

19 OCTOBER 2021

KEY DECISION? ~~YES~~/NO

### BUDGET STRATEGY 2022/23

**SUMMARY:**

This report sets out the budgetary framework to support the preparation of the 2022/23 budget.

The report also provides a summary of the financial position of the Council and sets out how members will be kept informed of material changes in the forecast over the medium-term for financial planning purposes. Final decisions on the overall budget and Council Tax level will be made by Council in February 2022.

**CABINET RECOMMENDS TO COUNCIL** that a contribution of up to £50,000 towards the purchase of Tices Meadow by Surrey County Council as outlined in section 5 of Appendix A

**CABINET is RECOMMENDED to:**

- (i) Approve the Budget Strategy for 2022/23 as outlined in section 3 of Appendix A
- (ii) Note the forecast for Capital Receipts and the pooling of capital receipts to support the capital programme as outlined in section 5 of Appendix A

## 1. INTRODUCTION/BACKGROUND

- 1.1. This report informs members of the current financial position (as outlined in [FIN2113](#) and [FIN2115](#) at Cabinet in September 2021) and sets out how members will be kept informed of the strategy for addressing the projected core budget deficit highlighted in the MTFs published in February 2021.
- 1.2. Section 3 of the report in Appendix A outlines the approach that will be taken when setting the detailed revenue and capital budgets for 2022/23. Members are asked to endorse this approach as part of the strategy for addressing the projected core deficit.

## 2. SUMMARY OF STRATEGIC ISSUES

- 2.1. In common with many local authorities, Rushmoor Borough Council continues to face significant financial challenges over the medium term. The

Council will need to continue to take difficult decisions around resource allocation.

- 2.2. There are several key drivers of change that affect the way in which the Council's financial plans are developed – Population, Economy, Policy Decisions, CREP and ICE Programmes. Whilst these drivers are still relevant and can assist members in decision making, the level of uncertainty around national policy issues (recovery from Covid-19 and Levelling-up in particular) and the global economy makes it more difficult to predict the impact on the Council in the near-term.
- 2.3. Given the level of uncertainty around the national economic and political environment, this report will provide members with an overview of the key economic factors that are likely to have an impact on revenue budget and MTFS update. A more detailed review of these factors will be undertaken in the coming weeks, with a further report in December. This report will focus on specific issues including the Local Government Funding context and reviewing the key assumptions that inform the MTFS 2022/23 to 2025/26.
- 2.4. A detailed review of the Council's financial position and the Budget Strategy for 2022/23 is set out in Appendix A of this report. The section below sets out the key strategic issues discussed in the Appendix and should give members a good overview.
- 2.5. **A significant funding gap was identified in the February 2021 MTFS.** As the table shows, the indicative position outlined for 2022/23 is a deficit of £3.1m, as reported to Council in February 2021. It was noted at the time that a revised approach to Savings Plan was required given the deficit position forecast over the MTFS period.

	2021/22 (£'000)	2022/23 (£'000)	2023/24 (£'000)	2024/25 (£'000)
<b>Funding Gap forecast in MTFS</b>				
Draft Revenue Budget (before Savings)	13,125	13,301	14,423	15,103
TOTAL Funding	11,855	9,561	9,616	10,175
<b>Funding Gap</b>	<b>1,270</b>	<b>3,739</b>	<b>4,807</b>	<b>4,928</b>
Savings identified	(256)	(605)	(751)	(751)
<b>Residual Funding Gap After Savings</b>	<b>1,014</b>	<b>3,134</b>	<b>4,056</b>	<b>4,177</b>
Use of Stability & Resilience Reserve	(1,014)	(3,134)	(4,056)	(4,177)
<b>Stability &amp; Resilience Reserve Y/E Balance</b>	<b>4,550</b>	<b>1,416</b>	<b>(2,641)</b>	<b>(6,818)</b>

- 2.6. Whilst the Council may benefit from further Government Funding (e.g., one-off grant funding, additional NHB), the downward trend in Government funding will frame the Council's revenue budget in future years.

- 2.7. It was recommended that the Council continued to review not only the costs of services but considered the nature and scope of services being delivered.
- 2.8. The Council will need to identify additional savings to mitigate the impact of any savings that cannot be achieved in full or in the timeframe required, as this would put additional financial pressure on the Council.
- 2.9. **Forecast for 2021/22 is for an adverse variation against the revenue budget putting additional pressure on the Stability and Resilience reserve.** Shortfalls of income from Car Parks and the Crematorium are the main concerns given material income shortfalls are forecast for the year. It is likely that the revenue budget will remain under pressure and further adverse variations are expected, with risk and uncertainty around Waste and Recycling costs as the Food Waste service changes take effect
- 2.10. **CPI inflation** is currently above the Government's target at 3.2% and is expected to rise further in the near term, to slightly above 4% in 2021 Q4, owing largely to developments in energy and goods prices.
- 2.11. The forecast for **Interest Rates** is for the bank base rate to remain at 0.10% in the near term but may rise from Q2 2022.
- 2.12. There has been little additional progress from the Government on other local government finance issues such as New Homes Bonus and Council Tax referendum limits
- 2.13. **The Government have announced a multi-year Spending Review** which will set resource and capital budgets for 2022-23 to 2024-25 and conclude on 27 October 2021, alongside Autumn Budget 2021. In a letter from the Prime Minister and the Chancellor to all Government departments, the SR21 will focus on the Government's priorities and support the economic recovery
- 2.14. The 2022/23 **Budget Strategy** is informed by the financial impact from Covid-19 in the current year. The strategy below sets out the key assumptions that will be made when reviewing the Council's revenue budgets for 2022/23.
- 2.15. The level of uncertainty around the Council's financial position is unprecedented and makes the forecasting of income and expenditure budgets for 2022/23 very difficult. As such, a number of broad assumptions are set out below that will allow budgets to be updated.
  - Starting point for reviewing budgets for 2022/23 is the assumption that budgets will remain to near/close to pre-Covid levels.
  - All budgets to be reviewed with a focus on cost reductions and savings. This is a separate review to any opportunities identified through the Cost Reduction and Efficiencies Programme (CREP).
  - High risk income and expenditure areas that have been identified through budget monitoring as a risk will be reviewed in detail with options identified to mitigate any income shortfall or budget pressure

