Introduction

The Council has a responsibility to approve a Capital Strategy before 1 April 2019.

The Capital Strategy shall demonstrate that the Council takes capital investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability in the long-term context.

This Capital Strategy is based on existing principles and looks at the demand for capital expenditure and the predicted availability of capital resources to identify the gap between demand and supply to inform decision making.

The Elmbridge Borough Council (EBC) Capital Strategy 2019 to 2039 draws together existing good practice contained within the Council into a single document.

Executive Summary

The principles and guidelines set out below represent the EBC Capital Strategy 2019 to 2039:

- The Council will take investment decisions in line with policy and service objectives taking account of stewardship, value for money, prudence, sustainability and affordability in the long-term context;
- The Capital Strategy shall be reviewed each year as part of the budget setting process;
- The Council will seek to maintain and extend the Council’s asset base and reflect the life cycle of capital assets;
- The Council will take a long-term view on the requirements for capital, the availability of capital resources and the long-term implications for the revenue account in terms of borrowing costs, potential loss of investment interest and the impact on the day-to-day running costs of services;
- Capital investment should recognise and take account of development and facilities in neighbouring authorities;
- The Council acknowledge that capital contributions may be required to lever additional investment into the Borough or to accelerate delivery timescales subject to an assessment whether the new assets may create additional maintenance, management or risk obligations;
- The Council will keep under review its capital bid evaluation process to weigh the relative priority of individual schemes;
- New capital projects should use the Corporate Project Management Policy and Project Management Toolkit to plan and manage projects;
- The acquisition and management of Non-Financial Assets shall be in accordance with paragraphs 7.4 to 7.6 of this Strategy;
- The Council may make loans for capital purposes if justified in accordance with paragraph 8.2 of this Strategy;
- The new housing companies shall be operated in accordance with the Council resolution of 18 July 2018;
• The use of capital receipts shall be limited to approximately £750,000 per annum and not to exceed an aggregate of £2 million in any rolling three-year period;
• The balance of capital receipts shall be not less than £5 million and held as a contingency against unforeseen capital spending;
• There will not be any contribution from the revenue account to finance the capital programme except from earmarked revenue reserves as set out in paragraph 12.3;
• The Council may authorise borrowing for capital purposes provided that the costs of borrowing are affordable, and the amount of additional debt is assessed to ensure it does not prejudice the Council’s debt ratio;
• The Council confirm the allocation of the fee income from the Community Infrastructure Levy in accordance with paragraph 12.6 of this Strategy and that at least 10% of the total capital expenditure on asset renewal and refurbishment from 2022/23 onwards will be financed from Community Infrastructure Levy (CIL) receipts;
• The Council will only accept grants and contributions from third parties after a full review of the impact upon the revenue account and the risk associated with the project;
• Complex financial structures can be examined in the future subject to the usual constraints of financial prudence and thorough due diligence;
• Capital expenditure shall be monitored at regular intervals throughout the financial year in accordance with paragraph 13.2.

Elmbridge Borough Council Capital Strategy 2019 to 2039

1. Background

1.1 The Capital Strategy demonstrates that the authority takes capital investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability. The Capital Strategy also sets out the long-term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes. Decisions around capital expenditure, investment and borrowing should align with the processes established for the setting and revising of the budget for the local authority and the Capital Strategy shall be reviewed each year as part of the budget setting process.

1.2 The Capital Strategy should also be tailored to the authority’s individual circumstances and should include capital expenditure, investments and liabilities and treasury management. For Elmbridge, the Treasury Management Strategy drawn up in line with the Treasury Management Code will continue to be published as a separate document and this will remain separate to differentiate between the demand and assessment of capital expenditure and the management of the investment and borrowing portfolio.
2. **Policy Context**

The Council Plan defines the Council’s Five-Year Vision (2018-23) to be:

- “A responsive and effective Council, protecting and promoting the interests of residents and businesses and safeguarding our environment, while maintaining a community for all.”

The Priorities to support this Vision are:

- **Character and Environment** – we will make EBC a sustainable and attractive place.
- **Quality Services** – we will work in partnership to ensure services are efficient, effective and offer value for money.
- **Economic Development** – we will facilitate economic growth, including improved infrastructure and housing.
- **Community Wellbeing** – we will listen to all of our residents and support communities to become healthier, empowered and safe.

The Vision and Priorities are underpinned in turn by Council Objectives and Service Objectives as part of the ‘golden thread’ that links everything that the Council is seeking to achieve.

2.2 The Capital Strategy is an important policy document in delivering the Council’s Vision in terms of maintaining and extending the Council’s asset base but needs to take a longer-term view to reflect the life cycle of capital assets. The life cycle of capital assets, often known as non-current assets, will range between 5-60 years or even longer if land is acquired. Decisions made now will affect residents, business and other stakeholders for many years to come.

2.3 The Capital Strategy has links to many existing Council documents including the Asset Management Plan (AMP). The AMP aims to manage assets in the most cost-effective way and to protect and optimise the value of the Council’s assets whether operational or non-operational. The AMP will be reviewed and updated during 2019/20.

3. **Capital Programme**

3.1 Spending on schemes within our existing capital programme specifically covers acquiring or improving assets (for instance, land, buildings and equipment) in order that EBC can continue to provide services. This includes expenditure to maintain and improve EBC assets, but also grants EBC give to others for the acquisition or improvement of assets by them (such as modifications to homes by offering Disabled Facilities Grants or building of new affordable housing for the local community).

