Nottinghamshire County Council Capital Strategy

Purpose and Aims

1. The Prudential Code for Capital Finance in Local Authorities was updated by the Chartered Institute of Public Finance and Accountancy in December 2017. The framework established by the Prudential Code supports local strategic planning, local asset management planning and proper option appraisal.

2. The objectives of the Prudential Code are to ensure that the capital expenditure plans of local authorities are affordable, prudent and sustainable and that treasury management decisions are taken in accordance with good professional practice and in full understanding of the risks involved.

3. The Prudential Code requires authorities to look at capital expenditure and investment plans in the light of overall organisational strategy and resources and ensure that decisions are made with sufficient regard to the long run financing implications and potential risks to the authority.

4. The Prudential Code sets out that in order to demonstrate that the authority takes capital expenditure and investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability, authorities should have in place a capital strategy. The capital strategy should set 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.

5. This capital strategy sets out a framework for the self-management of capital finance and examines the following areas:

    - Capital expenditure and investment plans
    - Prudential Indicators
    - External debt
    - Treasury Management

National Context

6. It is important to set out the external environment in which Nottinghamshire County Council is currently operating. Some of the key factors that impact directly on the capital programme are outlined below:

    - The Council continues to operate in a challenging financial landscape with funding for local authorities expected to undergo fundamental structural changes over the next few years. Increased demand in areas such as Adult and Children's Social Care alongside the postponement to a new Business Rates Retentions Scheme, the delayed Fair Funding Review, the stalled Adult Social Care Green Paper and any implications that may arise from Brexit negotiations make the current financial position particularly challenging for local authorities.

- The Government has chosen to prioritise high-value investment, specifically in infrastructure and innovation that will directly contribute to raising Britain's productivity.

- Mechanisms for distributing government funding continue to evolve through the Government's devolution agenda specifically through the Local Growth Fund (LGF) and the increased role of Local Enterprise Partnerships (LEPs) in the strategic oversight of regional areas.

- The LGF now totals over £12 billion (including devolution deals) of capital investment. This presents both opportunities and risks to existing levels of government service delivery and investment, as LEPs with the strongest Strategic Plans will gain the greatest share.

Managing the Future – Nottinghamshire County Council's Strategic Response

7. The County Council's strategic plan for 2017 - 2021, Your Nottinghamshire, Your Future, is a four-year plan, reviewed annually, that sets out the strategic ambition for the future of Nottinghamshire and the Council.

8. "Your Nottinghamshire, Your Future" is structured around four vision statements:

   - A great place to bring up your family
   - A great place to fulfil your ambition
   - A great place to enjoy your later life
   - A great place start and grow your business

9. In addition, four detailed departmental strategies have been developed to ensure that each Department is designed to offer the best possible services whilst making best use of the Council's resources.

10. As reported to Policy Committee in October 2019, given the context of ongoing financial pressures, increased and complex demand and changing resident expectations, a new model for transformation is proposed to support the organisation to move forward and build on our strong foundations. The following three tier approach is proposed to reposition the Council and help achieve future transformation objectives :-

    - Tier 1 – Strategic Review of Outcomes (Achieve)
    - Tier 2 – Targeted Cross Cutting Transformation Reviews (Transform)
    - Tier 3 – Ongoing efficiency as part of continuous improvement (Save)

11. This new approach to transformation will lay the foundations for a review of the Council Plan in 2021. A key part of this work is in cementing the County's position as a leading authority recognised by Government, partners and communities for providing excellent services, future proofed for a changing world.

12. To help the Council deliver the departmental strategies and hence the Council Plan it is essential that necessary long term fixed assets continue to be made available. The provision of long term assets is further defined as being capital expenditure.

13. There are a number of local influences that help shape the need for capital investment across the county as follows:

    - Nottinghamshire remains an area that is experiencing significant population growth. This is contributing to significant pressure being placed on school places and infrastructure.
    - There is pressure on budgets to keep pace with the deterioration of roads from exceptional weather conditions and increased usage.
    - In line with the national context, safeguarding of children remains a challenging area for all local authorities.
    - The Council is committed to investing to stimulate the Nottinghamshire economy in order to place the county at the forefront of business, commerce, jobs and economic prosperity.

Corporate Property Strategy

14. As reported to Policy Committee in October 2019, the Council has embarked upon a Property Transformation Programme to drive improvements in the operation of our property services, which provide essential support to Council services, and to re-align them to ensure maximum impact on investment and growth of the Nottinghamshire economy.

15. As part of this strategy, a Corporate Property Strategy was approved by Policy Committee in October 2018. The purpose of the Corporate Property Strategy and the associated Property Asset Management Plan is to provide a framework to support the development and management of the Council's land and property assets to achieve our ambition of delivering collaborative property solutions which achieves corporate objectives.

16. Work is on-going to develop Service Asset Management Plans which will be used to articulate service land and property needs. They will be updated on a yearly basis and reviewed by Senior Officers and members. They will inform bids for capital investment and will enable the Council to develop a strategic approach to addressing the services asset requirements within the overall Property Asset Management Plan.

What is Capital Expenditure?

17. An understanding of what constitutes capital expenditure is fundamental to realising the benefits that an authority can obtain under the Prudential framework. Unless expenditure qualifies as capital it will normally fall outside the scope of the framework and be charged to revenue in the period that the expenditure is incurred. If expenditure meets the definition of capital, there may

be opportunities to finance the outlay from capital receipts or by spreading the cost over future years' revenues.

18. There are three ways in which expenditure can qualify as capital under the framework:-

- The expenditure results in the acquisition, construction or enhancement of fixed assets (tangible and intangible) in accordance with 'proper practices'.
- The expenditure meets one of the definitions specified in regulations made under the 2003 Local Government Act.
- The Secretary of State makes a direction that the expenditure can be treated as capital expenditure.

