

CYNGOR SIR POWYS COUNTY COUNCIL.

Governance and Audit Committee

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REPORT TITLE: Capital Workstreams Working Group

REPORT FOR: Discussion

During the autumn of 2021 a working group of Governance and Audit Committee was formed to address the concerns previously expressed at both Governance and Audit and Finance Panel surrounding the affordability of the projected strain on the revenue budget from loan repayment costs arising from the Council's ambitious capital programme.

The objective of the work was to form an opinion on the affordable level of revenue allocated to debt servicing that can be sustained into the future and advise cabinet and Council accordingly. Full Terms of Reference are attached as Appendix 1.

Three meetings have been held, the first a scoping meeting with group members only, the latter two involving the Capital Accountant and Director of Finance. The group is grateful for the preparatory work and contribution of both officers.

Current Situation

Background

The Council's ambitious capital programme was initially funded from cash reserves assisted by the proceeds resulting from the Minimum Revenue Provision (MRP) changes approved by Council since 2016. However, the budget for 2021/22 predicted that debt would double by 2026/27.

Finance Panel and the Audit Committee each raised concerns surrounding affordability within council resources, particularly when pipeline and other unspecified projects were added to the appraisal. In particular, the group had concerns surrounding the Wave 2 and Wave 3 21C Schools proposals, announced in the press, which would alone potentially add some £300m to the capital programme (PCC share c.£105m).

Capital Finance Requirement (CFR)

The group has been able to compare the latest projections of the CFR requirement and compare it to the schedule approved by Council within the 2021/22 budget.

HRA = Housing Revenue Account

| £'m | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 | 2026/27 |
|------------------|---------------|---------------|--------------|---------------|---------|---------|
| CFR – non HRA | 352.95 | 383.3 | 398.71 | 399.32 | 399.38 | 399.48 |
| CFR – HRA | 115.62 | 126.14 | 136.19 | 142.96 | 144.29 | 145.14 |
| Total CFR | 468.58 | 509.45 | 534.9 | 542.28 | 543.66 | 544.62 |

CFR as 2022/23 Budget

| £'m | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 | 2026/27 |
|------------------|---------------|---------------|---------------|---------------|---------------|---------------|
| CFR – non HRA | 323.53 | 349.71 | 364.61 | 373.44 | 385.2 | 387.28 |
| CFR – HRA | 106.83 | 118.63 | 137.8 | 156.93 | 166.88 | 174.66 |
| Total CFR | 430.36 | 468.34 | 502.41 | 530.37 | 552.08 | 561.94 |

Several points are worthy of note:

- Outturn for 2021/22 is lower than expected. This is due to project delays and rescheduling principally due to Covid.
- No further major capital projects have been authorised in the current year, this allows the budget for 2022/23 to be well within that approved for this year.
- In spite of the above, as the project programme unfolds, total CFR for the Council Fund by 2026/27 is projected to be very similar to that in the current budget.
- Expected non-HRA (Housing Revenue Account) debt is still projected to be around £6,500 per household by 2026/27.
- The CFR for the Housing Revenue Account shows a considerable uplift due, we understand, to a more extensive housing programme. Since this is self-funding, it is immaterial to the conclusions of this report.
- Although the list of projects in the capital programme has been expanded and specified in general terms for some sectors, e.g. highways, the list of specific projects within the 21C programme has not changed since the last budget. This is of concern and is discussed below.

Capital Receipts

A key factor in the CFR calculation is the level of Capital Receipts (revenue from asset sales) that are included. The Table below comparing last year's budget to the proposals going forward shows a substantial increase from last year in the overall contribution from capital receipts. However, in relation to the overall capital programme it represents a rather small contribution. The group were advised that the forthcoming Asset Report will identify considerable opportunities to develop a considerably more ambitious programme.

| £'m | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 | 2026/27 |
|---------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| 21/22 Budget | 3.795 | 3.848 | 0.248 | 0.248 | 0.248 | 0.248 |
| 22/23 Budget | 4.27 | 2.25 | 3.25 | 2.25 | 1.25 | 1.25 |

Financing Costs

The tables below compare the resulting financing cost projections through to 2027/27 compared to that approved for the current budget.

Financing costs as 2021/22

Budget

| £'m | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 | 2026/27 |
|--------------|--------------|-------------|--------------|-------------|--------------|--------------|
| Council Fund | 13.59 | 16.55 | 17.61 | 17.71 | 17.54 | 16.67 |
| HRA | 5.75 | 6.35 | 6.98 | 7.59 | 8.02 | 7.79 |
| Total | 19.34 | 22.9 | 24.59 | 25.3 | 25.56 | 24.46 |

Financing costs as 2022/23

Budget

| £'m | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 | 2026/27 |
|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Council Fund | 10.85 | 11.29 | 12.17 | 12.85 | 13.53 | 13.94 |
| HRA | 4.53 | 4.89 | 5.49 | 6.21 | 6.76 | 7.13 |
| Total | 15.38 | 16.18 | 17.66 | 19.06 | 20.29 | 21.07 |

It is clear that for the reasons given above, cost of finance through to 2026/27 is substantially less than that projected at the time of the last budget. Whilst this is certainly true for the current year and probably next, it must be noted that, particularly for 21C schools, 'pipeline' projects are not included.

- Assumptions on future settlements from Welsh Government and Council Tax may not be consistent across all authorities. In recent years Welsh Government have only provided settlement figures for the current year and no indication of any future year settlements.
- Authorities that have purchased assets for yield in the past, would have higher financing costs as a result as the income for these is not included in the figures shown.
- Each authority makes its own assumptions on future borrowing rates, and each will have a different cost of their existing debt portfolio and varying maturity dates which will impact on future costs.
- Determining an appropriate MRP policy is up to each authority, as you can see from the chart the impact from changing Powys' MRP policy.
- Whether they are under borrowed like us with minimal investments or have a more proactive investment approach is taken.
- The figures would have been produced during December 2020 and January 2021, this information is almost 12 months old so may not reflect the current position. The latest figures will be available as part of the 2022/23 budget setting process usually approved by each authority during February and March 2022.

Nevertheless, the slope of both lines upwards in spite of the reduced expenditure through Covid is in stark contrast to most other Authorities and indicates that vigilance needs to be maintained after 2023/24.

The Wales Government

Enquiries have been made regarding the strategies adopted by other Authorities, a figure of 8% was mentioned for one LA but it was unclear whether it was directly comparable.

Alternative Financing Methods

We understand that the Wales Government has set aside substantial funds for what it calls a 'Mutual Investment Model' (MIM) essentially similar to Public Finance Initiatives (PFIs) but without, it is said, some of their drawbacks. MIMs are only for major projects and specifically not available for developments with swimming pools nor for special schools. As such they will not figure in the PCC plans for pipeline projects.

Peer Review

The recently published OGC Gateway (peer) review, picking up the point that 'pipeline' projects had not been included, as one of its recommendations states that the council should:

“Develop a roadmap to assist in planning potential resources and funding needs during the Band D implementation”

The report adds that the 'roadmap' should set out the various potential projects into timescales and groupings. The document to be used purely as a confidential internal planning tool. This we understand has been accepted by Cabinet and agreed that the work will be completed by the end March 2022.

The review also emphasised the importance of asset sales to support the 'more ambitious' next phase of the schools programme.

Conclusions

- 1. The capital programme for 2022/23 and 2023/24 is based on realistic expenditure against the currently authorised project programme. As such it is well within the limits approved by council when setting the current year's budget and can be considered affordable.**
- 2. Greater emphasis should be given to the potential contribution of revenue from Capital Receipts to the programme going forward. Once the Asset Review is available a selling strategy should be developed with ambitious targets subject to regular reviews.**
- 3. Looking forward, based on a continuously updated roadmap as described above we recommend that Finance Panel and the G&A committee in their respective roles repeat this exercise on, at least, an annual basis.**
- 4. An arbitrary *warning* limit of 6% of Forward Net Revenue Budgets be set on projections from the above. This limit is not to limit Council options but to provide an early flag that special attention needs to be paid to the programme's affordability.**
- 5. Specialist training should be given to future working groups on capital financing methods, especially off-balance sheet methods, and evaluation.**
- 6. The second stage of the exercise should be undertaken as soon as practicably possible**

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