3.2 The capital programme represents expenditure on:

- Refurbishment and improvement of existing property assets
- Health and safety requirements
• Upgrading car parks
• Investment in IT development
• Providing affordable and private sector housing grants
• Upgrading leisure and cultural amenities
• Acquiring property for economic development purposes
• Replacement of furniture and equipment
• Replacing vehicles

A summary of the existing asset portfolio is attached at Appendix B.

3.3 The proposed capital programme provides for the 2019/20 spending plans with commitments and priority schemes for the following 2 years. The fundamental change with the Capital Strategy is to take a much longer-term view on the requirements for capital, the availability of capital resources and the long-term implications for the revenue account in terms of borrowing costs, potential loss of investment interest and the impact on day-to-day running costs of services.

4. **Elmbridge today and in 2039**

4.1 The Office for National Statistics predicts that the population of EBC will increase from over 132,000 in 2016 to over 150,000 by 2039. It is also predicted that the proportion of residents over 65 years of age will increase from 18% to 24%.

4.2 The English Indices of Deprivation 2015 show that EBC is one of the five least deprived local authority areas in England although this does not mean that the overall statistics may not conceal localised areas of relative deprivation. EBC scores highly in terms of incomes and employment but does less well in terms of housing, air quality and road traffic accidents.

4.3 The Capital Strategy acknowledges population growth and indicators identified in the Indices of Deprivation. Although it is difficult to predict exactly what will happen in the next 10 to 20 years the basic demand for local authority services is likely to increase.

**Part 1 – Capital Expenditure**

5. **Elmbridge and Other Agencies and Organisations**

5.1 EBC is a two-tier structure with Surrey County Council (SCC) providing a range of important services including children and social care services, highways infrastructure and maintenance as well as libraries. The SCC 2018/19 budget reports unprecedented demand for services and an objective to work more closely with Surrey’s districts and boroughs. SCC is currently undertaking a major programme of transformation and remodelling of their services and their plans for schools, roads and the rationalisation of their other assets to align service requirements may influence EBC’s own capital planning.
5.2 The SCC School Organisation Plan (January 2018) describes some expansion of school/Academy places but that no further provision is planned. The SCC Asset Management Programme 2017-21 in turn refers to highway resurfacing and reconstruction based on condition survey information. There is also a modest programme of capital works on social care and health and a recognition of provision for fire station reconfiguration and land for waste. In October 2018 the SCC Cabinet also approved an Asset & Place Strategy intended to redesign their operational estate in conjunction with the Surrey districts and boroughs local plans.

5.3 EBC is within the area of the Enterprise M3 (EM3) Local Enterprise Partnership. EM3 has a remit to lead economic growth and job creation and has awarded up to £1.875 million to provide greater travel choice and improved sustainable accessibility between Brooklands Business Park, Weybridge station and Weybridge town centre. The award of funding is reliant on an element of local match funding of up to £625,000. The Enterprise Elmbridge Action Plan 2019-2021 is currently being updated.

5.4 Highways England is responsible for major trunk roads in the area such as the M25 and A3. In their Road Investment Strategy 2015 to 2020 the major initiative potentially affecting EBC is the proposed improvements to the A3/M25 Junction 10 interchange at Wisley. EBC is also within the scope of the M25 south-west quadrant strategic study where the preferred or pragmatic solution to relieve congestion on the M25 appears to be to increase the capacity of nearby roads and transport, reduce demand for road space generally and consider improved strategic bus links.

5.5 Network Rail is another major influence in the provision and maintenance of infrastructure within the Borough and has published their Strategic Business Plan 2019-2024. Network Rail predict that overall passenger numbers are expected to increase by 40% by 2043 and are looking to the smarter use of information and technology to improve punctuality as well as investment and redevelopment at Clapham Junction affecting the services connecting to Elmbridge. Improved service resilience is also promised on the Windsor line which terminates at Weybridge.

5.6 The Environment Agency have a role to protect and enhance the environment and promote sustainable development, create better places for people and wildlife as well as flood protection and are another agency with a key role within the Borough. Their 25 Year Environment Plan launched in January 2018 includes the River Thames scheme that the Council considered in November 2017 and agreed in principle to a potential contribution of £1.8 million if the existing funding gap on the overall scheme can be either financed or mitigated and the project goes ahead.

5.7 The Surrey and Borders Partnership NHS Foundation Trust has a Strategic Plan 2014-19 that describes their core purpose as ‘to work with people and lead communities in improving their mental and physical health and well-being for a better life; through delivering excellent and responsive prevention, diagnosis, early intervention, treatment and care’. The Strategy describes local authorities
as a key stakeholder in the delivery of their objectives including the development of community hubs and a radical rationalisation of their property from 63 sites down to 25 sites.

5.8 In addition, the Council has recently considered an application for £140,000 CIL funding from the North West Surrey Clinical Commissioning Group to create the physical infrastructure to improve GP services at Walton Community Hospital. This is just part of the wide scope of CIL funding to support infrastructure issues within the Borough. The important role of CIL funding is set out in more detail in paragraph 12.6.