Approach to Capital Investment

19. Nottinghamshire County Council's Capital Strategy defines and outlines the Council's approach to capital investment and is fundamental to the Council's financial planning processes. It aims to ensure that:

- Capital expenditure contributes to the achievement of the Council's strategic plan.
- An affordable and sustainable capital programme is delivered.
- Use of resources and value for money is maximised.
- A clear framework for making capital expenditure decisions is provided.
- A corporate approach to generating capital resources is established.
- Access to sufficient long term assets to provide services are acquired and retained.
- Invest to save initiatives to make efficiencies within the Council's revenue budget are encouraged.
- An appraisal and prioritisation process for new schemes is robust.

Governance Arrangements

Capital Programme Approvals

20. The Authority's constitution and financial regulations govern the capital programme as set out below:

- All capital expenditure must be carried out in accordance with the financial regulations and the Council's Constitution.
- The expenditure must comply with the statutory definition of capital purposes as defined within this document and wider financial standards.
- The Capital Programme approved by Full Council as part of the Council's annual budget report sets the capital funding availability for the Council, the prioritisation of funding and the schemes receiving entry into the Capital Programme.
- All schemes are formally approved into the capital programme by following a process as set out in the financial regulations.

- Officers are not authorised to commit expenditure without prior formal approval as set out in the financial regulations.
- Each scheme must be under the control of a responsible person/project manager.
- Corporate Directors must take a Latest Estimated Cost report to Finance and Major Contracts Management Committee where the capital cost is over £1 million.
- Any agreements (such as section 106) which contractually commit to procure capital schemes will need to follow the same approval process as other capital expenditure before it can be formally incorporated into the capital programme.

Capital Programme Bodies

21. The main internal bodies that are responsible for the governance and management of the capital programme are the Full Council, Policy Committee, Finance and Major Contracts Management Committee and the Corporate Asset Management Group.

22. **Full Council:**

- Approves the capital programme as part of the Annual Budget Report within the strategic boundaries set by the Council.
- Approves capital schemes into the approved capital programme to enable commencement of delivery and schemes to start to incur expenditure.

23. **Policy Committee / Finance and Major Contracts Management Committee:**

- Approves additional schemes into the capital programme and cost variations to existing schemes.
- Receives Latest Estimated Cost reports where the capital costs are in excess of £1m.

24. **Corporate Asset Management Group (CAMG)** – CAMG is a cross-service group of officers with a finance, service and property management background. It is responsible for ensuring that the County Council has a clear and cohesive strategy for managing its physical assets and to oversee the development and delivery of the County Council's capital programme in support of that strategy.

Funding Streams

25. Nottinghamshire County Council's Capital Programme is funded from a mix of sources including:-

- **Prudential Borrowing** – The introduction of the Prudential Code in 2004 allowed the Council to undertake unsupported borrowing itself. This borrowing is subject to the requirements of the Prudential Code for Capital Expenditure for Local Authorities. The Council must ensure that unsupported borrowing is affordable, prudent and cost effective. This funding can also be used as an option to front fund development to stimulate growth. This has provided the Council with the flexibility to raise capital funding as demand and business need have dictated. This type of borrowing has revenue implications for the Council in the form of financing costs.

- **External Grants** – The largest form of capital funding comes through as external grant allocations from central government departments such as the Department for Transport and Department for Education.

- **Section 106 and External Contributions** – Elements of the capital programme are funded by contributions from private sector developers and partners. Growth in Nottinghamshire has resulted in Section 106 contributions from developers accounting for significant elements of funding of the capital programme in recent years.

- **Revenue Funding** – The Council can use revenue resources to fund capital projects on a direct basis and this funding avenue has been used in the past. However, the impact of austerity on the Council's revenue budget has reduced options in this area and therefore the preference is for Invest to Save options to be adopted where feasible.

- **Capital Receipts** – The Council is able to generate capital receipts through the sale of surplus assets such as land and buildings. The Council seeks to maximise the level of these resources which will be available to support the Council's plans.

26. The size of the Capital Programme will be influenced by funding sources and financing costs. The main limiting factor on the Council's ability to undertake capital investment is whether the revenue resource is available to support in full the implications of capital expenditure, both borrowing costs and running costs, after allowing for any support provided by central government, now mainly through capital grants.

Overview of the Capital Programme

27. The following table shows Nottinghamshire County Council's overall Capital Programme by Committee and how it is funded from 2019/20 to 2023/24:-

Table D1 - Capital Programme by Committee

	Revised 2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	TOTAL £m
Committee:						
Children & Young People*	31.494	33.731	17.137	5.500	5.500	93.362
Adult Social Care & Public Health	3.328	0.409	0.000	0.000	0.000	3.737
Communities & Place	50.854	56.682	35.393	23.086	20.450	186.465
Policy	33.111	23.933	8.550	4.400	4.400	74.394
Finance & MCM	0.150	0.180	0.180	0.180	0.180	0.870
Personnel	0.128	0.249	0.000	0.000	0.000	0.377
Contingency	-	2.200	2.200	2.200	2.795	9.395
Capital Expenditure	**119.065**	**117.384**	**63.460**	**35.366**	**33.325**	**368.600**
Financed By:						
Borrowing	62.656	53.405	33.233	11.330	11.395	172.019
Capital Grants	53.995	62.192	29.697	23.175	21.422	190.481
Revenue / Reserves	2.414	1.787	0.530	0.861	0.508	6.100
Total Funding	**119.065**	**117.384**	**63.460**	**35.366**	**33.325**	**368.600**

*This table excludes funding that is given directly to schools.

