4 in covers risk but also governance and reflects the potential move to a committee system from May 2021 (if it is approved at an Extraordinary Council meeting in late March). This includes specific reference to the setting up of a sub-committee of the policy and resources committees to review and monitor all the Councils development projects (as agreed at the Extraordinary Council meeting on 21 January 2021. The detailed operation of the sub-committee will be developed by the Committees Task Group.

5. Sustainability/Climate Change Implications

5.1 Sustainability and climate change are one of the three core elements of the Capital Strategy. The document sets out at a high level what the Council is aiming to achieve and identifies a number of key areas of activity that the Council will be looking at (e.g. green fleet). This core element will be developed considerably over the coming months by the Climate Change Task Group and it is envisaged that any actions and recommendations relating to capital which that Task Group put to Cabinet (before May) or to a Committee (after May) for approval will feature in future versions of this Capital Strategy.

6. Timetable for implementation

6.1 Recommendations from Overview and Scrutiny on this draft Capital Strategy will be taken to Cabinet on 24 February, where they will formally consider those recommendations and make a decision on whether or not to accept some or all of them. In addition, recommendations form O&S will be fed back to Cabinet immediately after this meeting so that they are aware of them. Cabinet will then advise officers what changes are required so that these can be fed into a final document.

6.2 The final version of the Capital Strategy will be considered by Cabinet on 24 February, which will make a recommendation to Council on the matter. Council will make the final decision on whether or not to adopt the Capital Strategy 2021 on 25 February at the annual budget Council meeting.

Background papers:

None

Appendices:

1 Draft Capital Strategy 2021 (This gives residents, councillors and other stakeholders an overview of why, where and how we intend to spend capital to provide services and meet some of the Council's wider strategic aims)
2 Appendix 1 of draft Capital Strategy (Historical Background)
3 Appendix 2 of draft Capital Strategy (Investment Parameters)
4 Appendix 3 of draft Capital Strategy (Housing information)
5 Appendix 4 of draft Capital Strategy (Risk and decision making)
6 Appendix 5 of draft Capital Strategy (Treasury Management)
7 Appendix 6 of draft Capital Strategy (Our commercial activity)
8 Appendix 7 of draft Capital Strategy (Key performance indicators)

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The Capital Strategy of Spelthorne Borough Council

Will have new logo

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1. Introduction

This document sets out Spelthorne Borough Council's Capital Strategy. It gives residents, councillors and other stakeholders an overview of why, where and how we intend to spend capital to provide services and meet some of the Council's wider strategic aims. Supported by other documents including Asset Management Plans and Treasury Management Strategies, it spells out our priorities in the short-, medium- and long-term.

In particular, this document demonstrates how our Capital Strategy will help to deliver two key goals contained in our Corporate Plan:

- **To deliver much-needed housing** in order to help reduce homelessness locally, increase affordable provision and help meet the overall need for additional homes- the Council is seeking to ensure that on all its developments at least 50% of the units are affordable or keyworker rental units
- **To regenerate our town centres** and ensure that all development is high quality and well -designed, and contributes positively to the development of truly sustainable communities, in economic, social and environmental terms.

Capital Strategies help ensure that Councils take a long term planned approach to how they identify their need to incur capital expenditure and how they will manage and finance that expenditure.

How capital expenditure is defined

Capital expenditure is money used by the Council to acquire, upgrade, and maintain physical assets such as property, operational buildings and equipment which will provide benefits to the Council and its residents over more than one year. Capital expenditure can include everything from installing new windows with enhanced glazing or purchasing a piece of equipment or vehicle through to constructing a brand new building. Capital expenditure is different to revenue expenditure, which is the money used by the Council for the day-to-day delivery of services, staffing and supplies.

2. What is our Capital Strategy?

2.1 Put simply, the key element of our Capital Strategy is to deliver affordable homes as part of our regeneration strategy

- We are **delivering** the affordable homes for our residents which the market fails to provide and we are prioritising people who are on our Housing Register
- We are aiming at **regeneration** of key sites which will produce more affordable and sustainable homes alongside mixed use development to ensure the development of sustainable communities within the borough and Staines-upon-Thames in particular.
- We are looking to deliver on our pledge of taking positive actions on both **green initiatives and the climate change** agenda as a result of this Council declaring a Climate Emergency in October 2020.
- Historically we have invested in commercial property which, delivers an ongoing sustainable income stream to support these activities and maintain existing services.

2.2 Given the economic impact of COVID-19 regeneration projects will become even more important. Beyond housing, regeneration and green initiatives, our Capital Strategy will also help us meet our need to upgrade and maintain:

- Operational buildings, to include sustainable measures in upgrades
- Infrastructure in the borough, including green network initiatives
- Our vehicle fleet – as we move to greener options over the next 3 years
- Our ICT infrastructure – to ensure supports office and remote working.

Our duty to look after public money

2.3 As a Council, we have a duty to look after the public purse, and residents and businesses expect us to do so in a sensible and rational way. This Capital Strategy will demonstrate how we:

- **Finance our spending** largely through prudent borrowing, specific grants , revenue contributions to capital or use of reserves (called capital financing) within the borrowing within the approved Prudential Debt parameters sets out in accordance with the Prudential Code (Operational Boundary and Authorised Borrowing Limit)
- **Spend wisely and safely**, especially in relation to the investment portfolio that we hold (called commercial activity) and planned development and regeneration activates in the borough

- **Manage risk and make decisions**, ensuring we have the appropriate skills and expertise, and taking a measured approach to investment, development and regeneration and risks associated with climate change.
- **Ensure we have enough money** immediately to hand to keep services running on a day-to-day basis and to maintain the assets on an ongoing basis
- **Maximise our returns** on monetary investments (called treasury management)

2.4 Underpinning the whole Capital Strategy is the need to ensure that the Council is financially sustainable in the future (this is another Corporate Plan priority), something that is especially challenging in the current financial landscape (due to the impacts of COVID-19 and the road to recovery, plus exiting the EU with no deal).

2.5 The Council acknowledges the need to positively address climate change and will look to actively embed sustainability in all its Capital investment, development and spending decisions moving forwards.

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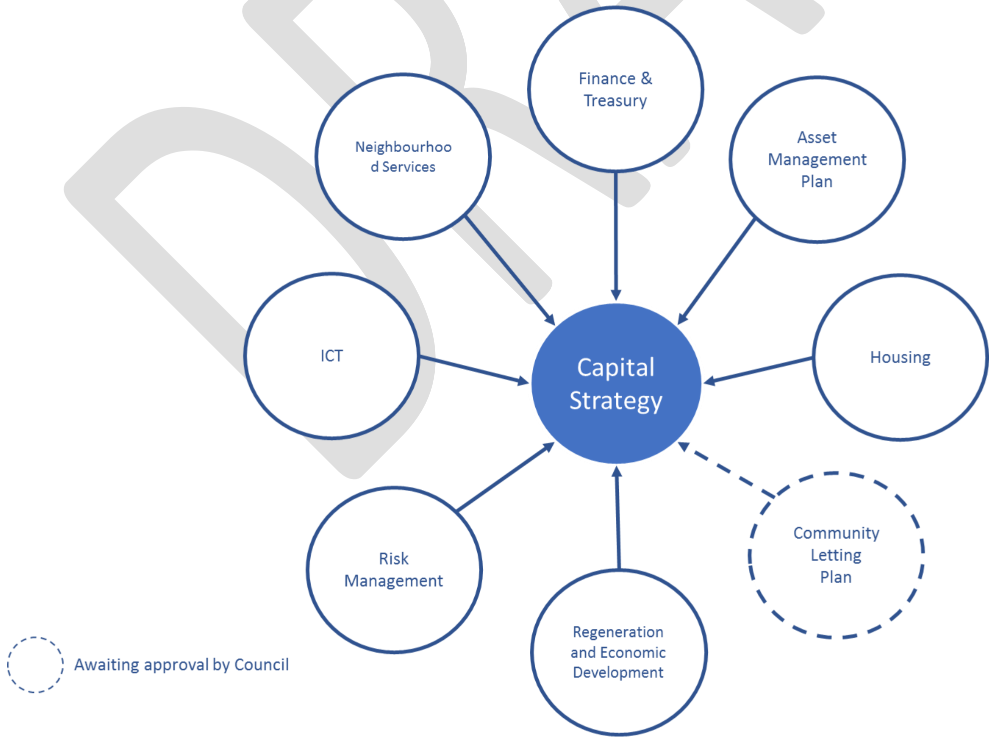
3. How do existing plans feed into the Capital Strategy?



3.1 The Council already has several strategies in place which cover various aspects of spending. We appreciate that it can be difficult to understand how all of these elements mesh together to form a 'whole', which is where the Capital Strategy comes in. By bringing everything together in one document, we can show how the need to invest in assets – such as building a new waste depot, for example – has a range of implications.

An overview of our individual strategies

3.2 The various strategies that we currently have in place are set out below, although some are being updated to reflect the intentions set out in this document. Please follow the links if you would like to read them in full.

3.3 **Medium Term Financial Strategy** (also known as the Council's Outline Budget) – how the Council sees our need for revenue funding in the next five years, and its strategy for ensuring the financial sustainability of the Council

3.4 **Treasury Management Strategy** and Investment Strategy– how the Council properly manages the money we have at hand (cash flow) to make sure money is always available to run the Council and deliver services and to fund future developments and capital expenditure

3.5 **Asset Management Plan** – how the Council's assets support our corporate objectives and the services we provide. It sets out principles, priorities and action to ensure our assets are used and managed as efficiently and effectively as possible.

3.6 **Housing and Homelessness Strategy** – detailing the Council's strategic approach to ensure that there is a choice of housing options available to people living in Spelthorne, including supporting those who are homeless or at risk of homelessness, and preventing people from becoming homeless.

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4 Where does the Council get its money from and what does it spend it on?

Our sources of income

4.1 The Council gets its money from a variety of sources – for 2021/22, our revenue funding is coming from: The 2021/22 figures are yet to be updated and are subject to Council approval in February 2021

Funding	£	%
Interest earned	1,340,000	6
General grants from government	551,100	2
Our share of Council Tax	8,282,500	35
Our share of Business Rates	3,800,000	16
Income from our investment properties	9,924,800	41
TOTAL	**23,898,400**	**100**

Table 1: Sources of income

What we fund

4.2 Our income is used to fund the range of services we provide – for 2021/22, this covers:

The 2021/22 figures are yet to be updated and are subject to Council approval in February 2021

FUNDING	NET COST AFTER CHARGES GRANTS ETC £	%
Electoral Registration & Elections	262,700	1
Democratic and Corporate Services	2,979,000	13
Grants to community organisations	209,600	1
Housing benefits	384,200	2
Housing and Homelessness	1,948,000	8
Planned maintenance	1,284,100	5
Planning and Economic Development	1,140,600	5
Asset management	799,300	3
Environmental Services & compliance	1,740,900	7
Refuse collection	1,426,700	6
Street cleaning	925,900	4
Grounds maintenance	1,689,200	7
Community wellbeing	822,600	3
Support services and central overheads	6,127,300	26
Project Delivery Fund	1,408,300	6
Revenue contribution to capital	750,000	3

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TOTAL	**23,898,400**	**100**

Table 2: Funding of services

Our capital expenditure plans

4.3 In 2021/22, the Council is planning capital expenditure of £65.6m as summarised below:

The 2021/22 figures are yet to be updated and are subject to Council approval in February 2021

	2018/19 ACTUAL £m	2019/20 FORECAST £m	2020/21 BUDGET £m	20/21/22 BUDGET £m	2022/23 BUDGET £m	2023/24 BUDGET £m	2024/25 BUDGET £m
Other Services Programme	376.9	42.9	31.1	56.5	23.7		
Housing Investment Programme	3.7	24.1	34.1	46.1	33.9		
ICT	0.3	0.2	0.2	0.1	0.6		
Environmental	0.2	0.5	0.2	0.1	0.1		1.3
TOTAL	**275.3**	**67.7**	**65.6**	**102.8**	**58.3**		

Table 3: Prudential indicator: estimates of capital expenditure in £ millions

4.4 Our capital projects include:

- Property development projects for operational purposes eg for supporting housing service needs (expenditure: £58.271m 2020/21, £39.952m 2021/22, £25.523m 2022/23)
- New Leisure centre development (original budget estimate for build costs and fees: £40m)
- Various corporate projects including facilities improvements and IT (including wireless infrastructure, cabling, network kit, document management system, property management system, telephony hardware and software)
- Waste, parks and parking includes new waste vehicles, reducing carbon footprint, improving management of parks and open spaces and enhancing CCTV.

