

SCRUTINY COMMITTEE

Thursday 14 March 2019

REVIEW OF THE COMMERCIAL INVESTMENT STRATEGY (SCR 01/19)

EXECUTIVE SUMMARY

1. The Scrutiny Committee – at its meeting on 17 May 2018 – requested a formal report for its review and consideration on the Council’s Commercial Investment Strategy.
2. This report provides the Committee with the information requested, exploring in particular depth:
3. The updated East Suffolk Commercial Investment Strategy (including outline business case and proposal for Commercial Investment and Trading) presented to, and adopted by, Simultaneous Cabinet on 18 February 2019; and
4. The East Suffolk Capital Strategy 2019/20 to 2021/22 presented to, and adopted by, Shadow Council on 28 February 2019.
5. Overall, the report summarises the way in which the Council has now developed and adopted a mixed delivery model (entailing in-house and arms-length delivery through a company) for commercial investment and trading on the basis of a detailed outline business case. The commencement of trading in the individual commercial elements of the model is subject to the approval of a series full business cases.
6. The report also sets the Commercial Investment Strategy (along with the Council’s Treasury Management and Investment activity) in the wider context of the East Suffolk Capital Strategy, which is a new requirement under the updated Prudential Code.

Is the report Open or Exempt?	<p>The main body of the report together with Appendix B are Open.</p> <p>Appendix A of the report is Exempt.</p>
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	<p>Appendix A to the report contains Exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972 (as amended) in that it includes information relating to the financial or business affairs.</p> <p>It is considered that the public interest in not disclosing the Exempt information outweighs the public interest in disclosing the public interest as the Appendix contains commercially sensitive information.</p>
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Wards Affected:	All Wards in the District
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Cabinet Members:	<p>Cllr Stuart Lawson</p> <p>Cabinet Member with responsibility for Resources</p>
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Supporting Officer:	<p>Simon Taylor</p> <p>Chief Finance Officer and Section 151 Officer</p> <p>(01394) 444570</p> <p>simon.taylor@eastsuffolk.gov.uk</p>
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1 BACKGROUND

1.1 The Scrutiny Committee – at its meeting on 17 May 2018 – requested a formal report for its review and consideration on the Council's Commercial Investment Strategy. The specific remit and scope of the request was as follows:

- *To seek information on the Council's proposals for a Commercial Investment Strategy and its links to the 2015-23 Business Plan's aspirations for "financial self-sufficiency and a more business-like and entrepreneurial approach"*
- *Such information to include all aspects but including, for example:*
 - *How the Business Plan's ambitions for the Council to adopt a complementary approach of increased commercial skills as well as trading and income generation opportunities will be approached and achieved*
 - *How governance requirements and the security of the Council's funds and investments will be assured*
 - *How the requirements of the following will be encompassed:*
 - *The Local Government Act 2003 requirement of local authorities to set an annual Investment Strategy for the management of its investments and the priority to be given to the security and liquidity of those investments*
 - *The Ministry of Housing, Communities and Local Government's revised guidance on local authority investments and minimum revenue provision (published February 2018); and*
 - *The advice of the Council's external Treasury Management advisors on the creditworthiness of institutions in order to inform investment decisions.*

2 INTRODUCTION

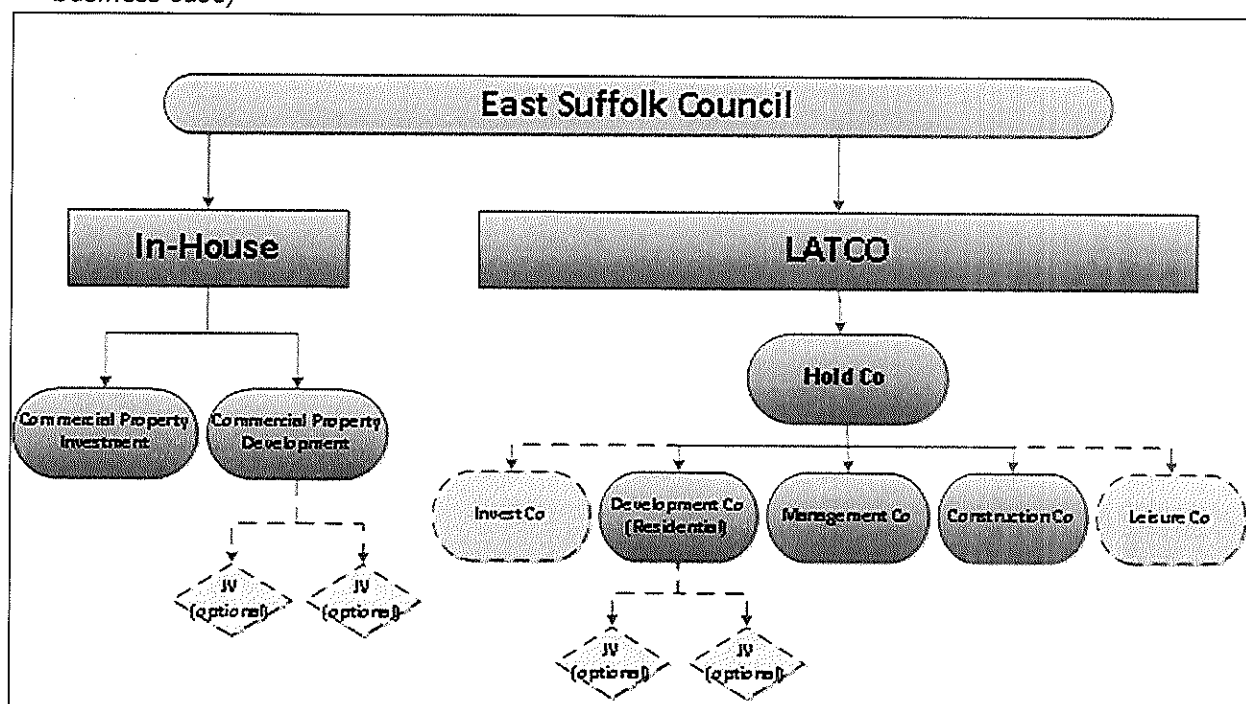
- 2.1 The East Suffolk Business Plan (2015-2018) sets out "Financial Self-Sufficiency" as a major strategic priority, emphasising that simply continuing to improve efficiency and reducing costs will not be enough to enable the councils (both Suffolk Coastal and Waveney) to deliver on their ambitions, or to ultimately maintain core services at existing levels.
- 2.2 Building on the commitments in the Business Plan, a draft Commercial Investment Strategy for East Suffolk was adopted by both Councils in September 2017.
- 2.3 The draft Strategy provided further context and identified the need for commercial investment, introducing the idea of creating an arms-length trading company, wholly owned by the shared services partners. Although there was a major emphasis on commercial property investment in the Strategy, diversification within a company structure was also highlighted as an opportunity to realise returns from alternative income streams.
- 2.4 In approving the draft Strategy, Simultaneous Cabinet instructed officers to take further legal and financial advice with a view to potentially setting up an arms-length company for future investment and trading purposes.
- 2.5 As instructed, officers subsequently completed a more detailed review, culminating in the development and presentation of an updated Commercial Investment Strategy, including an outline business case (OBC) for commercial investment and trading aimed at generating additional income streams, whilst at the same time supporting key strategic priorities including Housing, Regeneration and Tourism.