Description of Major Schemes

28. The main capital projects / programmes of work that are incorporated into the Authority's capital programme are identified below:

- **Schools Building Improvement Programme (SBIP) –** The SBIP focuses on the most immediate condition issues relating to heating, lighting and power, windows and roofing of the County Councils' maintained school building stock.
- **School Places Programme** - The School Places Programme focuses on the Council's statutory duty to provide sufficient school places. This applies to sufficiency planning across all schools, including academies. It is expected that local authorities will work closely with academies and the voluntary aided sector to meet this statutory responsibility and function. The fulfilment of this duty is described as meeting Basic Need. Children and Young People's Services analyse the pupil projection data available to identify schools which would be

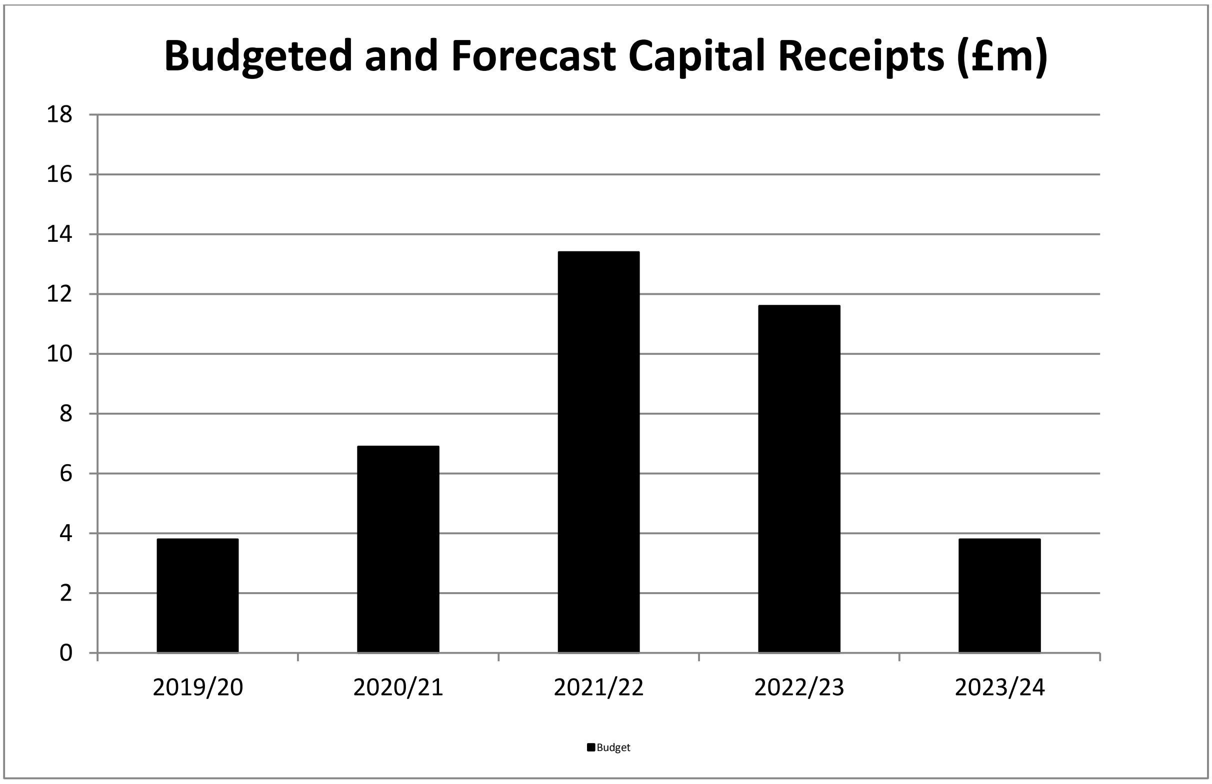
best suited to fulfil the Basic Need requirement and secure diversity of provision and increase the opportunity for parental preference.

- **Replacement Schools** – As part of the programme to ensure that there are sufficient school places across the county four new replacement schools are to be built in Bestwood, Newark, Hucknall and West Bridgford.
- **Roads Maintenance and Renewals -** This major programme of work supports local highway maintenance across the County and is funded mainly from Department for Transport grant with a local top up funded from capital allocation.
- **Integrated Transport Measures (ITM) -** The ITM is a package of capital schemes developed to support the Local Transport Plan and is funded mainly by direct grant from Government with a local top up funded from capital allocation.
- **Gedling Access Road (GAR) -** This major transport scheme will enable the realisation of a key strategic development site in Gedling. It will also fulfil the long term proposal to provide a bypass around Gedling village. The project is to be delivered by key public sector partners working jointly towards achieving common objectives for the future redevelopment of the former Gedling Colliery site.
- **Building Works -** The building works capital budget funds essential capital works to maintain the condition of the Council's property portfolio.
- **Homes England** – The Council has been successful in securing Homes England Local Authority Accelerated Construction Fund funding to assist the development of three sites in its ownership. The fund aims to make the best possible use of public sector land to increase the supply of new homes by removing the barriers facing local authorities with development on their sites.
- **Toton Land Purchase** – As reported to Policy Committee in November 2019, approval was given to fund key acquisitions in Toton that will directly influence development around the HS2 hub which will enable Council and a locally led delivery body to guide the delivery of the Toton Growth Strategy.
- **Superfast Broadband** - The Council has contributed to and secured external funding from Broadband Deliver UK, European Regional Development Fund, Local Growth Fund and other local authorities to enable Superfast Broadband to be rolled out to 97% of Nottinghamshire premises.

Capital Receipts / Disposals

29. Anticipated capital receipts are reviewed on a regular basis by the Finance and Major Contracts Management Committee. All forecasts are based on estimated disposal values of identified properties and prudently assume a slippage factor based on risks associated with each property.

30. The chart below shows the budgeted capital receipts for the four years to 2023/24:



31. Local authorities have been given the opportunity to use capital receipts to fund one off costs associated with transformation to 2021/22. This approach will be reviewed on an annual basis. It is proposed that capital receipts to 2021/22 are, in the first instance, used to fund transformational costs associated with the Programmes and Projects Team and the implementation of the IT Cloud platform. Any excess capital receipts will be set against previous years' borrowing thereby reducing the impact of the Minimum Revenue Provision on the revenue accounts.

2020/21 PRUDENTIAL INDICATORS FOR CAPITAL FINANCE

32. This section of the capital strategy sets out the prudential indicators and outlines how expenditure will be financed by borrowing in an affordable, prudent and sustainable way.

Information and Advice

33. The Local Government Act 2003 enables local authorities to determine their programmes for capital investment and associated borrowing requirements, provided they have regard to the Prudential Code for Capital Finance in Local Authorities developed by CIPFA and also take advice from the Section 151 Officer.

34. The Executive Summary of the Code states that “The framework established by the Prudential Code should support local strategic planning, local asset management planning and proper option appraisal. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice.”