4.5 The Council also plans to incur £65.6m of capital expenditure on housing and regeneration within the Borough (as per the table above). For full details of the Council's Capital Programme, including the project appraisals undertaken, view the Capital Programme.

4.6 All capital expenditure must be financed from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing and leasing). The Council intends to ensure its Capital Strategy and Capital Programme is consistent with the requirements of the new terms of the Public Works Loan Board. The planned financing of the above expenditure is as follows:

Where our borrowing comes from

Will need updating to reflect draft 2021-22 Capital Programme

	2020/21 AS AT END OF Nov 20 £'000	2020/21 REMAINDER OF YEAR £'000	2020/21 FORECAST £'000	2021/22 BUDGET £'000	2022/23 BUDGET £'000	2020-22 TOTAL £'000
Public Works Loan Board	0	77,678	77,678	67,000	29,000	173,678
Of which to be used for refinancing existing debt	0	0	0	0	0	0
Other sources	49,890	8,385	58,275	35,480	25,290	119,045
Of which to be used for refinancing existing debt	0	0	0	0	0	0
Total PWLB and other sources	49,890	86,063	135,953	102,480	54,290	292,723
Of which to be used for refinancing existing debt	0	0	0	0	0	0
Of which to be used funding new long term borrowing	**49,890**	**86,063**	**135,953**	**102,480**	**54,290**	**292,723**

Table 4. Source of borrowing

Historical Background

4.7 Excluding the emergency COVID-19 funding provided in 2020, since 2013 the Council has seen a year-on-year reduction in the funding we receive from central government. In response in 2014 the Council put in place a transformation programme called “Towards A Sustainable Future” which included growing long term sustainable income streams to make up for the loss of grant. The Council had to take a view on how to offset the loss of general Revenue Support Grant, with these the only viable options:

(1) Grow income

(2) Reconfigure, reduce or deliver services in a different way

(3) A combination of both the above

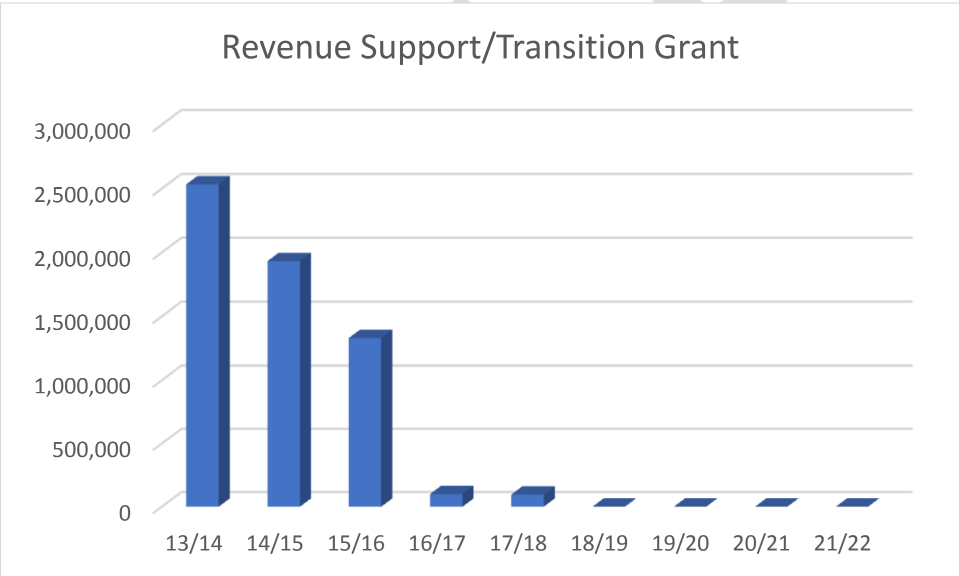

Illustration 1: Reduced Government funding

Our investment so far

4.9 Although this Capital Strategy looks forward, it is worth noting the significant level of investment activity that the Council has already undertaken. *Appendix 1* sets out the historical background to our acquisitions up to 2018, including our first major acquisition - the BP international campus in Sunbury. Information is included to explain why we set out on this journey, our previous ‘Towards a Sustainable Future’ programme, and our activity up to 2018. Since 2018 the Council has ceased purchasing investment properties and its focus is on delivery housing and regeneration within the Borough and delivering schemes such as the new Leisure Centre.

4.9 Total commercial investments are currently valued at £959m, providing a net income yield of 5.20%. The Council has chosen, after taking account of interest and repayment of debt, to accept a net surplus contribution of 1% and to set aside a significant contribution into sinking funds to ensure we have funds available in future to cover voids and refurbishments. This is a comparable net return to that being achieved by pension funds on commercial assets.

Assets	Town	Sector	Purchase Price £m	Purchase Date	2020 Valuation £m
BP Campus, Sunbury Business Park	Sunbury	Offices	385	Sept 2016	391.73
12 Hammersmith Grove	London	Offices	170	Jan 2018	165.90
Charter Building	Uxbridge	Offices	136	Aug 2018	131.20
Thames Tower	Reading	Offices	119	Aug 2018	126.80
The Porter Building	Slough	Offices	66	Aug 2018	69.90
World Business Centre 4	Heathrow	Offices	47	Sept 2017	45.80
3 Roundwood Avenue	Heathrow	Offices	21	July 2017	20.10
Elmbrook House	Sunbury	Offices	7	Dec 2016	7.24
Station Road	Sunbury	Offices	0.4	Mar 2018	0.36
Total			951.4		959

Table 5: The Council's commercial assets portfolio

Regeneration portfolio

The Council now has an ambitious housing and regeneration programme underway

Assets	*Town*	*Sector*	*£m*	*Purchase Date*	*2020 Valuation £m*
Communications House	*Staines*	*Offices*	*11*	*July 2018*	*14.5*
Summit Centre	*Sunbury*	*Offices*	*14*	*Sept 2019*	*13.5*
Elmsleigh Centre	*Staines*	*Retail*	*39.33*	*Feb 2020*	*39.33*
Total			*64.33*		*67.33*

Table 6: *The Council's Regeneration portfolio*

4.10 On our commercial asset acquisitions, the overall initial net yield is 5.20%. As there are upwards only reviews to either market rent or indexation of the rental every five years on most of the assets, the yield is likely to rise over time. After taking account of paying off loan instalments each year, interest, supervision costs and setting aside sinking funds to cover future potential costs (such as refurbishments of assets on lease expiry and rent-free periods), the net surplus contribution to the Council's Revenue Budget in 2021/22 will be £9.4m per annum. *Appendix 2* set out the Council’s Strategic Property Investment Parameters

5 The focus on housing and homelessness

5.1 Historically the Council was concerned with generating sufficient revenue to safeguard its basic services. The focus now is on providing affordable housing. Housing is one of the Council’s four strategic priorities in the **Corporate Plan,** reflecting the significant pressures the Borough is facing, with relatively high numbers of families in temporary accommodation, insufficient affordable housing provided by Registered Providers of social housing and a severe shortage of affordable private rental housing supply.

5.2 Going back to the 1990s, the Council used to provide traditional council housing. In the 1990s, it was decided to transfer the council housing stock to what was then Spelthorne Housing Association and is now part of A2Dominion. The main reason for the transfer of properties at the time was the need to bring the properties up to an acceptable state of repair, which the Council could not afford at the time. Since then, the Council has not had a direct role in developing new homes; this has been carried out by A2Dominion and other Registered Providers, as well as private developers. Fluctuation in the delivery of new housing has been dictated by the economy and the availability of grant funding to subsidise affordable housing.

5.3 The Council’s Housing Strategy 2020 – 2025 contains three strategic priorities which will contribute to achieving the overall vision of ‘ensuring best quality homes in a thriving and sustainable community’. Additionally, the Council is required to have a Homelessness Strategy, which outlines the Council’s approach to preventing homelessness.

5.4 In common with many other local authorities in the South East, Spelthorne has a growing demand for genuinely affordable housing and is facing a number of key challenges:

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- **Increasing numbers on the Housing Register and a lack of availability of existing affordable housing**: Over the past five years, the number of available social housing vacancies offered to the Council for re-letting has reduced by 21% See *Appendix 3* Table H2, with the numbers on the Council’s Housing Register now almost one third higher than five years ago See *Appendix 3* Table H1, The growing numbers on the Council’s housing register, and the lack of new supply affordable housing highlights the increasing challenges of meeting the needs of the most vulnerable in our community. The Covid-19 pandemic continues to have a significant effect on local residents, particularly those employed at Heathrow Airport.
- **High rates of statutory homelessness**: almost two thirds of households include children, and almost a quarter have some form of physical or mental ill health. See *Appendix 3* Table H3. The Council is accepting a homeless duty to an increased number of households since the Homelessness Reduction Act 2018 came into force.
- **High use of emergency and temporary housing for homeless households**: The average occupancy of temporary accommodation at the end of each quarter in the five years to 2019/20 was 110 households. See *Appendix* 3 Table H4. For example, the average cost to the Council to accommodate one homeless household in emergency housing is approximately £6,750 per annum.
- **Worsening affordability issues**: whilst the ratio of the median house price to the median wage improved nationally and regionally, it worsened at borough level in 2019/20. Median wages have been affected in a similar way – improving nationally and regionally in 2019/20, but falling at a borough level. Spelthorne is still less affordable for local people compared to other areas in the South East and England overall~~.~~ See *Appendix 3* Table H5
- **Lack of new-build affordable housing**: The net increase of provisions over the past five years has been just 185 units (with none on 2019/20) an average of 37 per year *See Appendix 3 Table H6*. The greatest need is for two bedroom four person homes, with waits for affordable housing for this type running into years.

The effect of our proximity to London

5.5 As well as the evident demand for affordable housing from local residents, there is also considerable pressure from London. The cost of housing in London is even higher than in Spelthorne, and London boroughs are actively placing homeless households from their boroughs into Spelthorne, as well as ‘block booking’ emergency accommodation facilities within Spelthorne for their homeless people, placing further demand on the already strained private sector.

Heathrow

5.6 Expansion plans are currently paused, pending the outcome of a judicial review of the Government's Airports National Policy Statement, which underpins the need for a third runway. The COVID -19 pandemic has also had a catastrophic impact on the aviation industry, which is likely to be felt for several years after the initial effects of the pandemic have eased. Heathrow Airport Limited (HAL) has not formally withdrawn its expansion plans but if the outcome of the judicial review means they can proceed to submit the Development Consent Order there is uncertainty as to if or when this would take place. HAL's current work has focused on recovery.