5.9 EBC has boundaries with five other Surrey districts and two London Boroughs as well as the two-tier relationship with SCC. These adjacent local authorities provide a similar range of services and amenities. Whilst some services are discrete to the area concerned some services such as recreation and community facilities will be used by residents according to personal convenience or choice irrespective of Council boundary lines. It is therefore helpful to be aware of developments in neighbouring local authorities and the impact their decisions may have on local choice or demand for services. For example, the Sports Hub will attract users from outside EBC and residents in parts of the Borough may use some amenities in adjacent districts. Capital investment should recognise and take account of development in neighbouring authorities.

5.10 The list above is not exhaustive and is subject to change with each body or organisation having different planning horizons and their own governance arrangements and service imperatives. Nevertheless, all these bodies will influence the capital landscape of EBC in years to come as well as all the private sector development likely to arise within the Borough. EBC acknowledge that capital contributions may be required to lever additional investment into the Borough or to accelerate delivery.

5.11 Whilst capital investment is welcome EBC must always examine whether the new assets will create additional revenue obligations in terms of maintenance and management or a longer-term liability to renew or refresh the asset.

6. The Demand for Capital Investment

6.1 There are many demands on the Council’s capital resources and this is addressed each year as part of the revenue and capital budget setting. Capital bids are invited and submitted each year based upon affordability and the Council’s priorities. The Council will only undertake capital investment that is prudent, affordable and sustainable. The main test of affordability is that the revenue implications can be contained within the revenue budget.

6.2 As part of the review process bids are considered by the Council Management Board and scored for submission to Cabinet and Council for approval. Bids are funded from a range of sources including capital receipts, S106 contributions, CIL, New Homes Bonus and Earmarked Reserves. The process works well but the forecasting horizon of three years is relatively short for capital planning.
6.3 The objective is to set capital decision making into a long-term context. Regularly reviewing the basis of assessing bids will help to achieve that objective. The forecasts within the Strategy identify a significant gap between predicted capital expenditure and available capital resources. This is not unexpected, but it is important to recognise that if the rationing of capital resources becomes more acute in the future the evaluation of projects needs to take a strategic approach.

6.4 The Council has introduced a basis for evaluating and scoring capital bids for 2019/20, 2020/21 and 2021/22 based on the fit to existing Council priorities, service plans etc. Each bid is scored on its merits to give a ranking relative to other competing bids and assist with prioritisation if capital resources are scarce. The basis of the evaluation should be reviewed and refined year on year to ensure prioritisation reflects long-term Council policy.

6.5 A particular issue for the Council is major expenditure beyond the existing three-year programme. In September 2018 Cabinet noted the recommendations in the Leisure Facilities Strategy that included an objective to prioritise investment into swimming pool provision. The priority is a refurbishment/replacement facility for Hurst Pool that could provide the opportunity to develop a larger learner pool, and/or a larger main pool, as well as additional pay and play fitness facilities, and reduce operating costs through the installation of new energy efficient technologies.

The Leisure Facilities Strategy did not provide an estimated cost, but any refurbishment/replacement of Hurst Pool is likely to be a multi-million-pound project. Inevitably this type of project has a long lead time in terms of consultation, design, planning consent (if required) and a thorough procurement process. EBC could explore various financing options (see paragraph 12.9 below) but the most straightforward approach would be to use capital receipts, borrowing or accumulated CIL balances. Whichever option is selected this would be a significant commitment of existing capital resources.

A major scheme like Hurst Pool (there may be others) should also be an exemplar for adopting best practice in terms of option appraisal, risk assessment and project planning. EBC already has an existing Project Management Policy and Project Management Toolkit and these guidelines provide sound principles for selecting the best scheme, identifying risk and the most efficient delivery process.

It is recognised that a number of schemes within the programme may be too small to incur the overhead of detailed project management but the need to select the best option and a cost-effective procurement should apply to every scheme irrespective of cost.

7. Non-Financial Investments

7.1 Although the majority of capital assets are held for the essential delivery of services the Investment Guidance recognises that local authorities may also legitimately hold non-financial investments for regeneration and to provide rental
income to the revenue account. Where a local authority holds a non-financial investment, it will normally have a physical asset that can be realised to recoup the capital invested. At 31 March 2018 EBC held £76.5 million of investment properties that fall into this category. Approximately 34% is retail property, 40% industrial property, 20% office buildings and 6% miscellaneous property.

7.2 The Council has built up its portfolio of investment property from just under £5 million in 2011/12 to a level of £76.5 million by the steady acquisition of suitable sites within the Borough that have regeneration potential and/or yield reliable income streams with good covenant tenants. The total portfolio is forecast to generate an annual revenue income yield of approximately 4.5% or over £3.4 million. A further property acquisition has recently been completed at a cost including fees and expenses of £18.2 million.

7.3 The current low level of interest rates (see also para. 12.5 below) has encouraged some local authorities to borrow significant sums to finance the purchase of land or property likely to realise a good revenue yield over and above the cost of borrowing. The EBC Capital Strategy is to acquire high covenant assets in accordance with the criteria set out in paragraph 7.6 below.

7.4 When an authority holds this investment type of asset it is appropriate to regularly consider whether the asset retains sufficient value to provide security of investment in accordance with international accounting standards. This Capital Strategy endorses that approach and expects that an annual report will be produced that on a fair value assessment the underlying asset provides security for the capital invested.

7.5 Where the fair value of non-financial investments is no longer sufficient to provide security against loss then the authority shall provide details of mitigating actions that the authority is taking or proposes to take to protect the capital invested. If necessary, the impact of any loss should be reported to full Council.