35. The Code sets out a number of prudential indicators designed to support and record local decision making and it is the duty of the Service Director – Finance, Infrastructure and Improvement (the Council’s Section 151 Officer) to ensure that this information is available to Members when they take decisions on the County Council’s capital expenditure plans and annual budget. Key issues to be considered are:

    - Affordability (e.g. implications for Council Tax)
    - Prudence and sustainability (e.g. implications for external borrowing and whole life costing)
    - Value for money (e.g. option appraisal)
    - Stewardship of assets (e.g. asset management planning)
    - Service objectives (e.g. alignment with the Council’s Strategic Plan)
    - Practicality (e.g. whether the capital plans are achievable).

Affordability

36. The fundamental objective in the consideration of the affordability of the Authority’s capital plans is to ensure that the level of investment in capital assets proposed means that the total capital investment of the authority remains within sustainable limits.

37. In considering the affordability of its capital plans, the Authority is required to consider all of the resources currently available to it and estimated for the future, together with the totality of its capital plans, income and expenditure forecasts.

38. The costs of financing capital expenditure are:

- Interest payable to external lenders less interest earned on investments; and
- Amounts set aside for repayments of amounts borrowed (including repayments of amounts relating to PFI schemes and other finance lease liabilities).

The relevant figures from the 2018/19 Accounts are as follows.

Table D2 – 2018/19 Capital Financing Costs and Net Revenue Stream

Capital Financing Costs	**£'m**
Interest Payable (incl. PFI/Finance Leases)	37.409
Interest and Investment Income	(0.823)
Repayment of Previous Years' Borrowing	0.681
Repayment of PFI/Finance Lease Liabilities	6.948
Other Amounts Set Aside for Repaying Debt	8.300
Total Capital Financing Costs	**52.515**

Net Revenue Stream	**556.740**

39. The Capital Financing Costs as a proportion of Net Revenue Stream for 2018/19 and future years are shown in the table below:

Table D3 – Capital Financing Costs as a Proportion of Net Revenue Stream

Capital Financing Costs as a proportion of Net Revenue Stream		
Actual	2018/19	9.4%
Estimates	2019/20	7.7%
	2020/21	9.8%
	2021/22	10.8%
	2022/23	10.7%
	2023/24	9.8%

40. The increase in future years proportions relates mainly to the reducing forecast Net Revenue Spend, re-instatement of full MRP charges following the full utilisation of the previously identified over-provision as well as the variation in the levels of capital receipts available to set against amounts previously borrowed. The proportion of capital financing costs to net revenue stream will be kept under review.

Prudence and Sustainability

41. The Prudential Code requires that the Authority shall ensure that all of its capital expenditure, investments and borrowing decisions are prudent and sustainable. In doing so it will take into account its arrangements for the repayment of debt and consideration of risk and the impact on the Authority's overall fiscal sustainability.

42. The Authority is required to make reasonable estimates of the total capital expenditure that it plans to incur in the forthcoming financial year and at least the following two financial years. These indicators, together with anticipated sources of finance, are as follows.

Table D4 – Estimates of Capital Expenditure

	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m
Capital Expenditure	**117.384**	**63.460**	**35.366**	**33.325**
Funded from:				
Borrowing	53.405	33.233	11.330	11.395
Grants and Contributions	62.192	29.697	23.175	21.422
Revenue / Reserves	1.787	0.530	0.861	0.508
Total Capital Financing Costs	**117.384**	**63.460**	**35.366**	**33.325**

43. The proposed level of borrowing under the Prudential Code for 2021/21 is £53.4m.

44. One of the features of the Prudential Code arrangements is the need to calculate the Capital Financing Requirement. This figure covers capital expenditure which has not yet been permanently financed through the revenue account. It is derived by consolidating a number of Balance Sheet items as follows.

Table D5 – Capital Financing Requirement 2018/19

	£m
Fixed Assets	1,398
Short-term Assets Held For Sale	1
Capital Adjustment Account	(415)
Revaluation Reserve	(232)
Capital Financing Requirement as at 31/3/19	**752**

45. The Code states that "In order to ensure that over the medium term net debt will only be for a capital purpose, the local authority should ensure that net debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years." This is a key indicator of prudence.

46. The Capital Financing Requirement needs to be rolled forward to the estimated position at the end of 2019/20:

Table D6 – Estimated Capital Financing Requirement 2019/20

	£m
Capital Financing Requirement 2018/19	**752**
Borrowing in 2019/20	63
Additional PFI/Finance Lease Liabilities in 2019/20	2
Repayment of PFI/Finance Lease Liabilities in 2019/20	(3)
Capital Receipts set against previous borrowing in 2019/20	0
Other amounts set aside for Repayment of Debt in 2019/20	(6)
Estimated Capital Financing Requirement 2019/20	**808**

47. The additional Capital Financing Requirements for the next 3 years are:

Table D7 – Estimated Capital Financing Requirements 2020/21 - 2022/23

	2020/21 £m	2021/22 £m	2022/23 £m
New Borrowing	53	33	11
Additional PFI/Finance Lease Liabilities	4	3	-
Repayment of PFI/Finance Lease Liabilities	(6)	(6)	(6)
Capital Receipts set against previous borrowing	(4)	(11)	(12)
Other amounts set aside for Repayment of Debt	(11)	(9)	(8)
Capital Financing Requirement Net Additions	**36**	**10**	**(15)**
Estimated Capital Financing Requirement	**844**	**854**	**839**

48. As such there is a requirement to ensure that net debt (the sum of borrowing and other long-term liabilities, net of investments) in 2020/21 does not, except in the short term, exceed £854m (i.e. the estimated CFR for 2021/22).

External Debt

49. The Local Government Act 2003 requires the County Council to set two borrowing limits for next year and the following two years with respect to external borrowing.

50. Operational Boundary – has to be set for both borrowing and long term liabilities. This measure encompasses all borrowing and is used in-year as a tool for monitoring the Council’s prudent borrowing requirements. The operational boundary is calculated by taking account of existing borrowing and long term liabilities, planned new borrowing, net change in long term liabilities and any amounts set aside for repayment of debt.

