

Council

23 February 2023



Title	Capital Strategy 2023/24
Purpose of the report	To approve the report
Report Author	Sam Masters Treasury Management and Capital Accountant
Ward(s) Affected	All Wards
Exempt	No
Corporate Priority	Community Affordable Housing Recovery Environment Service Delivery
Recommendations	<p>Council is asked to approve the recommendations below, as agreed at the Corporate Policy & Resources Committee meeting on 20th February:</p> <ol style="list-style-type: none">1. the Capital Strategy as set out in this report2. that all development and investment projects, along with all significant projects follow the previously approved business case governance process as set out in section 11 of this report3. that no financing sources, unless stipulated in regulations or necessary agreements, are ring fenced4. the Council plans to continue its use of capital receipts to fund the costs of eligible proposals (subject to full business cases for each project).5. the financing of the Capital Programme and revenue implications as set out in section 14 of this report.6. the financing of the Capital Programme being delegated to the Corporate Policy & Resources Committee to provide sufficient flexibility to allow for the most effective use of Council resources
Reason for Recommendation	The Council is required by law to approve before start of each financial year a Capital Strategy for the medium to long term setting out its approach to identifying needs for capital expenditure, managing capital expenditure, financing it, and managing risks associated with delivering capital objectives.

	<p>When long term investment decisions are undertaken, decision makers can rely on clear and informed information. This would include:</p> <ul style="list-style-type: none"> • A long-term view of capital expenditure plans and any financial risks to which the Council is exposed. • Ensuring due regard to the long-term financing, affordability implications and potential risks. • A clear overview of the Council's asset management planning arrangements and any maintenance requirements that have resource and business planning implications. <p>The Capital Strategy will continue to help support informed decision making in the delivery of Spelthorne Borough Council's long-term plans and ambitions.</p>
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1. Executive Summary

- 1.1 The report sets out the Council's Capital Strategy for 2023/24
- 1.2 The Capital Strategy has been updated to reflect the significant change to strategic approach agreed at Extraordinary Council Meeting (ECM) on 2nd February 2023 which was focused on ensuring the long term financial viability of the Council's housing delivery programme, underpinned by 50 year viability modelling. Whilst some of the analysis and tables in the Strategy are aligned with the proposed Capital Programme for 2023/24, the Strategy is seeking to look longer term in terms of ability of the Council to identify and fund its capital needs. Parallel to this, the Council will be updating its Sinking Funds reserves modelling over the next 50 years.
- 1.3 During the ECM a significant amount of funding was secured from Homes for England totalling some £54.9m. This, along with other capital receipts, grants and contributions, means that circa 27% of the scheme will be funded from non-borrowing sources, up from 6% in 2022/23, greatly reducing the council's reliance on external borrowing. Funding streams total £100.6m.
- 1.4 The proposed Capital Programme, as detailed in Appendix A, proposes a gross budget of £446.4m and a net budget of £345.8m after funding.
- 1.5 The Council's long term capital investment is underpinned by the objectives of the Corporate Plan. Capital proposals are considered within the Council's overall medium to long-term priorities, and the preparation of the Capital Programme is an integral part of the financial planning process. This includes taking full account of the revenue implications of the projects as part of the revenue budget setting process.
- 1.6 In addition to the capital budgets and revenue implications, the report sets out the following:
 - (a) Policy and contextual background
 - (b) The Council's asset base
 - (c) Delivery Strategies
 - (d) Budget setting and prioritisation

- (e) Governance
- (f) Key projects and programmes
- (g) Capital funding
- (h) Risk management

2. Policy and Contextual background

2.1 Spelthorne Borough Council's Corporate Plan 2021 to 2023 provides the starting point for this document, dealing with our five priorities:

- (a) Community
- (b) Affordable Housing
- (c) Recovery
- (d) Environment
- (e) Service Delivery

2.2 The Capital Strategy helps to underpin these plans.

2.3 In 2016, the Council embarked on an ambitious capital programme with a plan to invest over £1bn in investment properties, to generate sufficient funds to:

- (a) Support Council services
- (b) Support the regeneration and transformation of the Borough
- (c) Deliver much needed affordable housing for our younger residents and families in the Borough.

As part of investing for the future success and wellbeing of the population, and all its stakeholders in Spelthorne.

