Appendix D

CAPITAL STRATEGY

1. Introduction

1.1 The effective utilisation of the Council's assets and capital resources is fundamental to realising the Council's strategic outcomes and ensuring that services are provided in the most cost effective way.

1.2 The Comprehensive Spending Review 2010 has set a clear direction for Council services over the next four years and it is imperative during this period that capital resources are prioritised and capital spending is directed to priorities.

1.3 A number of budget principles have been established and approved by the Executive Board and these apply to capital expenditure as well as revenue expenditure. These are:

- The Council should aim to achieve maximum financial benefit from procurement and commissioning
- The Council will develop locality based management arrangements where appropriate
- Common business activities across the Council should be centralised and/or should be managed from a central point in the organisation where this can demonstrate better value for money
- Fees and charges should be set at a level to recover full cost, or set at a market rate. Where charges are not at full cost, the financial subsidy should be transparent and be justified in the achievement of outcomes for service users
- Provision of services should be by the most appropriate provider taking in to account value for money, quality of service, maturity of the market, in-house resilience etc.
- Funding of external organisations should all be on the basis of service agreements and should take account of other public sector funders
- Opportunities will be identified and pursued where appropriate, to provide services in collaboration with other local authorities, or other public organisations within the city and if appropriate beyond
- Capital investment will be targeted at priorities. As a general principle, borrowing will only be used to fund projects which generate savings in excess of the cost of borrowing. Other capital investment should therefore be funded by external funding sources or receipts from the sale of assets.

1.4 This Capital Strategy is prepared in the context of the 2010 Comprehensive Spending Review which covers the 4 year period through to March 2015 and must therefore recognise the overriding restriction on resources during that period. At a time when large revenue budget reductions are expected, it is right to also review capital investment plans and expectations to ensure that capital commitments and the impact on the revenue budget are affordable and sustainable. It is also important that, where reduced capital investment decisions are supported for new development and refurbishment schemes, whole life appraisal techniques are embedded within the evaluation, in order that the revenue impact on future energy, carbon and maintenance costs is minimised.

1.5 This capital strategy sets out a capital resources framework within which the Council will operate and highlights the vision for its services.

2. <u>Citywide Context</u>

2.1 The Council has a key role to play in ensuring that the city has the infrastructure and facilities to support its aspiration to be an internationally competitive city. Two current major infrastructure needs are in respect of transport infrastructure and flood alleviation. Both of these projects are major capital investments and require financial support from external funders which in the current economic climate is a significant challenge. The Council will continue to seek to secure funding for the major infrastructure needs of the city.

<u>Service Capital Strategies</u>

3. Adult Social Care

3.1 Demographic factors form a key element of the strategic context; people are living longer and with a higher level of needs. As a result of these increased demands the way care is delivered needs to change and there is a move towards more people being supported to live at home. There is a changing focus from providing help to helping people help themselves.

3.2 In terms of capital investment needs the main issues are:

- Investment in opportunities for vulnerable adults to access universally provided services, including the provision of changing places toilets at key locations within the city
- Investment in telecare, equipment and adaptations to support people living at home
- Investment in appropriate technology and business systems to enable the personalisation and direct access by people to health and social care support leading to improved outcomes

3.3 In contrast there will be a significant reduction in directly provided residential and day care provision in response to reducing demands for these services. This move could release assets for disposal but there is also a need to ensure that the remaining facilities, required for more specialised and re-abling services, are fit for purpose.

4. Children’s Services

4.1 Demographic change also places a significant pressure on Children’s Services in the need to provide additional primary school places to meet the demand resulting from rising birth rates, expected to continue until 2018. There is a need to provide 300 to 400 additional reception places every year and this scale of response cannot be met through the existing schools estate. The limit has been reached in terms of expansion possible in the majority of the primary school estate and therefore there is no other option but to investigate new sites and buildings. This will mean that sites will be taken from the capital receipts programme reducing the overall level of receipts that can be obtained.

4.2 Clearly as these rising pupil numbers move on to secondary school there will be a similar pressure on secondary school places.

4.3 One of the key capital investment issues for Children's Services continues to be the school rebuilding programme which in recent years has received significant funding through the Building Schools for the Future programme. Due to grant reductions there is doubt as to whether the remaining 3 schemes will be delivered as originally expected.

5. City Development

5.1 The City Development Directorate has the lead responsibility within the Council for the economic, physical and cultural development of Leeds, with its focus being to maintain its ongoing development as a regional economic and cultural capital and facilitating its economic recovery.