5.7 Some joint work has already been undertaken across several Councils to understand the potential impact of any future expansion of Heathrow on the need for additional housing. Early indications are that it will not have a significant impact on the need for additional permanent housing in the short, medium or longer term. Any emerging data will be fed into the strategy as required. However, there will be shorter term impacts from construction workers who require accommodation for the term of the expansion (up to 2050) which may affect the ability of the Council to access the private sector market as readily

Key worker accommodation

5.8 The Covid-19 pandemic has once again highlighted the need to deliver appropriate housing and services to key workers in our community. Whilst housing affordability is a significant issue in general, it acutely affects key workers, who help to run the essential local services such as schools, hospitals, doctors' surgeries and fire stations. According to Government statistics released in 2019, the latest records available, the median income for employed households within Spelthorne is £33,597, although the same for essential local workers is much less at £27,159. Whilst the median income at borough level is higher than regional and national median incomes, when compared to local house prices, it highlights the significant affordability issues that local residents face. We know anecdotally that key worker staff are moving further and further away from Spelthorne into Hampshire and Berkshire and commuting to work. This means that when they look for their next promotion they are more likely to look in those areas; this is another factor leading to loss of workforce. Whilst some key workers are being recruited from London, one of the main factors which will keep them in Spelthorne is availability of affordable housing.

5.9 In 2020, the Council commissioned an independent study of the housing needs of local key workers, in order to inform the basis of a key worker housing scheme to be delivered by the Council through our housing company Knowle Green Estates Ltd. The study used a local agreed definition of key workers:

- **Health and social care:** Doctors, nurses, midwives, paramedics, social workers, care workers, other frontline health & social care staff.

- **Education and childcare:** Childcare, support and teaching staff, specialist education professionals [including FE teachers and Early Years/nursery teachers; Local authority Therapists, including Occupational Therapists and Speech and Language Therapists; and Local authority Educational Psychologists].

- **Public safety and national security:** Police and support staff; Armed forces personnel[1]; Fire and rescue service employees; Prison and probation staff.

The study concluded that:

- An estimated 24% of employed Spelthorne residents aged between 16 and 64, totally around 12,000, are key workers
- The majority of these key workers are in education and health, followed by social care and lastly public order
- Just under half have at least one child
- Approximately 12% of key workers in Spelthorne are in need of affordable accommodation, around half of which are in education

Strategic objectives

5.10 In 2018, Government and CIPFA guidance to local authorities changed with regards to borrowing to invest in commercial properties. The Council has carefully considered this guidance and this Capital Strategy reflects both that guidance and our strategic objectives of borrowing to support housing investment.

Subsidies are key

5.11 As affordable housing is provided at up to 80% of the market rate, subsidies are essential to make it viable. A private developer who pays market rate for land, finance, supplies and labour has to sell their properties at market rate to make a profit. When Spelthorne Council is acting as the developer, even if we forgo the profit element, it is still difficult to deliver truly affordable housing.

5.12 Housing for rent can pay for itself over a period of time because of the rental income which it generates. However, the Council needs to be in a position to forward fund such developments and the cost of finance for the acquisition, development and construction

[1] Retaining this status "for a period after discharge" according to the Armed Forces Covenant.

stages is prohibitive for councils unless they receive Government subsidy. This is similar to the way Housing Associations operate – having a market rate product to sell and rent, the surplus of which subsidises the affordable elements of their business.

5.13 The bottom line is that, even with the Government grant funding available through Homes England, affordable housing developments need significant capital investment and cash flow to deliver.

Spelthorne's Housing Development Programme

5.14 Spelthorne has a pipeline of properties for residential development with the aim of delivering 50% affordable housing across the portfolio, with an emphasis on maximising the delivery of two-bedroom four person units. Wherever possible, rents will be capped at the relevant Local Housing Allowance.

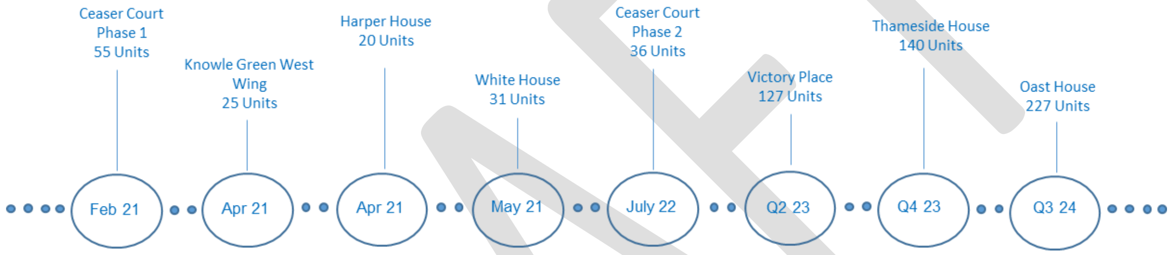

Illustration 2: Projected funding

Knowle Green Estates Ltd (KGE)

5.15 The Council formed its housing company in 2016 when we acquired Harper House in Ashford for emergency accommodation. Demolition of this property began in January 2020 in order to redevelop the site to provide brand new fit for purpose temporary accommodation for 20 families.

5.16 We also identified a need to promote our own affordable housing schemes, and KGE is the vehicle we use to deliver them to residents. We currently have a number of projects in the pipeline which will deliver 22% of the Borough's assessed 5-year land supply requirement in the Local Plan (738 units to be delivered by the Council out of a required 3,343).

5.17 KGE, recognising the scale of its ambitions, has recruited two additional experienced Non-Executive Directors with residential management and financial experience and expertise to strengthen the Knowle Green Estates Board.

Development costs

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5.18 As our various housing delivery schemes come on stream, this will in the short term add some financing costs into the revenue budget. However in the longer term the council will receive a net margin or surplus representing the difference between the rates it accesses loan finance at and the market rates at which its housing delivery company Knowle Green Estates will repay loans to the Council at.

6 The focus on regeneration and economic development

6.1 Economic development and recovery from the economic impacts of the COVID-19 Pandemic is another one of the Council's four strategic priorities and reflects the importance that the Council places on stimulating more investment, jobs and visitors to Spelthorne in order to further the overall prosperity of the Borough and its residents. How we look to achieve this is set out in the Economic Strategy. Importantly, a vibrant economy also provides income through our share of business rates, helping the Council to be financially sustainable. Where and how we invest our capital plays a central role in terms of economic development.

6.2 It is true for all local authority areas that, if they do not pay close attention to the economic development and vitality of their area, they will move backwards as other areas around them move forwards. In previous years, the Council has made significant changes to Staines-upon-Thames which have revitalised the town centre. These include contributing to the development of the Two Rivers shopping centre, pedestrianisation of the High Street and the upgrading of the Riverside area around Memorial Gardens and Market Square.

6.3 The Council has significant landholdings in Staines-upon-Thames, and has made a number of acquisitions in line with our investment parameters to further cement our position. We bought back the long leaseholds of both Communications House, the Elmsleigh Centre and Thameside House so we now have control over a key portion of the town centre close to the River Thames. The Council also acquired Hanover House, which sits on the River adjacent to Bridge Street car park and represents a major redevelopment opportunity. The Council has entered into a development agreement with the Arora Group for a high end hotel complex development on the River Thames waterfront. We will continue to acquire properties but only where it makes strategic sense to do so for regeneration purposes. A recent example is the acquisition in 2019 of the Oast House, and the adjoining car park and a number of buildings on Kingston Road.

6.4 Further work needs to be done in Staines-upon-Thames and that there is considerable scope for improvement around Sunbury Cross and Ashford. So the aspirations of the Council should therefore be bold and ambitious. We have followed this ambition through by acquiring the Summit Centre in Sunbury (2019).

Planning to meet housing need

6.5 The current review of the Council's Local Plan initially identified a need to create around 606 housing units each year over the next 15 years. As part of its Issues and Options Consultation in summer 2018, the Council consulted on four main ways to meet this significant requirement for new housing:

- Brownfield development
- Green belt development
- Staines development
- Combination development

6.6 The Issues and Options stage was followed by a Preferred Options consultation between November 2019 and January 2020. This took forward the fourth option (combination) that was agreed by Cabinet to meet our housing need, with intensification of brownfield sites, additional development in Staines (facilitated by a masterplan) and some limited release of weakly performing Green Belt sites. Since the consultation, it has been agreed that Spelthorne will prepare its Local Plan on the basis of a revised methodology for calculating housing need that was consulted on by the Government. This brings our housing need down to 489 homes per year. It is anticipated this will mean removal of some or all of the previously identified Green Belt allocations from the Plan and a greater focus on finding opportunities to maximise brownfield sites, particularly in Staines.

The Strategic Housing Availability Assessment (SLAA) 2019 estimates that the 5-year housing land supply in the Borough is 3,343 units on 52 sites. Over 1,500 of these units are expected to be delivered in Staines- upon-Thames, with at least 400 to be delivered on Council-owned sites. In the medium term (next 6 to 15 years), Council-owned sites could deliver another 750 units (with other sites not owned by Spelthorne bringing forward approximately 250).

6.7 The preferred approach of focusing on Staines-upon-Thames as the major residential opportunity area requires a Masterplan to be developed as part of the new Local Plan which will focus in detail on where and how this new development can best be accommodated, in order to ensure we achieve a sustainable (financial, environmental and social) solution for the town.. This is now known as the Staines Development Framework and consultants working with officers and Members have now reached the Issues and Options stage. Progress has been delayed due to the pandemic and it is expected that the Framework will be completed by mid 2021.

6.8 The Council's landholdings within the town centre (including our strategic acquisitions) provide a clear opportunity to bring forward at least 1,420 units ((50% affordable) in the next 10 years. In the next five years, the level of investment that the Council aims to make is likely to be a minimum of £300m. As the land owner, we are confident that we can deliver this level of residential development whilst retaining sufficient car parking to sustain the town centre (though some sites may well be reconfigured to make more efficient use of the land that we have). The consultants are engaging with landowners and developers, including Knowle Green Estates, where schemes are in the pipeline but are likely to be consented or commenced prior to adoption of the Framework to ensure its outputs are not prejudiced.

6.9 The SLAA has identified that, within the town centre, the Council is able to develop the following housing units as a minimum (within the immediate confines of the town centre):

Thameside House	flatted	140 units	Years 1 - 5
Hanover House and Bridge Street car park	mixed use	75 Units and 150-250 bed space hotel	Years 1 – 5
Riverside car park (subject to re-provision)	flatted	100 units	Years 6 – 10
Elmsleigh Centre and adjoining land	mixed use	650 units	Years 11 - 15

Table 7: Minimum housing units identified to develop

6.10 The Council is currently part of a consortium promoting a light rail link to Heathrow from Staines-upon-Thames – the Southern Light Rail (SLR). A proposal was made to the Department for Transport setting out the details of the scheme, and making clear that it will be entirely privately funded (this is known as a market-led proposal). There are a number of potential investors and it is not envisaged at this stage that the Council will be contributing to the capital cost of c£375m. Heathrow agreed in 2019 that the SLR was its first Innovation Partner and work is progressing on how this scheme can be moved forwards.

7 The focus on green initiatives and climate change

7.1 The Council has joined a growing number of domestic and international authorities in declaring a climate emergency and adopting a carbon-neutral target. A Climate Change Task Group has been set up and the Council is at an early stage of fully assessing and identifying our own carbon footprint along with developing a carbon trajectory to reach carbon neutrality. This work will help to inform where investment will be required to meet our targets.

7.2 Focus areas for capital investment in green measures will include the transition of our fleet of vehicles to low carbon alternatives and the decarbonisation of Council owned buildings. Best practice environmental design will be built into our developments

7.3 A Green Fleet review is underway which will inform future decisions and options on our vehicle transition. We are committed to reviewing the refuse collection fleet in 2023 and aspire to transition 50% to electric or hydrogen at this time with the remaining fleet replaced by 2027.

