

For general release

REPORT TO:	SCRUTINY AND OVERVIEW COMMITTEE 3rd NOVEMBER 2015
AGENDA ITEM:	X
SUBJECT:	CAPITAL BUDGETS
LEAD OFFICER:	Nathan Elvery, Chief Executive
CABINET MEMBER:	Councillor Simon Hall, Cabinet Member for Finance and Treasury
PERSON LEADING AT SCRUTINY COMMITTEE MEETING:	Richard Simpson, Assistant Chief Executive (Corporate Resources and Section 151 Officer)

ORIGIN OF ITEM:	This item is contained in the Committee's work programme
BRIEF FOR THE COMMITTEE:	<p>The Committee seeks answers to the question: how is the council's capital budget developed and spent?</p> <p>The Committee seeks to review the Council's capital programme by receiving information on the projected expenditure of schemes based on the latest round of monitoring returns and in the context of the budget strategy ie:</p> <ul style="list-style-type: none"> ☺ scheme progressing on time or within budget ☹ scheme progressing on time but not within 5% of budget or scheme progressing on time but not within expected timescales ☹ scheme neither progressing within expected timescales nor within 5% budget

1. EXECUTIVE SUMMARY

- 1.1 The Council is required, on an annual basis, to set a budget for both its revenue and Capital expenditure. Capital expenditure is used for investment in the purchase or delivery of assets and infrastructure to support and enable the provision of the services of the authority, deliver our statutory duties and to achieve the desired outcomes of the administration. It is also used to maintain the assets and infrastructure that the Council already owns in a fit state.
- 1.2 This report sets out the rationale behind the setting of the capital programme each year and how this then translates into the capital budget as well as

providing information on the asset management strategy. It also provides a summary of the major sources of funding that are being accessed and the possible impact that any borrowing used to support the programme has on the revenue position of the Council.

- 1.3 An explanation of the Community Infrastructure Levy (CIL) and S106 funding and how it is being used to support the capital programme is explained
- 1.4 The process by which the progress of the programme is monitored is provided and an analysis of possible issues in providing accurate information and mitigation to improve the current process are explored.
- 1.5 Details of the current capital programme are provided in Appendix 1 and a review on the latest financial position of the major projects within the programme is provided within the report.

2. SETTING THE CAPITAL BUDGET

- 2.1 The Council has published a suite of plans which provide detail on the direction that the Authority plans to take in delivering services and providing desired outcomes for the residents of Croydon in future years.
- 2.2 These three plans are the Corporate Plan, the Growth Plan and the Independence and Liveability plan. The ability to succeed in delivering on the aspirations in these plans is reliant on the availability of sufficient funding to provide the services required but also the availability of the necessary assets and infrastructure to enable delivery.
- 2.3 An analysis of the assets and infrastructure requirements for the delivery of the required outcomes provides the initial basis for setting the Capital Programme for the organisation for the next 3 years. The capital requirements will often exceed the availability of potential funding so the value to the organisation of each proposed scheme has to be evaluated to look at its importance, alternative methods of delivering the same outcome and more cost effective opportunities. This process was carried out in the Autumn of 2014 via an officer Gateway panel led by the section 151 Officer to derive the proposed programme for 2015/18.
- 2.4 In a similar manner the decision to review the asset portfolio of the Council to ensure that the use of its assets also supports the current strategies and direction adopted by the Council was taken. As a result the council adopted a new Asset Management strategy in 2014.
- 2.5 The Asset Strategy challenges services to make better use of properties and assets and reviews opportunities to deliver housing and schools through the use of existing land rather than purchasing new sites which would otherwise add to the demand for capital expenditure.
- 2.6 This approach will enable the Council's assets to help support the capital programme through:

- Direct contribution of capital sums through the disposal of surplus assets
- Reduce capital expenditure on ageing assets that are no longer fit for purpose by looking at alternative uses or redevelopment. Backlog maintenance is now estimated to be circa £30m and a number of buildings have reached the end of their expected life and require significant capital funding to repair them.
- Better utilisation of assets to help deliver redevelopment opportunities that will generate capital and revenue opportunities for example through direct sales, new homes bonus and increased business and council tax income.

2.7 The current state of repair of the Council’s assets is also a factor in considering the level of capital funding that will be required to maintain the estate in a safe and fit for purpose condition in the future. Whilst the review undertaken as part of the asset management strategy identified an estimated backlog of £30m on Council buildings the situation for the backlog in infrastructure assets is more complex.

2.8 The requirement to maintain the highway in its current state is estimated to be £15.4m p.a. which is less than the capital funding currently being allocated. As a result the condition of the highways is predicted to gradually deteriorate. As the highways estate is not deemed to be in a desirable condition currently, deterioration will lead to an increasing backlog of work required to bring the assets up to the desired condition. An estimate of the capital funding requirement in order to bring the assets up to this condition is estimated to be £133m.