51. Authorised Limit – this higher measure, is the upper limit on the level of gross indebtedness which must not be breached without County Council approval. If it appears that the Authorised Limit might be breached, the Service Director –

Finance, Infrastructure and Improvement has a duty to report this to the County Council for appropriate action to be taken.

52. The Operational Boundary for external debt for the next three years is built up from the existing level of external borrowing, which was £482m, and the level of relevant liabilities (including finance lease liabilities), which was £117m, on the Balance Sheet at 31 March 2019.

53. These figures can be rolled forward to provide the proposed Operational Boundaries for 2020/21 and subsequent years.

Table D8 – Operational Boundaries 2020/21 – 2022/23

	Borrowing £m	Other Long-Term Liabilities £m	TOTAL £m
External borrowing at 31 March 2019	482	-	482
Other Long-Term Liabilities at 31 March 2019	-	117	117
Net new borrowing in 2019/20	(4)	-	(4)
Net change in PFI/finance lease liabilities	-	(1)	(1)
Estimated external borrowing at 31 March 2020	478	116	**594**
Capital expenditure financed by borrowing 2020/21	53	-	53
Amounts set aside for repayment of debt	(15)	-	(15)
Net change in PFI/finance lease liabilities	-	(3)	(3)
Contingency for changes in cash flow forecast	40	-	40
Operational Boundary 2020/21	556	113	**669**
Capital expenditure financed by borrowing 2021/22	33	-	33
Amounts set aside for repayment of debt	(19)	-	(19)
Net change in PFI/finance lease liabilities	-	(3)	(3)
Contingency for changes in cash flow forecast	40	-	40
Operational Boundary 2021/22	610	110	**720**
Capital expenditure financed by borrowing 2022/23	11	-	11
Amounts set aside for repayment of debt	(20)	-	(20)
Net change in PFI/finance lease liabilities	-	(6)	(6)
Contingency for changes in cash flow forecast	40	-	40
Operational Boundary 2022/23	641	104	**745**

54. The Authorised Limits should not need to be varied during the year, bar exceptional purposes. It is proposed to add a further £25m to the Operational Boundaries for Borrowing to provide sufficient headroom for events such as unusual cash movements. The proposed Authorised Limits are:

Table D9 – Authorised Limits 2020/21 – 2022/23

	Authorised Limit		
	Borrowing £m	**Other Long-Term Liabilities £m**	**Borrowing and Other Long-Term Liabilities £m**
2020/21	581	113	694
2021/22	635	110	745
2022/23	666	104	770

55. Both the Authorised Limits and Operational Boundaries are less than the Capital Financing Requirement because best practice in treasury management means that actual borrowing is below the notional underlying borrowing requirement.

56. The Prudential Code indicator in respect of treasury management is the adoption of the CIPFA Treasury Management Code of Practice. The County Council has formally adopted the code and approves an annual Treasury Management Policy and Strategy. This includes setting the treasury indicators:

- upper limits for fixed and variable interest rate exposures
- upper limit for investments over 364 days
- upper and lower limits for the maturity structure of borrowing.

Value for money – option appraisal

57. The County Council's Capital Programme is driven by the desire to provide high quality, value for money public services and is monitored by the CAMG. Business cases for proposed new capital schemes are reviewed by this group against an agreed prioritisation criteria. The results of this exercise are presented to Finance and Major Contracts Management Committee.

Stewardship of Assets

58. The Council's Asset Management Plan sets out the condition of its assets and the arrangements for managing these effectively. The Council's Corporate Property Strategy enhances these arrangements, including increasing the awareness that efficient use of property is an important element of maximising the value obtained from the Council's overall resources.

Service Objectives

59. The option appraisal of proposed capital schemes overseen by CAMG considers, amongst other factors, the following:

- How the proposal helps achieve the objectives and priorities set out in the Council's Strategic Plan 2017-2021.
- How the proposal will help achieve objectives set out in Departmental Strategic Plans.
- The service improvements and other anticipated benefits expected to be delivered from the investment.

60. **Practicality / Monitoring**

- Capital budget holders are responsible for providing monthly forecasts to the Financial Strategy and Accounting Team. Any slippage on schemes is identified as soon as possible.
- All forecasts are collated by the Financial Strategy and Accounting Team and reported to Finance and Major Contracts Management Committee on a monthly basis.

Recommendation

61. It is recommended that the Prudential Indicators in Table D10 are approved as part of the 2020/21 budget.

Table D10 – Prudential Indicators 2020/21 – 2022/23

	2020/21	**2021/22**	**2022/23**
Estimated capital expenditure	£117.3m	£63.5m	£35.4m
Estimated Capital Financing Requirement	£844m	£854m	£839m
Authorised limit for external debt	£694m	£745m	£771m
Operational boundary for external debt	£669m	£720m	£745m
Financing costs as a % of net revenue stream	9.8%	10.8%	10.7%

Report of the Service Director (Finance, Infrastructure & Improvement)

Treasury Management Strategy 2020/21

Introduction

62. Treasury Management is defined by the Chartered Institute of Public Finance and Accountancy (CIPFA) as:

> "the management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

63. The Local Government Act 2003 (the Act) requires local authorities "to have regard –
    (a) to such guidance as the Secretary of State may issue, and
    (b) to such other guidance as the Secretary of State may by regulations specify for the purposes of this provision."

64. The Local Authorities (Capital Finance and Accounting)(England) Regulations 2003 state that:

> "In carrying out its capital finance functions, a local authority must have regard to the code of practice in 'Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes' (regulation 24)."

65. The 2003 regulations further require local authorities to have regard to the code of practice entitled the 'Prudential Code for Capital Finance in Local Authorities' (published by CIPFA), when considering how much they can afford to borrow. Both the Treasury Management Code (the Code) and the Prudential Code were updated in December 2017.

66. With regard to investment of funds, the Secretary of State issued revised guidance in 2010 that requires local authorities to prepare an annual investment strategy which has the key objectives of security and liquidity of funds.

67. The Code has 3 key principles which are:

- the establishment of 'comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury activities'.
- the effective management and control of risk are prime objectives and that responsibility for these lies clearly within the organisation.
- the pursuit of value for money and the use of suitable performance measures are valid and important tools.