7.4 The decarbonisation of our buildings will require further investment in energy efficiency and renewable energy measures. To meet climate change targets we also need to adopt the use of sustainable materials in our builds and other efficiency measures e.g. on water use (Nov 2020) the Council is proactively undertaken studies which will inform future investment requirements for our buildings in relation to energy.

7.5 Plans are underway to redevelop Spelthorne Leisure Centre to be the first fully compliant Passivhaus leisure centre in the Country demonstrating the Council's commitment to tackling climate change.

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7.6 The River Thames Scheme will reduce flood risk to people living and working near the Thames, enhance the resilience of nationally important infrastructure, contribute to a vibrant local economy and maximise the social and environmental value of the river. The scheme which involves the building of channels to take the extra flow in a flood will protect and reduce flooding to residents and businesses in Spelthorne. The aspiration for the River Thames Scheme is to be more than just a flood scheme through also providing opportunities for landscape enhancement, habitat creation and recreational opportunities. The River Thames Scheme is expected to cost (including contingencies) £640 million. Partners have committed to funding their share of the scheme and are finalising the mechanisms to do this. Surrey County Council has agreed to provide £270 million for long term flood risk management work. This includes a £237 million contribution to the River Thames Scheme, enabling the next steps of the scheme's delivery. To date Spelthorne has committed £49k per year in revenue costs towards the development of the scheme given its importance to reducing flood risk in the Borough and protecting our communities. In early discussions partners agreed a contribution to the capital costs as well. This was identified as £1.3M for Spelthorne and with the scheme progressing as now expected this spend would take place between 2023 and 2025 - most likely with the Development Consent Order for permission to build together with the build timetable this will be in 24/25.

8 How we finance our capital spend

8.1 As referred to in Table 4, Section 3, above, we finance our capital expenditure from a range of sources. These include:

- Revenue Contributions to Capital – beginning in 2018-19, we are now funding £750,000 per annum of our capital programme from the Council's Revenue Budget contribution. This covers most of the capital items which are not funded by grant or will not generate revenue savings or revenue income streams. This puts these elements of the Capital Programme on a more sustainable basis
- Grants – principally Disabled Facilities Grant. The Council will also seek to explore grant funding opportunities for its housing and development schemes and has successfully bid for grant assistance from Homes England for its single person hostel and family emergency accommodation schemes

- Community Infrastructure Levy (CIL) - the Council will apply our share of CIL to support capital schemes which meet the CIL criteria
- S106 funds (planning contributions from developers) – we will use s106 funds to support affordable housing schemes
- Capital receipts – these are generated from either the Council's share of Right to Buy proceeds on housing stock, which used to belong to the Council before the transfer to Spelthorne Housing Association (now A2D) in the 1990s, or from sales of other assets. As Knowle Green Estates starts to make larger principal repayments this will be capital receipts which can then be used by the Council to help finance capital expenditure
- Borrowing – mainly from the Public Works Loans Board (PWLB) at fixed rates. Some borrowing on a shorter term basis from other local authorities. In future, further borrowing will be focused on financing directly housing and regeneration within the Borough and service projects such as the new Leisure Centre

However, it is the case that PWLB and loans from other councils will continue to be a very important funding source. In November 2020, the Government published its response to the consultation on Public Works Loan Board Terms, dropping with immediate effect the margin on its loan rates by 100 basis points but requiring authorities to confirm that when applying for PWLB finance that they do not plan to purchase any commercial assets within next three years primarily for income. This Council has no plans to purchase any such assets in the coming years. The loans rates reduction will help make any new Council housing and regeneration delivery and the leisure centre more affordable to finance from borrowing

9 How we manage risk and ensure sound decision-making

9.1 The Council needs to ensure that we have clear ways of mitigating the risks that are inherent in acquiring property and in bringing forward development. We must also show that we have the right decision-making processes in place with robust checks and balances (this is called governance). *Appendix 4* sets out our risk management approach in more detail.

Risks

9.2 From a risk management perspective, and in order to ensure the Council's investments are as safe as possible, we have employed a range of due diligence techniques, including:

- Evaluation of tenants by external global property advisers
- Using industry-standard information sources such as the credit rating agency Dunn and Bradstreet

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- Modelling the impact of tenant failure (and securing parent company guarantees where necessary) and setting aside money from investments to establish sinking funds to cover worst-case scenarios and possible future voids
- Maintaining assets to ensure they are fit for purpose
- Key Performance Indicators (KPI's) *see Appendix 7*

9.3 The Council will keep the performance of our portfolio of commercial assets under continuous review We have developed a series of Key Performance Indicators, (*Appendix 7*) to ensure the portfolio is performing as we want it to and is monitored. This will allow us to take appropriate action as required

9.4 Under the Council's constitution, risk management is overseen by the Audit Committee, which reviews the Corporate Risk Register at each meeting. The Council is currently refreshing its corporate Risk Policy and approach to maintaining the Corporate Risk Register. The Corporate Risk Register is also reviewed by Cabinet. Risk management is an integral aspect of the Council's project methodology, with projects required at initiation to identify risks and how they mitigate them, and to maintain a project risk register. The approach to risk management includes planning and identification, monitoring and review for all risks and projects throughout their lifecycle. The Corporate Risk Register includes details of commercial investments. A key focus of our approach to commercial assets is to ensure that we understand the full range of risks – including the financial robustness of tenants and guarantors, legal risks, and physical and locational risks – so that we put in place appropriate risk mitigation measures. Increasingly with climate change we need to be aware of how a changing climate may impact on our buildings particularly in terms of cooling, and associated costs/carbon impact.

Skills

9.5 The changing nature of our portfolio has meant that we have enhanced our property team to ensure that we have with the right mix and level of skills and commercial experience. The Council also employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions (including treasury management). The cost of strengthening our property team has been met through funding and management set-asides from investment income. There is now an 11-strong asset management team which includes a manager of the property unit formerly employed by BAA who brings considerable expertise in the commercial property market around Heathrow; a development manager with significant experience of building residential property in the private sector; and a property manager formerly at a commercial fund. In October 2019 the Council undertook a training session on risk management for members of audit committee. During 2021 we will be doing some refresher training sessions on risk management for officers and councillors.

9.6 The Council will ensure that the assets team continues to grow in proportion to the size of our investment and development activity. We have added further resources to our in-house finance and legal teams to support this acquisition and development activity. We also encourage our professional staff to complete ongoing continuous professional development, ensuring expertise levels are maintained. We have increased the resilience of our insurance functioning by bringing in, from 1 October 2020, London Borough of Sutton's larger insurance team to provide support on claims handling management in respect of the Municipal portfolio. This gives us access to a larger pool of expertise.

9.7 Where we do not have the necessary knowledge and skills within the Council, we use external advisers and consultants that are specialists in their field. These include Clyde and Co (legal), Cushman and Wakefield (property and valuation), Dunn and Bradstreet, Arlingclose Limited (treasury management), Deloitte and Carter Jonas (valuation and financial evaluation). This ensures that we have access to experts who can help us to operate in line with our risk appetite. We also seek to ensure that our councillors' knowledge on our approach to investments (both treasury management and commercial) is appropriately maintained. A training session on treasury management for councillors was provided in January 2021

Governance

9.8 The Council needs to ensure that we consider all opportunities in a managed way, and that we do so as transparently as we can (bearing in mind we are making commercially sensitive decisions). The Council is committed to following local government guidelines and we take appropriate legal and technical advice to ensure we are always doing so.

9.9 Under the current Cabinet system all property acquisitions are currently overseen by a group of senior councillors and officers. This group forms a Property and Investment Committee (PIC), which is a sub-committee of Cabinet including the Leader of the Council, one of the Deputy Leaders and portfolio holder for Assets and the portfolio holder for Finance. Councillors are involved at key stages of the process (which is set out at the end of *Appendix* 4).

9.10 Following the change of Administration and moving to no overall political control the Council is looking to significantly increase transparency around decision making. This includes strengthening governance arrangements at key stages throughout any acquisition or development to ensure the appropriate level of councillor oversight.

9.11 This is linked to and sits alongside a move away from a Cabinet model of governance to a Committee System, with five main committees plus four others. It is currently proposed that Assets (acquisitions and developments) will be reporting to the Policy and Resources Committee. Under this new system the aim is to ensure that acquisitions are thoroughly scrutinised, and development projects are kept under review at key 'project gateways' and progress against budgets are monitored. A Sub Committee will be set up with Councillors to undertake this critical role with external advisors providing advice where necessary..

9.12 The Council has recently finished consulting with residents on this proposed move to a Committee System. If approved by Council, this will come into effect from May 2021. The governance arrangements set out above will continue until this point in time. Any changes as a result of this move will require this capital strategy to be updated 'in year' to reflect this.

9.13 As part of the Council's preparations for implementing the new CIPFA Financial Management Code, in February 2020 the Council ran a workshop with CIPFA to review the extent to which its governance arrangements are contributing towards resilience. In November 2020, at the Council's invitation, the LGA undertook a review of our finance and property arrangements to help the Council identify further opportunities for improvement. We will shortly be publishing the positive and constructive LGA Finance Peer Review report and putting in place an action plan to address its recommendations. The Council completed a Self-Assessment against the CIPFA FM Code which it reported to the Audit Committee and it will keep the self-assessment under regular review.

10 How we ensure we have enough money day-to-day and maximise return on investment

10.1 Treasury management is all about keeping sufficient but not excessive cash available to meet the Council's spending needs, whilst managing the risks involved. Surplus cash is invested until required, and a shortage of cash is met by borrowing – this avoids excessive credit balances or overdrafts in the bank current account. The Council is typically cash-rich in the short-term as revenue income is received before it is spent, but cash-poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

Current borrowings

10.2 Based on acquisitions and investment decisions up to 31 December 2020, the Council currently has £1,085m borrowing (£1,114m full year forecast) (finance to provide figures at an average interest rate of 2.2%, and £36.8m pooled and medium-term treasury investments at an average rate of 4.7%. *Appendix 5* sets out in detail how this is achieved with the headline information set out below.

Factors shaping our borrowing decisions

10.3 From a borrowing point of view, the Council needs to achieve a low but certain cost of finance whilst retaining flexibility should plans change in future. This requires striking a balance between cheap short-term loans and long-term fixed rate loans where the future cost is known, but higher. Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. This is the approach that the Council takes.

10.4 In addition to the above, the Council is legally obliged to set an affordable borrowing limit (also termed the 'authorised limit for external debt') each year and to keep it under review. In line with statutory guidance, a lower 'operational boundary' is also set as a warning level should debt approach the limit. *Appendix 5* provides more detail on the boundary and the limit.

10.5 The Council's policy on treasury investments is to prioritise security and liquidity over yield – in other words, we focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the Government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely.

10.6 In addition to debt of £1,085m detailed above, the Council is committed to making future payments to cover the pension fund deficit (valued at £51.128m). We have also set aside £2m to cover risks of business rates appeals, and £6m per annum into sinking funds to cover future liabilities on our investment properties.

10.7 Sound treasury management also has to consider the impact on the Revenue budget. Although capital expenditure is not charged directly to the Revenue Budget, interest payable on loans and Minimum Revenue Provision (i.e. repayment of loans) / loans fund repayments are charged to Revenue, and this is offset by any investment income (details of the revenue implications of capital expenditure can be found in the 2021/22 revenue budget).

10.8 Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years, or longer (in one recent example 70 years) into the future. The Chief Finance Officer is satisfied that the proposed Capital Programme and recent capital expenditure decisions are prudent, affordable and sustainable. 50-year forecasting is undertaken on an expected and worst case basis for commercial assets to estimate future liabilities – this ensures that future risk is evaluated and sufficient funds are set aside in sinking funds to meet those liabilities. It is the responsibility of the Section 151 Officer to agree what, how and when monies held in the Sinking Fund account are spent on our commercial investment assets. This ensures our sinking funds are protected. Since the first COVID-19 lockdown in March updated 10 year expected and worst case scenarios for the sinking funds have been reviewed on a weekly basis to ensure that despite the impacts of COVID-19 the Sinking Funds are more than sufficient to insulate the revenue budget and council tax payers from the impacts of any short term reductions in rental income.