5.2 The capital programme will support this vision through the construction of the Leeds Arena, and refurbishment of the adjacent Woodhouse Lane multi-storey car park, along with the completion of the project to refurbish the City Varieties Music Hall, and provision for expenditure on essential work at Kirkgate Market.

5.3 Transport will be key to the delivery of these priorities, specifically through completion of the A65 Quality Bus Initiative, delivery of the Local Transport Plan, and the continued programme of Highway Maintenance. The New Generation Transport project continues to be a priority, with a revised offer made to Government in January 2011.

5.4 Future capital pressures include proposals to modernise and relocate the Urban Traffic Management Control unit, the development of the visitor offer at Lotherton Hall and Estate, and provision to fulfil legal obligations to reduce mercury omissions at the city crematoria.

5.5 Any further capital investment needs will focus on maintaining the quality and integrity of the current operational estate, and strategic investment supported by a formal business case, particularly relevant for future investment requirements in the Council's recreation and cultural portfolio.

6. Environment and Neighbourhoods

6.1 The priorities for the Directorate are ensuring that the city is safe and clean, that it helps meet people's housing needs and assists people to find work. The priorities sit together within a wider programme of contributing to and promoting a sustainable approach to the environment and regenerating the most disadvantaged areas of the city.

6.2 The Council is committed to delivering a minimum of 50% recycling by 2014, both as an environmental objective and to meet the commitment to the PFI contract for a Residual Waste Facility to remove residual waste from landfill.

6.3 There is a clear strategy to achieve these aims, incorporating phased service developments. The revenue costs have been incorporated into the Medium Term Financial Plan and as well as the Residual Waste Facility the development of a Transfer Loading Station at Kirkstall is required.

6.4 Population growth brings a continued requirement for growth in accessible and affordable housing and for improvements to existing and private sector stock. The current Strategic Housing Market Assessment (SHMA) for Leeds estimates that the city needs 1,890 new affordable homes per year to meet current and projected demand. A number of programmes have been put in place to help meet the shortfall including new build housing delivered by local RSLs and private developer partnerships, Council New Build and PFI schemes at Little London, Beeston Hill & Holbeck.

6.5 In the future the Council will need to develop asset based models utilising its land portfolio in the most effective way to achieve its housing growth, affordable housing priorities and regeneration ambitions. The models could include 'deferred land value', 'public land initiative' and other viable mechanisms.

6.6 The Leeds Disabled Peoples Housing Strategy promotes the capacity of disabled people to exercise choice and control over their housing options to enable them to live independently. The Disabled Facilities Adaptations Programme is an annual programme of mandatory works for owner occupiers and is anticipated that it will need to continue at current investment levels. In recognition of the future demand for the service and the adaptations undertaken by ALMOs and the RSLs a strategy has been developed and is being implemented within a cross service project.

6.7 There are significant issues that need to be addressed in the existing private and public sector housing stock in Leeds. The Leeds Private Sector Stock Condition Survey 2007 estimated total investment backlog £1.4billion, needed to address issues of disrepair, non-decency and deficiencies in back-to-back housing. There are 19,500 back-to-back houses in Leeds concentrated mainly in its underperforming neighbourhoods. Over 90% of these are privately rented and many fail to comply with the Housing Health and Safety Rating System.

6.8 There are approximately 58,000 Council owned homes in Leeds, which are managed by our four Arms Length Management Organisations (ALMOs) operating across the City delivering the functions delegated to them by the Council:

6.9 The Council's housing stock will achieve the decency standard at the end of 2010/11 and decency funding comes to an end. Investment for future years will be largely reliant on the Major Repairs Allowance. The Council's recent review of options for the future service delivery model for its housing stock has concluded that existing management arrangements should continue but with the establishment of a Shared Service Centre and a Strategic Governance Board. A prime purpose of the change is to improve Asset Management and ensure informed, consistent and prioritised resource spending decisions are made to maintain the asset base.

6.10 The Government in October, 2010 announced its intention to replace the existing HRA subsidy system with a reformed system of council house finance. The impact of this on the Council's ability to invest in its housing stock will need to be assessed when proposals are finalised.

7. Central and Corporate Functions

Corporate Property Management is responsible for managing Council property and miscellaneous land, including void properties, pending disposal or reassignment to another service (excluding schools, social housing, parkland and public open space and highways). Buildings within this portfolio are valued at in excess of £700m and are used to deliver a number of varied services.