- 2.6 The updated Commercial Investment Strategy (including the OBC) was adopted by Simultaneous Cabinet on 18 February 2019.

3 COMMERCIAL INVESTMENT AND TRADING: ADOPTED DELIVERY MODEL (APPENDIX A)

- 3.1 The updated Commercial Investment Strategy was developed with professional support provided primarily by Trowers & Hamlins (on legal matters) and Grant Thornton (on financial and other matters) with the OBC following HM Treasury “Green Book” principles (recommended practice for public sector business cases).
- 3.2 The core proposal within the Strategy is a delivery model for commercial investment and trading comprising a mixture of in-house/direct delivery and arms-length delivery through a local authority trading company (LATCO) and is presented below Figure 1.

Figure 1: adopted delivery model for Commercial Investment and Trading (subject to full business case)

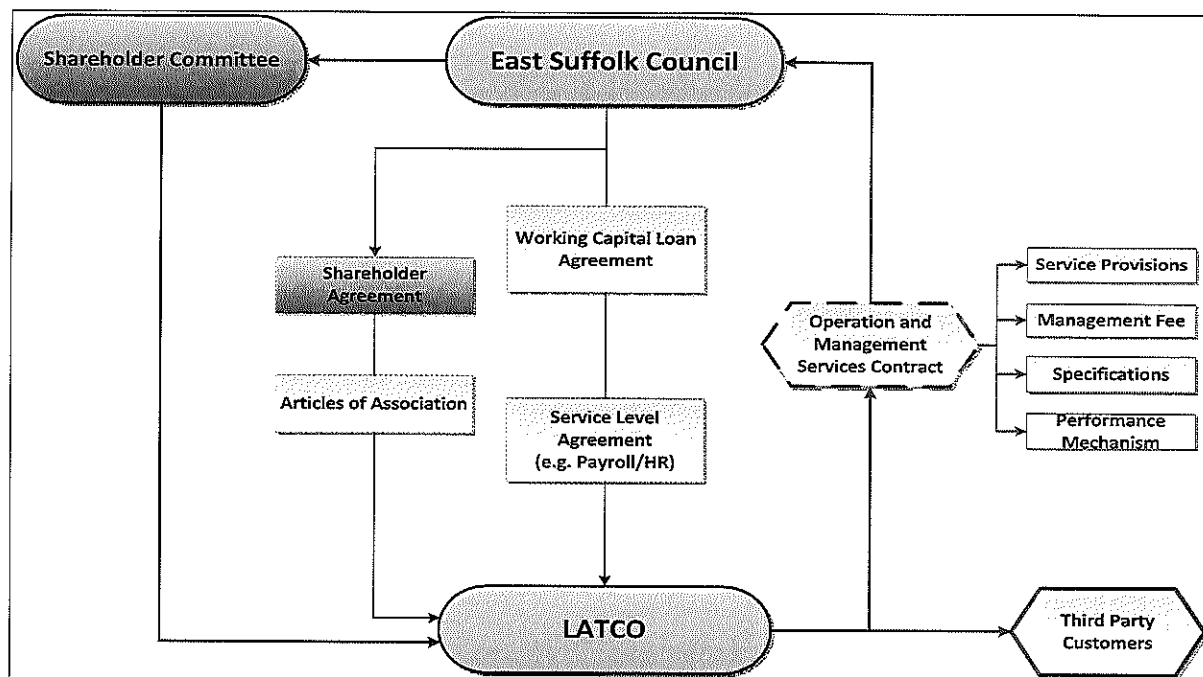


- 3.3 In summary, the delivery model comprises the following features:

- In-House/Direct Provision – for commercial property investment and development; and
- Arms Length Company (LATCO) – wholly-owned by the Council and comprising a Group structure, headed by a Holding Company, with the following subsidiaries:
 - Development Company – for the development of residential properties
 - Investment Company – for holding and letting developed residential properties
 - Property Management Company – for the delivery of property management services
 - Construction Company – for the delivery of construction services; and
 - Leisure Company – for the management of tourism-related assets and services.