Since 2018/19 the focus of the Capital Strategy has been on a) managing effectively investment assets already acquired but not purchasing any more and b) delivering an ambitious housing (mainly affordable and key worker rental) programme and service capital schemes such as the new Leisure Centre.

2.4 As at the 31 March 2022 the draft unaudited accounts show that the Council had total assets with a net book value as shown in the table below:

Asset type	£000
Land & Buildings - Municipal	85,540
Vehicles Plant & Equipment	1,760
Community Assets	191
Assets under Construction	42,220
Heritage Assets	215
Investment Property	916,375
Intangibles	337
Total	1,046,638

- 2.5 The majority of the capital expenditure is planned to be spent on land and buildings to provide affordable and keyworker housing through Knowle Green Estates Ltd. (KGE) the Council's wholly owned subsidiary and temporary accommodation through the Council. Private rental accommodation will be provided at Thameside and Benwell Phase II. The other significant capital scheme is the new Leisure Centre currently under construction with an expected completion in summer 2024.
- 2.6 All the land and building acquisition costs together with all design and construction expenditure incurred prior to completion of the final premises are included in the above table and will move into the appropriate category once the project is completed.
- 2.7 The Council has a planned maintenance budget for these properties.
- 2.8 The COVID-19 pandemic and global economic downturn has impacted on the Council's asset valuations and the investment property portfolio has seen a further decrease of £23.m as at 31 March 2022 (£51.9m as at 31 March 2021). Following on from the Pandemic we are now experiencing a cost of The Council, as a long term holder of assets has no immediate plans to sell off any of its properties and over the long term the value of property has always performed well. However over the short term values have suffered because of the COVID-19 pandemic, inflationary cost and the general economic downturn. However, in line with refreshed Chartered Institute of Public Finance and Accountancy guidance whether considering major investment decisions relating to individual assets as part of the options appraisal process disposal will be considered as one option.

3. Key projects

- 3.1 There are several key projects and programmes that require future capital investments for the Council to achieve its strategic goals and these are shown below:
- (a) Several large-scale developments to deliver 558 apartments as part of our Housing Strategy and commitment to the residents of the Borough, particularly young families.
 - (b) A new leisure centre in Staines-upon-Thames the first of its kind being built in the UK to Passivhaus standards, to deliver a greener building, to protect the wellbeing of our residents over the coming years and making the building carbon neutral.
 - (c) Continued investment in municipal infrastructure, such as local parks.
 - (d) An ongoing investment in digital transformation, where we aim to utilise technology to continue to deliver efficient, good quality services.
- 3.2 Our Capital Programme's delivery objectives continue to take place against a background of financial challenges. The potential impact of the Fair Funding Review could have a significant negative impact on the Council and some difficult decisions lay ahead, as the Council looks to ensure that despite further funding pressures it may encounter it can continue to ensure balanced budgets across all four years of the Outline Budget period.
- 3.3 It is therefore vital that the Council's Capital Strategy delivers a return on investment that is financial, such as capital receipts or new revenue streams, or delivers key strategic priorities

3.4 The Capital Strategy is intended to evolve each year, it is a dynamic plan that will respond to threats, opportunities and will change over time. For example the need to invest in Climate Change mitigation and de-carbonisation measures will become increasingly important.

3.5 The strategy is set over 5 years but is updated annually and includes short-, medium- and long-term investment revenue streams, or delivers key strategic priorities.

4. Our delivery strategies

4.1 The Council’s capital programme is categorised into four main areas, the net costs per area and detailed below.

- (a) Regeneration £49.9
- (b) Affordable and keyworker housing £288.2m
- (c) Efficiency £1.5m
- (d) Operational £6.2 m, including decarbonising the Council’s service delivery.

<p>Ongoing Investment Assets and Regeneration Assets Portfolios</p> <ul style="list-style-type: none"> • Support Council services • Invest in regeneration projects • Provide for the future 	<p>Affordable and Keyworker Housing</p> <ul style="list-style-type: none"> • Regeneration of key strategic sites • Provide affordable housing for the residents of SBC
<p>Efficiency</p> <ul style="list-style-type: none"> • Produce ongoing revenue savings and additional income • Digital transformation enabling residents to have better access services 	<p>Operational</p> <ul style="list-style-type: none"> • Reduce running costs • Greener outcomes • Rationalise property portfolio

5. Regeneration

For 2023/24 – 2026/27 the Council requires £49.9m to support the regeneration and transformation of the Borough. These are non-housing schemes to transform the built environment.