One of the main objectives of the service is to improve the condition of assets, reduce backlog maintenance and ensure that assets are fit for purpose. Alongside this there is an ongoing programme of asset rationalisation to drive out efficiencies across the Council asset portfolio and also seeking to engage other public sector bodies in asset rationalisation opportunities where appropriate.

The Council has embarked upon a **Business Transformation** programme to deliver efficiencies across the Council. Some of these initiatives require capital investment, largely in terms of ICT development, to drive out efficiencies. Specific examples include the Electronic Document Records Management system (EDRMS) and the Employee and Managers Self Services developments.

One major initiative is the 'Changing the Workplace' project which will seek to change the way employees work across the city. By introducing flexibility in how and where people work it is possible to improve productivity and reduce the amount of office accommodation required. The initial focus for this project is the city centre but will apply equally to locality working in the following phases of the project. One major objective in the city centre is to reduce the number of office locations to create a more efficient office environment and this will require investment.

With regard to **ICT Services**, the number one priority for ICT Services is to ensure that the Council's fundamental ICT infrastructure and software is up to date and appropriate to support the daily operation of the Council. This is set out in the ICT Strategy and is being delivered through the Essential Services Programme (ESP), and the accountability for delivering this lies with ICT Services.

The priority two areas for ICT Services, involve assisting the business in delivering their priority programmes of work e.g. the procurement and implementation of a Social Care replacement system for Childrens Services and the development of the Web and Intranet replacement. Business cases are also being developed by service areas based on the other high priorities agreed in the ICT Strategy - including a replacement system for Adult Social Care, Locality Based Working and delivering efficiencies.

The ESP programme is underway and involves refreshing ageing parts of the Council's core ICT infrastructure - refreshing the software on 12,000 devices with a new desktop based on MS Windows 7 and MS Office 2010 and also providing modern collaboration capabilities based on MS Sharepoint 2010. ESP also includes replacing critical infrastructure components, parts of our data centres and parts of our telephony. The ESP programme will also deliver the solutions to equip our increasingly mobile workforce with the tools needed to underpin more flexible service delivery and working – including locality based working. The new desktop and the capability to provide solutions to enable flexible working are fundamental strands of the Council's 'Changing the Workplace' (CTW) initiative.

The 'Web and Intranet Replacement Project' (WIRP) will see the replacement of the Council's ageing web and intranet facilities. This also underpins the Council's "Delivering Efficiencies Programme" comprising of the 'CTW', 'Business Management' and 'Customer Focus' sub programmes. ICT Services will be developing and delivering key ICT solutions as part of these efficiency driven initiatives e.g. electronic service delivery and managing the implementation of the new electronic document management system (EDRMs).

Approach to Funding Capital Investment

8. External Grants and Contributions

8.1 Some capital projects are financed through external grants and contributions which can be specific to projects and cannot be used for another purpose. These are a valuable source of capital finance and the Council will continue to explore ways to lever in external funding.

8.2 In some cases external grants require a match funding element. As Council resources are extremely scarce, opportunities should be sought for securing match funding from third party sources, rather than from the Council's own funds.

8.3 From 2011/12, Government funding that has previously been provided through supported borrowing, is now provided through capital grant. Some of these are specific grants whilst others are not ringfenced to specific services and therefore the Council has flexibility in how these resources are used. There is however an expectation from government departments that the Council will meet relevant targets and priorities for which the resources are provided.

9. Borrowing

9.1 A large proportion of resources used to finance the Council's capital expenditure comes from borrowing. In previous years some borrowing has been supported by Government who pay the revenue costs of borrowing through Revenue Support Grant. As referred to above, from 2011/12, Government support for capital investment will be in the form of grant rather than borrowing, which is expected to decline over the coming four years as the Government seeks to reduce the economic deficit.

9.2 Since 2004, the Council can take up unsupported borrowing, subject to the requirements of the Prudential Code for Capital Expenditure in Local Authorities. The revenue cost of this borrowing is met by the Council and therefore decisions to raise capital finance from this source must be prudent and affordable.

9.3 Unsupported borrowing gives the Council an opportunity to use borrowing where it is more cost effective than existing funding sources and also gives real choices in terms of whether revenue resources are used to fund direct service delivery or the revenue costs of borrowing.

9.4 In light of the tight funding restrictions and uncertainty in financial markets, it is essential that proposals using unsupported borrowing are robust and realistic. Proposals must be made using a business case setting out the costs and financial benefits that will accrue. As a general principle, unsupported borrowing will only be used to fund projects which:

- invest in core infrastructure
- invest for the long term
- generate savings in excess of the cost of borrowing.

