Lee Valley Regional Park Authority **LEE VALLEY REGIONAL PARK AUTHORITY** **EXECUTIVE COMMITTEE** **17 DECEMBER 2020 AT 12:30**	**Agenda Item No:** **6** **Report No:** **E/702/20**

CAPITAL STRATEGY AND PRUDENTIAL INDICATORS 2020/21 TO 2024/25

Presented by the Head of Finance

EXECUTIVE SUMMARY

This paper sets out a capital strategy that gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services. This strategy integrates the Capital Programme, the Annual Investment Strategy and the Land and Property Strategy.

It also includes the prudential indicators to be approved by the Authority.

RECOMMENDATIONS

Members Approve:

(1) the Capital Strategy as an overarching strategy which encompasses the Capital Programme, Land and Property Strategy, and Annual Investment Strategy; and

(2) the Prudential Indicators for 2020/21 to 2024/25 as set out in paragraphs 4 to 25 of this report

BACKGROUND

1 Publication of CIPFA's Prudential Code 2017 and Treasury Management Code 2017 introduced a change to the reporting requirements around investment within local authorities.

2 The Capital Strategy is an overarching document with a simple guide on the capital programme, borrowing, investments and sets out the prudential indicators that the Authority defines as parameters to work within when setting a prudent and sustainable approach to its investment to meet service needs.

3 The Capital Programme provides more details on capital expenditure and financing from the information provided in the Capital Strategy.

PRUDENTIAL INDICATORS

4 The CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code) requires a range of Prudential Indicators which provide

assurance that the Authority's capital expenditure plans are affordable and proportionate.

5 There are five Prudential Indicators which are defined and quantified within this strategy.

The Prudential Indicators are:

- Estimates of Capital Expenditure;
- Estimates of Capital Financing Requirement;
- Gross Debt and the Capital Financing Requirement;
- Authorised Limit and Operational Boundary for Borrowing; and
- Proportion of Financing Costs to Net Revenue Stream.

CAPITAL EXPENDITURE AND FINANCING

6 Capital expenditure is the money the Authority spends on assets, such as equipment, property and vehicles, which will be used for more than one year. The Authority's capital development programme is geared to the management and development of its existing assets, legacy venues on its land and business development schemes to generate further income for the Regional Park. The capital programme reflects the Authority's key role as a development and enabling organisation and includes a number of projects which are crucial in achieving the objectives set out in the Strategic Business Plan.

7 The current projected capital programme and financing is shown elsewhere on this agenda, Paper E/703/20, and is summarised below. It includes current estimates for capital expenditure for 2020/21 and beyond.

Table 1 : Prudential Indicator: Estimates of Capital Expenditure

	2019/20 Actual	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2025/25 Estimate
Capital Expenditure	**£3.6m**	**£2.9m**	**£14.1m**	**£14.3m**	**£5.1m**	**£1.1m**
Financed by						
External resources*	£0.0m	£0.0m	£0.0m	£0.0m	£0.0m	£0.0m
Internal resources*	£3.6m	£2.9m	£1.1m	£1.3m	£1.1m	£1.1m
Total Financed	**£3.6m**	**£2.9m**	**£1.1m**	**£1.3m**	**£1.1m**	**£1.1m**
Unfinanced Expenditure	**£0.0m**	**£0.0m**	**£13.0m**	**£13.0m**	**£4.0m**	**£0.0m**

8 External resources are principally from grants made to the Authority. Internal resources include capital receipts, existing capital reserves and revenue.

Debt is where the Authority does not fully finance capital expenditure in year, but uses its own cash reserves, which is termed as internal borrowing, or external borrowing from loans. However, all debt must be repaid and this is therefore replaced over time by other forms of financing, usually from revenue which is known as the minimum revenue provision (MRP), or from capital receipts used to finance external debt.

ESTIMATE OF CAPITAL FINANCING REQUIREMENT

9 The Capital Financing Requirement (CFR) is a measure of the amount of capital spending that has not yet been financed by capital receipts, capital grants or

contributions from revenue income. It measures the underlying need to borrow for a capital purpose, although this borrowing may not necessarily take place externally. The Authority has been able to make prudent use of cash that it has already invested for long-term purposes. In doing so, the level of funds we hold for longer-term investment does not reduce but we have been able to adopt an efficient and effective treasury management strategy. This practice is known as 'internal borrowing' and is common in local authorities and means there is no immediate link between the need to borrow to pay for capital spending and the level of external borrowing.