6. Asset Management Plan

6.1 The 2020/21 Asset Management Plan for our current property portfolio is available on the Spelthorne Borough Council’s website <https://www.spelthorne.gov.uk/article/19655/asset-management-plan>

7. Affordable and Keyworker Housing developments

7.1 For 2023/24 – 2026/27 the Council requires £288.2m to develop the following properties and deliver 558 apartments based on the Cabinet meetings in February to April 2021 (these number are continuing to evolve) as shown below:

- (a) Oast House – 184 affordable rental apartments
 - (b) Ashford MSCP site– 48 affordable rental apartments
 - (c) Victory Place– 127 key worker and affordable apartments
 - (d) Benwell Phase 1 – 55 private rentals. Apartments (Delivered)
 - (e) Benwell Phase 2 – 39 private rental apartments
 - (f) Thameside – 105 private rental apartments
 - (g) Total - 558 apartments
- 7.2 Upon completion these properties (other than Thameside and Benwell II) will be transferred, at cost to Knowle Green Estates Ltd (KGE) who will own and manage the buildings and tenants.
- 7.3 Going forward, it is Council strategy to continue to build new affordable homes across the Borough, where suitable, affordable premises can be found, this could also include existing houses that are suitable for multiple occupancy.
- 7.4 Each case will be evaluated on its own merits and consider how it assists the Council to achieve its Housing Strategy for residents, in the Borough.
- 8. Knowle Green Estates Ltd (KGE)**
- 8.1 KGE is a wholly owned subsidiary of Spelthorne Borough Council and following a restructure of its property portfolio in the year end 31 March 2020, effectively started from scratch.
- 8.2 The Company has been established to manage each property as mentioned in 7.2 above and is looking at a 50-year time horizon for its properties.
- 8.3 The model approved by the KGE Board is based on the meetings with Cabinet between February and March 2021 and provides most of its apartments for affordable housing.
- 8.4 Affordable Housing tenants will include:
- (a) Key workers, nurses, police, and teachers
 - (b) Younger residents
 - (c) The elderly and vulnerable
- 8.5 There will be a small element of private rental tenants.
- 8.6 The Council is introducing a new Componentisation Policy, in accordance with the CIPFA accounting code, to use different rates of depreciation for each component of the building, e.g., land at 0% and roof 4%, which reflects the different useful economic lives of each component part of the building.
- 8.7 Whilst the initial 50-year projections indicated that KGE would be able to provide substantial revenue contributions to SBC over the period and given the profiling of our tenants, will be operating on a small cash surplus based on the properties being delivered to time and to the number of apartments specified, the impact in 2022 of rising construction inflation, and rising interest rates has required the Council and company to revisit the model to ensure it continues to be financially sustainable
- 8.8 The Extraordinary Council Meeting on 2nd February 2023 considered the viability challenges and agreed a new strategy including seeking to maximise

Homes England grant funding for affordable and key worker units, increasing the number of units to be delivered across the portfolio and a capital injection into KGE.

9. Efficiency

- 9.1 The £1.5m of schemes in this category include improved use of technology to support our car parks and improve the customer experience, as well as investing in IT network storage upgrades and new hardware for improved ways of working.

10. Operational

- 10.1 The Council's operational capital strategy amounting to £6.2m is centred on capital improvement works to the Council's operational asset portfolio. This falls into two main categories:
- (a) Land and Buildings, includes new community assets including toilet facilities, extensions to our day centres and new pavilions in our parks.
 - (b) Infrastructure, this includes new flood defences along the River Thames, replacement refuse vehicles and improvements to the River Ash broad walk improvement.
- 10.2 The main objectives of the operational element of the Capital Strategy are to ensure assets meet health and safety standards, are fit for purpose in terms of statutory guidance and legislation, as well as helping the Council to reduce costs and reduce its environmental footprint.
- 10.3 Another key objective of the operational element is to ensure that the Council continues to invest in its current buildings and long-term assets to avoid incurring significant future costs. As well as our municipal buildings, we have other operational assets, including vehicles, plant, and equipment.
- 10.4 The Council has a scheduled programme of condition surveys which ensures the Council's operational estate is fit for purpose.
- 10.5 Every 5 years on a rolling basis, the Council will review its municipal and land and buildings to identify sites, were there are development opportunities for both the Council and others, such a small strip or parcels of land, as well as, looking to pass over the running of community assets, such as village halls, to the community.