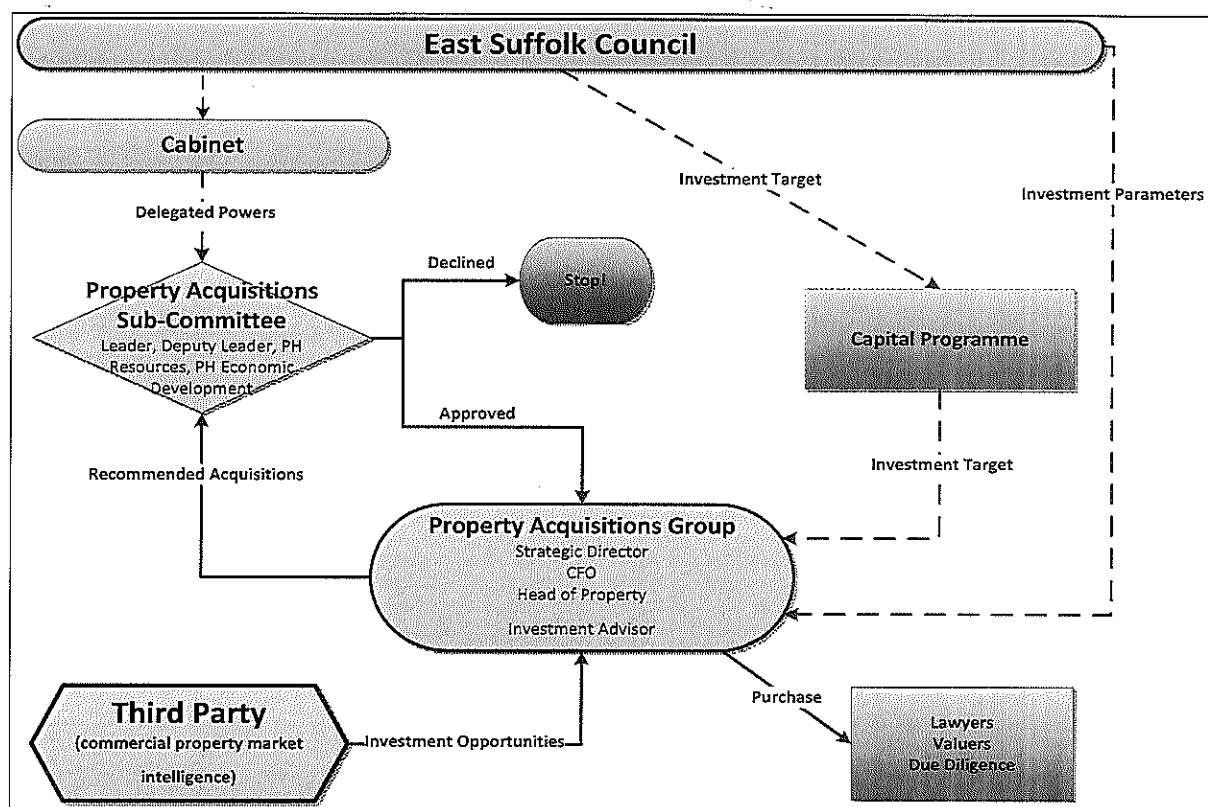
- 3.4 It is expected that the model will provide the optimal solution for realising a range of commercial opportunities. These include – particularly – the opportunity to develop Council owned land and property for both residential and commercial purposes in a way that supports the Council’s social objectives, whilst making a profit for reinvestment in core services and corporate priorities. A range of other commercial opportunities are also catered for including commercial property investment, operational services and tourism.
- 3.5 The LATCO – in its dormant form – is now scheduled to be incorporated in April 2019. However, the commencement of trading in each area of commercial activity is to be preceded by a series of supporting full business cases (FBCs), for consideration and approval by Cabinet, which meets good practice requirements (Green Book principles) and is legally compliant with Regulation 2 of the Local Government (Best Value Authorities) (Power to Trade) (England) Order 2009 (“the 2009 Order”), which requires a business case to be prepared and approved by the Council before a LATCO can begin trading. Trading (subject to supporting FBCs) is to be phased in, beginning in 2019/20 with residential property development, and roofing and scaffolding (“Construction Services”).
- 3.6 The commencement of trading in the in-house elements of the model (commercial property investment and development) will also be subject to an approved FBC.
- 3.7 Detailed governance arrangements have yet to be decided and will form part of each individual FBC. The dormant LATCO is to be constituted with ‘generic’ Articles of Association, agreed in principle by Simultaneous Cabinet on 18 February (and subject to further delegations). The new East Suffolk Council – once elected – will then have the opportunity to amend the Articles should they choose to do so. The new Council will also consider detailed proposals for tailored governance arrangements as the FBCs are presented. A typical governance structure for a LATCO is presented in Figure 2 below.

Figure 2: a typical LATCO governance structure



- 3.8 The OBC also assumes that commercial property investment (an in-house activity) will also require special governance arrangements with the need for 'speed of decision-making' a particular consideration. One possible structure is presented in Figure 3 below.

Figure 3: example governance structure for in-house Commercial Property Investment



- 3.9 In developing the approach to commercial investment and trading, including the delivery approach, officers have been conscious to progressively develop the commercial capacity and skills required for successful delivery. This began with deliberately seeking the appropriate professional expertise at the outset and applying best practice methodology in order to minimise risk and maximise the chances of success.

- 3.10 That approach is set to continue with the aim of achieving an appropriate commercial skill set in LATCO appointments (whether directly or in arms length governance roles), whilst embedding a sense of realism and a learning culture (e.g. the delivery approach caters for the use of joint ventures as it is recognised that – in the early days at least – the Council/LATCO will not have sufficient in-house capacity or expertise to deliver larger projects.

4 COMMERCIAL INVESTMENT AND TRADING: A KEY PART OF A WIDER CAPITAL STRATEGY (APPENDIX B)

- 4.1 As explained above in Paragraph 2.1, the Council's Commercial Investment Strategy has its origins in the priorities contained within East Suffolk Business Plan (2015-2018), but it is also important to recognise its role as part of a wider strategy.
- 4.2 Although local authorities are responsible for determining their own programmes for capital investment, they are required by regulation to have regard to CIPFA's "Prudential Code" when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003.

- 4.3 CIPFA published its first Prudential Code in 2004. The primary objective of the Code is to ensure that – within a clear framework – capital expenditure plans 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 and how these risks will be managed to levels that are acceptable to the organisation.
- 4.4 The 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 being made with sufficient regard to the long run financing implications and potential risks.
- 4.5 CIPFA published an updated Prudential Code in December 2017, which introduced the requirement for local authorities to produce a Capital Strategy for the first time (by April 2019). The East Suffolk Capital Strategy 2019/20 – 2022/23 was adopted by the Shadow Council on 28th February 2019.
- 4.6 The Capital Strategy – developed on the basis of professional advice procured from Arlingclose (the Council’s Treasury Management advisors) – provides a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services in East Suffolk, along with an overview of how associated risk is managed and the implications for future financial sustainability. Key content includes:
- Capital Expenditure and Financing
 - Asset Management
 - ***Treasury Management (including Investment Strategy)***
 - Investments for Service Purposes; and
 - ***Commercial Investment***
- Treasury Management (including Investment Strategy)*
- 4.7 As with previous years (as two separate councils), the Shadow Authority adopted – on 28th January 2019 – the East Suffolk Council Treasury Management Strategy for 2019/20, setting out the Council’s approach to borrowing and investing for treasury management purposes. This included the approach to containing borrowing within prudent, affordable and sustainable limits as well as managing investment risk (e.g. through approved counterparties and limits).
- 4.8 At the same time, and in accordance with the Ministry of Housing, Communities and Local Government (MHCLG) Statutory Guidance on Local Government Investments (3rd Edition) – effective from 1 April 2018, the Shadow Authority also adopted a separate Investment Strategy. The Strategy is to prioritise security and liquidity over yield; focussing on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with other local authorities or selected high-quality banks, to minimise the risk of loss.
- 4.9 From 2019/20, the Council plans to operate a more diverse strategy than in the past for longer-term funds, which will be invested more widely, including into bonds, loans, property and shares; this will better balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

Commercial Investment

- 4.10 The approach to Commercial Investment generally is described in Section 3 above and summarised in the Capital Strategy. However, specifically with regard to Commercial Property Investment, at the time of preparing this report, CIPFA guidance on borrowing to invest is awaited following a recent announcement in which they had expressed concern at what they perceive to be, the increasing risk taken on by local authorities following a sharp increase in Public Works Loan Board (PWLB) borrowing by councils to invest in commercial property (which arguably appears to run counter to recent MHCLG guidance noted above in Paragraph 4.8).
- 4.11 Intelligence at this stage suggests that – rather than an outright ban on borrowing to invest in commercial property – councils will in future have to demonstrate that such investments are “proportionate” to their resources. The East Suffolk approach will incorporate the CIPFA guidance when it is published as part of the FBC to justify the commencement of trading.