2.8 The £133m estimated additional capital required is spread across a number of categories:

Carriageway	£60 million	
Footway	£45 million	
Structures	£20 million	renewals of strategic bridges
Drainage	not yet determined	Investment to mitigate flooding

2.9 By considering the condition of our assets, the projects to be delivered and the best options for delivering them, the capital expenditure required to deliver the programme can be ascertained and the funding options considered.

2.10 By their very nature, capital projects generally take a number of years to complete so it is important to capture both the total project expenditure required as well as the expected requirement for funding in each financial year which will then form the basis of the capital budget.

2.11 The proposed capital programme for the Authority is presented to Council in February each year for approval. The 15/16 capital programme is shown in Appendix 1.

3. Funding for the Capital Programme

- 3.1 Capital expenditure is funded from a number of sources, including capital grants and capital receipts from the sale of assets. The extent to which the capital programme exceeds those grants, receipts and so forth is the amount of unsupported capital expenditure. Unsupported capital expenditure is funded through borrowing. This borrowing can be internal, that is to say from cash balances held for other purposes, but of course this is only a short-term method. In the longer term, unsupported capital expenditure must be financed by debt, raised from a range of government or commercial lenders, but borrowed as and when needed, or according to treasury factors.
- 3.2 The unsupported capital expenditure shown as funded by borrowing in Table 1 will, over a period of time, need to be funded by debt. The debt will have an impact on the revenue account in terms of interest payable to service the debt. The borrowing requirement shown in Table 1 for 15/16 of £32.932m will cost the council £1.265m in interest payable in 2015/16. The total interest payable budget for 15/16 is £22.355m.
- 3.3 Not all of that debt will be borrowed immediately but the availability of the required funds will be determined by the requirements of the capital programme phasing. However, the timing of any borrowing being taken up will be subject to market factors. It is therefore important to enable the most efficient treasury management, to maximise the effectiveness of the capital expenditure and forecasting process.
- 3.4 At the end of August 2015 the Council had a debt portfolio amounting to £760m comprising £438m of loans to support current and previous capital expenditure investment and a further £322m borrowed to take Croydon out of the old Housing Subsidy regime. Effective application of treasury principles has ensured that this debt is both affordable and sustainable. At present the average cost of interest on these loans is 3.84% and this figure has been used to calculate the forecast cost of additional borrowing.

Table 1 Funding of the Capital Programme

Funding	Budget 2015/16 £m	Budget 2016/17 £m	Budget 2107/18 £m	Budget 2018/19 £m	Total £m
Capital Receipts	15.038	9.500	14.000	9.393	47.931
Targeted & Basic Needs	53.608	32.983			86.591
TFL	4.138	3.336	3.336	3.336	14.146
GLA	4.354				4.354

S106	2.045				2.045
Revolving Investment Fund (RIF)	10.470				10.470
Borrowing	32.932	90.656	69.572		193.160
Other grants and funding	5.308	3.768	1.610	1.610	12.296
Total General Fund	127.893	140.243	88.518	14.339	370.992
HRA	42.957	36.621	36.621	36.210	152.409
Total	170.851	176.864	125.139	50.549	523.402

3.5 The capital programme for 17/18 and 18/19 and therefore the funding required, appears significantly lower than 15/16 and 16/17 and this is mainly due to the fact that at this stage the programme is less well defined.

3.6 The future capital programme is looking to reduce the borrowing requirements of the Council while still delivering the Growth and infrastructure required for Croydon's ambitions plans.

3.7 The Council is doing this in a number of ways, by seeking further devolution and powers through the Croydon Growth Zone, and by setting up a Revolving Investment Fund (RIF)

3.8 The main focus of the RIF will be to support the delivery of new homes across the borough although it could also invest in commercial opportunities where they arise.

3.9 The Council has also been able to reduce its borrowing costs through accessing a loan facility from the European Investment Bank (EIB). A contract has been signed with the EIB that will offer cheaper alternative sources of long term financing relating to the Council's Education Strategy, generating substantial savings of interest payable on the Authority's overall debt in the future.

3.10 Cabinet acknowledged in the Autumn Financial Statement in September that the current Education Estates Strategy has become unaffordable given the reducing revenue grant of the council. As a result the council is investigating a policy to only provide school places where they are funded by central government, and allowing other providers to fill the gap.

4. Community Infrastructure Levy (CIL) / Section 106 and their apportionment

4.1 CIL and Section 106 are resources secured by the Council to offset the impacts of development. Since 2013 CIL has largely replaced S106 as a mechanism for infrastructure (capital) financing.