10.9 The Council has approved the maintenance of our operational assets on a more sustainable basis by increasing the planned maintenance budget by £750,000 per annum over last two financial years and addressing a number of backlog maintenance issues at the Council Offices as part of a refurbishment project. The Council has also put the funding of our Capital Programme on a more sustainable basis.

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APPENDICES

1. **Historic background**
2. **Investment parameters**
3. **Housing information**
4. **Risks and decision making**
5. **Treasury Management**
6. **Our Commercial Activity**
7. **Key Performance indicators**

Historical Background

After the financial crash in 2008 and the austerity imposed on local authorities since 2010, the Council received less and less general revenue grant from government to support its Revenue Budget for the provision of services to residents. Over the years from 2008 to 2016, the Council made savings/income of about £8m or equivalent to 54% of the net 2008/09 budget.

Although no cuts were made to front-line services during this time, the gradual reduction of staff from front-line and support services, did have an impact on the Council's operations. It is fair to say that by 2014 the gradual "salami slicing" of the Budget had reached a stage where some services were becoming unsustainable. The Council launched a programme "Towards a Sustainable Future" with different strands aiming to make a difference to the Council's longer-term finances:

- Investing in property
- Continuing to maximise returns on its financial investments
- Investigating different ways of delivering council services through partnerships and companies/public sector mutuals
- Restructuring the Council

In addition to this ambitious plan, in 2016, a change in administration set a new priority for the Council: provision of much-needed affordable housing for residents. It was against this background of needing to make big changes and find new sources of funding to tackle big social issues, that in 2016 the Council had an opportunity to purchase the BP Campus in Sunbury.

Until 2016, the Council's most significant investment asset was the freehold of the Elmsleigh Shopping Centre in Staines upon Thames. The Council receives a 13.445% share of profits from the shop rents, but the difficult financial trading environment in the retail sector since 2008 had reduced our income from the Elmsleigh Centre.

Against this reducing income the Council had made savings across the Council whilst at the same time it had protected frontline services for residents. However the financial landscape meant that further government cuts and changes to business rates meant that the savings requirements were still there. Protecting front-line services was becoming harder. Acquiring the BP Campus in September 2016 brought about a significant change in the Council's finances.

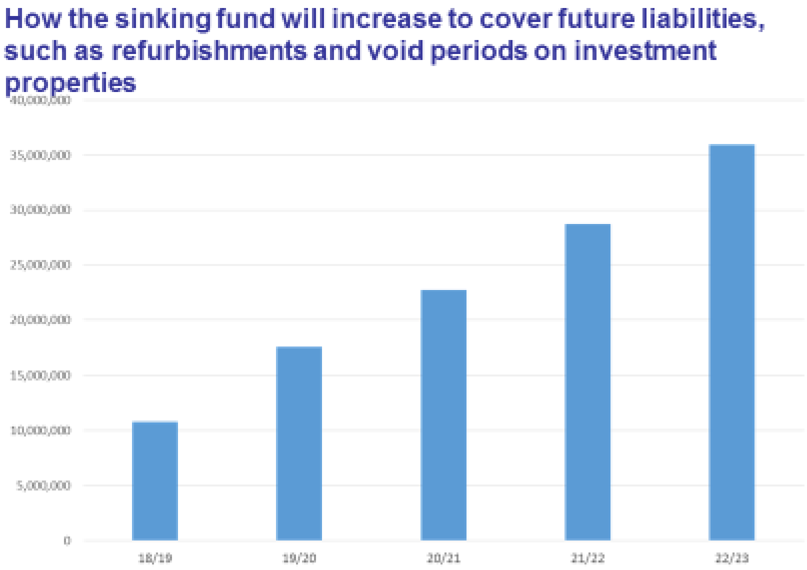
BP campus

This transaction is worth a special mention because it is so significant that it has on-going importance. The chance to purchase the BP Campus was a once in a generation opportunity. BP has been in Sunbury for 100 years. Its campus was significantly enlarged and improved in 1990s. BP wanted to sell its campus to raise money, in return, it would sign a lease on the premises for 20 years, guarantee increases in rent and provide a parent company guarantee. In a separate transaction shortly afterwards, the Council also purchased research buildings on the same campus (known as the south-west corner).

The combined purchase price of the Campus was £380m, which the Council borrowed with a number of 50 year loans (by taking 50 loans out rather than one single loan the Council saved a significant amount of money) from the Public Works Loans Board (PWLB). The PWLB is a government agency which exists to provide funding to public bodies for capital projects. The interest payable on these loans was fixed at the time the loans were taken out at extremely low rates of interest. Statutory guidance from the Secretary of State and CIPFA governs the way that councils can borrow and how they must repay the money they have borrowed. In taking out this finance, the Council was advised by leading professional practices so that the decision was based on robust due diligence. The Council repays these loans on what is called a "fully prudential basis", i.e. like a repayment mortgage it repays the principal loan alongside the interest as it goes along.

The significance of the BP acquisition is that it made a big contribution to council finances even after:

- Repaying the loans and interest
- Setting aside money for the management costs of the buildings (which are well constructed and well maintained by the tenants)
- Setting aside a sinking fund for refurbishment or redevelopment costs when the lease ends. This also provides a cushion to protect against potential periods between tenants leaving and new tenants starting to pay rent



The additional income provides significant funding on a long term ongoing basis to offset the loss of general Revenue Support Grant and to reverse the impacts of the previous years's salami slicing which was beginning to put the sustainability of services at risk

Longer term strategy for the BP Campus

With the leases for BP running for 20 years and with the finance running for 50 years, the obvious risk for the Council is that BP may give up its lease at the end of the contract. The Council considered that a number of likely alternative uses were highly probable; use as another business park with one or more tenants; redevelopment as housing or a use related to the near-by airport. It has already started the work of reviewing the options available at the end of the lease with a view to looking to the long-term uses for the site.

Diversification of the portfolio

Although the BP acquisition went a substantial way to stabilising the finances of the Council, a number of factors meant that the Council had to consider further acquisitions:

- The need to ensure that "not all the eggs were in one basket"
- Government policy to remove all council general grants
- Government policy to introduce negative grant allocations

Why the Council continued to invest in property after the BP deal

Residents will understand from recent newspaper headlines that many local authorities are having to cut services in order to adjust to the austerity measures imposed by the government budgets of since 2010. One council in Northamptonshire has already failed and questions have been asked about the sustainability of other local authorities including Surrey County Council and others. The National Audit Office has reported on the financial sustainability of local authorities in 2018. It is fair to say that there is, within local government, a major change to the way in which it was financed.

The BP acquisition provided a very helpful opportunity for the Council to stop making cuts and to put itself back onto a more sustainable footing. We have not had to make cuts in services because we have had better finances than most councils.

From 2016 to 2018 the focus of the Council was on achieving financial sustainability and making investments in order to bolster its revenue budget by deploying surplus income from investing in commercial property. This strategy has been successful and the 2019/20 budget of the Council will include around £10 million of net income for the revenue budget which is derived from successful investments made by the Council since the acquisition of BP in 2016.

Strategic Property Investment Parameters

Spelthorne Borough Council currently invests in property for one of three primary reasons:

- Revenue generation
- Social investment, and
- Strategic purposes

1. Revenue Generation

1.1 Purpose

To deliver additional ongoing income to support the revenue budget to:

a. Offset funding reductions from external sources (central government and the county council) and other budgetary pressures, and
b. Aspirationally to go beyond that to increase the quality and quantity of services we deliver to the residents of Spelthorne.

Our aim is that the Borough Council becomes financially self-sufficient.

Net income generated is calculated net of all costs associated with the investment, including interest, provisions to cover refurbishment and possible future rent-free/void periods, external professional fees etc.

These investments are intended to deliver a surplus to be used to support the provision of services but can carry significant risk. Approximately 5% target gross return dependent upon covenant.
At this margin a small loss can have a disproportionate negative effect.

We therefore need to have clear guidelines and underwriting criteria.

1.2 Investment Guidelines

i. We will always undertake thorough due diligence to ensure that the Council understands the risks associated with a particular proposed acquisition and how those risks are mitigated.

ii. Preference is given to investing within borough, or in an adjoining area that is economically important to Spelthorne (for example Heathrow / areas immediately south of Staines Bridge). Properties outside this preferred area should represent a lower risk and higher return.

This is because:

a. local investment ensures that we are best placed to know all the facts surrounding a property, its history, potential developments in the area etc. and, as the planning authority, the borough can optimize the benefits that provides, and

b. any loss-mitigating exit strategy that may be required and that may result in a change of use or conversion of the investment from profit-making into a non-profit-making social investment (e.g. conversion from rented offices to emergency, social or affordable housing) will benefit residents of Spelthorne i.e. the taxpayers who are funding the investment. Variation from this requires a better return to mitigate above considerations.

iii. We have a clear view of the asset security curve.

iv. We have a clear exit strategy, fully costed, at the various critical points in the investment (lease break points etc.).

v. We do not attempt to second-guess what a tenant may do in the future. We always rely solely on the contractual obligations and plan for the worst-case scenario.

vi. We do not make speculative investments for revenue-generation purposes. The properties should ordinarily be complete, free of any ongoing redevelopment work and occupied by creditworthy tenants with a minimum of 10 years' lease remaining.

vii. Any exposure to interest rate fluctuations must be mitigated. We will ordinarily only borrow at fixed interest rates.

viii. Once completed (funding drawn down and purchase completed), the funding arrangements for investment should require only minimal supervision or intervention, avoiding technically complex, long-term refinancing exercises (e.g. bond issues, dependence on future refinancing) or dependence on external professionals or professional, specialist knowledge from councilors or officers (who may well have left the Council by the time the decision-making point arrives).

ix. We do not invest in incomplete builds, conversions, etc unless a water tight pre-completion occupier lease is in place

x. We will not normally invest in retail units, unless it forms part of a wider potential regeneration scheme.

xi. We do not engage with sellers or tenants who may present a significant reputational risk

xii. The credit rating of all incumbent tenants is to be understood, recorded at the time, and must be sufficiently strong for the level of investment. We aim for primarily "Blue Chip" covenants.

xiii. We do not engage in high-risk / high-reward investments.

xiv. We do not invest in properties that have a material flood risk (1/100 years or more frequent) unless robust flood mitigation has been designed in.

2. Social Investments

2.1 Purpose

To deliver projects that improve quality of life for our residents, such as emergency, social and affordable housing, community infrastructure and well-being projects, flood prevention and flood relief infrastructure.

These investments do not have to generate additional income/profits but must provide the taxpayer with value for money (a legal requirement on the council) and should be self-financing (although exceptions may be made if the social benefit warrants a small subsidy from taxpayers' money).