- Review of salary budgets to ensure only posts from the agreed structures are included within the revenue budget.
  - Savings Plan will be reviewed in detail to ensure the Council can set a balanced budget for 2021/22 and address and deficit over the medium-term
  - Council Tax/Business Rates income assumptions will be reviewed
  - Capital Programme will be reviewed with evaluation of any new or revised schemes with reference to the Union Yard Scheme approved by Council in July 2021.
  - Adequacy of reserves will need to be considered
- 2.16. The 2020/21 Outturn position on the General Fund Revenue budget highlighted a **significant issue around business rates income and the deficit on the Collection Fund**. The report to Cabinet highlighted further analysis was needed of the Collection Fund deficit position to understand the timing and financial impact of financing the deficit over the MTF5 period
- 2.17. The Government provided **further guidance and clarification on the revised PWLB Lending Terms** in August 2021 with details set out in Appendix B
- 2.18. The **Government also set out their views on the local authority capital finance framework**. Whilst the Government have recognised the importance of local government capital investment, they are concerned at the risks some local authorities have taken around investment in commercial property.
- 2.19. **Council approved the Union Yard Regeneration Scheme**. Negotiations are yet to conclude with the Hills Partnerships Limited in respect of the fixed price JCT Design and Build Contract. Therefore, the capital programme and capital financing position will not be updated until the final contract sum is agreed and the profile of expenditure over the duration of the project is available.
- 2.20. The Council is expected to receive **capital receipts** from the Parsons Barracks scheme and asset sales in the latter half of the financial year. The level of anticipated capital receipts for the year is likely to be £1.25m at the lower end of expectations and £2.25m at the higher end depending on the timing of receipts.
- 2.21. The emerging policy position is to pool all receipts from the sale of all assets sold to support the Capital Programme in line with funding the Council's priorities (as published in the Council Business Plan) which will include the potential sale of any investment properties or other property assets.
- 2.22. Cabinet recommends to Council that a **contribution of up to £50,000** is made to Surrey County Council for the purchase of **Tices Meadow** as outlined above; to be funded from anticipated capital receipts

**BACKGROUND DOCUMENTS:**

**CONTACT DETAILS:**

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### 1. ECONOMIC OUTLOOK

- 1.1. There is some uncertainty in the national and global economic outlook with the unwinding of Covid support for businesses and inflationary pressures in the economy. The commentary below reflects the position at the time of writing (late September 2021), and will, of course, be subject to change.
- 1.2. It is expected that the financial impact from Covid-19 will continue to have an impact on the Council's budgets over the short to medium-term as the national and local economic activity recovers and rebalances.
- 1.3. The 2021/22 Budget Monitoring report ([FIN2115](#)) to Cabinet in September 2021 provided members with an initial view for the financial year with an adverse variation forecast. Variations identified in the report will provide some context to the budget setting process for the coming financial year. This is shown in Table 1.
- 1.4. The main variations on the revenue budget in the current year is due to a shortfall in income from Car Parks and the Crematorium. Additional expenditure has been forecast in the IT service due to pressures around staffing costs given the need to maintain service delivery and support to Council projects.
- 1.5. It is likely that the revenue budget will remain under pressure and further adverse variations are expected, with risk and uncertainty around Waste and Recycling costs as the Food Waste service changes take effect.
- 1.6. The Council will receive financial support from the Government through the Sales, Fees & Charges Compensation Scheme which was extended for Q1 2021/22. A claim is due to be made by the end of October 2021.
- 1.7. Given the scale of the financial impact on the revenue budget in the current financial year and the nature of the pandemic, it can be expected that income and expenditure budgets will remain under pressure over the short to medium-term. Careful consideration will also need to be given to the impact on Council Tax and Business Rates in terms of both collection rates and forecast of growth or decline in the tax bases.

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**Table 1: 2021/22 Budget Monitoring position (September 2021)**

	2021/22 Original Budget (£'000)	2021/22 Latest Budget (£'000)	2021/22 Outturn Forecast (£'000)	2021/22 Variation (£'000)
<b>General Fund Revenue Budget</b>				
Corporate Services	5,184	5,189	5,249	60
Customer Experience & Improvement	55	310	425	115
Major Projects & Property	(5,434)	(5,289)	(5,166)	123
Operational Services	9,869	10,069	10,307	238
Planning & Economy	2,303	2,303	2,303	0
ICE Programme	536	536	536	0
<b>SUBTOTAL</b>	<b>12,513</b>	<b>13,118</b>	<b>13,654</b>	<b>536</b>
Less: Reversal of Accounting entries	(2,901)	(2,901)	(2,901)	0
<b>Net Service Revenue Expenditure</b>	<b>9,612</b>	<b>10,217</b>	<b>10,752</b>	<b>536</b>
Corporate Income & Expenditure	3,616	3,247	3,247	0
C19 Expenditure Pressures	0	0	0	0
C19 Risk	0	0	0	0
Movement in Reserves	(103)	(103)	(225)	(123)
Savings Plan	(256)	(256)	(256)	0
<b>Net General Fund Revenue Budget</b>	<b>12,869</b>	<b>13,105</b>	<b>13,518</b>	<b>413</b>
Funded by:				
Council Tax	6,928	6,928	6,928	0
Business Rates	3,574	3,574	3,574	0
New Homes Bonus	863	863	863	0
Covid-19 Emergency Funding	589	589	589	0
Covid-19 Income Loss	101	101	200	99
Other Funding	(200)	(200)	(200)	0
<b>TOTAL Funding</b>	<b>11,855</b>	<b>11,855</b>	<b>11,954</b>	<b>99</b>
<b>Core (Surplus) or Deficit</b>	<b>1,014</b>	<b>1,250</b>	<b>1,564</b>	<b>314</b>
Balanced by:				
General Fund Balance				0
Service Improvement Fund				0
Workforce Reserve				0
Stability & Resilience Reserve	(1,014)	(1,250)	(1,564)	(314)
<b>Core Surplus or Deficit after Transfers</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

### Economic Outlook commentary

- 1.8. At its meeting ending on 22 September 2021, the Monetary Policy Committee (MPC) voted unanimously to maintain Bank Rate at 0.10%. The Committee voted 7-2 to maintain the current level of UK Government Bond purchases at £875bn.
- 1.9. Since the August MPC meeting, the pace of recovery of global activity has slowed. With robust goods demand and continuing supply constraints, global inflationary pressures have remained strong and there are some signs that cost pressures may prove more persistent. Some financial market indicators of inflation expectations have risen, including in the United Kingdom
- 1.10. The Bank of England has revised down their expectations for the level of UK GDP in 2021 Q3 by around 1% since the August Report, leaving the expected level of Q3 GDP around 2.5% below its pre-Covid level. This



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downward revision in part reflects the emergence of some supply constraints on output. These have been evident in supplier delivery times and backlogs of work, significant material, and labour shortages in several sectors, and lower than normal levels of inventories. Momentum in services has picked up and spending and consumer confidence has remained steady.