4.2 The Council has been collecting CIL since April 2013 when the charging schedule was adopted. The 13/14 year saw limited receipt as most

developments that were CIL liable were not commenced (the trigger for payment). The total borough CIL receipt to date is £1,824,138 (2013/2014 - £249,537, 2014/2015 - £899,392 and 2015/2016 as at 1/10/15 - £675,209). CIL is assigned in accordance with the Regulation 123 list in the table below which was approved by Cabinet alongside the charging schedule and sets out the infrastructure projects to be funded in full or in part by CIL.

4.3 The CIL receipts collected above have not been allocated to date. It is proposed that any assignment should not been done until the outcome of the Council's Growth Zone submission to the Government is known.

Infrastructure projects or types that will, or may be, wholly or partly funded by CIL.
Provision, improvement, replacement, operation or maintenance of <u>education facilities</u>
Provision, improvement, replacement, operation or maintenance of <u>health care facilities</u>
Provision, improvement, replacement, operation or maintenance of those projects listed in the <u>Connected Croydon Delivery Programme</u> dated April 2013 and any projects as may be added to the said Programme after April 2013 as approved by Cabinet.
Provision, improvement, replacement, operation or maintenance of <u>public open space</u>
Provision, improvement, replacement, operation or maintenance of <u>public sports and leisure</u>
Provision, improvement, replacement, operation or maintenance of <u>community facilities</u> (as defined by the Croydon Local Plan – Strategic Policies)
<u>Local Meaningful Proportion</u>
Authority's administrative proportion

4.4 Discussions regarding the CIL '*Local Meaningful Proportion*' (the proportion of CIL to be allocated to local communities - 15% without a Neighbourhood Plan (NP) in place/ 25% with a NP) are on-going, with the suggestion that the original allocation through the 16 places of Croydon is refined to reflect allocation through a smaller number of place regeneration plans.

4.5 In 2015 the Council has £11m S106 capital held on account, around £3.5m of this has been allocated to existing projects, an additional £4m is notionally allocated including to the to the Council's emerging Homes delivery programme

and School Places delivery programme pending detailed applications. The residual is yet to be allocated to projects/activities and officers are working across the organisation to attract suitable applications for release of funds.

- 4.6 S106 agreements are legally binding documents between developers and the Council. Funds can only be used as set down in the agreement; failure to comply with the terms of the agreement could result in contributions being claimed back by developers and will result in reputational damage which could negatively affect our relationship with developers in the future. The geographical conditionality of some S106 agreements can restrict development of projects; additionally some wording of permissible use can make allocation challenging. Details of the current S106 funds held and proposed allocation are shown in Appendix 2

5. MONITORING THE CAPITAL BUDGET

- 5.1 As part of the implementation of the One Oracle system across the Council a new capital monitoring package, Oracle Projects, has been implemented and can provide detailed reporting on actual expenditure and forecasts for each of the projects in the Capital Programme. Regular meetings between the Project managers and finance staff ensure that the information is as accurate and up to date as possible.
- 5.2 The capital programme is overseen by Growth board, chaired by the Executive Director of Place, which has membership from key stakeholders within the Council, including the Section 151 officer and Directors from all three departments.
- 5.3 A review of the capital programme took place at the beginning of this financial year to ensure that the capital budgets reflected the most recent information on the progress of schemes. This resulted in a reprofiling of the Education programme to reflect the anticipated spend profile over the next three years. This was approved by Growth board and then by Cabinet.
- 5.4 The revised capital programme for 2015/16 amounts to £170m, a detailed breakdown of the programme can be found in Appendix 1.
- 5.5 The high level of slippage that has occurred recently and over the past few years has highlighted the need to improve the initial profiling of the project expenditure processes and also for reviewing progress on all the major projects at regular intervals to improve the quality of the forecasting. Earlier identification of delays or cost issues in the delivery of projects and recognition of the impact that this will have on the overall timescale and budget will allow for improved accuracy of forecasts. In turn this will allow for more accurate profiling of budgets and the timing of required funding which will have a positive impact on the treasury management surrounding the capital programme and will allow the interest payable on financing to be minimised.

5.6 The progress of the major capital projects in the current programme is summarised below, highlighting schemes that are not progressing within the anticipated timeframes or budget.

⊗ **scheme neither progressing within expected timescales nor within 5% budget**

5.7 A small number of schemes fall within this category. The following table sets out why the schemes are at this position and any mitigation currently in place to bring these back on track.