7.6 Cabinet received the first annual report on the Council’s investment property portfolio on 4 July 2018. Cabinet reviewed the Property Acquisition Strategy approved in 2012 and then again in 2014 and confirmed that the previously agreed investment criteria were still valid, as follows:

- There are measurable benefits (in addition to financial) within a maximum period of 15/20 years;
- Effective intervention will expedite agreed key strategies for the Borough;
- Acquisition involves partnering arrangements;
- Acquisition will consolidate the Council’s existing land holding portfolio to facilitate larger developments;
- Acquisition will assist in the modernisation of the Borough’s business infrastructure and/or encouraging inward investment, relocation and business start-up within the Borough;
- Acquisition will not conflict with strategic planning policies;
- Acquisition will not increase the Council’s ongoing revenue costs in the longer term;
• Acquisition type; Good quality commercial property in traditional sectors, i.e. retail, office and industrial;
• Return of at least 2% above borrowing costs bearing in mind there will be exceptions depending on future potential;
• Security: Medium to long-term strategy – Acquisitions should normally be pre-let to tenants of good covenant on fully repairing and insuring terms, with an unexpired term of at least 5 years;
• Each investment will have to be looked at on its own merit; and
• Strategic value; Where a property has a strategic value to the Council, some of the above criteria may be relaxed e.g. land capable of development or required to enable development.

These criteria have been used to identify potential regeneration and investment opportunities and undertake several purchases to increase the non-financial investment portfolio. All acquisitions have been within the EBC boundaries.

The strategy is to not place too much reliance on a specific sector and to ensure a balance is created and the risk is spread across all sectors, albeit still within the EBC boundaries. In addition, an increased focus should be on regeneration benefits of purchasing certain assets within the Borough; not necessarily at the expense of income on the asset but an additional consideration/benefit in considering whether to purchase an asset. The hold period of the asset should also be considered on purchase and as part of the approval process, whether short-term to meet regeneration requirements or long-term where a single let investment provides a stable long-term rental income for the Council.

The strategy is also that borrowing costs should always be included as part of any proposal to acquire non-financial assets.

The principles for non-financial investments were approved by Council on 18 July 2018.

8. Loans for Capital Purposes

8.1 Any local authority may choose to make loans to local enterprises, local charities, wholly owned companies and joint ventures as part of a wider strategy for local economic growth even though those loans may not have such a strong covenant as normally required for treasury management purposes.

8.2 Elmbridge can continue to make these types of loan if they can demonstrate that:

• Total financial exposure to these types of loans is proportionate;
• The Council has adopted proper practices to measure the credit risk of their loan portfolio;
• They have appropriate credit control arrangements in place to recover overdue payments; and
• The Council has formally agreed the total level of loans by type that it is willing to make and their total loan book is within their self-assessed limit in the Treasury Management Strategy.
8.3 The criteria above describes a similar level of risk assessment and due diligence that the Council has recently exercised in agreeing a start-up loan to the two new housing companies at Council on 18 July 2018. The criteria set out in paragraph 8.2 above shall therefore form part of the Capital Strategy.

9. Housing Programme

9.1 On 18 July 2018 the Council approved the establishment of two wholly owned Housing Companies, EBC Investments Ltd and EBC Homes Ltd, to play a significant role in delivering new homes across EBC with a focus on:

- Housing at affordable rents
- Temporary accommodation for homeless households
- Key worker accommodation
- Market rent
- Market sale

The Business Plan set an ambitious target of over 250 new homes to be delivered over the life of the 5-year plan.

9.2 Financing this major programme of works could be achieved by the Council and/or EBC Homes Ltd receiving affordable housing contributions or borrowing either from the Public Works Loans Board or from other suitable external lenders. The relationship between the Council and the companies is based on several key principles including:

- Finance provided by the Council to EBC Homes Ltd must be state aid compliant (ie. state aid can occur whenever state resources are used to provide assistance that gives organisations an advantage over others).
- Land transferred across from the Council must be valued independently for both regulatory and State aid purposes.
- The companies will act within their delegated powers at all times, without exception.

9.3 The companies detailed development proposals outlined in their Business Plans is commercially sensitive and excluded from the financial Appendix C. The basis on which the companies will operate is set out in accordance with the Council resolution.

10. Price Base, Inflation and Other Assumptions

10.1 Forecasts are based on broad assumptions of cost, but in most cases without stakeholder consultation, detailed site inspections, specifications, designs or pricing schedules. There will be some allowance for contingencies, but estimates are largely based on current costs. Inevitably for schemes later in the programme a detailed option appraisal and risk assessment will be undertaken, and price inflation will need to be applied to the costs before any project becomes a firm commitment.
10.2 Estimates for the first 10 years of the forecast have been provided by service managers as set out in Appendix C. The predictions are intended to very broadly indicate the gap between capital requirement and the availability of capital resources rather than an accurate works programme. A detailed forecast has not been prepared for the ten years after that, but a trend can be plotted based on the preceding period. The outcome of this exercise is summarised below.