11. Governance

- 11.1 The main forum for reviewing all financial aspects of the Capital Programme is the Corporate Policy & Resources Committee who will make recommendations to Council.
- 11.2 The Development Sub Committee looks after the Council's investment, development and regeneration properties and makes recommendations to the Corporate Policy & Resources Committee
- 11.3 The Corporate Policy & Resources Committee review the strategic direction of the Capital Programme, ensures outcomes are aligned with a viable Business Case and that Value for Money (VfM) is delivered for the Council. It also monitors the expenditure and funding requirements of the capital programme and subsequent revenue impacts.

- 11.4 All business cases will require approval by Corporate Policy & Resources Committee and although development projects may have a budget allocation in the capital programme the approval to draw down the budget will only be obtained via Corporate Policy & Resources Committee approval and will align to the business case stage the project is at.
- 11.5 Assessment of the business cases will ensure that all aspects of a potential schemes are analysed and the impact on all the Borough's stakeholders identified. Therefore, the Council will be able to gain a full understanding on how a specific scheme will comply with the current Corporate Plan, and how it will influence the Council's overall strategy, local business economy, residents, officers, and impact on the resources of the Council.

12. Capital Funding

12.1 The Council is required to have a funded capital programme that is affordable, i.e., all capital expenditure should have a source of funding and if that funding source is borrowing, the cost of the borrowing should be built into a balanced revenue budget without adversely impacting on the delivery of services.

12.2 The key sources of funding for the Council are:

- (a) Grants, including Homes England
- (b) Contributions
- (c) S106/Community Infrastructure Levy
- (d) Capital Receipts (including principal repayment of loans from KGE and SDS which are accounted for as capital receipts)
- (e) Direct Revenue Funding
- (f) Borrowing

12.3 Grants

12.4 These are predominantly government grants and are usually provided to the Council for the specific use of funding either revenue or capital expenditure for certain schemes and programmes, including Disabled Facilities Grant (DFG) can also include Homes England grants. In the future we will want to explore potential for grant funding to support carbon reduction programme. As highlighted the Council is looking to maximise funding from Homes England (potentially in the region of £50m) to help funding the housing delivery programme, this will help reduce the amount of borrowing required to fund these schemes.

12.5 Capital Contributions

12.6 In comparison to grants, capital contributions are specific contributions received for projects and are normally provided by the government, external agencies, or private companies, who have a specific output or outcome they would like achieved through the capital works the Council is providing. Quite often, the scope of these projects is dependent on this external funding, without which the Council may decide to reduce the objectives and scope of a scheme.

12.7 Community Infrastructure Levy/ Section 106 Receipts.

12.8 Community Infrastructure Levy (CIL) is a planning charge introduced by the Planning Act 2008. The Council started charging CIL in May 2016.

Developers must pay a levy linked to planning applications - this is based on a Council approved policy and charging schedule. The income from this levy is held corporately and the Council decides how to allocate these funds via a Council.

- 12.9 The majority of CIL funding is used to fund strategic infrastructure projects with Surrey County Council. Where practical Council should utilise this resource to fund the capital programme.
- 12.10 S106 differs from CIL, as it is essentially a contract between a developer and the Council and like capital contributions they must be used for specific projects and outcomes rather than a more general objective.

12.11 **Capital Receipts**

- 12.12 Capital receipts are generated from the sale of non-current assets (i.e. strips of land), and apart from special circumstances, can only be used to fund the capital programme.
- 12.13 The Council holds all capital receipts corporately, which ensures they can be used to fund the overall programme; therefore, individual services are not reliant on their ability to generate capital receipts.

Once the schemes in the current housing delivery programme are completed this will mean a more significant stream of capital receipts will be available in future years to help fund the Capital Programme going forward.

12.14 **Direct Revenue Financing**

- 12.15 The Council, can, if it chooses to, fund capital expenditure via its revenue budget. Currently it is making Revenue Contributions to Capital of £750k per annum, the Council will keep under review whether it feels this is the appropriate level. This can be through in year underspends or via general or earmarked revenue reserves. Any funding of the capital programme via revenue resources would have to be considered considering the Council's overall revenue budget and the Medium-Term Financial Plan.