2.2 Conditions of investing

i. Some element of speculation may be inevitable and acceptable (e.g. building affordable housing when the housing market is subject to market pressures).
ii. We do not ordinarily invest outside the borough (these social investments are designed to benefit the residents/taxpayers of Spelthorne). Consideration will be given for investments nearby where we can ensure Spelthorne residents benefit.
iii. Any exposure to interest rate fluctuations must be mitigated. We will ordinarily only borrow at fixed interest rates.
iv. Once completed (funding drawn down and purchase completed), the funding arrangements for investment should require only minimal supervision or intervention, avoiding technically complex, long-term refinancing exercises (e.g. bond issues, dependence on future refinancing) or dependence on external professionals or professional, specialist knowledge from councilors or officers (who may well have left the Council by the time the decision-making point arrives).
One exception to this is the ongoing operational management of rented/leased (social or affordable) accommodation and emergency housing. Where practical, these ongoing responsibilities may be transferred to the Council's wholly-owned property company, Knowle Green Estates Ltd..
v. We do not engage with sellers or tenants who may present a significant unmitigated reputational risk.
vi. We do not invest in properties that have a material flood risk (1/100 years or more frequent) unless robust mitigation measures designed in unless robust flood mitigation has been designed in.
vii. Social investments are not an alternative to proper funding and provision by the County Council of infrastructure and services that the County Council is required to provide. Spelthorne does not intend these social investments by the Borough Council to alleviate the financial and social responsibilities borne by the County Council.
viii. In all cases the Council will structure investments to give maximum control, financial and social benefit to itself and Spelthorne residents and priority will be given to retaining ownership and receipt of revenue.

3. Strategic purposes

3.1 Purpose

To augment either Revenue Generation or Social Investments, for example to increase the value of an existing asset value by "marriage" or where it facilitates or enhances another project / investment covered above.

Investment criteria and funding to be in accordance with relevant purpose and criteria.

Cllr Tony Harman, Cabinet Member for Finance, Spelthorne Borough Council. and Cllr Ian Harvey, Leader of the Council and Council Policy co-ordination,

Note:
The Council will pay due attention to prevailing laws, statutory regulations and Chartered Institute of Public Finance and Accountancy guidance and best practice recommendations. The Government on 10th November issued several consultations on the statutory parameters for local authorities' investment activity. Once the Government confirms in the New Year the final guidance we will need to review and update this document.

Housing and homelessness

Table H1: Number of applicants on the Council's Housing Register

	2016	2017	2018	2019	2020
Number on Housing Register as at 1 April	1,598	1,869	2,186	1,245[1]	2,098

Source: In-house monitoring

Table H2: Number of social housing vacancies offered to the Council for re-letting

	2015/16	2016/17	2017/18	2018/19	2019/20
Number of lettings	249	197	199	170	196
Ratio applicants to vacancies	6:1	9:1	11:1	7:1	11:1

Source: In-house monitoring

Table H3: Number of households accepted as unintentionally homeless, in priority need, and owed the "Main Duty"

	2015/16	2016/17	2017/18	2018/19	2019/20
Number of households owed rehousing duty	120	115	116	61[2]	72

Source: In-house monitoring

Table H3a: Priority need category for "Main Duty" acceptances

Priority need category	Number 2019/20	% of Total 2019/20
Household includes dependent children	47	64.4%
Mental health problems	9	12.3%
Physical disability / ill health	9	12.3%
Household includes a pregnant woman	2	2.7%
Domestic abuse	1	1.4%
Young applicant	1	1.4%
Old age	0	0%
Homeless because of emergency	0	0%
Other	4	5.5%

Source: In-house monitoring

[1] In 2018/19, a new Housing Allocations Policy was introduced which resulted in a full re-registration process. This figure represents the number of applicants who had successfully re-registered by 1 April 2019.

[2] The Homelessness Reduction Act 2017 was implemented from April 2018 which introduced two new duties – to prevent homelessness and relieve homelessness. This figure represents the number of applicants who were owed the "main duty" under s193(2) Housing Act 1996 (as amended) following the end of the prevention and relief duties.

Table H4: Number of households in temporary accommodation per quarter

2015/16				2016/17				2017/18				2018/19				2019/20			
Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
113	139	131	121	117	117	108	104	103	91	111	108	109	116	110	106	104	96	95	110
Average 126				Average 112				Average 103				Average 110				Average 101			
Average 110																			

Source: In-house monitoring

Table H5: Ratio of median house prices to median wages by region

	2015/16	2016/17	2017/18	2018/19	2019/20
Spelthorne	9.39	10.42	11.16	11.06	11.61
South East	8.81	9.43	9.79	9.93	9.74
England	7.53	7.72	7.91	8	7.8

Source: ONS House price to residence-based earnings ratio

Table H5: Median gross annual residence-based earnings by region

	2015/16	2016/17	2017/18	2018/19	2019/20
Spelthorne	34,066	34,997	35,250	34,669	33,597
South East	30,074	30,741	31,664	32,230	33,357
England	27,838	28,500	29,085	29,869	30,661

Source: ONS House price to residence-based earnings ratio

Table H6: Number of affordable homes completed under s106 by tenure

Year	Affordable dwelling completions (Gross)	Affordable dwellings lost (Gross)	Affordable dwellings completed (Net)	Rented (Gross)	%	Shared Ownership (Gross)	%
2015-16	138	14	124	82	59%	56	41%
2016-17	46	0	46	46	100%	0	0%
2017-18	9	0	9	5	55%	4	45%
2018-19	6	0	6	6	100%	0	0%
2019-20							
Total							

Source: In-house monitoring

Risk management and sound decision making (also called governance)

Risk management

In order to ensure the council's investments are as safe as possible we have employed a range of robust due diligence techniques including:

- Evaluation of the tenant by one of our agents Cushman and Wakefield, by our in-house asset management team and utilising industry-standard information sources such as Dunn and Bradstreet
- This includes modelling over the 50 year funding period future capital expenditure needs relating to the assets and identifying and quantifying potential void periods
- The Council model models the impact of tenant failure and when necessary secures parent company guarantees from tenants.
- Second opinions are taken on all of the above work by Deloitte to give the Council further reassurance
- The Council models financial projections on a basic and worst-case scenario
- Following acquisition there is ongoing management of the property and monitoring of key financial metrics and performance metrics by qualified asset managers. This includes the appointment of appropriate qualified asset management firms particularly with the larger multi-tenant buildings.
- The Council has set aside money from investments to establish sinking funds to cover worst-case scenarios and also planned future voids (i.e the periods between one tenant leaving and the next occupying) and rent free periods at end of term and refurbishment works

All this is in accordance with good asset management practice.

Diversification – spreading the risk

In any commercial property portfolio it is important to achieve a level of diversification in order to ensure that, “not all the eggs are in one basket”.

Portfolio can be diversified by:

- property type e.g. office, residential, industrial or retail
- sector e.g. pharmaceutical, media, fin-tech et cetera
- geography e.g. south-east, national or international

It can be seen from the Council's portfolio that it is heavily weighted towards south-east office market although the tenant mix is diversified. The Council has not acquired any assets for investment purposes since 2018 and is not currently intending to do so in the future.

Skills and expertise

Another feature of good risk management is to have professionally qualified, experienced staff in sufficient numbers that they can look after the acquisitions of investments, the development of properties and ongoing asset management.

Prior to 2016 the council had a small internal team which was focused on the needs of a typical municipal portfolio. Since that time the focus of the team has shifted considerably and the resources which are being put into it have also been increased. The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions in line with Financial Regulations and the Scheme of Delegations to Officers. For example, the Chief Finance Officer is a qualified accountant (CIPFA, ICAS) with 29 years' experience. The strengthening of this team has come from funding, management set-asides from investment income itself, and we have focused on bringing in individuals with significant commercial experience.

There is now an 11 strong asset management team including:

- a manager of the property unit formerly employed by BAA and with considerable expertise in the commercial property market around Heathrow
- two development managers with considerable experience from building residential property in the PRS sector
- a property manager formerly at a commercial fund in the city, and another who has extensive experience of large residential and retail portfolios
- a property account manager who has experience of dealing with commercial property management systems

The Council will ensure that the team continues to grow if the portfolio grows and diversifies. It has also added further resources to its in-house finance team and legal team to support this acquisition and development activity. The Council pays for junior staff to study towards relevant professional qualifications including CIPFA, encourages its professional staff to undertake ongoing continuous professional development.

Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field which it can rely on including:

- Clyde and Co-– these solicitors have worked with Spelthorne Borough Council since the development of the Elmsleigh centre and Two Rivers shopping centre
- Cushman and Wakefield – commercial acquisition property advisers, who have worked with the council since the development of the Elmsleigh Centre and the Two Rivers shopping centre
- Arlingclose Limited– a leading treasury management consultancy
- Dunn and Bradstreet – A financial services company which has been brought in to provide ongoing credit assessments of our commercial tenants
- Deloitte – well-known accountants and auditors provide a second opinion on valuation and other aspects of advice. They provide independent triangulation on the robustness of approach and on tenants' financial health
- Carter Jonas – property consultants dealing with valuations of our portfolios (including the investment portfolio)
- Jones Lang LaSalle – leading commercial retail property advisors

This approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

We also seek to ensure that our councillors' knowledge on our approach to investments both treasury management and commercial is appropriately maintained. The Finance Portfolio Holder attends quarterly briefings with Arlingclose our Treasury Management advisers. We have run sessions on our property investment approach for members of our Overview and Scrutiny Committee and we have provided induction training for the fresh intake of councillors following the May 2019 elections. Councillors also receive one to one briefings where these are requested.

Governance

As a council we need to ensure that we consider all opportunities in a managed way, and that we do so as transparently as we can (bearing in mind we are making commercially sensitive decisions). This process needs to include both officers and councillors (who at the end of the day are the people who are accountable to the electorate and need to ensure the council spends its money wisely).

Current position (Cabinet model of governance)

All potential economic development and regeneration property acquisitions are overseen by a small group of senior councillors and officers including Leader of the Council, Councillor John Boughtflower, one of the Deputy Leaders Councillor Jim McIlroy (with responsibility for Assets) and Cllr Satvinder Buttar the Finance Portfolio Holder. The whole of Cabinet are also briefed on a monthly basis on the development programme,

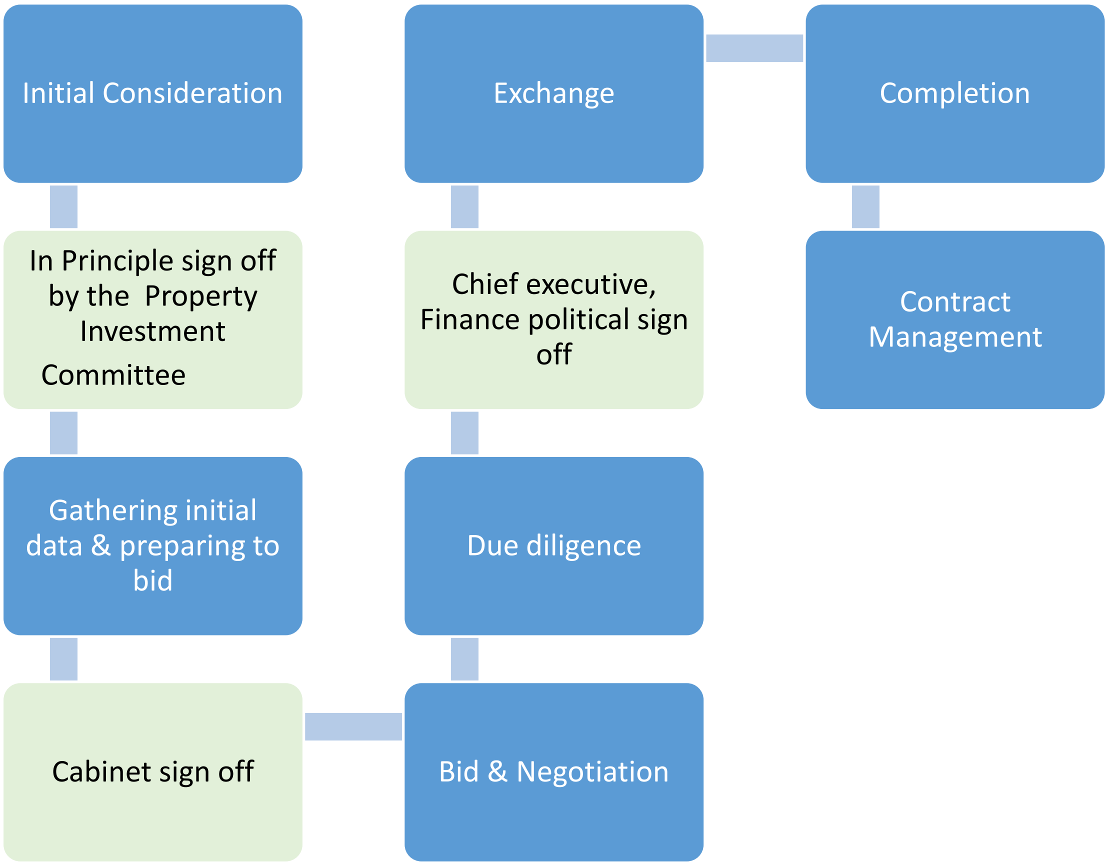
Councillors are involved at key stages of the process. The Leader, Deputy Leader and Finance Portfolio Holder attend a Property and Investment Committee (PIC) on a regular basis where they are presented with details of potential economic development and regeneration acquisitions and development schemes. This is also attended by the Chief Executive, the Deputy Chief Executive who is also the S151 officer and the Property and Development Manager. An informed decision is then made by that Sub Committee of Cabinet on whether an economic development or regeneration acquisition/proposal should proceed to the next stage. Those that do go through a further due diligence process is carried out before Cabinet (where required) sign off the acquisition/development and the price/budget. In order to streamline the actual completion process of an acquisition, delegations are given to the Chief Executive, S151 officer, Leader and Finance Portfolio Holder. Economic development or regeneration acquisitions are also capital expenditure and purchases will therefore also be approved by the full Council as part of the Capital Programme.

Future position (Committee System)

Moving forward, the Council is looking to significantly increase transparency around decision making on both future economic development and regeneration investments and our residential development projects which are focused on delivering affordable housing. This includes strengthening governance arrangements at key stages throughout any acquisition or development to ensure the appropriate level of councillor oversight. The aim is to ensure that acquisitions are thoroughly scrutinised, and development projects are kept under review at key ‘project gateways’ and progress against budgets are monitored. A sub-committee will be set up with Councillors to undertake this critical role with external advisors providing advice where necessary..

This is linked and sits alongside a move away from a Cabinet model of governance to a Committee System, with five service committees plus four other committees being for administrative and regulatory matters. It is currently proposed that Assets (acquisitions and developments) will be reporting to the Policy and Resources Committee. The Council has recently finished consulting with residents on this proposed move to a Committee System. If approved by Council, this will come into effect from the Annual Council meeting in May 2021. The governance arrangements set out above will continue until this point in time. Any changes as a result of this move will require this capital strategy to be updated 'in year' to reflect this.

Current arrangements (Cabinet System)



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Treasury Management Appendix 2021/22

1. Capital Expenditure and Financing

1.1 Capital expenditure is where the Council spends money on assets, such as property or vehicles, which will be used for more than one year. In local government, this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling those bodies to buy assets. The Council has some, limited, discretion on what counts as capital expenditure. For example, the Council could set a limit on the amount capitalised and charged to revenue during the year.

1.2 In 2021/22, the Council is planning capital expenditure of £45.8m as summarised in Table 1.

Table 1: Prudential Indicator: Estimates of Capital Expenditure

	2019/20 actual	2020/21 forecast	2021/22 budget	2022/23 budget	2023/24 budget
	£m	£m	£m	£m	£m
Housing & Regeneration	18.6	26.4	35.4	69.7	53.7
Leisure Centre Development	0.8	0.3	7.3	23.3	7.1
Community Wellbeing and Housing	0.8	0.9	1.9	0.9	0.9
Corporate Management	0.1	0.3	1.0	0.1	0.1
Compliance, Waste & Risk	0.3	0.2	0.2	0.1	1.3
Housing Opportunities	57.5	0.3	0.0	0.0	0.0
TOTAL	78.1	28.4	45.8	94.1	63.1

1.3 The focus is on regeneration within the Borough and delivery of our housing investment programme.

1.4 **Governance:** Service managers bid annually around October to include projects in the Council's capital programme. Bids are collated by the Finance Team who calculate the financing cost (which can be nil if the project is fully externally financed). Cabinet appraises all bids based on a comparison of service priorities against financing costs and makes recommendations to Council. The final capital programme is then presented to Cabinet and to Council in February each year.

1.5 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing). The planned financing of the above expenditure is as follows:

Table 2: Capital expenditure financing

	2019/20 actual	2020/21 forecast	2021/22 budget	2022/23 budget	2023/24 budget
	£m	£m	£m	£m	£m
General Fund Reserves	0.8	0.6	1.4	0.2	0.2
Homes England funding	0.0	2.8	0.0	0.0	0.0
Capital Receipts	0.6	0.2	0.3	0.1	0.6
Other funding	0.7	0.8	3.2	0.8	0.7
Total Financing	2.1	4.4	4.9	1.1	1.5
Net Financing Need	76.0	24.0	40.9	93.0	61.6
TOTAL	78.1	28.4	45.8	94.1	63.1

1.6 Debt is a temporary source of finance only, since loans and leases must be repaid. The replacement of debt finance from revenue is through the Minimum Revenue Provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance.

1.7 The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £28.5m during 2021/22. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 3: Prudential Indicator: Estimates of Capital Financing Requirement

	31.3.2020 actual	31.3.2021 forecast	31.3.2022 budget	31.3.2023 budget	31.3.2024 budget
	£m	£m	£m	£m	£m
Opening CFR	1,051.1	1,116.1	1,128.2	1,156.7	1,237.1
CFR - General Fund	65.0	12.1	28.5	80.4	48.5
TOTAL CFR	**1,116.1**	**1,128.2**	**1,156.7**	**1,237.1**	**1,285.6**
Change in financing required	65.0	12.1	28.5	80.4	48.5
Movement in CFR represented by:					
Net Financing Need for the year	76.0	24.0	40.8	93.0	61.6
Less: Minimum Revenue Provision (MRP)	(11.0)	(11.9)	(12.3)	(12.6)	(13.1)
MOVEMENT IN CFR	**65.0**	**12.1**	**28.5**	**80.4**	**48.5**

1.8 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds (capital receipts) can be spent on new assets or to repay debt. The Council is currently also permitted to spend capital receipts on service transformation projects until 2021/22. Repayment of capital grants, loans and investments also generates capital receipts. The Council anticipates receiving £0.25m of capital receipts in the coming financial year as follows:

Table 4: Capital receipts

	2019/20 actual	2020/21 forecast	2021/22 budget	2022/23 budget	2023/24 budget
£m to 3 decimal places	£m	£m	£m	£m	£m
Capital Receipts	0.565	0.148	0.250	0.100	0.576

2. Treasury Management

2.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

2.2 Due to decisions taken in the past, the Council has £1,144m borrowing as at 30 November 2020 at an average interest rate of 2.3%, and £34.6m medium-term treasury investments at an average rate of 3.5%.

2.3 **Borrowing strategy**: When borrowing, the Council's main objectives are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at less than 0.1%) and long-term fixed rate loans where the future cost is known but higher.

2.4 Projected levels of the Council's total outstanding debt are shown below, compared with the capital financing requirement (see above at 1.7).

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

	31.3.2020 actual	31.3.2021 forecast	31.3.2022 budget	31.3.2023 budget	31.3.2024 budget
	£m	£m	£m	£m	£m
Debt	1,110	1,082	1,087	1,127	1,082
CFR	1,116	1,128	1,157	1,237	1,286

2.5 Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from Table 5, the Council expects to comply with this.

2.6 **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that cash and investment balances are kept to a minimum of £50m at each year-end including £10m investments. This benchmark is currently £1,201m and is forecast to rise to £1,393m over the next three years.

Table 6: Borrowing and the Liability Benchmark

	31.3.2020 actual	31.3.2021 forecast	31.3.2022 budget	31.3.2023 budget	31.3.2024 budget
	£m	£m	£m	£m	£m
Outstanding borrowing	1,110	1,082	1,087	1,127	1,082
Liability benchmark	1,049	1,061	1,090	1,170	1,218

2.7 The Council expects to borrow up to or more than its liability benchmark for the current year. Up to now, a deliberate decision has been made to borrow sums at fixed low rates for investment property acquisitions to generate rental streams that will enable increased financial sustainability. In the future, the focus will be on regeneration within the Borough and delivery of our housing investment programme, and capital expenditure and related borrowing requirements will therefore be reduced.

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

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt

	2020/21 limit	2021/22 limit	2022/23 limit	2023/24 limit
	£m	£m	£m	£m
Authorised limit – borrowing	1,250	1,300	1,350	1,450
Operational boundary – borrowing	1,350	1,400	1,450	1,500

2.9 **Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

2.10 The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is, to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments, summarised in Table 8, may be held in pooled funds, where an external fund manager makes decisions on which investments to buy and the Council may request its money back at short notice.

Table 8: Treasury management investments

	31.3.2020 actual	31.3.2021 forecast	31.3.2022 budget	31.3.2023 budget	31.3.2024 budget
	£m	£m	£m	£m	£m
Near-term investments	35	91	91	91	91
Longer-term investments	31	35	40	40	40
TOTAL	**66**	**126**	**131**	**131**	**131**

2.11 **The £35m longer-term investments forecast for 2020/21 includes £32m pooled funds. The COVID-19 crisis resulted in a reduction in the capital value of these funds in March 2020 to £28m, at the time of the first lockdown. This reduction is expected to be temporary and has since partially recovered from the pre-COVID £32m level.**

2.12 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Chief Accountant and staff, who must act in line with the treasury management strategy approved by Council. Half yearly reports on treasury management activity are presented to Council. The Overview and Scrutiny Committee is responsible for scrutinising treasury management decisions.

3. Investments for Service Purposes

3.1 The Council makes investments to assist local public services, including making loans to local service providers, local small businesses to promote economic growth, and the Council's subsidiaries that provides services. The Council will lend to its subsidiaries Knowle Green Estates Ltd and Spelthorne Direct Services Ltd, both of which are used in delivery of services (housing-related and commercial waste respectively). In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to generate a profit overall after all costs.

3.2 **Governance:** Decisions on service investments are made by the relevant service manager in consultation with the Chief Finance Officer and must meet the criteria and limits laid down in the Treasury Management Strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme. Officers and the Finance Portfolio Holder meet on a quarterly basis with the Council's Treasury Management advisers to review both investment and debt portfolios.

4. Commercial Activities

4.1 With central government financial support for local public services declining, the Council has invested in commercial property mainly for financial gain. Total commercial investments are valued at £987m as at end March 2020 (the largest being the BP International Campus site), providing a net return after all costs of 1% (5% gross, before costs).

4.2 The Council has not acquired investment property since 2018/19, after which the Council decided to focus on regeneration and housing objectives. The Council accepted higher risk on commercial investment than with treasury investments. The principal risk exposures include property vacancies and decreases in asset capital value. These risks are managed by having a high specification investment property portfolio, with detailed market and tenant appraisals which started before acquisition, and employment of professional property and facilities management to maintain high property and tenancy standards.

4.3 **Governance:** Decisions on commercial investments are made by the Council in line with the criteria and limits approved by Cabinet in the investment strategy. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme.

5. Liabilities

5.1 In addition to the debt detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £50m). The Council has modelled potential future liabilities on its investment properties to cover future voids, rent free periods and refurbishments and is currently setting aside £7m per annum into sinking funds with an anticipated balance of £20m as at end 2020/21. [figures in this paragraph are to be reviewed]

5.2 **Governance:** Decisions on incurring new discretional liabilities are taken by service managers in consultation with the Chief Finance Officer.

6. Revenue Budget Implications

6.1 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants. As highlighted above, the table below ignores the rental income being generated which is equivalent to about two times the value of the interest being paid on the loans financing the commercial assets.

Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream

	2019/20 actual	2020/21 forecast	2021/22 budget	2022/23 budget	2023/24 budget
£m to 3 decimal places	£m	£m	£m	£m	£m
Net Revenue Stream (£m)	65.640	65.529	65.402	65.924	65.267
Financing costs (£m)	22.945	23.249	23.212	23.188	23.036
Financing as % of net revenue	35.0%	35.5%	35.5%	35.2%	35.3%

6.2 **Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Chief Finance Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable because the objective underlying investment and borrowing decisions is security and liquidity before yield, and borrowing is at fixed rates, taking advantage of low rates currently available.

6.3 **IFRS 16 Leases:** Councillors are reminder that IFRS 16 has been delayed to 1 April 2022, as noted in a CIPFA LASAAC Statement on the Deferral of the Adoption of IFRS 16 Leases. In the meantime, and in preparation, officers will be conducting a balance sheet review of the financial impact on the Council, its capital strategy, TM strategy and revenue budgets, with the aim to report on this in July 2021. As part of that process, *de minimus* levels on leases will be determined so that the impact on revenue is budgeted for effectively, and that capital impacts are authorised appropriately.

[END]

Our commercial investment activity

1.1 Since 2016, the Council has made a number of prime commercial investments, all of which are in the Heathrow economic area. The Council considers that defining an economic area restricted to Spelthorne only is to ignore the reality that Heathrow Airport is the real driver of the economy for West London, North Surrey and the Thames Valley. We are part of that economic zone and the airport plays an important role in our local economy. 7% of our residents (6,700 in 2018) work at Heathrow, and this figure increases to 25% in our two northernmost wards. For every 10 direct jobs at Heathrow, there are 26 jobs created locally within the supply chain. The airport also contributes significantly to local training and education. For example, the Heathrow Academy provides training to those wanting to work at the airport, schools outreach programmes are used to promote STEM subjects, and the Heathrow careers fair attracts around 7,000 young people annually.

The future expansion of the airport is something that the Borough has supported for a number of years, as long as the proposed scheme comprehensively and effectively mitigates the impacts on our communities, businesses, services and environment.

1.2 **An overview of our assets and approach**

The Council has chosen to invest in best-in-class assets located in the Heathrow economic area and are very well sited next to transport hubs.

Illustration 1: Location of our commercial assets

Investment Criteria

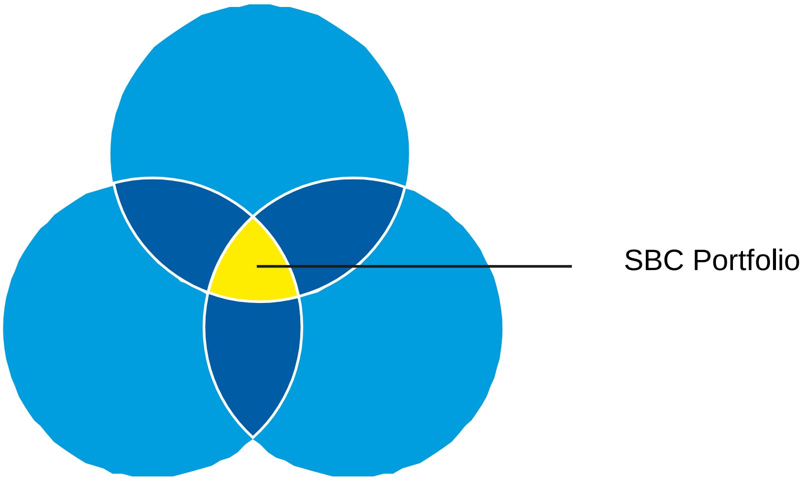

Illustration 2: Factors shaping our investment decisions

1.3 The Council has invested in properties that have attracted a strong and diverse tenant mix from different sectors of the economy. These are blue-chip tenants which provide good levels of security for the Council's investment activities.

1.4 **Repayment allocation - as at August 2018**

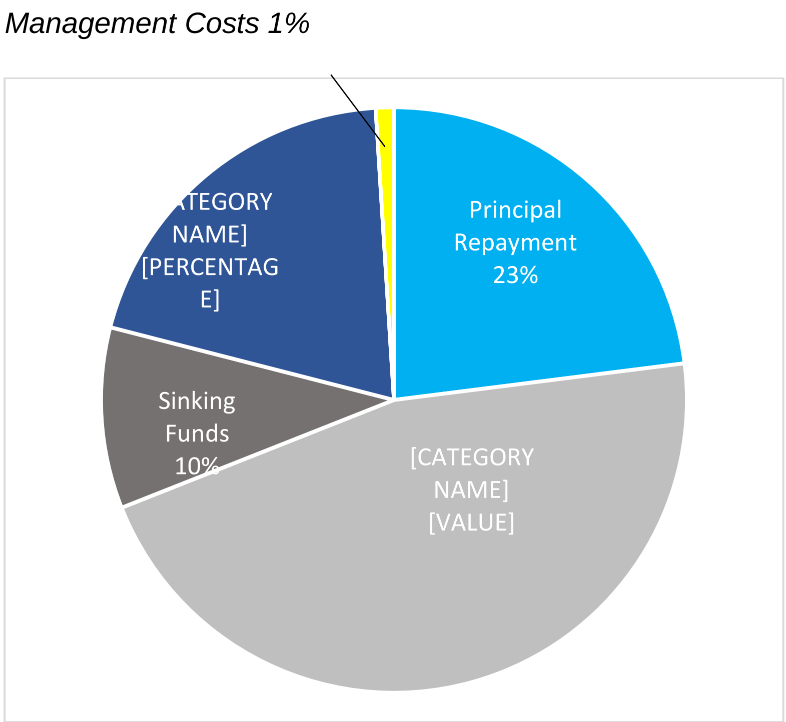

illustration 3: How loans are repaid and money allocated

The income from our investments (see Table 1, above) has made a substantial impact on the stability of the Council. In 2020/21 the net surplus (after making allowances for management costs, interest etc.) will be £9.9m.

1.5 **Our reasons for investing**

In order to fund our developments we have acquisition parameters, which are set out in full in *Appendix 2***,** but these are the primary reasons we have previously invested:

- to generate income to offset reducing Government funding and other pressures in order to support provision of services for residents
- for housing development
- for strategic purposes to allow for regeneration either now or in the future.

Having achieved our objective of significantly boosting our income to support provision of services, our focus is now on the second and third objectives set out above. It is also important to note that we maintain the assets which we purchased in 2016-2018 and which support the revenue budget. We regularly review and update our acquisition parameters.

What if we had not invested?

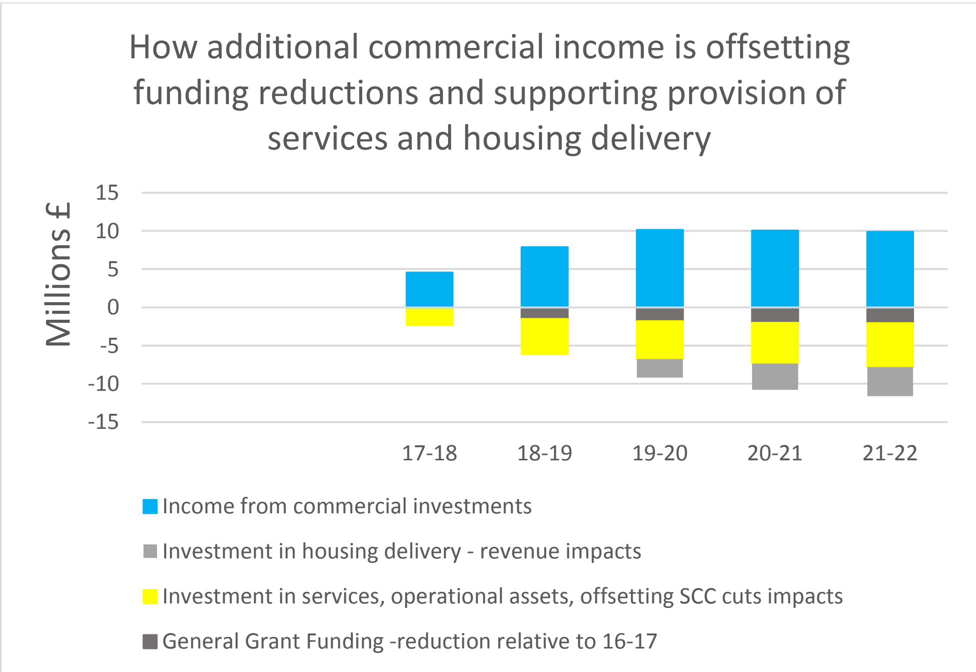

Table 1 : Increase in property income to offset decline in government funding

2.1 **Our Investment so far**

If the Council had not taken the decision to invest to deliver significant commercial income from 2016-2018, this would have led to major cuts in services, particularly the services we are not under a statutory duty to deliver such as:

- Day Centres (net cost of £452.800)
- Meals on Wheels (net cost of £30,100)
- Spelride Community Transport net cost (£153,700)
- Extension of the Greeno Centre (additional £130,000 capital investment) and the Fordbridge centre (£130,000 capital investment) to provide additional facilities for older people
- New Meals on Wheels vans (£126,000) or Spelride vehicles (£250,000)
- Laleham Park Pavilion (£250,000 capital investment)

2.2 It would also have led to a reduction in the overall capacity of the Council to deliver for residents, leading to:

- Reduced maintenance of parks and open spaces
- Reduced waste collection frequency
- No ability to Increase budget for planned maintenance of frontline operational assets supporting service delivery (up to an additional £750,000 per annum)
- Need for revenue contributions to capital expenditure to cover projects not financed by grant, receipts or generating revenue savings/income (£750,000 per annum)
- Increased fees and charges, such as significantly increasing car parking charges
- Inability to plug the considerable gaps which are emerging as a result of Surrey County Council cuts on social care services (estimated impact on Spelthorne budget to date is approximately £500,000)

Some of these cuts would have hit older and vulnerable residents the hardest.

The additional income the Council has generated has enabled us to put our Revenue budget on a more sustainable footing by ceasing to use reserves to support the Revenue Budget (In the 2016/17 Budget - £786,000 needed to be taken from reserves)

KPI	Risk Category	Responsibility	Frequency	Purpose	Comments
Portfolio Capital Growth	Fund	Asset Management	Annual	To measure the long term capital performance of the fund	A=Previous Valuation B=Current Valuation **(B/A)-1 = Capital Growth**
Net Initial Yield	Fund	Asset Management	Annual	To ensure a sufficient income return after interest / loan repayment	A=Rental Income B=Capital Value **A/B = Yield**
Sinking Fund Net Income Cover	Fund	Asset Management	Annual	To establish the amount of cover in months of the triple net income provided by the sinking fund.	A=Sinking Fund B=Triple net income **A-B=Rent Cover**
Investment Cover Ratio	Fund	Asset Management	Annual	To establish the total net income from property investments compared to the interest and loan repayment expense	A=Net Income B=Cost of Debt **1: A/B = Investment Cover Ratio**
Vacancy Rate	Income	Asset Management	Quarterly	To monitor vacancy levels to ensure income is protected	A=Total Accommodation Let B=Total Portfolio Accommodation **1-(A/B) = Vacancy Rate by Floor Area** A=Total Net Rent Received B=Total Market Rent **1-(A/B)=Vacancy Rate by Market Rent**

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