- 1.11. The unemployment rate fell to 4.6% in the three months to July, slightly below the August Report forecast, while HMRC payroll data suggest that employee numbers (which include furloughed jobs) surpassed their 2019 Q4 level in August. The number of full and part-time furloughed jobs has continued to decline but based on the most recent reported number of 1.7 million in July, to a materially lesser degree than estimated in the August Report. There have been few signs of any increase in redundancies, and the stock of vacancies has increased further, as have indicators of recruitment difficulties. Estimates of underlying pay growth has picked up, to above its pre-pandemic rate. Uncertainty around the outlook for the labour market has increased, including how the economy will react to the end of the furlough scheme.
- 1.12. Twelve-month CPI inflation rose from 2.0% in July to 3.2% in August, compared with the 3.0% figure expected in the August Report. Core inflation also rose to 3.1% in August, its highest rate since November 2011. While base effects accounted for the majority of the increase in CPI inflation between July and August, global cost pressures have continued to affect UK consumer goods prices. To a lesser degree, the reopening of the economy has led to a further increase in some consumer services prices.
- 1.13. CPI inflation is expected to rise further in the near term, to slightly above 4% in 2021 Q4, owing largely to developments in energy and goods prices. The material rise in wholesale gas prices since the August Report represents an upside risk to the MPC's inflation projection from April 2022. Most other indicators of cost pressures have remained elevated. The Committee's central expectation continues to be that current elevated global cost pressures will prove transitory.
- 1.14. The impact on the Council is likely to be through the level of Inflation and Interest Rates. This will affect the cost of service delivery and decisions around treasury management and the affordability of the Capital Programme supported by debt financing. In addition, weaker global economic growth may have a direct impact on the local economy.
- 1.15. The Council will also need to consider the impact of changes in the housing market. The Council's regeneration programme and other significant housing schemes may be at risk if there is a downturn in the housing market. House prices have remained buoyant over the last 12 months but may react to cost pressures within the economy.

### 2. LOCAL GOVERNMENT FUNDING

- 2.1. There has been little additional work on other local government finance issues such as New Homes Bonus and Council Tax referendum limits.
- 2.2. The Government have announced a multi-year Spending Review which will set resource and capital budgets for 2022-23 to 2024-25 and conclude on 27 October 2021, alongside Autumn Budget 2021. In a letter from the Prime Minister and the Chancellor to all Government departments, the SR21 will focus on the Government's priorities and support the economic recovery.
- 2.3. There are some fiscal constraints that SR21 will need to operate within which were set out in the letter:
  - The fiscal envelope for Spending Review 2021 will follow the path of resource and capital spending that was set out at Budget 2021, with the addition of the net revenue raised by the new Health and Social Care Levy and increase to dividends tax rates
  - a need to put the public finances on a sustainable path in the medium term
  - Departments have been asked to identify at least 5% savings and efficiencies from their day-to-day budgets as part of SR21, which will be reinvested in the Government's priorities.
- 2.4. Members will be kept informed of any local government funding announcements in the reports to Cabinet over the coming weeks, although it is unlikely there will be any substantial update until late November or early December with the Autumn budget due on 27 October 2021.

### 3. 2022/23 BUDGET STRATEGY - ASSUMPTIONS

- 3.1. The 2022/23 Budget Strategy is informed by the financial impact from Covid-19 in the current year. The strategy below sets out the key assumptions that will be made when reviewing the Council's revenue budgets for 2021/22 and 2022/23.
- 3.2. The level of uncertainty around the Council's financial position is unprecedented and makes the forecasting of income and expenditure budgets for 2022/23 very difficult. As such, a number of broad assumptions are set out below that will allow budgets to be updated.
  - Starting point for reviewing budgets for 2022/23 is the assumption that budgets will remain to near/close to pre-Covid levels.
  - All budgets to be reviewed with a focus on cost reductions and savings. This is a separate review to any opportunities identified through the Cost Reduction and Efficiencies Programme (CREP).
  - High risk income and expenditure areas that have been identified through budget monitoring as a risk will be reviewed in detail with options identified to mitigate any income shortfall or budget pressure
  - Review of salary budgets to ensure only posts from the agreed structures are included within the revenue budget.

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- Savings Plan will be reviewed in detail to ensure the Council can set a balanced budget for 2021/22 and address and deficit over the medium-term
- Council Tax/Business Rates income assumptions will be reviewed
- Capital Programme will be reviewed with evaluation of any new or revised schemes with particular reference to the Union Yard Scheme approved by Council in July 2021.
- Adequacy of reserves will need to be considered

### Government Funding & Council Tax

- 3.3. As discussed earlier in the report, there is very little certainty around the level of Government Funding that the Council will receive in future years.
- 3.4. The position on the introduction of 75% Business Rates Retention and the Review of Relative Needs and Resources is not clear. This was postponed until April 2022 but given the impact from Covid on Local Government finances this may be delayed further.
- 3.5. Further information may come through in the Autumn Budget, but it is likely that the detailed position for the Council will not be known until December 2021 when the Local Government Finance Settlement is announced.
- 3.6. The table below sets out the assumptions made on Government funding for 2022/23 that were included in the February 2021 MTFS ([FIN2106](#)). These assumptions will be updated in subsequent reports to members.