<table>
<thead>
<tr>
<th>Period (Years)</th>
<th>Forecast Capital Expenditure £m</th>
<th>Forecast Allocation of Capital Resources £m</th>
<th>Shortfall in Allocated Capital Resources £m</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019/20 to 2028/29 (first 10 years)</td>
<td>92.2</td>
<td>69.3</td>
<td>22.9</td>
</tr>
<tr>
<td>2019/20 to 2038/39 (total cumulative 20-year forecast)</td>
<td>118.7</td>
<td>79.4</td>
<td>39.5</td>
</tr>
</tbody>
</table>

11. **Bids Received 2019-2029**

11.1 The forecast expenditure is based on looking after the Borough’s existing asset base with renovation and refurbishment when required to maintain the functionality of the asset. Some assets such as vehicles or ICT equipment will need replacing but generally on a like-for-like basis. The programme excludes any major new initiatives although some service rationalisation or spend to save schemes may ultimately create a new asset. New facilities can always be added in later if a source of finance is identified. The Capital Strategy is based on maintaining the existing EBC asset base.

11.2 Community Support Services will need to replace one vehicle every year and have identified a need to provide an annual rolling programme for equipment replacement at community facilities.

11.3 Highways and Transport includes estimates for the replacement of recycling bins and the automatic number plate recognition equipment towards the end of the 10-year period. The joint waste fleet will also be 10 years old towards the end of the period. A similar cycle of replacement has been extrapolated for the following 10-year period.

11.4 For ICT development the basic premise is to maintain the existing hardware and software assets without trying to predict unknown technology changes. There is a baseline requirement to replace devices on an annual rolling basis with a more fundamental requirement to refresh systems software and equipment on a four-year cycle. The ICT Digital Strategy 2019-21 will inform the development of the future capital programme requirements.
11.5 The Resources forecast is informed by a limited amount of condition data and also local knowledge of the individual sites. The Civic Centre is predicted to require an on-going programme of capital refurbishment as well as investment in centres for the community, pavilions and cemetery buildings.

11.6 The Leisure forecast is based on refreshing and refurbishing a diverse range of amenities from parks and commons to the tennis courts, leisure facilities, skateparks and play areas.

11.7 Expenditure figures are provided at portfolio/major scheme level in Appendix C along with the shortfalls in allocated capital resources. The shortfall amount fluctuates from year to year but overall there is a gap between the forecast and the allocated finance in total of nearly £23 million by 2028/29. Some of the schemes may be eligible to be financed from CIL receipts, earmarked reserves or external grants but a shortfall of available resources in the range £20 million - £25 million still appears probable.

11.8 Although forecasts were provided for the first 10-year period a further 10-year profile is then used to informally extrapolate the period up to 2038/39. It is difficult to be too precise about the period beyond 2029 but the indications are that based on current predictions the requirement for capital investment is likely to continue to exceed capital resources unless there is a radical change in expenditure patterns or the availability of capital resources. This forward projection increases the shortfall of capital resources to over £39 million without factoring in inflation.

Part 2 – Sources of Capital Finance

12. Types of Capital Funding

12.1 There are two distinct aspects to the Capital Strategy. Determining the level of capital expenditure is based on the Council’s policy and strategy requirements but financing the spending is based on the availability of capital resources. This section examines the future availability of funding sources.

12.2 Capital Receipts

Capital receipts are derived from the sale of Council assets and provide a useful source of finance for capital projects. They cannot be used for revenue purposes.

The financial year 2017/18 was an exceptionally good year for capital receipts with the sale of land at Stompond Lane to fund the Sports Hub, land at Rydens School and the Molesey Centre that with other minor receipts raised over £26 million. After financing the capital programme elsewhere on this agenda the balance of capital receipts at 31 March 2022 is forecast to be £10.5 million.

At present there are no major asset disposals planned although the Council will continue to monitor strategic planning opportunities and seek to identify surplus or under-utilised operational property. Wherever possible sites will be identified
for new homes. The Asset Management Plan notes that the ‘scope for disposal is somewhat limited after EBC embarked on a disposal programme in the 1990’s’.

Since the Council transferred the housing stock to Elmbridge Housing Trust in 2000 the Council has received a proportion of the proceeds derived from the sale of council houses under right-to-buy. This has been a valuable source of capital receipts in past years but in 2017/18 there were no receipts due to be paid to the Council after costs and only £265,000 this year to date. This source of funding may not yield significant capital receipts in future years.

Forward projections therefore do not forecast any major boost to capital receipts. The 2019 – 2022 programme introduces for the first time a principle to ration capital receipts to approximately £750,000 per year from 2019/20 onwards and no more than £2 million for the forward three-year period. This principle should be extended to the long-term programme and the balance of usable capital receipts should not fall below a minimum of £5 million to give the Council some capacity to respond to capital cost pressures that may arise unexpectedly. The use of capital receipts will reduce the Council’s cash balances and consequently reduce investment interest but will avoid borrowing (see para. 12.5 below)

12.3 Revenue and Reserves

Capital expenditure can be financed from revenue (but not vice versa) either directly from the revenue account or from other earmarked reserves. Some reserves such as the Property Acquisition Reserve (£1.8 million forecast at 31 March 2020) have been set up specifically to finance capital expenditure. Other reserves such as the Capital Expenditure and Repairs & Maintenance Reserve (£540,000 forecast at 31 March 2020) and Car Park Maintenance Reserve (£290,000) are more versatile and can be used for either revenue or capital purposes.

The Property Acquisition Reserve was set up from New Homes Bonus receipts (see para. 12.8 below) and should be retained for that purpose when a suitable property is identified. The Capital Expenditure and Repairs & Maintenance Reserve can be used for any project that satisfies the broad criteria whether revenue repairs or capital refurbishment.

The Car Park Maintenance Reserve is created from top-slicing 5% of the annual off-street parking income and is available for any approved revenue or capital works to the Council’s car parks. For the purposes of this Strategy an annual contribution of £150,000 from parking income to the Car Park Maintenance Reserve has been assumed.