Project	Position	Mitigation
High Streets – Old town and Central	The project is now reaching completion but has faced delays due to unexpected delays caused by Tram related constraints and changes to the context in the town centre since the scheme was conceived inc. Whitgift redevelopment.	Additional funding has been sought from the Greater London Authority (GLA) and Transport for London (TfL) to cover increasing delivery costs.
West Croydon Interchange	The build programme for this project has been delayed due to additional constraints placed on the project by Tramlink; these delays have increased costs. The project will be complete by Summer 2016.	TfL have absorbed the loss of revenue during the extended tram possession. Additional funding has also been granted by the GLA to deliver this project to deliver additional outcomes.
New Addington Central Parade	The project has been delayed due to interdependencies with the wider regeneration ambitions for New Addington and a desire to avoid abortive works. The first phase of improvement works will be complete by summer 2016. The costs for this project are higher than anticipated due to construction inflation and the current buoyant market	Additional funding has now been secured through Section 106 for this project additional funding from TfL is being sought to manage budget over-runs.
Christ Church Cof E Primary	The permanent build solution for this school has been delayed due to	The governance and briefing process for education estates delivery

	complexities in agreeing the brief with stakeholders. The permanent solution is on track for delivery for the 2017 in-take and temporary modular units will be installed for the 2016 in-take. The temporary solution has increased delivery costs.	was reviewed in 2015 to resolve programme issues and delays caused by the briefing and agreement process between schools.
Heavers Farm	The permanent build solution for this school has been delayed due to complexities in agreeing the brief with stakeholders. The permanent solution is on track for delivery for the 2017 in-take which has increased delivery costs.	The governance and briefing process for education estates delivery was reviewed in 2015 to resolve programme issues and delays caused by the briefing and agreement process between schools.
Quest Academy Secondary	This school was completed on time, however external ground-works have been delayed due to asbestos contamination and subsequent compensation claims from contractor. The discovery of asbestos and subsequent management plan has resulted in the project exceeding set budget.	The Council is working with the contractor and seeking expert advice to reduce costs relating to management of the asbestos issue.

☹ scheme progressing on time but not within 5% of budget or scheme progressing within 5% of budget but not within expected timescales

There are a number of schemes which fall within this category, they are as follows:

Project	Position	Mitigation
East Croydon Interchange Phase 1	The project is within budget but has been delayed due to unexpected delays caused by Tram related constraints.	The Council will continue to work with partners to better manage the permissions and approvals process for public realm works.
Connect 2	The project is on budget but has faced delays while seeing agreement through public consultation and	Dedicated resource has been allocated to this project to tie in consultation with the cycle forum

	policy discussion as to cycling in parks. =	scheduled for November 2015.
Wellesley Road Phase 1	The scheme is on budget but has been delayed due to the changing context in the metropolitan centre and the desire to reduce abortive works. The project is affected by changes to road layout required by the Whitgift redevelopment and the Dingwall Loop Tram project; the scheme has been rescope and redesigned in partnership with the GLA, TfL and developers to accommodate broader changes.	The project is predominantly funded by the GLA. The GLA, TfL and Croydon Limited Partnership have been party to decisions to delay the programme to ensure integrated delivery of transport infrastructure projects in the Metropolitan Centre.
East Croydon Interchange Phase 2	The project is on budget; the scope is being revised and the project implementation timetable may be delayed as the demolition of the Royal Mail site is not progressing as originally envisaged. The delay is intended to minimise abortive works costs caused by the redevelopment of the Royal Mail site.	The decision to delay implementation due to changes beyond our control have been made with TfL the major funder and stakeholder for this work.
Ark Oval Primary	The project is delayed due to complexities in agreeing the brief with stakeholders.	An off-site prefabricated build solution is proposed to ensure accommodation for 2016 intake,
Oasis Fiveways Primary	This project is on budget but delayed due to pre-app planning advice that the initial plan of a 4FE school would be over development of the site and would not be supported primarily due to transport related matters.	Alternative design solutions are currently being scoped to resolve planning issues.
Heathfield academy (Aberdeen road)	Initial cost estimates were circa 20% higher than anticipated. Work to reduce this has been	Mitigations will include temporary accommodation at Robert Fitzroy and the use of hybrid modular and

	ongoing and has resulted in the project being delivered within 5% of budget, but this has adversely affected the timescale of the project.	traditional build solutions to mitigate delays.
Chipstead Valley Primary	The delay in finalising the project brief has delayed the start of the Project, however it is estimated to be completed within budget	The governance and briefing process for education estates delivery was reviewed in 2015 to resolve programme issues and delays caused by the briefing and agreement process between schools.
St Johns Cof E Primary	The delay in finalising the project brief has delayed the start of the Project, however it is estimated to be completed within budget	

☺ **scheme progressing on time or within budget**

The majority of Capital schemes (over 80%) are progressing on time and within budget.

Appendices

Appendix 1 Capital programme 2015-19

Appendix 2: S106 summary balance sheet and allocation

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BACKGROUND DOCUMENTS: