

The Capital Strategy of Spelthorne Borough Council

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1. Introduction

This document sets out Spelthorne Council's Capital Strategy. It gives residents 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](#):

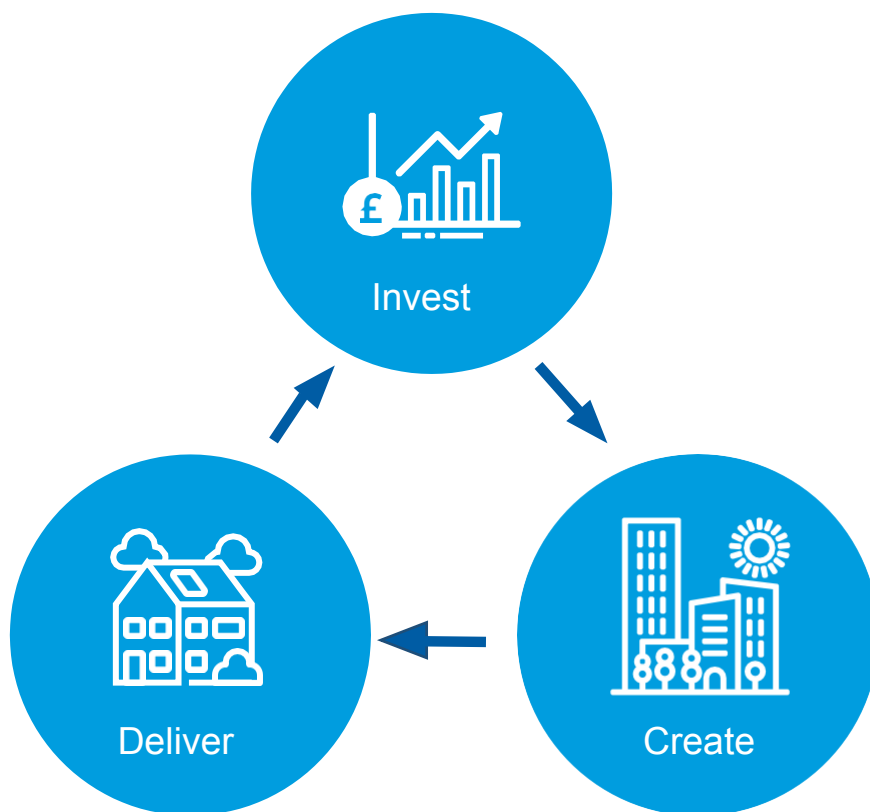
- **To deliver much-needed housing** in order to help reduce homelessness locally, increase affordable provision and help meet the overall need for additional homes
- **To regenerate our town centres** so that we can contribute to the economic development of the Borough

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. Capital expenditure can include everything from repairing a roof or purchasing a piece of equipment 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, our Capital Strategy is to **Invest, Create, Deliver**.



- We are **Investing** in commercial property which will deliver an ongoing sustainable income stream to support development activity
- We are **creating** new housing for residents and regenerating our town centres in particular Staines-upon-Thames
- We are **delivering** the affordable homes which the market fails to provide and we are prioritising people who are on our Housing Register

2.2 Beyond housing, our Capital Strategy will also help us meet our need to upgrade and maintain:

- Operational buildings
- Infrastructure in the borough
- Our vehicle fleet

- Our ICT infrastructure

2.3 Our duty to look after public money

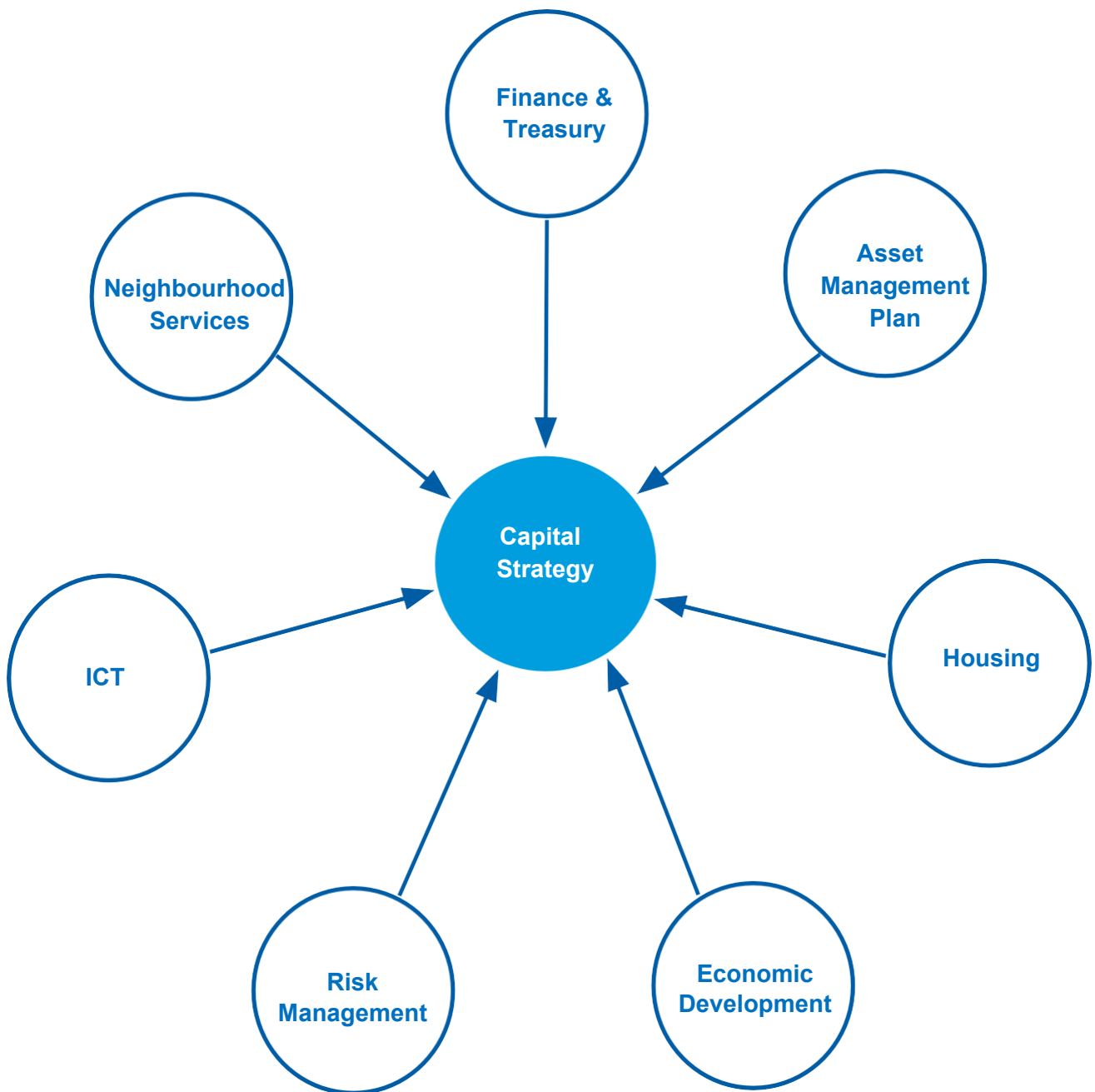
As a Council, we have a duty to look after the public purse, and residents and businesses expect us to do so in a sensible and rational way. This Capital Strategy will demonstrate how we:

- **Finance our spending** through prudent borrowing or use of reserves (called capital financing) within the upper level of our borrowing (called the external debt boundary)
- **Spend wisely and safely**, especially in relation to the investment portfolio that we hold (called commercial activity)
- **Manage risk and make decisions**, ensuring we have the appropriate skills and expertise, and taking a measured approach to investment
- **Ensure we have enough money** immediately to hand to keep services running on a day-to-day 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 financial sustainable in the future (this is another [Corporate Plan](#) priority), something that is especially challenging in the current financial landscape.

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

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



3.1 The Council already has a number of 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.

3.2 **An overview of our individual strategies**

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
- 3.4 **Treasury Management 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
- 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. (Link to follow)
- 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.

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

4.1 **Our sources of income**

The Council gets its money from a variety of sources – for 2020/21, our revenue funding is coming from:

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 investments	9,924,800	41
TOTAL	23,898,400	100

Table 1: Sources of income

4.2 What we fund

Our income is used to fund the range of services we provide – for 2020/21, this covers:

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
TOTAL	23,898,400	100

Table 2: Funding of services

4.3 Our capital expenditure plans

In 2020/21, the Council is planning capital expenditure of £65.6m as summarised below:

	2018/19 ACTUAL £m	2019/20 FORECAST £m	2020/21 BUDGET £m	2021/22 BUDGET £m	2022/23 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	0.1
Environmental	0.2	0.5	0.2	0.1	0.1
TOTAL	381.1	67.7	65.6	102.8	57.8

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

4.4 Our capital projects include:

- Investment property acquisitions to generate revenue income streams
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)
- Leisure centre refurbishment / development (original budget estimate for initial fees: £2m.
- Various corporate projects including facilities improvements and IT (including 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 planned financing of the above expenditure is as follows:

Where our borrowing comes from

	2019/20 AS AT END OF DEC 19	2019/20 REMAINDER £'000	2019/20 BUDGET £'000	2020/21 BUDGET £'000	2021/22 BUDGET £'000	2019-22 TOTAL £'000
Public Works Loan Board	5,000	33,000	38,000	14,000	21,000	73,000
Of which to be used for refinancing existing debt	0	0	0	0	0	0
Other sources	29,500	0	29,500	30,000	60,000	119,500
Of which to be used for refinancing existing debt	0	0	0	0	0	0
Total PWLB and other sources	34,500	33,000	67,500	44,000	81,000	192,500
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	34,500	33,000	67,500	44,000	81,000	192,500

Table 4. Source of borrowing

4.7 Background

Since 2013 the Council has seen a year-on-year reduction in the funding we receive from central government.

Making up the shortfall

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

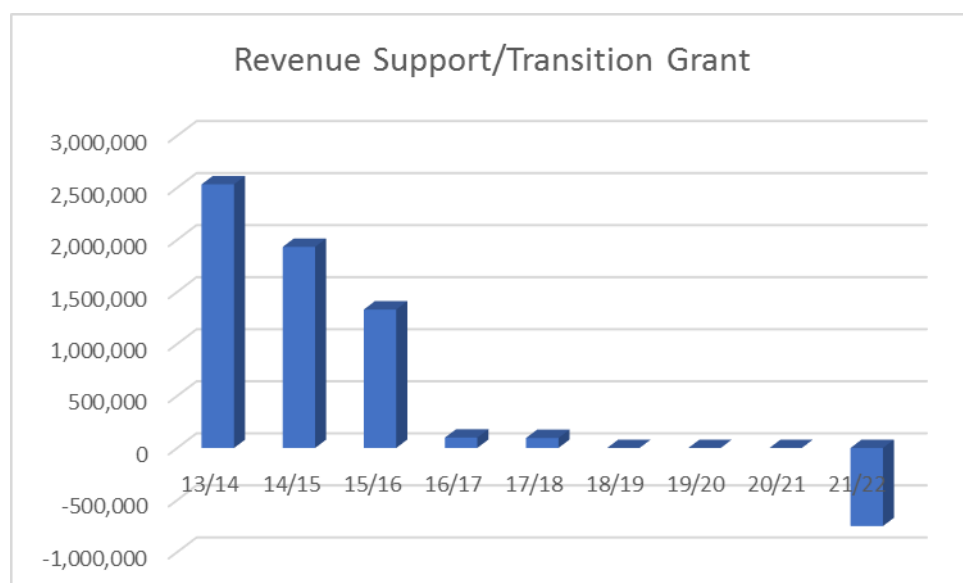


Illustration 1: Reduced Government funding

4.8 Our investment so far

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.

- 4.9 Total commercial investments are currently valued at £999m, providing a gross average return of 5.03%. 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	£m	Purchase Date	Valuation as of March 2019 £m

BP Campus, Sunbury Business Park	Sunbury	Offices	385	Sep 2016	389
12 Hammersmith Grove	London	Offices	170	Jan 2018	171
Charter Building	Uxbridge	Offices	136	Aug 2018	136
Thames Tower	Reading	Offices	127	Aug 2018	127
The Porter Building	Slough	Offices	73	Aug 2018	71
World Business Centre 4	Heathrow	Offices	47	Sep 2017	47
3 Roundwood Avenue	Heathrow	Offices	21	Jul 2017	21
Communications House	Staines	Offices	11	Jul 2018	15
Summit Centre	Sunbury	Offices	14	Sep 2019	14
Elmbrook House	Sunbury	Offices	7	Dec 2016	8
Station Road	Sunbury	Offices	0.4	Mar 2018	-
Total			991.4		999

Table 5: The Council's commercial assets portfolio

4.10 On our commercial asset acquisitions, the overall initial net yield is 5.03%. As there is upwards 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 2020/21 will be £9.4m per annum.

5 What if we had not invested?

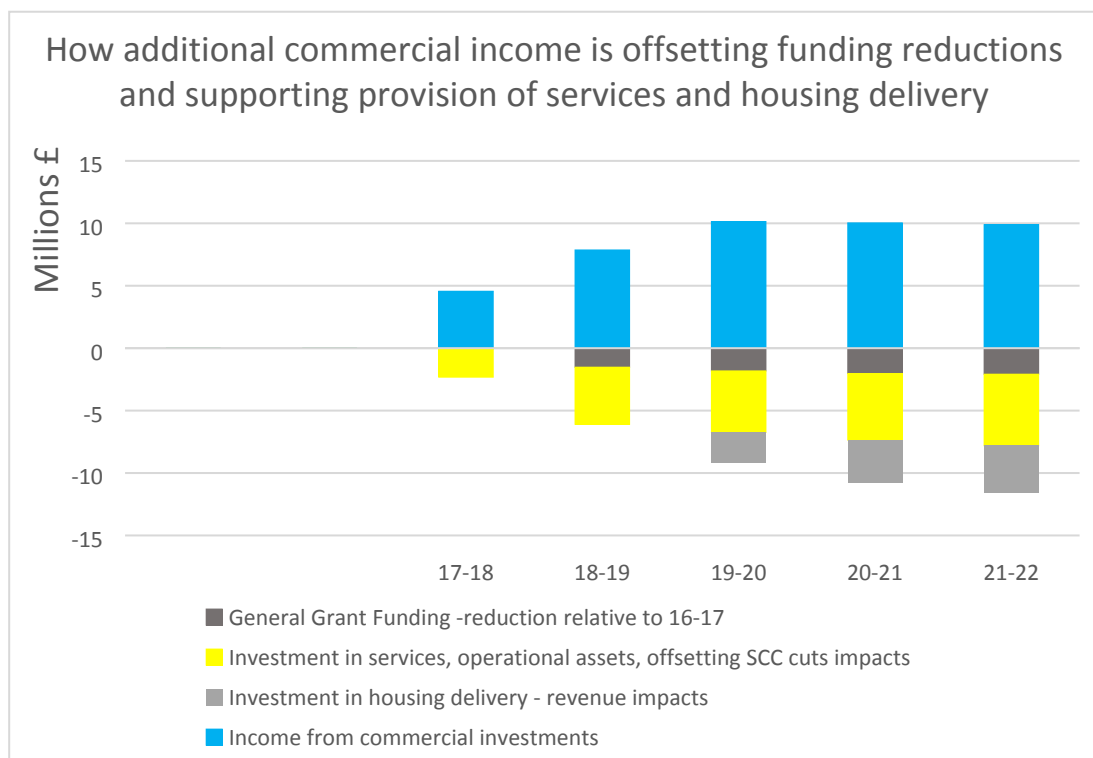


Table 6 : Increase in property income to offset decline in government funding

5.1 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 (additional £130,000 investment)
- New Meals on Wheels vans (£126,000) or Spelride vehicles (£250,000)
- Laleham Park Pavilion (£250,000 capital investment)

5.2 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)

6 Our commercial investment activity

- 6.1 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.

6.2 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 2: Location of our commercial assets

Investment Criteria

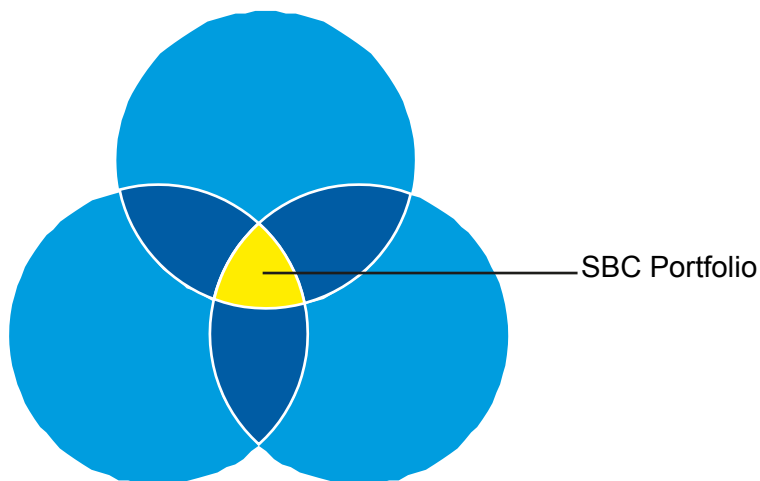


Illustration 3: Factors shaping our investment decisions

6.3 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.

6.4 Repayment allocation - as at August 2018

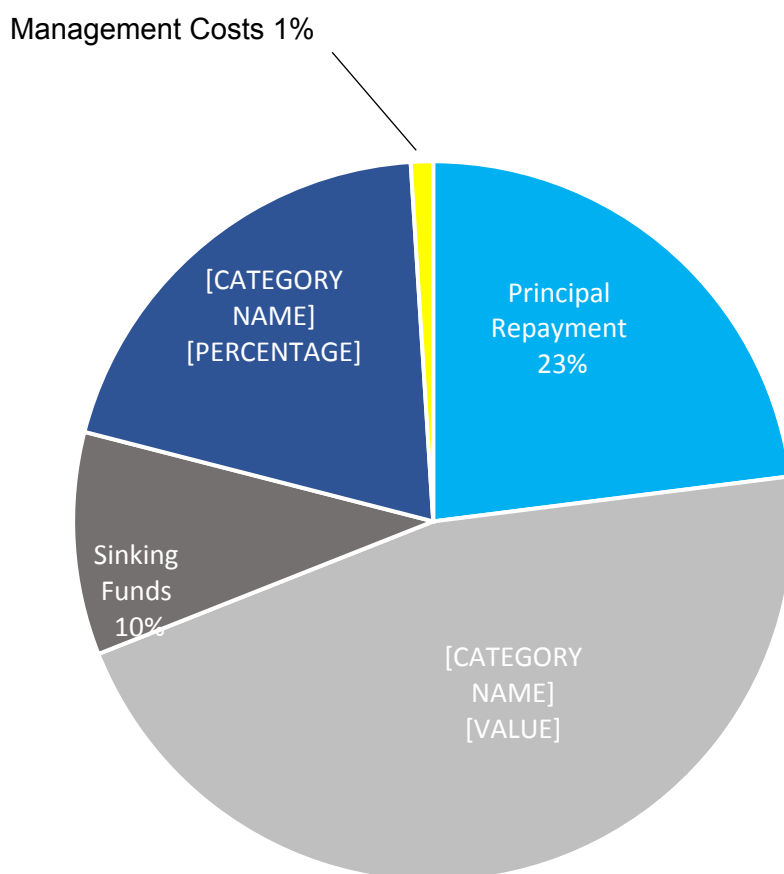


illustration 4: How loans are repaid and money allocated

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.

6.5 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.