12.16 **Borrowing**

- 12.17 Borrowing can take the form of internal or external borrowing.
- 12.18 **Internal borrowing** is a temporary position where the Council uses its cash balances instead of externally borrowing at that point in time. If not used for internal borrowing, these cash balances would be invested on a medium to long term basis providing the Council with a return on investment. As such there is an opportunity cost associated with internal borrowing that is built into the revenue implications of the capital programme.
- 12.19 The Council's main objective when borrowing externally is to achieve an appropriate balance between securing low interest costs and achieving cost certainty over the period for which funds are required, particularly when dealing with assets under construction, which are funded via the short-term money market, as interest rates are currently cheaper.
- 12.20 **External borrowing** occurs when the Council borrows money from the open market, via financial institutions and investors or the government, via the Public Works Loan Board (PWLB). The current certainty rate at 27th January for 50-year maturity is 4.29%.

- 12.21 In September 2021, the PWLB implemented new lending criteria so that councils focus on housing delivery, regeneration, and service delivery projects rather than invest for a return to support services. The Council intends to only undertake capital expenditure which relates to these categories. SBC must regularly assess how to finance its external borrowing needs and the financial viability of capital projects in their capital programme particularly following the recent increases in the cost of local authorities' borrowing.
- 12.22 The Council have built this into the interest cost as part of the revenue implications of the programme.
- 12.23 Although the Capital Programme may identify a need to borrow to fund capital expenditure, the timing and type of borrowing (internal/external) is dependent on cashflow modelling in line with the Council's Treasury Management Strategy, which is also being presented to Council at this meeting.
- 12.24 As a general principle, SBC will borrow from the short-term money market as the loan interest rates are cheaper than borrowing from PWLB. Although it must be noted that the short-term money market is geared to the bank of England base rate which can be volatile and quick to react to market changes. Whereas the PWLB interest rate is dependent on the more stable Gilts Rate.
- 12.25 The Council's total borrowing requirement based on capital expenditure incurred historically but to be financed is represented by the Capital Financing Requirement (CFR). This is published in the statement of accounts, and as at 31 March 2022 was £1,117.7m.
- 12.26 All capital financing costs, i.e., interest costs and minimum revenue provision must be treated as a revenue cost and built into the Council's MTFP. In essence, the more the Council borrows, the greater the call on the revenue budget which then requires further service savings to be identified to fund this in the longer term. For this reason the Council monitors carefully its borrowing limits and prudential indicators.

12.27 .

13. Capital Programme Funding: 2023/24 to 2026/27

- 13.1 The table below summarises the Council's funding of the proposed Capital Programme as outlined in this report:

Type of Funding	2023/24 Estimated £000s	2024/25 Estimate d £000s	2025/26 Estimate d £000s	2026/27 Estimate d £000s	Total
Capital Receipts, CIL and S106 funding	3,000	3,000	3,000	41,000	50,000
External Funding - Disabled Facilities Grant	973	973	973	973	3,892
Homes England Grant	7,031.4	26,504.3	4,110	17,300	3,000

Revenue Contributions to capital outlay	750	750	750	750	54,946
Grants & Other Contributions	1,051.4	804.3	250	250	2,356
Borrowing	43,997	116,635	156,069	15,512	332,214
Total	56,803	148,667	165,152	75,785	446,407

13.2 In total £114.2m (25.5%) of the programme is to be funded via external or internal sources of funding, with the remainder via borrowing (both internal and external).

14. Revenue implications of the programme

14.1 A summary of the revenue implications of the Capital Programme is shown below:

	2023/24	2024/25	2025/26	2026/27	Total
	£000s	£000s	£000s	£000s	£000s
Planned New Borrowing	43,997	116,635	156,069	15,512	332,214
Capital Financing Costs - Existing Borrowing	39,394	39,496	39,587	39,669	158,146
Commercial Income	(46,129)	(49,233)	(53,389)	(54,120)	(202,871)
Financed by:					
Net revenue stream	(13,608)	(13,608)	(12,611)	(12,234)	(52,133)
Sinking fund net contributions	1,037	875	2,891	3,668	8,471
	(12,571)	(12,733)	(9,720)	(8,566)	(43,662)