**Table 2: Government Funding assumptions (Council, Feb 2021)**

Item	Original 2020/21 (£'000)	Revised 2020/21 (£'000)	2021/22 (£'000)	2022/23 (£'000)	2023/24 (£'000)	2024/25 (£'000)
Business Rates	3,767	3,767	3,574	2,500	2,550	2,601
New Homes Bonus	1,169	1,169	863	211	0	0
Lower Tier Services Grant	0	0	101	0	0	0
<b>Subtotal Government Funding</b>	<b>4,935</b>	<b>4,935</b>	<b>4,539</b>	<b>2,711</b>	<b>2,550</b>	<b>2,601</b>
Covid-19 Expenditure Pressures	0	1,478	489	0	0	0
Sales, Fees & Charges Scheme (Est.)	0	684	100	0	0	0
<b>Subtotal Covid Funding</b>	<b>0</b>	<b>2,162</b>	<b>589</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>TOTAL Government Funding</b>	<b>4,935</b>	<b>7,098</b>	<b>5,128</b>	<b>2,711</b>	<b>2,550</b>	<b>2,601</b>

- 3.7. The MTFS assumed a reduction of £1.2m in Business Rates income and a reduction of £0.6m in New Homes Bonus. As outlined in paragraph 4.4 there may be a further delay changes to the way Local Government is financed. In the event of a further delay, it is likely that business rates income for 2022/23 will revert towards the level forecast for the current financial year. However, the impact from Covid-19 on the business rates base will need to be considered and this may have a material impact on the forecast.

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- 3.8. The MTFS also assumed a phasing-out of New Homes Bonus income. At the time of writing there is no indication of what scheme will be in place for 2022/23.
- 3.9. In terms of Council Tax assumptions, these will be reviewed given the impact from Covid-19 on collection rates in the current year. The MTFS assumed that there would be growth in the Council Taxbase of around 1% per annum, and that Council Tax would be increased (subject to Government guidance around referendum limits). The CTB1 return (due mid-October) will give an early view on the Taxbase with more detailed work being undertaken in November and December on the Taxbase and Collection Fund position.
- 3.10. It should also be noted that the 2020/21 Outturn position on the General Fund Revenue budget highlighted a significant issue around business rates income and the deficit on the Collection Fund. The report to Cabinet highlighted further analysis was needed of the Collection Fund deficit position to understand the timing and financial impact of financing the deficit over the MTFS period. The following paragraphs were included in the 2020/21 Revenue Budget Outturn report ([FIN2113](#)) and outlines the complexity of the business rates position:

*The end of year position on business rates clearly illustrates the complexity and scale of the impact from Covid. When the level of business rates income was estimated in January 2020 (in the NNDR1 Return) it was assumed that around £49.985m of business rates income would be collected, with around £3.767m of this retained locally under the Business Rates Retention Scheme.*

*The outturn position on business rates (in the NNDR3 return) showed that £25.824m of business rates income had been collected. Whilst the Council received Section 31 Grant to compensate for the reduced level of income (£11.3m), the accounting treatment for the different elements of business rates income means that the Council must account for a significant deficit on the business rates collection fund of £26.027m. Whilst 50% of this deficit is shared with Central Government, Rushmoor's share is in excess of £10m. This deficit is transferred to an earmarked reserve in accordance with proper accounting practice and guidance from CIPFA to fund Rushmoor's share of the deficit which will need to be budgeted for over the next 3 years.*

*It is likely that it will take some time for the impact from Covid on business rates income to unwind. At the time of writing this report, the relevant accounting treatment has been applied to ensure the General Fund revenue budget is protected in the current year. Further work will be undertaken over the coming weeks to work through the implications on the Council's MTFS*

- 3.11. Therefore, whilst there is scope for some improvement in the funding position when compared to the February 2021 forecast, there are a number of other factors that will have an adverse impact on these funding streams, with particular concern around the Business Rates position.

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### Pay and Price Inflation

- 3.12. The budget will be prepared on a 'standstill' basis in that no price inflation will be added other than to contractual commitments to pay an annual inflationary increase such as contracts and software licence agreements.
- 3.13. Salary budgets for 2022/23 will be increased by 2.00% in line with assumptions made in previous years. The Government's position on public sector pay is set out in the Spending Review launch letter.

*To help protect jobs at a time of crisis and ensure fairness between the private and public sectors, SR20 temporarily paused pay rises for public sector workers earning £24,000 or more. NHS workers were exempted from this pause. Those working in the public sector have, on average, better remuneration packages than those in the private sector, with Covid also demonstrating the significant value of job security. For reasons of fairness and sustainability of the public finances, we must continue to ensure that public sector pay growth at SR21 (including all elements of earnings growth and pay drift) retains broad parity with the private sector and is affordable*

- 3.14. Members will be aware that the 2020/21 pay award was settled at 2.75% with negotiations yet to conclude on the 2021/22 pay award. Inflationary provision for the pay award is included in the MTFS.
- 3.15. The increase in Employers National Insurance contributions to fund the Government's Social Care proposals (an additional 1.25%) will be included in the revised salary estimates. At a broad level it is estimated that the increased NI contribution would be £120k per annum although a more detailed calculation is required at post level. Although the Government have indicated that the public sector will receive funding to cover the increased costs it is unclear as to the extent of any funding commitment.
- 3.16. The ONS published the August CPI and RPI figures on 15 September 2021 with CPI rising to 3.2% and RPI at 5.0%. The September inflation figures due to be available on 20 October 2021. These figures are generally used as the basis for uprating of some welfare benefits. An allowance is made in the MTFS each year for the impact of inflation pressure within the General Fund and this will be reviewed over the Autumn.
- 3.17. The forecast for inflation was set out in paragraph 2.13 with inflation expected to remain above the Government's target in the near term.

### Fees & Charges

- 3.18. Cabinet approved the methodology for the annual review of fees and charges made for Council services ([Report No. FIN1624](#)). Budget holders are required to review the fees and charges as part of the budget setting process to ensure they are set at an appropriate level and that charges are transparent and show a clear methodology for their increase.
- 3.19. Whilst the focus is on the level of charge made for services, budget holders must review and understand the cost drivers within their service as cost control is an integral part of the annual review of fees and charges process.