In terms of direct capital financing from the revenue account the Medium-Term Financial Strategy highlights the challenges the authority faces to maintain services. The Strategy cannot anticipate any contribution from revenue balances unless held in earmarked reserves.
12.4 Capital Grants Unapplied

There are several balances held that relate to grants received where the conditions of grant entitlement have not yet been met. As and when expenditure is incurred that satisfies the grant conditions the balances can be drawn down. The most significant of these balances is the Enabling Fund that mainly comprises funds for affordable housing. The unallocated balance on the Enabling Fund currently stands at around £8 million. The nature of these balances means that they can only be used for their dedicated purpose and are not available to finance the remainder of the capital programme.

12.5 Borrowing

Local authorities have the power to borrow to finance capital expenditure provided they can meet repayment requirements within their balanced budget and without impacting on service delivery. More detail is provided on how the Council satisfies this requirement in the Treasury Management Strategy 2019/20.

In capital terms borrowing can be used to top up budget financing requirements when other sources of finance have been exhausted or where the rental income yield from a non-financial investment is greater than the cost of borrowing in accordance with the principles in paragraph 7.6.

In recent years borrowing has been used for the specific purpose of acquiring investment property where the estimated rate of return demonstrably exceeds borrowing costs and there are potential regeneration benefits. The rate of return after risk adjustment for potential rent default, voids and maintenance costs etc. should be at least 2% above borrowing costs. This is in accordance with the Investment Property Portfolio resolution of Cabinet on 4 July 2018.

The Council can borrow from the Public Works Loan Board (PWLB), a statutory agency of the government, at favourable rates but must make provision to meet the interest on the loan and repay the principal sum. Borrowing rates are historically low and locking into these rates at the present time limits the impact on the revenue account. Rates are predicted to rise slowly in line with market rates.

At present borrowing £1 million from the PWLB on the basis of a 10-year maturity loan would cost £123,000 per annum including annual provision for the repayment of the principal and annual interest on the outstanding sum. To put this into context £123,000 represents almost 1% of total EBC spending.

In authorising borrowing the Council should be mindful of the debt ratio on the Balance Sheet. This is the relationship between the value of the Council’s liabilities and assets. At the end of March 2018, the Council reported liabilities (debt) at 46% of their assets which represents a healthy net position derived from a strong asset base. Total assets including all property and short-term investments are £276 million and liabilities including loan debt, creditors and pension obligations are £126 million. A low ratio (the lower the better) is an
important indicator of financial health demonstrating capacity to finance debt. Increasing debt by borrowing will therefore increase the debt ratio although a new asset will also be recorded. The scale of commercial investment activity should be proportionate to the resources of the authority.

For the purposes of the Capital Strategy the policy is re-affirmed that the Council is prepared to borrow provided that the costs of borrowing, including interest charges and repayment of principal are affordable throughout the term of the loan, and the amount of debt outstanding at any time does not prejudice the Council’s debt ratio.

12.6 Community Infrastructure Levy (CIL)

CIL is a tool for local authorities to help deliver infrastructure to support the development of the area. CIL was introduced to address the growing scope and complexity of the Section 106 developer contributions made under the Town and Country Planning Act 1990 and often described as ‘planning gain’. CIL is intended to be fairer, faster, more certain and transparent. Where local authorities adopted CIL the Section 106 obligations were to be scaled back to address only the site-specific issues required to make development acceptable in planning terms.

Since adoption in 2013, EBC has been one of the highest collecting CIL authorities outside London. So far well over £23 million has been collected and it is predicted that income will continue to accrue at approx. £3 million per annum.

Regulations set out that a charging authority (ie EBC) must use CIL to fund the provision, improvement, replacement, operation or maintenance of infrastructure to support the development of the area. The levy can be used to fund a wide range of infrastructure, including roads and transport, flood defences, schools, medical facilities, sporting and recreational facilities and open spaces although affordable housing cannot be funded through CIL.

As set out in the CIL regulations, an initial 5% is retained by the Council for administration costs and in some areas of the Borough a levy for Suitable Alternative Natural Greenspace (SANG) is payable. The remaining CIL receipts are spent in accordance with the regulations and the approach adopted by Cabinet in July 2017 is as follows:

- 40% top slice of CIL collected (post allocation to administration and SANG) is ring fenced to fund a programme of strategic infrastructure projects;
- 35% of CIL is allocated through the Strategic Spending Board to more ad-hoc strategic improvements required to address the impacts arising from development across the Borough;
- 15% is allocated through the Local Spending Boards (and in the case of Claygate, to the Parish Council) as a ‘meaningful proportion’ to local areas where development comes forward; and
10% of CIL is ringfenced (post allocation to administration and SANG) for maintenance purposes.

After allowing for the potential allocations to the River Thames scheme (£1.8 million) and the Brooklands access scheme (£625,000) referred to in paragraph 5 there is just over £10.7 million of CIL receipts unallocated of which £1.8 million relates to the Local Spending Boards.

If a further £3 million per annum is received, then approximately £2.5 million per annum will potentially be available for capital purposes of which over £400,000 will be allocated through Local Spending Boards and approximately £1 million for the Strategic Spending Board. The balance of the £1.1 million that remains may then be used to either finance new infrastructure or eligible works on existing infrastructure.