68. In accordance with the CIPFA Code, the Council adopts the following:

(a) The Council will create, and maintain, as the cornerstones for effective treasury management:

- a Treasury Management Policy Statement, stating the policies, objectives and approach to risk management of its treasury management activities
- suitable Treasury Management Practices (TMPs), setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject to amendment only where necessary to reflect the particular circumstances of the Council. Such amendments will not result in the Council materially deviating from the Code's key principles.

(b) The Council will receive reports on its treasury management policies, practices and activities, including an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.

(c) The Council delegates responsibility for the implementation, scrutiny and monitoring of its treasury management policies and practices to the Treasury Management Group, comprising:

- Service Director (Finance, Infrastructure & Improvement)
- Group Manager (Financial Services)
- Senior Accountant (Financial Strategy & Accounting)
- Senior Accountant (Pensions & Treasury Management)

The responsible officer for the execution and administration of treasury management decisions is the Senior Accountant (Pensions & Treasury Management), who will act in accordance with the policy statement and TMPs.

69. With regard to cash balances that form part of the Nottinghamshire County Council Pension Fund, the Council delegates responsibility for the setting of treasury management policies and practices to the Pension Fund Committee.

70. This Treasury Management Strategy has been prepared in accordance with regulations, guidance and codes of practice to support the Council's Medium-Term Financial Strategy and in particular the financing of the capital programme and the management of cash balances. In addition to this strategy there is a Treasury Management Policy Statement in Appendix E that underpins the strategy, together with the TMPs that govern treasury management operations.

71. The strategy covers:

- Current treasury position
- Borrowing requirement
- Treasury Indicators
- Interest rate forecasts
- Borrowing strategy
- Investment strategy

Current Treasury Position

72. The table below shows the Council's forecast treasury position as at 31 March 2020:

Table 1		**Total** **£m**	**Average Interest Rate**
EXTERNAL BORROWING			
Fixed Rate	PWLB	397.8	4.18%
	Market loans	90.0	3.83%
Total External Borrowing		**487.8**	**4.12%**
Other Long Term Liabilities		114.9	
Total Gross Debt		**602.7**	
Less: Investments		(22.6)	
Total Net Debt		**580.1**	

Note 1: PWLB = Public Works Loans Board
Note 2: Figures exclude accrued interest

Borrowing Requirement

73. Under the Prudential Code, the Council is required to calculate the 'Capital Financing Requirement' (CFR). This represents the Council's underlying need to borrow for the approved capital programme. New capital expenditure, financed by borrowing or by credit arrangements such as finance leases and private finance initiative schemes, increases the CFR.

74. The Council also sets aside an amount each year as a provision for the repayment of debt. This is known as the Minimum Revenue Provision (MRP) and is, in effect, the principal repayment for the borrowing expected to be undertaken by the Council to finance its capital programme. MRP set aside reduces the CFR.

75. The difference between the CFR and the total of long-term liabilities and existing and new borrowing indicates that the Council has made temporary use of internal cash balances (from its own earmarked reserves and working capital) to finance the capital programme. This is known as "internal borrowing". Internal borrowing is a way of making short-term savings and avoiding the risks associated with holding large cash balances and is explained further in the "Borrowing Strategy" section below.

76. The Local Government Act 2003 and supporting regulations requires the Council to determine and keep under review how much it is prepared to borrow, termed the "Authorised Limit". This limit is determined for external borrowing (including both long-term and temporary borrowing and other forms of long-term liability, such as credit arrangements). This limit reflects the need to borrow for capital purposes. The Authorised Limit is set for at least the forthcoming financial year and two successive financial years. The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that its total capital investment is 'affordable, prudent and sustainable'.

77. In practice during the year the level of borrowing will be monitored against the "Operational Boundary". This represents the planned level of borrowing for capital purposes and, as shown in Appendix D, is made up as follows:
    - Existing borrowing and other long-term liabilities
    - Increased by:
        - planned new borrowing
        - net change in long-term liabilities
    - Reduced by amounts set aside for repayment of debt (referred to as Minimum Revenue Provision or MRP).
    - Contingency for changes to reserves forecast

78. The Operational Boundary is set for the forthcoming financial year and next two financial years. Any breach of this indicator would provide an early warning of a potential breach of the Authorised Limit and allow time for the Council to take appropriate action.

79. There are two main reasons why planned actual borrowing may be lower than that shown as being required to finance the capital programme. These are slippage in capital schemes and the Council temporarily making use of its cash reserves to delay external borrowing (the internal borrowing referred to above). The main components involved in calculating planned actual borrowing over the next three years are shown in the table below.

Table 2	2018/19 Actual	2019/20 Est.	2020/21 Est.	2021/22 Est.	2022/23 Est.
	£m	**£m**	**£m**	**£m**	**£m**
Closing Capital Financing Requirement	752.5	808.0	846.5	856.2	840.0
Less:					
- Long-term liabilities	-116.1	-114.9	-112.1	-109.2	-103.3
- Existing borrowing	-471.8	-487.8	-475.2	-464.4	-453.6
- Cap Ex to be financed by borrowing (a)			-53.4	-33.2	-11.3
- Replenishment/Replacement borrowing (b)			2.0	-41.5	-64.0
Internal borrowing	**164.6**	**205.3**	**207.8**	**207.8**	**207.8**
Cash and cash equivalents	60.3	22.6	20.0	20.0	20.0
Fixed investments	0	0	0	0	0
Y/E investment balances	**60.3**	**22.6**	**20.0**	**20.0**	**20.0**
Cumulative minimum borrowing req. (a+b)			**51.4**	**74.7**	**75.3**

80. The table above shows that, after factoring in internal borrowing, the Council is expecting to borrow approximately £75m from the financial markets over the next 3 years. This is a minimum, based on the latest capital expenditure, financing and reserves forecasts, and should not result in any surplus cash that could be held as long-term investments by the Council. Therefore, if reserve balances are used quicker than forecast, or if working capital is reduced, then additional borrowing will be necessary.