### Commercial Property

- 3.20. The Council is increasingly reliant on income from Commercial Property to provide funding for other Council services. Given the risk in holding commercial property (e.g. occupancy rates and fluctuations in the property market), income and expenditure budgets associated with the portfolio will be reviewed in light of Covid-19. This will help ensure the Council is budgeting at the appropriate level and that risks to income and expenditure changes across the medium term can be incorporate into the MTFs and Capital Programme.
- 3.21. Performance of the portfolio will continue to be monitored closely to ensure risks are mitigated through active asset management and early engagement with tenants. It should be noted that the change to PWLB Lending Terms from November 2020 mean that the Council is not able to actively manage and balance the commercial property portfolio through a disposal and acquisition model. The Council will need to understand the revenue and capital budget implications of any financial performance issues given the financing restrictions in place.
- 3.22. The budget setting process is likely to maintain the recommendation that a proportion of commercial income is set aside in the Commercial Reserve each year to provide and ongoing funding stream to manage the portfolio. The Commercial Property Reserve was established to provide funding to mitigate some of the financial risk associated with the portfolio.

### Local Government Pension Scheme (LGPS)

- 3.23. An actuarial review of the Local Government Pension Scheme was undertaken in 2019 with a revised funding schedule included in the current MTFs. The assumptions around employer contributions will not be updated until the conclusion of the next actuarial review which will commence in March 2022.

### Interest Rates

- 3.24. The Bank of England base rate was decreased from 0.75% to 0.10% in March 2020 and was held at this level at the Monetary Policy Committee meeting in September 2021.
- 3.25. Given the wider global economic position and uncertainties around Covid-19 and Brexit, it is difficult to predict what impact there will be on interest rates in the near future. The latest forecasts from our Treasury advisors (October 2021) suggest that the bank base rate will remain at 0.10% in the near term but may rise from Q2 2022.

*Arlingclose expects Bank Rate to rise in Q2 2022. We believe this is driven as much by the Bank's desire to move from emergency levels as by fears of inflationary pressure.*

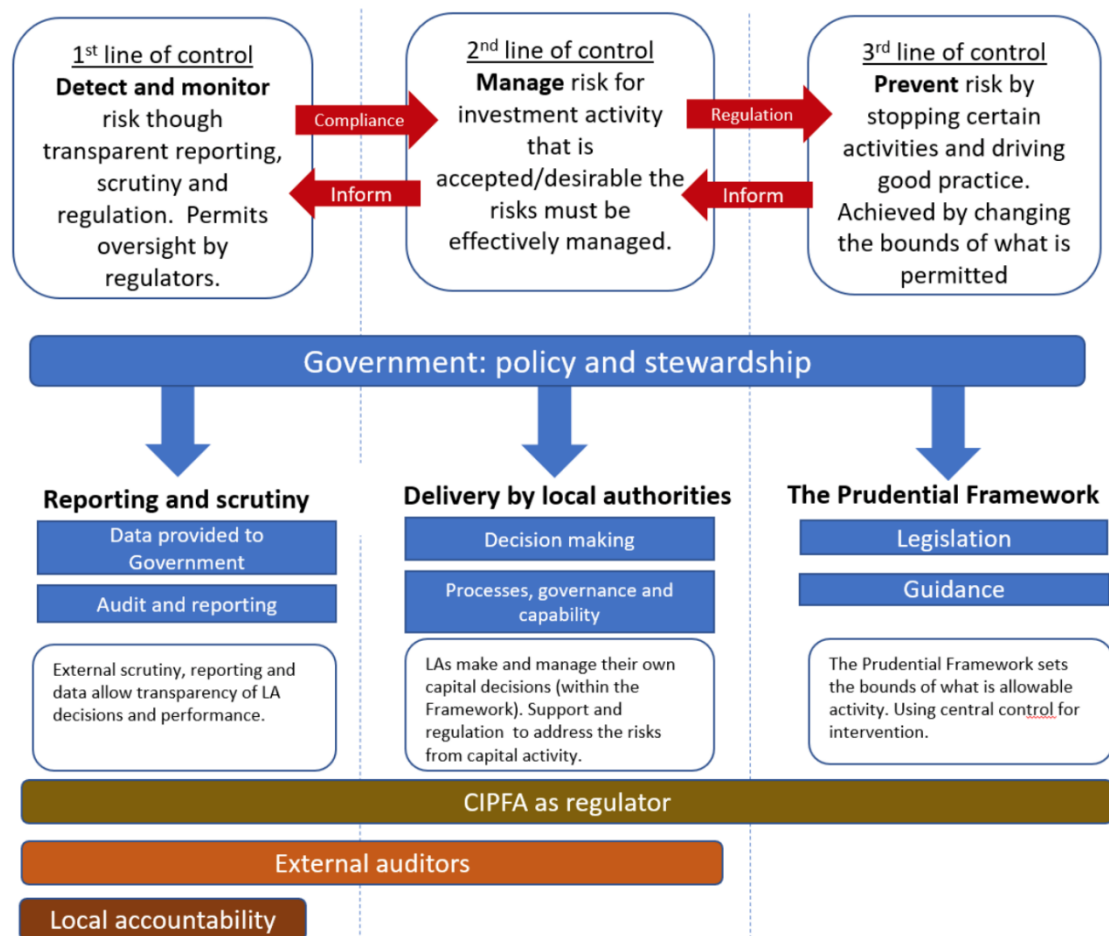
- 3.26. The table below indicates and expectation that the bank base rate will remain unchanged for the foreseeable future, with PWLB rates increasing

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slightly over the same period as they mirror projected Gilt rates with a margin on PWLB lending of 0.80%

- 3.27. The Government provided further guidance and clarification on the revised PWLB Lending Terms in August 2021. The key points are set out below.
- Any investment asset acquired after 26th November 2020 would result in the authority not being able to access PWLB in that financial year or being able to use the PWLB to refinance the transaction at any point in the future
  - authorities should provide details of capital plans, regardless of funding source, covering the whole current financial year and subsequent two financial years
  - Individual projects and schemes may have characteristics of several different categories. In these cases, the section 151 officer or equivalent of the authority should use their professional judgment to assess the main objective of the investment and consider which category is the best fit.
  - an asset that is held primarily to generate income which is used to support wider service spending, but serves no direct policy purpose, should not be categorised as service delivery
  - authorities cannot use receipts from primarily for yield assets to buy further primarily for yield assets
  - Capital expenditure to maintain existing properties or in order to increase their value where the local authority is planning to sell the property is permitted
- 3.28. An extract from the revised guidance which sets out the criteria for defining activity that is eligible under the revised PWLB lending terms is set out in Appendix B. The full guidance is available here:  
<https://www.dmo.gov.uk/media/17634/pwlb-guidance-for-applicants-august-2021-a.pdf>
- 3.29. The Government have also set out their views on the local authority capital finance framework. Whilst the Government have recognised the importance of local government capital investment, they are concerned at the risks some local authorities have taken around investment in commercial property.
- 3.30. A three-line model was outlined in proposals outlined in July 2021. This is illustrated in the diagram below.