7 The focus on housing and homelessness

- 7.1 The focus of the Council was previously to generate revenue in order 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.
- 7.2 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.
- 7.3 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.
- 7.4 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:
- **Increasing numbers on the Housing Register:** Over the period 2015 to 2018 the number of applicants on the Council's Housing Register has grown by 79%. See *Appendix 3 Table H1*
 - **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 19%. See *Appendix 3 Table H2*

- **High rates of statutory homelessness:** 69% of homeless households include children. See *Appendix 3 Table H3*
- **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 2018/19 was 111 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
- **Increasing affordability issues:** ratio of the median house price to the median wage eased slightly in Spelthorne in 2018/19, the gap widened regionally and nationally. 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 provision over the past four years has been just 158 units – an average of 32 per year. See *Appendix 3 Table H6*

7.5 The effect of our proximity to London

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.

7.6 Heathrow expansion

Another key issue that will have a significant impact on our community is the proposed third runway at Heathrow airport and the major expansion of works which are planned for Heathrow. Work on various parts of the airport and the surrounding infrastructure is likely to go on for around nine years (but could extend to several decades before final completion). This will introduce further pressure as people working on the Heathrow expansion seek to be housed close to their workplace.

Some joint work has already been undertaken across a number of Councils to understand the potential impact 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.

7.7 Key worker accommodation

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 2016, the latest records available, the mean income for employed households within Spelthorne is £34,669, although the starting salaries for essential local workers is much less. Whilst this 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. The Council is seeking to tackle this through our housing company Knowle Green Estates Ltd (paragraph 7.12).

7.8 Strategic objectives

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 in order to support housing investment.

As detailed above (see section 2), the Council's strategic objectives are to **invest, create, and deliver**.

7.9 Subsidies are key

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.

7.10 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 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.

7.11 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.

7.12 Spelthorne's Housing Development Programme

Spelthorne has a pipeline of properties for residential development:

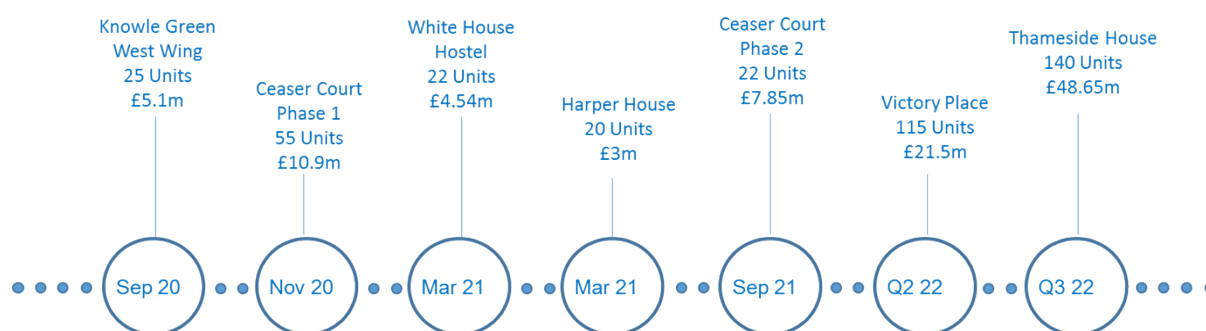


Illustration 5: Projected funding

7.13 Knowle Green Estates Ltd (KGE)

The Council formed its housing company in 2016 when we acquired Harper House in Ashford for emergency accommodation. Since then, the Council has made numerous improvements to make Harper House a safer and better managed solution for families who have been made homeless. 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.

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 20% 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 3,218).

7.14 Development costs

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.

8 The focus on economic development

- 8.1 Economic development 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.

8.2 Significant progress

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.

- 8.3 The Council has significant landholdings in Staines-upon-Thames, and has made a number of recent acquisitions in line with our investment parameters to further cement our position. We bought back the long leaseholds of both Communications House 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. We will continue to acquire properties 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.
- 8.4 Further work needs to be done in Staines-upon-Thames and that there is considerable scope for improvement around Sunbury Cross. So the aspirations of the Council should therefore be bold and ambitious. We have followed this ambition through by recently be acquiring (also in 2019) the Summit Centre in Sunbury.