- 14.2 The Council aims to maximise its Balance Sheet assets and as such can utilise cash balances derived from working capital (such items as the appeals provision, reserves, etc.) before it borrows externally to finance the net cost of the capital programme.
- 14.3 Over the four year Capital Programme it is currently estimated that the Council will incur net financial income, through its revenue budget of £52.1m. This is made up of £202.9m of commercial income less financing costs (including Minimum Revenue Provision) of £158.1m.
- 14.4 The revenue costs of the Capital Programme are not uniform across the four years of the capital programme and are subject to significant fluctuations in line with the profiling of capital expenditure and funding (particularly capital receipts).

15. Minimum Revenue Provision (MRP)

- 15.1 MRP is applied where the Council must set aside a revenue allocation for provision of debt repayments (borrowing in the capital programme). The Council aligns the majority of its MRP with its annual principal repayments of debt to enable the MRP to be applied on an annual basis, ie the Council is paying its debt down on a year by year basis. MRP replaces other capital charges (e.g., depreciation) in the statement of accounts and has an impact on the Council's bottom line.
- 15.2 MRP will increase in the next few decades as principal repayments increase and interest payments on existing debt falls MRP is sensitive to both expenditure and funding changes.
- 15.3 The Council will continue to balance the use of capital receipts, grants, internal borrowing, and external borrowing to ensure the most efficient use of resources, including the need to fund MRP.

16. Risk Management

- 16.1 Major capital projects require careful management to mitigate the potential risks that can arise. These risks include risk that construction and capital scheme costs will rise and prove higher than estimated and that financing costs are higher than expected. The effective monitoring, management and mitigation of these risks is a key part of managing the capital strategy.

16.2 General Risks

- 16.3 General risks are those that are faced because of the nature of the major projects being undertaken. Most of these risks are outside of the Council's control, but mitigations have been developed as part of the business planning and governance process.

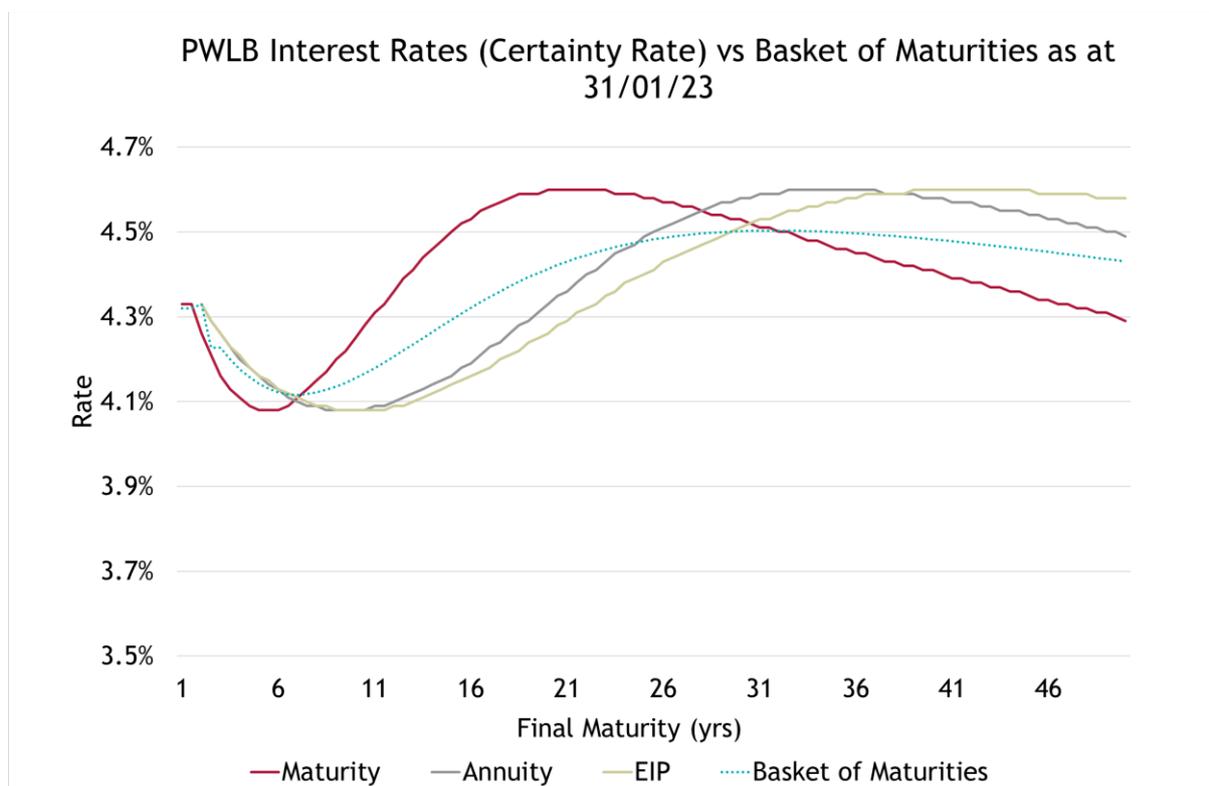
- 16.4 These risks are set out below along with key mitigations:

16.5 Interest Rate Risk

- 16.6 The Council is planning to externally borrow £332.2m, less internal sources of finance, as set out in this Capital Strategy over the next four years.

- 16.7 The Council will opt for fixed interest borrowing that matches the useful life of the asset, for purchases of land and buildings, this is 50 years and we are currently able to obtain a rate of 4.29% through PWLB.

- 16.8 The development aspect of each project is funded through the short-term money markets, where interest rates are currently around the 3.5% mark saving the Council significant sums.
- 16.9 The interest on development properties is capitalised, in accordance with the CIPFA Local Authority Accounting (capitalising borrowing costs) Code and rolled up into the total cost price of construction and on completion the short-term funds are repaid and a fixed term loan is taken out with PWLB.
- 16.10 Officers will use the above principles to mitigate our interest risk and also, look at the best options available through PWLB, which could mean that we obtain a basket of loans, including a mixture of annuity and maturity loans over the fifty-year period, in order to mitigate interest rate risk.
- 16.11 In some cases, officers have been able to reduce the total interest charge by significant sums by carefully monitoring the options available at the time of requiring a loan and this is best demonstrated by the chart below.



- 16.12 The chart shows the PWLB rates for Annuity, Maturity and Equal Instalments of Principal (EIP) loans, compared to a basket of maturities.
- 16.13 In the early years a maturity loan is more expensive than an annuity loan in terms of interest charge and cashflow. Around year 33 the benefits change, and a maturity loan becomes cheaper than the annuity loan.
- 16.14 Officers, in consultation with our advisers, will look at each loan and compare the PWLB rates over the next 50 years, to agree the actual loan, which could include a mix (basket) of annuity and maturity loans over the fifty-year term, in order to reduce cash outflow and mitigate interest risk for the Council.
- 16.15 **Inflation Risk**
- 16.16 Construction inflation over and above that budgeted by the council's professionals and advisors, and built into project budgets, could impact on the

affordability of the capital programme. A 1% rise in the cost of the affordable housing programme would increase the cost of the capital programme by approximately £2.8m.

- 16.17 Due to the delays in obtaining planning permission at Ashford Victory Place, we have seen that costs have increased by almost £4m, a 15% rise on the original budget, as building materials increase, the shortage of labour, and longer lead times take their toll.
- 16.18 If the 15% increase was to be the 'norm' it would increase the gross cost of the capital programme by over £67.0m.
- 16.19 Whilst officers have done everything, they can't inform Council of these potential issues caused by the delays in not progressing our development projects. It is going to be very difficult to mitigate these risks particularly as the time span for guaranteed pricing has reduced considerably over the last few months.
- 16.20 Officers will continue to mitigate through the provision of contingencies, updating estimates regularly as they change and monitoring the impact through governance processes, until these outstanding development projects receive both council and planning approval.
- 16.21 **Legislative Risks**
- 16.22 Change in Law Risk – Capital schemes need to comply with the latest law and regulations, changes in which can impact construction costs and may be retrospective in their nature. This risk is mitigated by awareness of pipeline legislative changes and provision of contingencies.
- 16.23 **Commercial Risks**
- 16.24 The Council's capital programme relies on commercial activity as a key supporting strategy. This involves generation of income from property letting, sales receipts and other revenue/capital financial flows such as land deals with developers. In some cases, the Council commits to large projects, based on assumptions about future asset values and potential income streams. Should market movements mean that these assumptions are inaccurate, then the Council may suffer financially.
- 16.25 To mitigate this risk, the Council relies on expert advice on future asset values in making its decisions.
- 16.26 **Supplier Financial Stability**, construction companies and developers contracting with the Council that experience financial instability pose a significant risk. They may not be able to raise funding to finance operations, and their potential insolvency could lead to a costly process of changing suppliers without any guarantee of remaining within the overall budget. The Council could suffer direct financial loss, and any defects or other issues may not be resolvable as anticipated.
- 16.27 To mitigate this risk, the Council carefully considers the financial robustness of any contractor and requests appropriate financial standing assurance and support wherever possible.
- 16.28 **Transfer Risk**