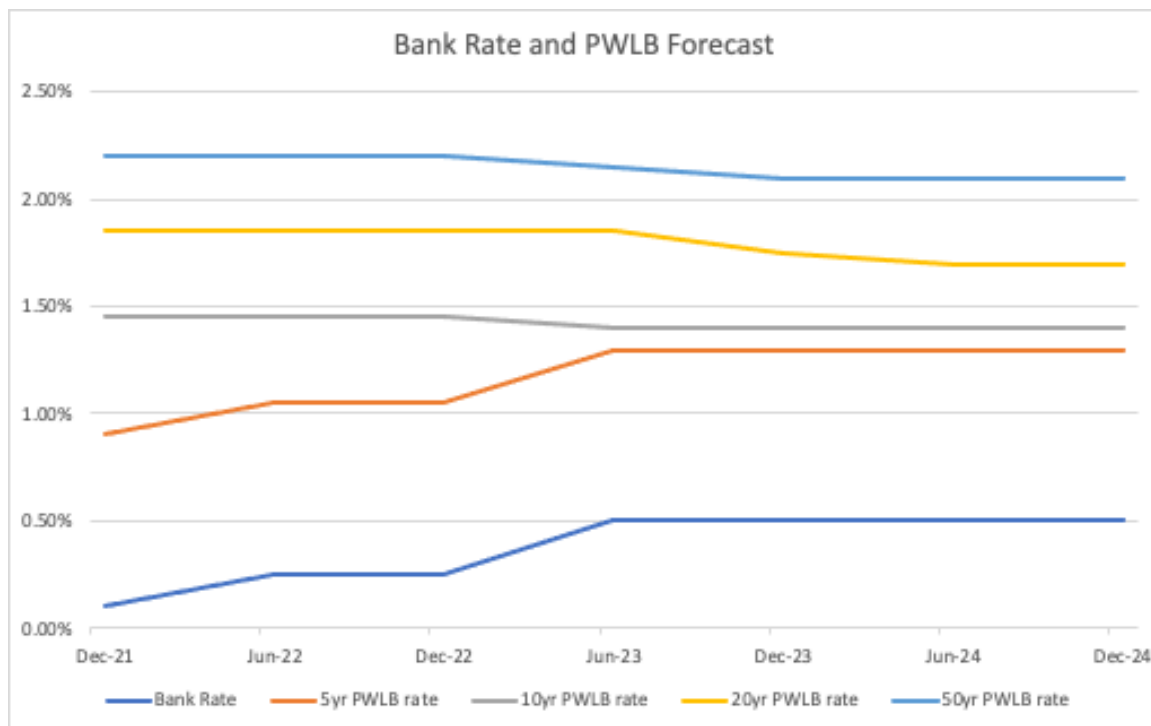
**Figure 1: Three-lines of control model for strengthening the capital system**



- 3.31. Alongside the Government’s improvement proposals, CIPFA are currently undertaking a consultation on the Draft Code for Capital Finance in Local Authorities. This is due to close on 16 November 2021.
- 3.32. The Government’s improvement proposals and the CIPFA Code consultation can be viewed as setting the parameters that local authority capital investment (and borrowing) will need to operate within from 2022/33.
- 3.33. Bank base rate and PWLB forecasts are due to be updated in November 2021 following the Bank of England’s monetary policy committee meeting in November. This will inform the Capital Strategy and Treasury Management Strategy for 2022/23 which will be considered by members in early 2022.



**Table 3: Bank Base rate and PWLB Rates**



	Dec-21	Jun-22	Dec-22	Jun-23	Dec-23	Jun-24	Dec-24
Bank Rate	0.10%	0.25%	0.25%	0.50%	0.50%	0.50%	0.50%
5yr Gilt	0.65%	0.65%	0.65%	0.60%	0.60%	0.60%	0.60%
10yr Gilt	1.05%	1.05%	1.05%	1.05%	0.95%	0.90%	0.90%
20yr Gilt	1.40%	1.40%	1.40%	1.35%	1.30%	1.30%	1.30%
50yr Gilt	1.30%	1.30%	1.25%	1.20%	1.20%	1.20%	1.20%
<b>Note: PWLB rates mirror Gilt rates +0.80% Margin</b>							
5yr PWLB rate	0.90%	1.05%	1.05%	1.30%	1.30%	1.30%	1.30%
10yr PWLB rate	1.45%	1.45%	1.45%	1.40%	1.40%	1.40%	1.40%
20yr PWLB rate	1.85%	1.85%	1.85%	1.85%	1.75%	1.70%	1.70%
50yr PWLB rate	2.20%	2.20%	2.20%	2.15%	2.10%	2.10%	2.10%

Treasury Management - Investment Returns

- 3.34. Treasury management income recovered during 2020/21 following an initial forecast of a significant reduction due to market volatility. Although treasury management performance in 2021/22 remains on target, there remains significant uncertainty around the global economic recovery which may impact future investment performance.
- 3.35. As outlined in the Treasury Management Strategy, the Council invests its surplus balances generating an income return of over £1m per annum. The Strategy sets out that the Council aims to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.
- 3.36. The Council has two broad classes of investments – Money Markey Funds (where balances are held for short periods until required) and Pooled Funds.