8.5 Planning to meet housing need

The current review of the Council's Local Plan has identified a need to create around 603 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

8.6 Following a Sustainability Appraisal, the professional opinion was that the fourth option (combination) should be taken forward, but with additional safeguards to take account of the public's views on loss of Green Belt. This has been agreed by Cabinet. Within this option, the focus will need to remain very much on realising the considerable latent potential of Staines-upon-Thames (but not to the absolute exclusion of housing development anywhere else in the borough).

The Strategic Housing Availability Assessment (SLAA) 2018 estimates that the 5-year housing land supply in the Borough is 3,448 units on 64 sites. Over 1,420 of these units are expected to be delivered in Staines-upon-Thames, with at least 420 to be delivered on Council-owned sites. In the medium term (6 to 10 years), Council-owned sites could deliver another 1000 units (with other sites not owned by Spelthorne bringing forward approximately 250).

8.7 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 solution for the town. Work on the Master Plan is expected to be complete in spring 2021.

8.8 The Council's landholdings within the town centre (including our recent strategic acquisitions) provide a clear opportunity to bring forward at least 1,420 units 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).

8.9 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 hostel	Years 1 – 5

Riverside car park (subject to re-provision)	flatted	100 units	Years 6 – 10
Elmsleigh Centre and adjoining land	flatted	650 units	Years 6 - 10

Table 7: Minimum housing units identified to develop

8.10 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

9 How we finance our capital spend

9.1 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

- 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
- Following the hike of 100 basis points in PWLB rates (work actually commissioned before the rise) the Council commissioned its treasury management advisers to review its debt portfolio and options for funding future capital expenditure. The advisers are currently evaluating a number of options. However, it is the case that PWLB and loans from other councils will continue to be an important funding source

10 How we manage risk and ensure sound decision-making

10.1 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.

10.2 Risks

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
- 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

10.3 We are also very clear on how we spread risk by diversifying the commercial assets portfolio. In any commercial property portfolio, it is important to achieve a level of diversification in order to ensure that 'not all of our eggs are in one basket'. Portfolios can be diversified by property type (e.g. office, residential, industrial or retail), sector (e.g. pharmaceutical, media or financial technology) and geography (e.g. local borough or Heathrow). The Council's portfolio is heavily weighted towards the south-east office market, but the tenant mix is diversified. We have more recently on a small scale acquired some light industrial units, to help diversify the mix.

10.4 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 6) to ensure the portfolio is performing as we want it to and is monitored. This will allow us to take appropriate action as required.

10.5 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.

10.6 **Skills**

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 2020 we will be doing some refresher training sessions on risk management for officers.

10.7 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 are increasing the resilience of our insurance

functioning by bringing in, from March 2020 London Borough of Sutton's larger insurance team to provide support on claims handling management. This gives us access to a larger pool of expertise

10.8 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), Landid (asset 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.

10.9 **Governance**

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). All property acquisitions are overseen by a small group of senior councillors and officers. This group forms the Property and Investment Committee including the Leader of the Council, who has a background in property investment and the Finance Portfolio Holder. Councillors are involved at key stages of the process (which is set out at the end of *Appendix 4*). As part of the Council's preparations for implementing the new CIPFA Financial Management Code, in February 2020 the Council is running a workshop with CIPFA to review the extent to which its governance arrangements are contributing towards resilience. In June 2020, at the Council's invitation, the LGA will be undertaking a review of our finance and property arrangements to help the Council identify further opportunities for improvement.

10.10 The Council is committed to following local government guidelines and we take appropriate legal and technical advice to ensure we are always doing so.

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

11.1 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.

11.2 Current borrowings

Based on acquisitions and investment decisions up to 31 December 2019, the Council currently has £1,085m borrowing (£1,114m full year forecast) 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.

11.3 Factors shaping our borrowing decisions

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.

11.4 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.

11.5 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.

11.6 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.

11.7 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 2020/21 revenue budget).

- 11.8 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 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 a best 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.
- 11.9 The Council has put 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.

APPENDICES

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