9.5 By adopting these principles, the Council can invest in efficiency and other spend to save projects. For service led business cases the cost of borrowing will be met by service revenue budgets. It is recognised however that sometimes the primary purpose of service relocation is to secure a capital receipt or avoid backlog maintenance, rather than service rationalisation. In addition there will be instances where the Council wish to use unsupported borrowing to provide a strategic facility or service and in such circumstances consideration will be given corporately to how borrowing costs will be funded .

9.6 It should be noted that for new unsupported borrowing in 2011/12 the budgeting arrangements require that only a half year's interest cost is provided for in the revenue account. In 2012/13 revenue provision will need to be made for a full years' interest plus a minimum revenue provision (see section 10 below).

10 Minimum Revenue Provision (MRP)

10.1 The Capital Finance and Accounting Regulations require councils to produce a statement of policy on making Minimum Revenue Provision (MRP). MRP is an annual revenue charge for the repayment of borrowing and other capital financing liabilities. Whilst the statutory guidance gives local authorities some discretion about how to calculate 'prudent provision' for MRP, the guidance steers authorities firmly towards a limited choice of options in which the key principles are demonstrating prudence and repaying borrowing over the period in which the capital expenditure provides benefits.

10.2 The requirement to make a prudent provision for MRP applies also to balance sheet liabilities in relation to finance leases and PFI schemes. These schemes are being treated in accounting terms as the acquisition of fixed assets and the liability represents the amount being paid towards the purchase of the asset itself rather than interest or service charges payable.

10.3 Statutory guidance allows the use of capital receipts to fund the payment of any liabilities in relation to finance leases and PFI schemes and the Council's accounting policies have now been amended to reflect this. The options considered in determining the policy are set out in more detail in an Appendix to the capital programme report.

11. Capital Receipts

11.1 The Council generates its own capital resources through the sale of surplus land and buildings and these resources can be used by the Council to invest in new capital projects. In recent years capital receipts have proved to be a significant source of capital funding. Whilst receipts have reduced in recent years and are expected to remain so in the near future due to the impact the recession has had on the property market, it is vital that the Council retains maximum flexibility on all capital receipts.

11.2 Capital receipts can be used to finance capital expenditure or could be used to redeem the Council's debt. As explained in paragraph 10.3 above, capital receipts can now also be used to fund liabilities in relation to PFI schemes and finance leases. The Director of Resources will fund capital expenditure and other liabilities using the optimum mix of capital resources which will ensure the most advantageous position for the Council.

11.3 A number of arrangements have been in place in the past that allow the ring fencing of receipts to specific projects / initiatives as an incentive to rationalisation. Whilst receipts are sometimes referred to as 'ringfenced', the disposal generating the capital receipt usually takes place after investment has been made in the replacement asset and so in reality, borrowing is used to fund the new asset and the capital receipt (which will often materialise in a later year) is used to fund the overall programme in a later year.

11.4 To ensure that the Council retains maximum flexibility on the use of capital receipts, the only circumstance in which capital receipts can be ringfenced to specific schemes is restricted to instances where the receipt is required to cover legitimate decanting/replacement costs and this will include capital investment required in order to release assets for disposal such as capital costs associated with relocating playing pitches where the land value can be enhanced, or other infrastructure costs.

12. Single Capital Pot

12.1 The Government's Single Capital Pot allocation is available to spend on any service in line with Council priorities, but in practice Government Departments expect it to be used largely to achieve their targets and objectives for the four major services; Education, Housing, Transport and Social Care. The Council's established approach currently is to allocate 100% of the Single Capital Pot allocations direct to the four services for which it is intended.

13. Section 106 Contributions

13.1 Through the Planning framework, external contributions are received by the Council towards works in a number of areas:

- Greenspace
- Transport
- Affordable Housing
- Education
- Public Realm
- Play Facilities

13.2 In all cases the agreement entered into by a private developer is to spend monies in a specific part of the city on one of the areas listed above.

13.3 In light of overall capital funding reductions, the Council must seek to use S106 monies to fund its overall priorities. It is proposed therefore that a number of overarching principles be established for the use of S106 monies within the Council:

- S106 agreements must seek to give maximum flexibility to the Council in the use of the funds secured
- In respect of Greenspace S106 agreements, priority will be given to the funding of community parks, play areas and sports pitches.