Five key areas have been identified where there are known/expressed infrastructure issues because of increased development pressure within the Borough:

- Schools – to support the increase in school age population because of new development;
- Transport – new development will add to existing pressures on the Borough’s road network. This will primarily be on the local road network with increasing pressure on local congestion hotspots and a need to ensure continued safety on our road network. More information on transport pressures is set out in Transport Strategy and Implementation Programme for EBC that was published by Surrey County Council in 2014;
- Medical facilities – to support the growth in services and capacity at medical practices due to increases in population linked to new development;
- Leisure and recreation – identified need for playing pitches and the need to encourage access and participation in sport; and
- Mitigation of development on the Thames Basin Heaths Special Protection Area.

The Infrastructure Delivery Plan is being updated to identify key deliverables to support new development within the Borough.

Some of these objectives will be led by other bodies and EBC may be requested to provide CIL funding for all or part of the scheme (see also paragraph 5 above).

At present the level of CIL receipts is forecast to remain relatively stable throughout the period of the Capital Strategy although it should be noted that the Government was due to respond in the Autumn to the paper prepared by the CIL Review Team titled ‘A New Approach to Developer Contributions’. The Government commissioned this independent review in November 2015 and the group submitted their report to ministers in October 2016. A key recommendation of the report was that CIL should be replaced by a hybrid
system of low-level Local Infrastructure Tariffs and Section 106 for larger developments. Section 106 contributions therefore appear likely to continue but are generally linked to specific infrastructure requirements and are omitted from the forward forecasts. The impact of these schemes should be cost neutral apart from timing differences that may have some marginal effect on cash flows.

As it stands CIL will provide a significant funding stream for the foreseeable future and can be used to finance a wide range of infrastructure projects whether sponsored by the Council or other partners.

The Capital Strategy expects that at least 10% of the total capital expenditure on asset renewal and refurbishment from 2022/23 onwards will be financed from CIL receipts.

12.7 Grants and Contributions

The receipt of general or specific capital grant or contribution can assist with the financing of the capital programme. In recent years the main source of grant has been direct from Government departments, but several other non-government organisations and third parties may also offer grants and contributions. Examples would be the Big Lottery Fund, Historic England, Natural England etc.

Most grants now tend to be for a specific purpose and will often meet a proportion of the total expenditure or will be capped at an upper limit irrespective of the final cost. The Capital Strategy should encourage the authority to attract capital grants and contributions but to also be aware of potential project risk in the event of cost overrun or unforeseen site problems. Additional revenue costs may also be incurred or a liability to maintain the asset in the longer term. A robust financial appraisal and risk assessment of any project is essential. The Council should be prepared to turn down grant offers if the conditions or revenue consequences are too onerous.

The only specific grant included in the capital projections at this stage is the MHCLG Disabled Facilities Grant (DFG). Originally this grant was paid direct to the Council but following the adoption of the Care Act this funding is now routed through the Better Care Fund which is intended to support closer integration and better outcomes in relation to health and social care. The result is that DFG is now paid via Surrey County Council in consultation with the local clinical commissioning groups to improve scrutiny and meet strategic objectives. In forecasting terms, the DFG is assumed to continue and that expenditure will match grant with a neutral impact on the programme.

12.8 New Homes Bonus (NHB)

The NHB was introduced from 2011/12 with the aim of encouraging local authorities to grant planning permissions for the building of new houses in return for additional revenue. Under the scheme, the Government initially matched the average Band D council tax raised on each new home built and empty property brought back into use in any year for a period of 6 years. Local authorities are
not obliged to use the NHB funding for housing development and have local discretion how the balances can be used for the benefit of the authority area.

Then in December 2016, the Government announced that it was changing how NHB would be calculated and that the number of years for which payments are made would be reduced from six to five years in 2017/18 and reduced further to four years from 2018/19. The change in methodology introduced a national baseline for housing growth of 0.4% from 2017 to ensure that ‘the money is used to reward additional housing rather than just normal growth’. The introduction of this so called ‘deadweight’ means that EBC now receives a significantly reduced level of grant. In 2016/17 NHB grant was almost £3 million, the provisional allocation for 2019/20 is £958,000 and potentially less than £240,000 in 2022/23. The Government has also retained the option of making an adjustment to the baseline in future years to reflect significant and unexpected housing growth and that from 2020/21 the Government will explore alternative ways of incentivising housing growth.

Since 2011 the Council has received almost £13.8 million in NHB grant that has generally been allocated to financing capital works and infrastructure, property acquisition or establishing a reserve to finance development and implementation of capital projects. The reduced funding is taken into account in the projections of finance available for future investment and is no longer a significant funding source.

12.9 Other Sources of Capital Funding

Capital receipts, revenue contributions, various types of grant and borrowing are the traditional form of local authority capital financing and have formed the basis of the Council’s financial planning for many years.

Some local authorities have also entered into more complex funding models. Design, build, finance and operate contracts are commonplace and other models are also being developed, often in a bespoke form, to meet the individual service needs of the authority. These are only usually suitable for large projects.

EBC has followed this innovative route in creating EBC Investments Ltd and EBC Homes Ltd to create a wholly owned housing company that will provide local people with affordable housing.

The Capital Strategy acknowledges that complex financial structures may be examined in the future. Any such approach would be subject to the usual constraints of financial prudence and thorough due diligence with the engagement of specialist advice as required. The housing experience can be used to guide forward thinking.