The capital financing requirement increases with new debt-financed capital expenditure and reduces with MRP and any capital receipts used to replace debt. The CFR is expected to decrease by £0.5m during 2020/21. The Authority's estimated CFR is as follows.

Table 2 : Prudential Indicator: Estimates of Capital Financing Requirement

	2019/20 Actual	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Opening CFR	**£12.7m**	**£12.2m**	**£11.7m**	**£24.2m**	**£36.7m**	**£40.3m**
Unfinanced Expenditure	£0.0m	£0.0m	£13.0m	£13.0m	£4.0m	£0.0m
Minimum Revenue Provision	(£0.5m)	(£0.5m)	(£0.5m)	(£0.5m)	(£0.4m)	(£1.2m)
Closing CFR	**£12.2m**	**£11.7m**	**£24.2m**	**£36.7m**	**£40.3m**	**£39.1m**

MINIMUM REVENUE PROVISION POLICY

10 Minimum Revenue Provision (MRP) for historic capital is calculated at 4% of the closing Capital Financing Requirement (CFR) for historic debt from the previous year.

11 For new borrowing the MRP should be linked to when the asset is brought into operational use and calculated on the expected life of the asset, on a straight line basis. The maximum allowable asset life to be used in calculating MRP is 50 years. With regards to the potential borrowing for the Ice Centre, the asset is expected to be brought into use in Autumn 2023 with a minimum useful valuation life of 40 years, so MRP will first be applied in the next full financial year, 2024/25, at a rate of 2.5% pa.

ASSET DISPOSALS

12 When a capital asset is no longer needed it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Authority, via the Land and Property Review/Levy Strategy Working Groups, has identified a number of potential opportunities for disposal of assets and would seek to utilise capital receipts generated from these disposals to support funding for future capital investment, so as placing less reliance in generating these resources from the tax payer via the levy. However, as there is currently no approval for disposal, or certainty that capital receipts will be achieved, estimates have not been included.

Table 3 : Estimate of Capital Receipts

	2019/20 Actual	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Capital Receipts	£1.1m	£0.0m	£0.0m	£0.0m	£0.0m	£0.0m

13 The Authority's future Capital Programme is subject to capital receipts being generated. Without these receipts the Authority will be limited to the amount of capital development investment it can make without the need for external borrowing. It would be prudent to make provision for external borrowing to allow capital development to continue without achieving any capital receipts. However, as previously mentioned, there will be a direct cost to the Authority in the form of MRP and interest repayment costs.

BORROWING STRATEGY

14 The Authority currently has no external borrowing, and has been free from external debt since March 2016. When the Authority is in the position where it needs to borrow, its main objectives would be to achieve low but a certain cost of finance, whilst retaining flexibility should plans change. These objectives are often conflicting and the Authority would seek to strike a balance between cheap short-term loans (currently available at around 1.0%) and long-term fixed rate loans where the future cost is known but higher (currently 1.0% to 2.0%).

15 Projected levels of the Authority outstanding debt, based upon a possible need to borrow up to £30m in the latter part of 2021/22 (subject to final approval of the Ice Centre redevelopment) for cash flow purposes to fund capital expenditure are shown below, compared with the projected capital financing requirement.

Table 4 : Prudential Indicator: Gross Debt and the Capital Financing Requirement

	2019/20 Actual	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
External debt	£0.0m	£0.0m	£30.0m	£30.0m	£30.0m	£29.0m
Capital financing requirement	£12.2m	£11.7m	£24.2m	£36.7m	£40.3m	£39.1m

16 Capital expenditure is usually financed from existing reserves and capital receipts. However, the uncertainty around capital receipts and potential expenditure from the latter part of 2021/22 indicate a need for external borrowing which, in turn, will have an impact on the CFR.

AFFORDABLE BORROWING LIMIT

17 Irrespective of plans to borrow or not, the Authority is required to set an affordable borrowing limit (also known as the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit. There are currently plans to borrow to fund the Ice Centre development in 2021/22, and whilst the actual borrowing amounts are subject to further Member approval, it would be prudent to set the limit for the next financial year to include the expected build cost.