- 16.29 When the Council plans and delivers projects, it is important to consider the risks associated with the project and whether the Council (or its subsidiaries such as KGE) is the best placed to take on that risk.
- 16.30 A key consideration for major capital schemes is whether these will be developer led or whether the Council will self-develop. For a developer led scheme the developer will take on a significant proportion of the risks associated with the project. However, the developer will price this risk in, so it will come at a cost.
- 16.31 Considerations can include whether there is resource capacity and expertise to take on specific risks in the context of the overall capital programme. The housing subsidiaries are newly incorporated and there may be an initial set-up risk as the company gains experience and embeds its delivery plan.
- 16.32 **Hybrid working** – a key issue with projects and overspending is the lack of communication between colleagues in the same office, with the onset of Hybrid Working, those small conversations had as you pass a colleague in the corridor or whilst having a cup of tea are going to be lost and the likelihood of missing a key element of the project are enhanced.
- 16.33 **Project Risks**, relates to the delivery of capital projects, which in many cases can be controlled, influenced, or directly mitigated in ways other than making contingencies available. These risks would mostly relate to unforeseen project delays and cost increases which could arise from a range of circumstances.
- 16.34 The effective management of these risks is mostly linked to the following strategies:

Project Risks

- (a) Projects are required to maintain a risk register, to ensure effective monitoring.
- (b) **Highlight reporting** - development projects, as an example, create monthly highlight reports to ensure stakeholders are aware of progress and risks of projects on an on-going basis.
- (c) **Appointment of professional teams** - the Development team has recruited and retained the services of experts to provide robust planning and review to advise on financial feasibility and to ensure timely delivery of projects.

Experts also cover key surveying and financial planning roles to give assurance on quality of work and assumptions.

- (d) **Risk of Revenue Write Off** – the Council commits to feasibility studies on many of its significant capital schemes at the point where spend is revenue in nature or when capital spend may be written off, should the scheme in question not progress.

This is managed through careful consideration and approval of all expenditure potentially at risk of revenue write-off. There is a further risk that any projects funded may not yield the required ongoing revenue savings and therefore may need to be written off to revenue.

- 16.35 The Council has an on-going Capital Programme and will continue to invest in capital projects beyond 2026/27 and will therefore need to ensure that funds are set aside for the future cost of borrowing.

17. Financial implications

17.1 Financial implications are set out in the main body of this report.

18. Legal considerations

18.1 The legal implications for each individual scheme within the capital programme will be considered when approval is sought for that scheme. Each scheme within the capital programme will be approved in accordance with the council's constitution.

19. Equality and Diversity

19.1 The Capital programme impacts on all residents across the Borough. In particular, the provision for new housing within the Borough will assist a substantial number of our 3,500 residents, on our housing waiting lists, many of whom are key workers, the young and most vulnerable residents to benefit from our affordable house schemes. Before major new projects and programmes are undertaken, equality impact assessments are undertaken.

20. Sustainability/Climate Change Implications

20.1 Each project will be required to provide details of its impact on the sustainability for the Borough and climate. Noting that at present, we are investing over £5.5m into green initiatives and reducing our carbon footprint in our properties, notably, £4m to build the first leisure centre in the United Kingdom to Passivhaus standards and spending £1.5m on heat pumps at our Ashford Victory Place development.

21. Timetable for implementation

21.1 The Capital Strategy will need to be approved by Council and can then be issued immediately thereafter.

Background papers: as presented at previous or current meeting(s)
2023/24 to 2026/27 Capital Programme
KGE 50-year projections