13. Managing the Capital Programme

13.1 The capital programme needs managing just like any other area of the budget.
13.2 To monitor the capital programme the Cabinet shall receive a quarterly capital monitoring report showing the variation at the end of each quarter against the annual estimated project costs as agreed by Council in the budget resolution in February each year. Budgets will be adjusted for slippage from the previous financial year and profiled according to the spending pattern predicted by the lead officer. Reasons for any change to the capital programme must be clearly explained. For this monitoring to be effective a clear distinction must be drawn between a genuine over or underspend and slippage arising from a change in the project programme. Only then will the process provide an appropriate level of monitoring to identify variations from the approved programme.

13.3 In addition, the Overview and Scrutiny Committee has powers to review and/or scrutinise decisions made, or actions taken in connection with the discharge of any of the Council’s functions and to make reports and/or recommendations to the Council and/or Cabinet in connection with the discharge of any functions. These powers may be exercised in respect of any element of the capital programme.

13.4 In most years a significant proportion of capital spend will relate to the property portfolio and in order to assist with the management of this works programme the Council has a long-established Corporate Property Group (CPG). The CPG comprises Heads of Service or their representatives from across the Council and reports directly to the Council Management Board and, if appropriate, to the Cabinet. The objectives of the CPG are wide ranging and have a potentially key role in programme development, management and project delivery.

13.5 Other areas of expenditure will include vehicle replacement and the specification, procurement and implementation of IT hardware and software which will be the responsibility of individual service managers.

13.6 It is quite common that the overall programme will appear underspent at the year end. In 2017/18 the Council spent 82% of the budget and in 2016/17 the Council spent 88% of the budget. In both years the difference was due to slippage in the programme rather than actual savings. The revised 2018/19 capital programme is also likely to slip. There may be several reasons for slippage, some of which will be outside the control of the Council, but often it may be due to over-optimism in project planning or through foreseeable delays in the approval and procurement process. The relatively short-term forward programme exacerbates the issue with the limited lead time between project approval and estimated start on site. On most schemes it is the approval of the funding that will trigger the procurement process to avoid potentially abortive costs on a project that may not proceed. A longer-term approach to capital planning should help to improve performance.

13.7 Valuable lessons can be learned from past projects and that experience has been used in this Strategy to estimate future costs. Past projects also provide experience of scheme risks and sensitivity analysis is a useful tool to assist with an assessment of how to quantify and mitigate project risk. Post project evaluation on capital projects to take account of outcomes against the objectives of the scheme is part of good programme management.
13.8 Using the Council’s existing Project Management Policy and Procedure will help managers be more realistic about the timeframes for programming and implementing their capital schemes. The Policy and Procedure uses well established project management principles and helps to identify and record potential scheme risk, barriers to implementation, guidance on managing change and the implications for cost and on the timetable. The default position should be to use the Project Management Policy and Procedure with an option to opt out on small or straightforward projects.

13.9 The Council employs staff with a wide range of experience, knowledge and skills to initiate, specify, design and procure capital projects. Training for Members and staff is provided where appropriate. There will also be instances where the nature of the project is specialised, or unusually complex and suitably qualified external resources should be employed.

14. **EBC Wider Role in the Community**

14.1 The priorities that support the Council’s Five-Year Vision 2018-23 (see also paragraph 2.1) include reference to facilitating economic growth, including improved infrastructure and housing. A lot can be achieved by direct capital spending but when resources are scarce EBC will have an important role in encouraging external bodies and companies to invest within the EBC boundaries. This wider role should form part of the overall Capital Strategy by providing the sort of environment to attract or facilitate external investment. The draft Economic Strategy 2019-2023 sets out how EBC can engage with sub-regional and national priorities to ensure that business and the local economy can benefit from any future funding or partnership opportunities to support ongoing success.

15. **Conclusions**

15.1 The authority has a balanced capital programme for 2019/20, 2020/21 and 2021/22 and will be able to carry forward capital receipts of approx. £10.5 million into 2022/23. This apparently healthy position disguises a longer-term shortage of capital resources heavily dependent on CIL funding and borrowing as other sources of finance are used up.

15.2 There is a significant annual cost in maintaining the Council’s existing asset base. The Civic offices and the community centres are aging assets and will require capital expenditure in the next 10 years and beyond.

15.3 The major project within the forward programme is the replacement or refurbishment of the Hurst Pool as referenced in the Leisure Facilities Strategy reported to Cabinet in September 2018. This will be subject to further consideration as part of the retender of the leisure contract.

15.4 As detailed in Appendix C there is a significant funding gap between forecast capital requirement and allocated capital resources of almost £23 million up to 2028/29 and over £39 million by 2038/39. The only way to currently finance this
shortfall is to generate new capital receipts, assign existing capital receipts (approx. £5.5 million after holding back £5 million as a contingency) and CIL receipts for maintaining existing assets or to increase EBC borrowing. With new capital receipts in short supply and ‘spare’ CIL balances also likely to be very limited it would appear borrowing will probably be required to meet the greater part of the shortfall in the region of £20 - £40 million.

15.5 At current PWLB borrowing rates the cost of a 10-year maturity loan of £1 million (principal and interest) would be £123,000 per annum. To borrow £20 million at those rates would result in an overall revenue cost of £2.46 million per annum. To borrow £40 million would cost £4.92 million.

15.6 The adoption of the principles and guidelines set out in this Capital Strategy will help EBC take capital investment decisions and manage the capital programme in accordance with best practice.