81. The total new long-term borrowing taken in 2019/20 is forecast to be £30m, and this is higher than the £6m reported in the 2019/20 Strategy Report, due to slippage from 2018/19 later being added to the 2019/20 capital programme. It should also be noted that in December 2019 £20m was borrowed on a short-term basis from another local authority. This is to be redeemed before the year-end and so is not included in the above table.

82. Under the capital finance regulations, local authorities are permitted to *fully borrow* (ie. use no internal borrowing) up to three years in advance of need as determined by the Capital Financing Requirement. This will only be done if cashflow dictates or if market conditions indicate that it is the best course of action. One possible reason for borrowing more than the minimal amount is to take advantage of, and lock in, low long-term interest rates, make long-term savings and also reduce the Council's exposure to variable interest rate risk. However, there will almost certainly be a short-term 'carry cost' to borrowing in advance of need when current investment rates are lower than long-term borrowing rates. This would be fully evaluated before any decision is taken.

83. Borrowing in advance of need also increases the level of temporary investments and makes the security of those funds even more important. However, the Council's treasury management practices ensure that the risks of investing funds are minimised.

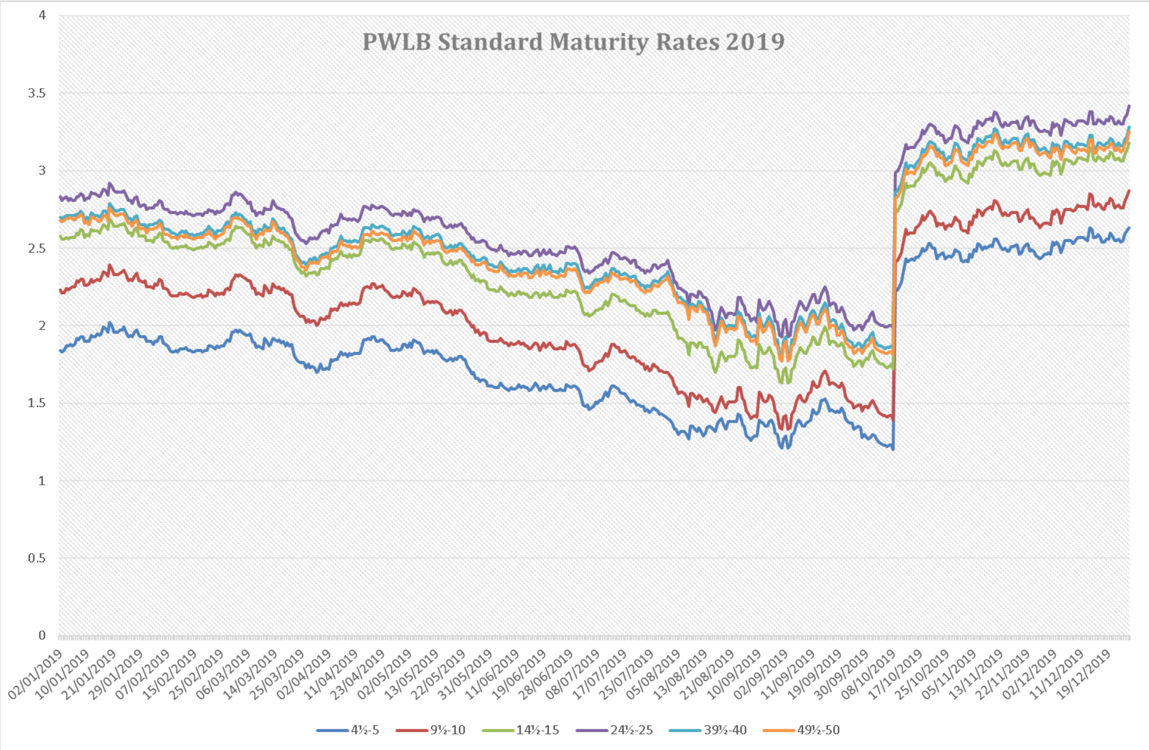
84. A summary of the proposed Treasury Management Indicators for 2020-23 are set out in tables 3 and 4 below.

Table 3 TREASURY INDICATORS	**Proposed 2020/21 £m**	**Proposed 2021/22 £m**	**Proposed 2022/23 £m**
Upper limit for Rate Exposure (fixed-term investments)			
Fixed Rate	100%	100%	100%
Variable Rate	75%	75%	75%
Upper limit for principal sums invested for over 364 days	Higher of £20m or 15%	Higher of £20m or 15%	Higher of £20m or 15%

Table 4. Maturity structure of fixed rate borrowing	**Lower limit**	**Upper limit**
under 12 months	0%	25%
12 months and within 24 months	0%	25%
24 months and within 5 years	0%	75%
5 years and within 10 years	0%	100%
10 years and above	0%	100%
Adoption of CIPFA's Treasury Management in the Public Services Code of Practice and Cross Sectoral Guidance Notes	Adopted	