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- 3.37. The Bank of England cut the base rate in March 2020 from 0.75% to 0.10%. Whilst the base rate cut will reduce investment income from Money Market Funds, it has not had a material impact on the Council's investment income.
- 3.38. The Council holds a more significant element of its surplus balances in Pooled Funds and has a diversified portfolio to mitigate risk with investments in Property funds, Multi-assets funds, Bonds and Equities.
- 3.39. The Council also receives interest income on service loans provided to third parties. The Council has two significant service loan commitments – Farnborough International Limited (FIL) and Rushmoor Homes (the Council's wholly-owned housing company). As set out in the Revenue Budget Monitoring Report P1 2021/22 to Cabinet in September ([FIN2115](#)), the Council has agreed with the other members of the funding consortium to defer interest on the FIL lending.
- 3.40. The Council, along with the other funding consortium partners (Barclays, Hampshire County Council, Enterprise M3 LEP) agreed to defer interest payments on loans to provide cashflow support to by Farnborough International Limited (FIL) following the cancellation of the 2020 Air show.
- 3.41. Legal documents have been drafted and reviewed that formalise the changes following a renegotiation of inter-creditor agreement between Barclays, FIL, and the public sector partners.
- 3.42. As reported to members in April 2021, the revised terms of the inter-creditor delays the repayment dates of the capital sums to 2026 and 2028 (subject to covenant tests).

Capital repayment	Repayment Date	Revised Repayment Date
£2,105,000	30 June 2024	30 June 2026
£2,500,000	30 June 2026	30 June 2028

- 3.43. Interest that was due in the current financial year on the FIL loans has been rolled-up and will be repaid in line with the revised agreement. The Treasury reserve was established last year to offset the impact on the Council's revenue budget in 2020/21 and 2021/22 in this interest being delayed. The reserve will allocate an equivalent amount in year to offset for the delayed investment income. At the point the rolled-up interest is received this will be allocated to the Stability and Resilience reserve.
- 3.44. The MTFS assumes Treasury Management income of £1.1m per annum in the current year increasing to £1.35m in 2022/23 and £1.6m in 2023/24. Projections on investment income will need to be considered carefully when preparing the 2022/23 budget and MTFS.
- Treasury Management - Borrowing costs and MRP
- 3.45. The Council has undertaken significant external borrowing to finance its capital programme and currently has external debt of £102m. The Council's Treasury Management Strategy, as approved by Council in February 2021, sets out the approach taken to borrowing.

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- 3.46. The Council's main objective when borrowing money is to maintain an appropriate low-risk balance between securing low interest rate costs and achieving cost certainty over the period for which funding is required. Given the low interest rate environment, there is a financial benefit to the Council of taking advantage of short-term borrowing (typically 3-6 month duration), but at the same time there is a risk around refinancing those short-term loans.
- 3.47. The Council has sought to mitigate the refinancing risk by borrowing over longer period (between 1 and 2 years). As the Council works through its asset management plans and revises the Capital Programme, there may be opportunities to refinance its borrowing over a longer period without incurring significant additional cost due to the current position on long-term PWLB borrowing.
- 3.48. The impact on interest rates outlined earlier in the report has allowed the Council to refinance a proportion of the debt portfolio over the short-term at very low interest rates, based on the advice from the Council's Treasury Management advisors concerning PWLB lending. However, there is an ongoing risk around ensuring the Council's external debt is managed in a balanced and sustainable manner over the longer-term.
- 3.49. Estimates for 2022/23 and medium-term will be undertaken once the Capital Programme has been reviewed and will be included in the budget papers for Cabinet and Council in February 2022.
- 3.50. The Council will consider the capital financing implications of the Regeneration Programme over the coming weeks and months. Whilst the Capital Programme and MTFs does take into account elements of the programme, these will need to be updated to ensure they reflect the nature and scale of each scheme.

### Balances & Reserves

- 3.51. The Council holds balances and reserves to provide financing for future expenditure plans. Members will be aware from the 2020/21 Revenue Budget Outturn report that the Council has increased the level of Reserves and Balances it holds, in part to mitigate the financial impact from Covid-19. The Council held £27.156m of earmarked reserves and £2m in balances at the end of the last financial year, as set out in Table 4.
- 3.52. The Council holds these sums for three main purposes:
- a working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing [Stability and Resilience Reserve, Commercial Reserve].
  - a risk-assessed contingency to cushion the impact of unexpected events or emergencies [General Fund Balance].
  - a means of building up funds to meet known or predicted requirements

Table 4: Balances and Reserves as at 31 March 2021

	Balance as at 31/03/2020 (£'000)	Transfers Out 2020/21 (£'000)	Transfers In 2020/21 (£'000)	Balance as at 31/03/2021 (£'000)
<b>Earmarked Reserve</b>				
COVID BRR Earmarked Reserve	-	-	10,812	10,812
Stability and Resilience Reserve	5,870	(1,293)	-	4,577
Commercial Reserve	2,000	(250)	-	1,750
Treasury Earmarked Reserve	-	(180)	580	400
Pension Reserve	-	-	669	669
Covid-19/Recovery Grant reserve	-	-	393	393
All Other Earmarked Reserves (excluding SANG/s106)	4,536	(1,597)	1,547	4,486
Commuted Sums/Amenity Areas	4,443	(480)	10	3,973
TAG Environmental Fund	110	(14)	-	96
<b>Total of all Earmarked General Fund Reserves</b>	<b>16,959</b>	<b>(3,814)</b>	<b>14,011</b>	<b>27,156</b>

- 3.53. Included with the Earmarked Reserves is £10.8m held in the Covid BRR Earmarked Reserve in recognition of the deficit on the Business Rates collection fund. This funding will be used to mitigate the impact of the timing difference between the business rates income streams over the MTFS period.
- 3.54. A review of the balances and reserves will be completed and presented to Cabinet and Council in February alongside the revenue and capital budgets for 2021/22. This will need to assess the adequacy of the reserves in ensuring the Council remains financially sustainable over the short to medium-term.

#### 4. MEDIUM TERM FINANCIAL STRATEGY 2022/23 TO 2025/26

- 4.1. This report will not update the MTFS or the strategy for addressing the Funding gap identified in February 2021. These will be considered in reports to Cabinet in November/December depending on the outcome from the Autumn Budget. The table below is an extract from the MTFS as approved by Council in February 2021 ([FIN2106](#)).