In addition, the Authority should set its limit to include provision for additional borrowing that may be required to deliver the operational strategy as well as for capital development.

The limit reflects the possible need to borrow, subject to timing of capital receipts, to finance the Capital Programme. It does not mean that the Authority will actually borrow, rather that it is authorised, subject to further Member approval, to borrow up to that limit.

Table 5 : Prudential Indicator: Authorised Limit and Operational Boundary for Borrowing

	2021/22 Limit	2022/23 Limit	2023/24 Limit	2024/25 Limit
Authorised limit	£35.0m	£35.0m	£5.0m	£5.0m
Operational limit	£2.0m	£2.0m	£2.0m	£2.0m

TREASURY INVESTMENT STRATEGY

18 Treasury management investments arise from the Authority receiving cash (from, for example, the levy and income from fees and charges) before it is required to pay for its expenditure in cash (e.g. paying staff and suppliers).

19 The Authority's treasury management investments range from overnight investments in interest bearing current bank accounts to longer term investments with established financial institutions. The principles which underpin these investments are contained within the Treasury Management Report and Annual Investment Strategy which is approved each year by Executive Committee.

20 Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Head of Finance and specifically nominated finance staff, who must act in line with the treasury management strategy.

REVENUE BUDGET IMPLICATIONS

21 Although capital expenditure is not charged directly to the revenue budget, the MRP, and if applicable, interest payable on loans are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount of revenue budget to be met from the Levy.

22 Currently the Authority does not have any external borrowing, so the financing costs for 2020/21 are made up of the MRP and investment interest received. The potential change in financing costs from 2021/22 is based on the Authority borrowing £30m in the latter part of 2021/22, with the costs being rolled up into the project and repayments commencing in 2024/25.

Table 6: Prudential Indicator: Proportion of Financing Costs to Net Revenue Stream

	2019/20 Actual	2020/21 Revised Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Financing Costs	£0.4m	£0.5m	£0.4m	£0.4m	£0.4m	£1.1m
Proportions of net revenue cost %	4.3%	4.8%	4.4%	3.8%	4.0%	11.6%

KNOWLEDGE AND SKILLS

23 The Authority employs professionally qualified and experienced staff in senior

positions with responsibility for making capital expenditure, borrowing and investment decisions.

24 Where Authority staff do not have the knowledge and skills required, or where further support is needed, use is made of external advisors and consultants that are specialists in their field. The Authority currently employs Tullet Prebon as treasury management advisors.

25 The Authority also has a service level agreement with the London Borough of Enfield for provision of Section 151 services and is able utilise this knowledge and experience to assist with its own decisions.

ENVIRONMENTAL IMPLICATIONS

26 There are no environmental implications arising directly from the recommendations in this report.

FINANCIAL IMPLICATIONS

27 These are dealt with within the body of the report.

HUMAN RESOURCE IMPLICATIONS

28 There are no human resource implications arising directly from the recommendations in this report.

LEGAL IMPLICATIONS

29 These are dealt with within the body of the report.

RISK MANAGEMENT IMPLICATIONS

30 There are no risk management implications arising directly from the recommendations in this report. However future capital expenditure and its phasing may require support from borrowing as the level of cash receipts is dependent on future land sales that are yet to be fully determined in both terms of value and timing.

EQUALITY IMPLICATIONS

31 There are no equality implications arising directly from the recommendations in this report.

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PREVIOUS COMMITTEE REPORTS

Executive	E/703/20	Proposed Capital Programme 2020/21 (Revised) to 2025/25	17 December 2020
Executive	E/671/20	Annual Report on Treasury Management Activity 2019/20 and Annual Investment Strategy 2020/21	21 May 2020
Executive	E/647/19	Capital Strategy and Prudential Indicators 2019/20 to 2023/24	19 December 2019

Executive	E/601/18	Borrowing Limits and Prudential Indicators 2018/19 (Revised) – 2022/23	13 December 2018

LIST OF ABBREVIATIONS

CIPFA	Chartered Institute of Public Finance and Accountancy
AAT	Association of Accounting Technicians
CFR	Capital Financing Requirement
MRF	Minimum Revenue Provision

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