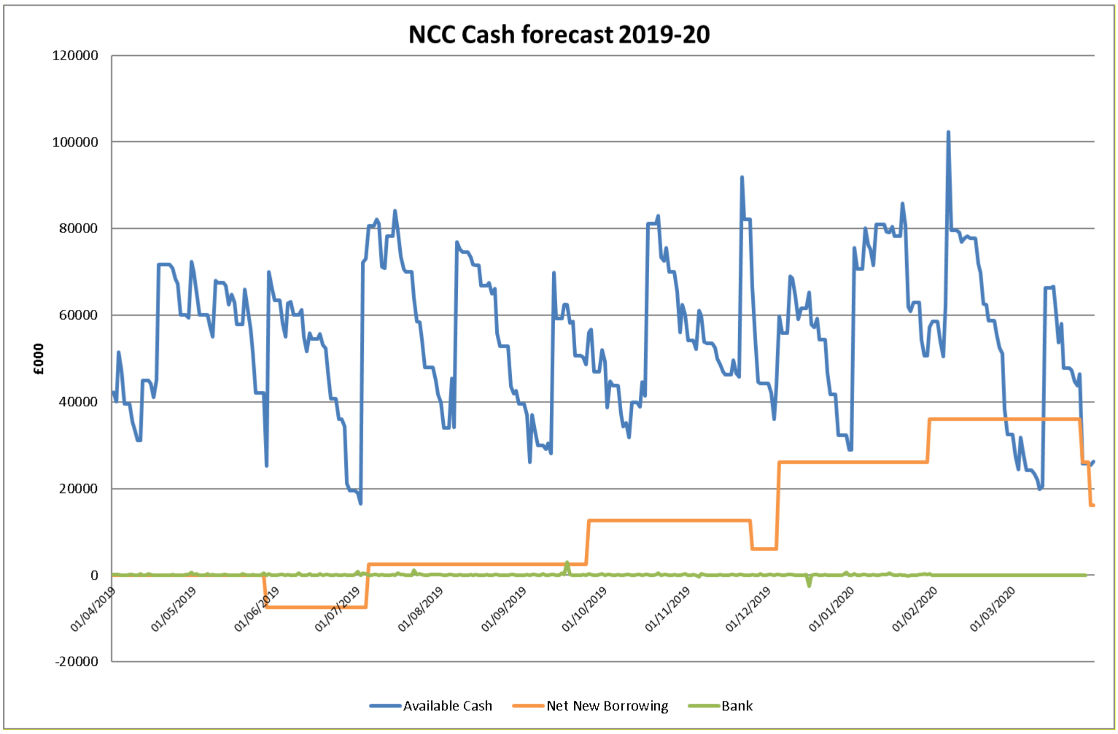
Borrowing Strategy

85. Over the course of 2019 PWLB rates showed a downward trend, reflecting the market's view of Brexit negotiations and the uncertainty surrounding the General Election. In October a change in PWLB policy added 1% to all loans, adding substantially to the cost of local authority borrowing. The rates are shown in the chart below:



86. The chart below shows how the Council's instant-access cash position has progressed over the financial year to January 2020 and how it is forecast to progress until the year-end. This position varies over the course of the year but averages about £54m. The line reflects the cumulative profile of the Council's revenue and capital expenditure, grant and precept income, together with any borrowing or fixed-term lending decisions made by the Council's treasury management team.

87. The lower line shows the Council's net new borrowing over the course of the year. It can be seen that for 2019/20 this was approximately £16m (that is, new borrowing of £50m less £34m of maturing debt).



88. Over the past several years the Council has financed the capital programme (on a temporary basis) mainly by using its cash balances. These are essentially earmarked reserves, general fund reserves and net movement on current assets. As the cash in these reserves is not required in the short term for the reserves' specific purposes, it has been utilised in order to reduce external borrowing, and is known as 'internal borrowing'.

89. The advantage to the Council of internal borrowing is that it costs less than external borrowing, the cost being the opportunity cost of interest foregone by not investing the cash (investment rates are typically around 0.8% for short-term deposits). It therefore generates short-term savings for the Council. Another advantage is that counterparty risk is reduced by having less cash to invest.

90. On the other hand, by postponing its long-term borrowing the Council is in effect increasing its exposure to interest rate risk, as rates will fluctuate in the intervening period until long-term fixed rate borrowing is taken. Treasury management staff monitor this risk, and regularly review interest rates.

91. As a result of all this, the borrowing strategy needs to provide funds not only to finance the capital programme but also funds (i) to replenish reserves as and when these are required and (ii) to cover principal repayments on any maturing debt. If long-term borrowing is not taken to cover these outflows of cash then the Council would need to consider other sources of finance (such as an ongoing bank overdraft facility or a series of short-term loans).

92. These strategic factors drive the Council's objective need to secure long-term debt finance, but there are a number of day-to-day factors – relating to market conditions and the Council's own revenue budget - that must be taken into account when deciding precisely when to borrow.

93. As at December 2019 short-term PWLB debt is around 0.6% cheaper than long-term debt. However, there would be a risk if the Council were to take only short-term debt. This is because short-term loans need more frequent refinancing and at such points the Council would find itself exposed to whatever the prevailing interest rates were at the time. If this happened the Council could find itself facing considerably higher interest rates, which would quickly undermine any saving made by taking short-dated debt.

94. Despite the recent rate-hike, the long-term rates being offered by PWLB remain relatively attractive. Occasionally, however, long-term loans offered by the market or by other local authorities can be a competitive alternative to PWLB loans, and these are worth considering.

95. In practice, a balanced portfolio will include a mix of:

- Temporary use of the Council's cash reserves
- Short-term debt provided by the market/other local authorities
- Short-term or variable rate debt provided by PWLB
- Long-term debt provided by PWLB
- Long-term debt provided by the market or other local authorities

96. Given these contingencies the amount, type, period, rate and timing of new borrowing will be an operational matter falling under the responsibility of the Service Director (Finance, Infrastructure & Improvement) exercised by the Senior Accountant (Pensions & Treasury Management) within the approved borrowing strategy, taking into account the following factors:

- expected movements in interest rates as outlined above.
- current debt maturity profile.
- the impact on the medium-term financial strategy.
- the capital financing requirement.
- the operational boundary.
- the authorised limit.

97. Opportunities to reschedule debt will be reviewed periodically throughout 2020/21 but the current structure of repayment rates from the PWLB indicate significant premiums to be paid on the premature repayment of existing loans which would not be compensated by lower rates available for new loans. Any decision to restructure LOBO debt can only be initiated by the lender.

Investment Strategy

98. During 2020/21 it is intended to keep cash balances at a low level with the aim of maintaining a minimal working cash balance of around £20m. This will provide a level of liquidity without recourse to temporary borrowing, ie. having to seek funds at short notice when availability may be restricted and therefore expensive.

99. The Council manages counterparty risk by monitoring the ratings of the institutions in which it could invest. Exposure to the Eurozone is limited by investing in UK banks and high credit quality overseas banks. The criteria for selecting counterparties are detailed in TMP 1 in Appendix E.

100. A further measure to ensure security of the Council's cash investments is to maintain the Council's exposure to the UK local authority sector and UK government securities. When lending to local authorities fixed term deposits would be used but these are subject to demand and cannot be relied upon in the same way as bank lending. The use of treasury bills and UK government gilts may be considered and would ensure priority is given to security and liquidity of funds.

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