5 FINANCIAL AND GOVERNANCE IMPLICATIONS

- 5.1 Key financial and governance implications are signposted within the report and explained within Appendices A and B.

6 OTHER KEY ISSUES

- 6.1 There are no other key issues arising from this report.

7 CONSULTATION

- 7.1 Consultation undertaken to date is specified in underlying strategies (Appendices A and B). Future consultation will be required in implementing the Commercial Investment Strategy and will be tailored to individual areas of commercial activity (e.g. any proposals to transfer staff to the LATCO will require strict compliance with the consultation elements of the “TUPE” regulations).

8 OTHER OPTIONS CONSIDERED

- 8.1 The report responds to a request for information from the May 2018 Scrutiny Committee. In this context, there are no alternative options to consider.

9 REASON FOR RECOMMENDATION

- 9.1 To enable the Committee to scrutinise significant emerging Council financial strategy and risk management.

RECOMMENDATION

1. That the Scrutiny Committee, having considered the report, comments upon the detail contained therein

APPENDICES	
Appendix A	EXEMPT: East Suffolk Commercial Investment Strategy (including outline business case and proposal for Commercial Investment and Trading) (18/02/19)
Appendix B	East Suffolk Capital Strategy 2019/20 to 2021/22 (28/02/19)

BACKGROUND PAPERS - none

East Suffolk Council

Capital Strategy 2019/20 – 2022/23

1) Introduction

- 1.1 This Capital Strategy is a new report for 2019/20, giving a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services in East Suffolk, along with an overview of how associated risk is managed and the implications for future financial sustainability. It has purposely been written in an accessible style to enhance understanding of what can be very technical areas.

2) Capital Expenditure and Financing

2.1 Expenditure

- 2.1.1 Capital expenditure occurs when the Council spends money on assets such as property or vehicles, which will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are not capitalised and are charged to revenue in year.
- 2.1.2 Further details on the Council's capitalisation policy can be found in the 2017/18 Statement of Accounts:
- Note 1 (n) of Suffolk Coastal Accounts; and
 - Note 1 (o) of Waveney Accounts.
- 2.1.3 In 2019/20, East Suffolk Council is planning capital expenditure of £52.6 million (and £207.5 million over the next four years) as summarised in Table 1 below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure

	2017/18 actual*	2018/19 forecast*	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget
	£000's	£000's	£000's	£000's	£000's	£000's
General Fund Services	6,125	14,573	34,360	38,409	36,519	37,130
Council Housing (HRA)	7,006	12,121	13,216	16,841	13,104	12,944
Capital Investments	-	-	5,000**	..**	..**	..**
TOTAL	13,131	26,694	52,576	55,250	49,623	50,074

* Figures represent the combined positions of Suffolk Coastal and Waveney

** The Council currently has £5 million allocated for Commercial Investment. The ongoing development and implementation of the Commercial Investment Strategy could see significant future allocations in the Capital Programme for this purpose.

- 2.1.4 The main General Fund capital projects scheduled for 2019/20 are as follows:

- *Lowestoft Flood Risk Management/Tidal Barrier (£11.1 million)* – currently the highest value scheme that the Council has with a 2019/20 budget allocation of £8.6 million included for Phase 1 works (Tidal Walls, Pluvial and Fluvial) and £2.5 million for Phase 2 works (the Tidal Gate);
- *Land Acquisitions (£5.0 million)* – a block allocation to finance strategic land acquisitions, aimed at advancing the Council's housing and regeneration priorities;
- *East Point Pavilion (£3.0 million)* – development of new restaurant/café premises;

- *Lowestoft Beach Hut Replacement (£2.5 million)* – replacement of beach huts along with the demolition, reconstruction and enhancement of the adjoining café and amenity block;
- *Bungay Leisure Centre (£1.8 million)* – major redevelopment of leisure centre;
- *Normanston Footbridge (£1.7 million)* – a new pedestrian/cycle bridge over the railway adjacent to the existing Network Rail bridge;
- *Leiston Leisure Centre (£1.6 million)* – major redevelopment of the sports centre and swimming pool including the installation of a gym and new changing rooms; and
- *Felixstowe Regeneration Project (£1.0 million)* – major investment in Brackenbury and Felixstowe Leisure Centres.

2.1.5 As noted in Table 1, the Council also has a £5.0 million budget allocated for Commercial Investments, which are detailed later in this report in Section 6.

2.1.6 The Housing Revenue Account (HRA) is a ring-fenced account which ensures that the Council's housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately, and includes £32.9 million allocated to the New Build Programme over the (four-year) forecast period, which is expected to deliver around 200 new homes.

2.2 Governance

2.2.1 The evaluation, prioritisation and acceptance of capital schemes onto the Capital Programme is carried out in accordance with strict criteria that ensures that added schemes reflect Council priorities and can be delivered within available resources (e.g. due priority is given to schemes yielding savings and/or generating income as well as meeting a Council priority). Proposals are shaped by senior managers in consultation with councillors and considered at an annual Capital Workshop (in October/November each year) by a panel comprising the Strategic Director responsible for property, the Chief Finance Officer (CFO) and the Head of Housing (feeding in on HRA issues).

2.2.2 The draft Capital Programme is then subjected to formal Scrutiny prior to setting the budget (followed by Cabinet and full Council approval). Full details of the Capital Programme can be found at this [link](#).

2.3 Financing

2.3.1 All capital expenditure must be financed, either from external sources (Government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing and leasing). The planned financing of the above expenditure is presented in Table 2 below.

Table 2: Capital Financing

	2017/18 actual*	2018/19 forecast*	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget
	£000's	£000's	£000's	£000's	£000's	£000's
External sources	1,711	2,317	14,804	21,650	27,671	38,616
Own resources	9,959	21,822	29,697	25,875	21,952	11,458
Debt	1,461	2,555	8,075	7,725	-	-
TOTAL	13,131	26,694	52,576	55,250	49,623	50,074

* Figures represent the combined positions of Suffolk Coastal and Waveney

2.3.2 Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as

“Minimum Revenue Provision” (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP and use of capital receipts are presented in Table 3 below.

Table 3: Replacement of Debt Finance

	2017/18 actual*	2018/19 forecast*	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget
	£000's	£000's	£000's	£000's	£000's	£000's
Own resources	671	636	830	1,055	1,082	1,082

* Figures represent the combined positions of Suffolk Coastal and Waveney

2.3.3 The Council's annual MRP statement can be found at Annex A below.

2.3.4 The Council's cumulative outstanding amount of debt finance is measured by the Capital Financing Requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £20.641 million in 2019/20. Based on the above figures for expenditure and financing, the Council's estimated CFR is presented in Table 4 below.

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement (CFR)

	31.3.2018 actual*	31.3.2019 forecast*	31.3.2020 budget	31.3.2021 budget	31.3.2022 budget	31.3.2023 budget
	£000's	£000's	£000's	£000's	£000's	£000's
General Fund services	38,001	37,420	58,261	77,536	88,261	89,561
Council housing (HRA)	77,750	77,750	77,550	77,550	67,264	67,264
Capital investments	-	-	-	-	-	-
TOTAL CFR	115,751	115,170	135,811	155,086	155,525	156,825

* Figures represent the combined positions of Suffolk Coastal and Waveney

3) Asset Management

3.1 Asset Management Strategy

3.1.1 The Council recognises the importance of ensuring that capital assets continue to be of long-term use and, especially in the move to a single council for East Suffolk and a rapidly changing operational and technological backdrop. Consequently at the time of preparing this Capital Strategy, a new Asset Management Strategy (AMS) is under development. Led by the Asset Management team and backed by a comprehensive review of Council assets, the AMS takes a longer-term view comprising:

- 'Good' information about existing assets;
- The optimal asset base for the efficient delivery of Council objectives;
- The gap between existing assets and optimal assets;
- Strategies for purchasing and constructing new assets, investment in existing assets, transferring of assets to other organisations and the disposal of surplus assets; and
- Plans for individual assets.

3.2 Asset Disposals

- 3.2.1 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 Council is also permitted to spend capital receipts on service transformation projects until 2021/22 (in line with its "Flexible Use of Capital Receipts Policy"). Repayments of capital grants, loans and investments also generate capital receipts. The Council operates a deliberately prudent policy of not assuming future capital receipts before they are actually received. Table 5 below summarises the overall projections for capital receipts.

Table 5: Capital Receipts

	2017/18 actual*	2018/19 forecast*	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget
	£000's	£000's	£000's	£000's	£000's	£000's
Asset sales	2,436	-	..**	..**	..**	..**
Loans repaid	160	160	160	160	10,446	160
TOTAL	2,596	160	160	160	10,446	160

* Figures represent the combined positions of Suffolk Coastal and Waveney

** The Council operates a deliberately prudent policy of not assuming future capital receipts within its capital income projections (see discussion on Melton Hill below)

- 3.2.2 At the time of preparing this Strategy, the former headquarters of Suffolk Coastal District Council at Melton Hill, Woodbridge is sold subject to contract and planning permission, with an agreed asking price of £6 million. The value of capital receipts assumed within the Capital Programme will be updated to reflect the actual sale proceeds from this asset, once a sale has been completed.
- 3.2.3 The Council's Flexible Use of Capital Receipts Policy is part of the General Fund Budget & Council Tax Report (Appendix C – Efficiency Strategy) to Shadow Council on 28th February 2019.

4) Treasury Management

4.1 Introduction

- 4.1.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

- 4.1.2 Due to decisions taken in the past, the Council currently (12th November 2018) has borrowing of £87.65 million at an average interest rate of 3.25% and £127.28 million in treasury investments at an average rate of 1.14%.

4.2 Borrowing

- 4.2.1 The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in the future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.75%) and long-term fixed rate loans where the future cost is known but higher (currently 2.0 to 3.0%).

- 4.2.2 Projected levels of the Council's total outstanding debt (which comprises borrowing and leases) are shown below in Table 6, compared with the Capital Financing Requirement (Table 4 above).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement

	31.3.2018 actual*	31.3.2019 forecast*	31.3.2020 budget	31.3.2021 budget	31.3.2022 budget	31.3.2023 budget
	£000's	£000's	£000's	£000's	£000's	£000's
Debt (incl. leases)	94,440	99,889	107,560	107,318	106,878	106,556
Capital Financing Requirement	115,751	115,170	135,811	155,086	165,811	167,111

* Figures represent the combined positions of Suffolk Coastal and Waveney

- 4.2.3 Statutory guidance is that debt should remain below the Capital Financing Requirement, except in the short-term. As can be seen from Table 6, the Council expects to comply with this in the medium term.

Liability Benchmark

- 4.2.4 To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the minimum amount of borrowing required to keep investments at minimum liquidity level. This assumes that cash and investment balances are kept to a minimum level of £30 million at each year-end. The Liability Benchmark is currently £94.775 million and is forecast to increase to £131.116 million over the next four years.

Table 7: Borrowing and the Liability Benchmark

	31.3.2018 actual*	31.3.2019 forecast*	31.3.2020 budget	31.3.2021 budget	31.3.2022 budget	31.3.2023 budget
	£000's	£000's	£000's	£000's	£000's	£000's
Outstanding Borrowing	87,734	93,024	100,939	100,779	100,619	100,459
Liability Benchmark	89,485	94,775	107,541	119,091	129,816	131,116

* Figures represent the combined positions of Suffolk Coastal and Waveney

- 4.2.5 Table 7 above shows that the Council expects to remain borrowed below its Liability Benchmark.

Affordable Borrowing Limit

- 4.2.6 The Council is legally obliged to set an affordable borrowing limit (also termed 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.

Table 8: Prudential Indicators: Authorised Limit and Operational Boundary for External Debt

	2018/19 limit*	2019/20 limit	2020/21 limit	2021/22 limit	2022/23 limit
	£000's	£000's	£000's	£000's	£000's
Authorised limit – borrowing	133,000	148,380	148,380	148,380	148,380
Authorised limit – leases	12,000	6,620	6,620	6,620	6,620
Authorised limit – total external debt	145,000	155,000	155,000	155,000	155,000
Operational boundary – borrowing	126,000	146,380	146,380	146,380	146,380
Operational boundary – leases	12,000	6,620	6,620	6,620	6,620
Operational boundary – total external debt	138,000	153,000	153,000	153,000	153,000

* Figures represent the combined positions of Suffolk Coastal and Waveney

- 4.2.7 Further details on borrowing are contained in the Treasury Management Strategy.

4.3 Investments

- 4.3.1 Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

(Treasury Management) Investment Strategy

- 4.3.2 The Council's Investment Strategy is to prioritise security and liquidity over yield; focussing on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with other local authorities or selected high-quality banks, to minimise the risk of loss.
- 4.3.3 From 2019/20, the Council plans to operate a more diverse strategy than in the past for longer-term funds, which will be invested more widely, including into bonds, loans, property and shares; this will better balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.
- 4.3.4 Table 9 below summarises the Council's current and forecast treasury investments.

Table 9: Treasury Management Investments

	31.3.2018 actual*	31.3.2019 forecast*	31.3.2020 budget	31.3.2021 forecast	31.3.2022 forecast	31.3.2023 forecast
	£000's	£000's	£000's	£000's	£000's	£000's
Near-term investments	92,860	102,480	105,200	111,530	114,225	119,100
Longer-term investments	4,800	4,800	4,800	5,000	5,000	5,000
TOTAL	97,660	107,280	110,000	116,530	119,225	124,100

* Figures represent the combined positions of Suffolk Coastal and Waveney

4.4 Governance

- 4.4.1 Treasury management decisions are made on a daily basis and are therefore delegated to the CFO, who must act in line with the Treasury Management Strategy approved by the Council. Annual outturn reports on treasury management are also approved by the Council (following recommendation from Audit and Governance Committee), whereas mid-year updates are reported exclusively to the Audit and Governance Committee.

5) Investments for Service Purposes

- 5.1 The Council will sometimes make investments for service delivery purposes where there is a strategic case for doing so. This is an approach that has been adopted for the delivery of a package of services including Refuse Collection, Cleansing and Maintenance whereby the Council has entered into joint ventures with the Norse Group. Given its public service objectives, the Council is willing to take more risk than with treasury investments, nevertheless the arrangements feature cost reduction incentives, from which the Council benefits in the form of Management Fee reductions.
- 5.2 As at 31st March 2018, the Council held net investments of £244,000, and achieved £590,000 in Management Fee reductions in 2017/18 as follows:
- Suffolk Coastal Norse Limited – the Council has held a 20% equity share since April 2009. The Council's share of Net Assets/(Liabilities) at 31st March 2018 was (£129,000) and Management Fee reductions of £330,000 were achieved in 2017/18; and

- Waveney Norse Limited – the Council has held a 19.9% equity share since April 2008. The Council's share of Net Assets/(Liabilities) at 31st March 2018 was £383,000 and Management Fee reductions of £260,000 were achieved in 2017/18.

Governance

- 5.3 Decisions on service investments are made by the Council's Cabinet and require the support of a full business case. The Council is also represented on the boards of both of the Norse joint venture companies.

6) Commercial Investments

6.1 Current Investments

- 6.1.1 In recent years, the Council has invested in commercial property in the district on a selective basis, usually where there is a fit with corporate priorities and a positive financial return that can be used to contribute towards the protection of local services. As at 31st March 2018, the commercial property portfolio comprised three shop units in Lowestoft with an estimated Fair Value of £2.882 million. Estimated net return (after all costs) for 2018/19 is expected to be £133,000 (0.3%).

6.2 Commercial Investment Strategy

- 6.2.1 However, in recognition of the continued shortfall in local government funding and commitments made in the East Suffolk Business Plan (2015-23), the Council adopted a draft Commercial Investment Strategy (CIS) in September 2017 with a view to achieving a step change increase in commercial investment and trading by the Council.
- 6.2.2 The CIS has now been developed into a business case advocating a wide ranging commercial investment and trading delivery approach, including the creation of a local authority trading company (LATCO). Adopted in January/February 2019, and due to be progressively phased in during 2019/20 (following the development and approval of a full business case in support of each commercial activity), it is a mixed delivery approach covering the following activities:
- In-House
 - Commercial Property Investment
 - Commercial Property Development
 - LATCO
 - Residential Property Investment
 - Residential Property Development
 - Property Management Services
 - Construction Services (initially Roofing and Scaffolding)
 - Leisure Services (e.g. Holiday Lets and Beach Huts).
- 6.2.3 With regard to Commercial Property Investment, at the time of preparing this Strategy, CIPFA guidance on borrowing to invest was awaited following a recent announcement in which they had expressed concern at what they perceive to be, the increasing risk taken on by local authorities following a sharp increase in Public Works Loan Board (PWLb) borrowing by councils to invest in commercial property.

6.2.4 Intelligence at this stage suggests that – rather than an outright ban on borrowing to invest in commercial property – councils will in future have to demonstrate that such investments are “proportionate” to their resources. The East Suffolk approach will incorporate the CIPFA guidance when it is published; this will enhance the other risk management features that are being developed; this includes a strict governance framework, the use of real estate investment experts and diversified portfolios. The aim is to offset principle risks such as falling capital values and ‘voids’. However, (within a tightly controlled framework) the Council ultimately accepts a higher risk on commercial investments compared to treasury investments.

6.2.5 As noted above (Paragraph 2.1.5), the Council currently has £5.0 million allocated in the Capital Programme for 2019/20 for Commercial Investment.

6.3 Governance

6.3.1 At the time of preparing this Strategy, the Governance arrangements for commercial investment and trading were under development. The business case referred to in Paragraph 6.2.2 above highlighted that tailored arrangements will be required for both the in-house and LATCO elements of the commercial investment and trading approach. Thus:

- *In-House* – Commercial Property Investment is an activity that requires quick decisions to be made if good commercial investment opportunities are to be realised. However, the requirement for speed must not be at the expense of professional expertise (e.g. on real estate investment) and strong oversight. Draft proposals include an officer “Property Acquisitions Group” - with provision for investment expertise – to consider and make recommendations on investment opportunities, overseen by a “Property Acquisitions Sub-Committee” with delegated decision-making powers; and
- *LATCO* – the arms length delivery of commercial investment and trading dictates a need for an appropriate balance between allowing the LATCO sufficient operational freedom to think and act with a commercial mind-set, but at the same time ensuring effective Governance arrangements are in place so that the strategic objectives of the Council are met and their general interest protected. Draft proposals include an independent LATCO Board with freedom to make day-to-day operational decisions, overseen by a Shareholder Committee appointed by Cabinet, being responsible for “reserved matters” (major decisions).

7) Other Liabilities

7.1 Outstanding Commitments

7.1.1 The Council also has the following outstanding commitments:

- A commitment to achieve a fully funded position on the Pension Fund (over a 20-year period from 2013 to 2033). The deficit was valued at £64.47 million as at 31st March 2018 and back-funding payments of £3.0 million are scheduled to be made in 2019/20. Required payments in 2020/21 and beyond will be reviewed as part of the next Triennial Valuation (scheduled for March 2019);
- The Council has also set aside £4.26 million (as at 31st March 2018) to cover the financial risk associated with Business Rates appeals lodged with the Valuation Office Agency (VOA); and

- The management and operation of the Council leisure service in the former Waveney district was transferred to an independent Trust (Sentinel Leisure Trust) in 2011. As part of the agreement, ownership of the facilities and equipment remained with the Council, including responsibility for financing the cost of major works. In 2017/18, the Council incurred £502,170 in capital financing payments to third parties in respect of these arrangements and, as at 31st March 2018, the Council was committed to further payments of £11 million over the next 15 years, in respect of completed works.

7.2 Guarantees

- 7.2.1 The Council became “self-financing” in respect of its retained housing stock (in the former Waveney district) from April 2012. The self-financing regime applied to all authorities and replaced the former housing subsidy system whereby the Council made annual subsidy payments to the Government funded from its HRA. Its introduction entailed a one-off redistribution of ‘debt’ between local authorities, and locally this resulted in the Council taking on PWLB loans, which it is required to service (instead of making housing subsidy payments).
- 7.2.2 A 30-year Business Plan for the Council’s HRA has been developed, which is currently generating sufficient rental income each year to run an efficient and effective housing management service, whilst at the same time servicing the outstanding debt (which is scheduled for repayment in full by March 2042 i.e. within the 30-year timeframe). However, if the HRA is unable to repay the outstanding debt at any point in the future, the Council (through its General Fund) is liable to repay any remaining balance. The remaining balance on HRA debt as at 31st March 2018 was £77.6 million).

7.3 Governance

- 7.3.1 Decisions on incurring new discretionary liabilities are taken by Directors and Heads of Service in consultation with the CFO. For example, in accordance with the Financial Procedure Rules (Part 3 of the Constitution, Paragraph 2.1.25), credit arrangements – such as leasing agreements – cannot be entered into without the prior approval of the CFO.

8) Revenue Implications

8.1 Financing Cost

- 8.1.1 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP 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 funded from Council Tax, Business Rates and general Government grants.

Table 10: Prudential Indicator: Proportion of Financing Costs to Net Revenue Stream (General Fund)

	2017/18 actual*	2018/19 forecast*	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget
	£000's	£000's	£000's	£000's	£000's	£000's
Financing Costs (£m)	329	619	939	1,242	1,269	1,364
Proportion of Net Revenue Stream	1.27%	2.36%	3.90%	5.16%	5.28%	5.67%

* Figures represent the combined positions of Suffolk Coastal and Waveney

Table 11: Prudential Indicator: Proportion of Financing Costs to Net Revenue Stream (HRA)

	2017/18 actual	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget
	£000's	£000's	£000's	£000's	£000's	£000's
Financing Costs (£m)	6,153	7,026	7,232	8,088	6,725	6,661
Proportion of Net Revenue Stream	30.68%	34.64%	35.34%	38.14%	30.52%	29.10%

8.1.2 Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for many [occasionally up to 50] years into the future.

8.2 "Prudence, Affordability and Sustainability"

8.2.1 The CFO is satisfied that the proposed Capital Programme (Section 2) is prudent, affordable and sustainable based on the following:

Prudence

- Prudential indicators 10 and 11 presented above (Paragraph 8.1.1) are within expected and controllable parameters. Thus:
 - *Prudential Indicator 10 (General Fund) - Proportion of Financing Costs to Net Revenue Stream* – the growth in financing costs reflects the Council's ambitions for capital investment in its strategic priorities over the medium-term. The projected indicator profile is relatively flat from 2020/21, remaining well below 10% at all times
 - *Prudential Indicator 11 (HRA) - Proportion of Financing Costs to Net Revenue Stream* – the indicator profile mirrors the HRA 30-Year Business Plan, which is a fully-costed strategy that will see all outstanding debt repaid by 2042/43
- *Underlying Prudent Assumptions* – a prudent set of assumptions have been used in formulating the Capital Programme. This is vividly illustrated in the approach to capital receipts whereby the proceeds are not assumed within projections until the associated sale is completed and the money received by the Council; and
- *Repairs and Maintenance* – the approach to asset maintenance is professionally guided with assets maintained in a condition commensurate with usage and expected life, addressing those items that could affect ongoing and future maintenance, in the most appropriate and cost effective manner.

Affordability

- The estimated 'revenue consequences' of the Capital Programme (£5.943 million over four years) have been included in the 2019/20 Budget and Medium-Term Financial Strategy (MTFS), extending to 2022/23; and
- The MTFS is underpinned by a Reserves Strategy, which includes contingency funds in the event that projections are not as expected (further supported by CFO report to Council under Section 25 of the Local Government Act 2003 on the robustness of estimates and the adequacy of financial reserves and balances).

Sustainability

- Capital schemes that are expected to deliver long-term revenue savings/generate income are given due priority. For example, the Lowestoft Tidal Barrier (unlocking brownfield development sites and providing a boost to future income from Business Rates and Council Tax), the Leisure Centre Development Programme (driving up usage, enabling Management Fee reductions) and Commercial Investment (e.g. generating rental income from commercial property investments).
- As explained in Section 3.1 above, the new Asset Management Strategy represents an enhancement to the Council approach to asset planning through (especially) taking a longer-term view. This includes providing for future operational need, balancing the requirement to achieve optimal performance, whilst taking account of technological change and managing the risk of obsolescence.

9) Knowledge and Skills

9.1 Officers

9.1.1 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Most notably:

- *Finance* - the Chief Finance Officer (CFO) is a qualified (CIPFA) accountant with many years of experience. The Council sponsors junior staff to study for relevant professional qualifications including AAT, CIPFA and ACCA. The Council also pays for (and ensures attendance on) training courses and conferences across all aspects of accounting, including (especially) Treasury Management to keep professional client status under “MIFID II” (the “Markets in Financial Instruments Directive”, incorporated into UK law in November 2017); and
- *Property* – the Asset and Investment Manager (AIM) – a qualified (MRICS) surveyor, with many years of experience – is responsible Asset Management within the Council. The Asset Management department is well resourced and comprises the Estates Management, Building Services and Development functions of the Council. Each function is headed by an appropriately qualified professional within their individual specialism (e.g. the Building Services team is led by Member of the Chartered Institute of Builders). As with Finance, the Council is strongly committed to supporting both professional and wider staff development within its Asset Management function, with the number of qualified RICS surveyors continuing to increase in recent years. The AIM will also play a key role in the Council’s approach to commercial investment and trading (highlighted above in Section 6).

9.1.2 The Council also has a separate Housing team that is responsible for overseeing social housing developments within the district.

9.2 External Advisors

9.2.1 Where the Council does not have the relevant knowledge and skills required, judicious use is made of external advisers and consultants that are experts/specialists in their field. The Council currently employs Arlingclose Limited as Treasury Management advisers, and the Asset Management team will appoint property advisors (e.g. development managers, valuers etc.) to support their work where required. The approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with risk.

9.3 Councillors

- 9.3.1 Newly elected councillors have been required to undertake induction training at both Suffolk Coastal and Waveney district councils for some years. However, May 2019 will see the inaugural election for the new East Suffolk Council, effectively bringing an influx of 55 'new' councillors. Duly elected councillors will therefore all receive training appropriate to their role in the new Council.
- 9.3.2 Specifically with regard to Treasury Management, the Council acknowledges the importance of ensuring that members have appropriate capacity, skills and information to effectively undertake their role. To this end, newly elected East Suffolk councillors with Treasury Management responsibilities will receive tailored training sessions from the Council's Treasury Management advisors (Arlingclose).

10) CFO Statement on the Capital Strategy

10.1 Prudential Code

- 10.1.1 Paragraph 24 of the recently updated Prudential Code determines that...."the Chief Finance Officer should report explicitly on the affordability and risk associated with the Capital Strategy".
- 10.1.2 Accordingly, it is the opinion of the CFO that the Capital Strategy as presented is affordable, and associated risk has been identified and is being adequately managed.

10.2 Affordability

- 10.2.1 The Capital Strategy is affordable and there is a range of evidence to support this assertion, including:
- *Capital Programme* – the Programme as presented above (in Section 2.1) is supported by a robust and resilient MTFS extending through until 2022/23 that contains adequate revenue provision, including sufficient reserves in the event that plans and assumptions do not materialise as expected;
 - *Asset Management* – as presented above (in Section 3.1) a new Asset Management Strategy is under development, which is taking a strategic longer-term (i.e. beyond 2022/23) view of the Council's asset base. A fundamental aim of the Strategy is to achieve the optimum balance between future operational need and affordability, which will be reflected in its component parts including strategies for purchasing and constructing new assets, investment in existing assets, transferring of assets to other organisations and the disposal of surplus assets; and
 - *Commercial Investment* – as presented above (in Section 6.2) the Commercial Investment Strategy is also under development. The primary aim of the Strategy long-term is income generation to replace the shortfall in Government funding. The Strategy is progressing positively towards the delivery stage and its success will be critical to the long-term affordability of the Capital Strategy.

10.3 Risk

10.3.1 The risk associated with the Capital Strategy has been identified and is being adequately managed. Evidence to support this assertion includes:

- *Treasury Management Strategy* – the Council has formally approved a Treasury Management Strategy for 2019/20 in accordance with CIPFA's "Treasury Management in the Public Services: Code of Practice 2017". That Strategy was developed by the Council's (professionally qualified and experienced) Finance team and informed by specialist advisors Arlingclose and other relevant and extant professional guidance;
- *Investment Strategy* – the Council has also formally approved an Investment Strategy for 2019/20 in accordance with MHCLG's "Statutory Guidance on Local Government Investments (3rd Edition) 2017". As with the Treasury Management Strategy, the Investment Strategy was developed by the Finance team and informed by specialist advisors Arlingclose and other relevant and extant professional guidance; and
- *Commercial Activities* – as noted above (in Paragraph 6.2) the Council is committed to significantly expanding the scale of its commercial activities in the medium-term as part of its Commercial Investment Strategy. It is recognised and accepted that increased commercial activity brings with it additional risk. The Strategy is therefore being developed in accordance with contemporary best practice. This includes the engagement of professional advisors on the commercial, financial and legal aspects of the project and the preparation of full supporting business cases prior to the commencement of both in-house and arms length trading activities, strictly in accordance with HM Treasury's 'five-case model' ("The Green Book: Central Government Guidance on Appraisal and Evaluation").

10.3.2 In addition (pending completion of the Asset Management Strategy), the CFO has sought, and obtained, further assurance in issuing this statement in reviewing the position and arrangements in place for maintaining Council's current assets. Based on a high level review (all assets with a Gross Book Value of £0.5 million+ were sampled), the CFO is satisfied that there are no major omissions – in terms of financial liabilities – from the Capital Programme in the medium-term. The new Asset Management Strategy will extend beyond the medium-term and will therefore – once completed – provide longer-term assurance with effect from 2020/21.

11) Capital Strategy Updates

11.1 The Capital Strategy is a 'living document' and will be periodically – usually annually – updated to reflect changing local circumstances and other significant developments. However, the development of the Asset Management Strategy and the Commercial Investment Strategy (explained above in Sections 3 and 6) are both major initiatives that could have a material impact on the Strategy as early as 2019/20, once full details are known. In the event that this happens, the Capital Strategy will be updated and re-presented to full Council.

Annual Minimum Revenue Provision Strategy

1. Where the Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Council to have regard to the Ministry for Housing, Communities and Local Government's Guidance on Minimum Revenue Provision.
2. The broad aim of the Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.
3. The Guidance requires the Council to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The following statement incorporates options recommended in the Guidance as well as locally determined prudent methods.
4. For capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset as the principal repayment on an annuity with an annual interest rate equal to the average relevant Public Works Loan Board rate for the year of expenditure, starting in the year after the asset becomes operational. MRP on purchases of freehold land will be charged over 50 years. MRP on expenditure not related to fixed assets but which has been capitalised by regulation or direction will be charged over 20 years.
5. Capital expenditure incurred during 2019/20 will not be subject to a charge until 2020/21.