13.4 Regulations are now in place to allow local authorities to introduce Community Infrastructure Levies (CILs) (after formal consultation and independent examination). Under the CIL proposals, individual S106 agreements linked to specific developments are likely to be replaced by a more general CIL. Any CIL proposals for Leeds will be reflected in this capital strategy as they are developed.

13.5 Another new initiative introduced from 2011/12 is the New Homes Bonus under which a payment is received from Government for each new home added to the Council Tax register (net of demolitions). As a new form of funding for the Council, the Director of Resources will ensure the bonus is used as flexibly as possible to support the Council's financial pressures and priorities.

14. Use of Council Land

14.1 In considering the use of Council land (or property), whether for operational use, new development or disposal, the following governance and underlying principles (summarised from the draft Asset Management Plan) must be applied:

Prioritising Scarce Resources

- In optimising the use of assets Council resources have to be prioritised. All major investment, development and disposal programmes will be considered by the Strategic Investment Board before recommendations for approval are made.

Corporate Decision Making

- The Asset Management Board oversees the delivery of those programmes and projects and informs the strategic use of the Council's land and property assets.

Acquisition

- All Council land (including property) is acquired and held for the purpose of delivering specific functions, but it is owned by the Council rather than operational services which use it.

Use:

- Through their service and financial planning processes, services will cease their use of land if it ceases to be affordable or support corporate and service priorities;
- When land is surplus to operational requirements, the retention for other purposes or disposal must be determined through the corporate asset management process, based on the following criteria.

Retention for other Purposes:

- If it is proposed to be used or developed for other purposes by the Council, to ensure effective use of assets, the opportunity cost of the land must be reflected in options appraisals and business cases;
- Used or developed for other purposes includes redevelopment for the same use as previously (e.g. new housing)
- Funding for development or refurbishment should be from borrowing underpinned by efficiency savings, external sources or capital receipts where necessary.

Disposal

- Clarity of purpose is required at the outset for all disposals because use of assets can be optimised in a number of ways depending on the strategic outcome. The default position is to maximise the capital receipt upon disposal, but other options exist including maximising financial return as deferred payments or as an income stream or social, economic or environmental benefits for the city. Therefore, where the primary aim of disposal is other than to maximise capital receipts, all alternative proposals will need the support of the Strategic Investment Board or Asset Management Board as appropriate.
- If declared surplus, the value of land on disposal is to be maximised in terms of either;
  - financial value to reduce the need to borrow or support the capital programme (i.e. capital receipts need to satisfy the statutory requirement to obtain ‘Best Consideration’). This is usually through sale competitively on the open market, but can be by private treaty in specific circumstances such as disposal to a regeneration or other partner, subject to payment of market value; or
  - ‘Best Value’ in defined circumstances to support specific Council priorities (disposals of land at ‘Less than Best Consideration’ using statutory powers). This includes transfers of land to partners of the Council, e.g. for affordable housing or community asset transfers or disposal to support regeneration programmes. Foregoing all or part of the capital receipt needs to be justified through robust options appraisals and business cases setting out the opportunity costs of the land in terms of cashable and other service benefits, external funding opportunities, risks and other options for delivery.

15. Demolitions and Dilapidations

15.1 When services vacate property which is surplus to their operational requirements, consideration is given to the future of the property in terms of whether it can be used for another service/purpose, whether it should be disposed of or whether property should be demolished and disposed of as a cleared site, especially if the site rather than the building has the higher value.

15.2 Sometimes demolition is the preferred solution to a site because the building has little intrinsic value but also because it reduces ongoing revenue costs associated with empty buildings such as security costs and empty rates and . reduces the health and safety risk of unauthorised access. The cost of demolition can be significant, particularly where buildings contain asbestos and the funding of demolition has and continues to be an ongoing problem but in part this cost is regained on the sale of the site as the purchaser would have previously deducted the cost of demolition from their offer . In order to ensure that resources are available to demolish property when required, it is proposed that when a building is vacated, the budget provision for National Non Domestic Rates (NNDR) transfers from the vacating service to the Corporate Property Management budget to support the cost of borrowing to fund demolition costs.

15.3 When a service vacates a leased building it is usual for the cost of dilapidations to be sought by the landlord. . The cost of borrowing to fund any dilapidations may need to be the first call on rental and other revenue savings which arise from vacating the premises. Where dilapidations arise as part of a wider corporate rationalisation programme, the cost will form part of the overall business case for the project,