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**Table 5: Summary MTFS (Council, Feb 2021)**

Item	Original 2020/21 (£'000)	Revised 2020/21 (£'000)	2021/22 (£'000)	2022/23 (£'000)	2023/24 (£'000)	2024/25 (£'000)
Portfolio Net Expenditure	8,753	11,926	9,612	8,275	8,311	8,311
Corporate Items	3,038	1,754	2,409	3,528	4,110	4,529
Inflation	0	0	0	561	1,121	1,682
<b>Portfolio + Corporate Items</b>	<b>11,791</b>	<b>13,680</b>	<b>12,020</b>	<b>12,364</b>	<b>13,542</b>	<b>14,522</b>
Additional Items & Budget Pressures	909	0	1,005	587	532	232
Budget Proposals	26	26	100	0	0	0
Risk items (Waste)	0	0	0	350	350	350
Savings Plan	(1,436)	(446)	(256)	(605)	(751)	(751)
<b>Draft Net Revenue Budget</b>	<b>11,290</b>	<b>13,260</b>	<b>12,869</b>	<b>12,696</b>	<b>13,672</b>	<b>14,352</b>
<b>Funded by:</b>						
Council Tax	6,705	6,705	6,928	7,137	7,352	7,574
Business Rates	3,767	3,767	3,574	2,500	2,550	2,601
New Homes Bonus	1,169	1,169	863	211	0	0
Covid Funding	0	2,162	589	0	0	0
Other Funding	267	0	101	0	0	0
Council Tax/NNDR Surplus or (Deficit)	(270)	(270)	(200)	(286)	(286)	0
<b>TOTAL Funding</b>	<b>11,637</b>	<b>13,533</b>	<b>11,855</b>	<b>9,561</b>	<b>9,616</b>	<b>10,175</b>
<b>Core (Surplus) / Deficit</b>	<b>(347)</b>	<b>(273)</b>	<b>1,014</b>	<b>3,134</b>	<b>4,056</b>	<b>4,177</b>
<b>Deficit Funding</b>						
<b>Stability &amp; Resilience Reserve</b>						
Balance b/f	5,871	5,871	5,563	4,550	1,416	(2,641)
Planned use		(307)	(1,014)	(3,134)	(4,056)	(4,177)
<b>Balance c/f</b>		<b>5,563</b>	<b>4,550</b>	<b>1,416</b>	<b>(2,641)</b>	<b>(6,818)</b>

- 4.2. As the table shows, the indicative position outlined for 2022/23 is a deficit of £3.1m, as reported to Council in February 2021. It was noted at the time that a revised approach to Savings Plan was required given the deficit position forecast over the MTFS period.

Funding Gap forecast in MTFS	2021/22 (£'000)	2022/23 (£'000)	2023/24 (£'000)	2024/25 (£'000)
Draft Revenue Budget (before Savings)	13,125	13,301	14,423	15,103
TOTAL Funding	11,855	9,561	9,616	10,175
<b>Funding Gap</b>	<b>1,270</b>	<b>3,739</b>	<b>4,807</b>	<b>4,928</b>
Savings identified	(256)	(605)	(751)	(751)
<b>Residual Funding Gap After Savings</b>	<b>1,014</b>	<b>3,134</b>	<b>4,056</b>	<b>4,177</b>
Use of Stability & Resilience Reserve	(1,014)	(3,134)	(4,056)	(4,177)
<b>Stability &amp; Resilience Reserve Y/E Balance</b>	<b>4,550</b>	<b>1,416</b>	<b>(2,641)</b>	<b>(6,818)</b>

- 4.3. Whilst the Council may benefit from further Government Funding (e.g., one-off grant funding, additional NHB), the downward trend in Government funding will frame the Council's revenue budget in future years.
- 4.4. It was recommended that the Council continued to review not only the costs of services but considered the nature and scope of services being delivered.

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- 4.5. The Council will need to identify additional savings to mitigate the impact of any savings that cannot be achieved in full or in the timeframe required, as this would put additional financial pressure on the Council.
- 4.6. Therefore, at this stage of the budget setting process, the expectation is that the level of the core deficit will reduce as detailed revenue budgets are prepared, the savings plan is updated, and the revenue impact of the capital programme is updated.

### 5. CAPITAL PROGRAMME AND FINANCING

#### Union Yard

- 5.1. At their meeting on 29 July 2021 the Council approved the Union Yard Regeneration Scheme. This is a significant undertaking for the Council and will increase the amount of external debt the Council will need to manage above the current level of £102m.
- 5.2. Negotiations are yet to conclude with the Hills Partnerships Limited in respect of the fixed price JCT Design and Build Contract. Therefore, the capital programme and capital financing position will not be updated until the final contract sum is agreed and the profile of expenditure over the duration of the project is available.

#### Capital Financing – Anticipated Capital Receipts

- 5.3. The Council is expected to receive capital receipts from the Parsons Barracks scheme and asset sales in the latter half of the financial year. The Capital Financing Statement included in the Revenue Budget, Capital Programme and Council Tax Level report to Cabinet in February 2021 ([FIN2106](#)) did not forecast any capital receipts due to the uncertainty around timing and value.
- 5.4. The level of anticipated capital receipts for the year is likely to be £1.25m at the lower end of expectations and £2.25m at the higher end depending on the timing of receipts.
- 5.5. The Council's Capital Programme is predominantly financed from Prudential Borrowing, with a Table 8 in the February budget report forecast highlighting £34.4m additional borrowing over the medium-term plan period. The Council decision to approve the Union Yard scheme in July 2021 will increase the level of borrowing over Capital Programme period. A detailed profile of expenditure will be required upon agreement to the contract sum which will inform the borrowing requirements.
- 5.6. The Council's Borrowing Strategy is set out in the Annual Treasury Management Strategy and Annual Non- Treasury Investment Strategy 2021/22 ([FIN2104](#)) with an alternative strategy outlined based on redeeming long-term investments. Given the reliance on prudential borrowing and the revenue impact of the strategy, it is considered prudent to utilise capital

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receipts against the approved capital programme or to use flexibly in-line with approved Strategy for the Flexible Use of Capital Receipts.

- 5.7. The emerging policy position is to pool all receipts from the sale of all assets sold to support the Capital Programme in line with funding the Council's priorities (as published in the Council Business Plan) which will include the potential sale of any investment properties or other property assets.
- 5.8. The Capital Programme for 2021/22 to 2025/26 will include a capital receipts target. All capital receipts received should be allocated to support this target and not allocated to new schemes, subject to any potential use of capital receipts under the Flexible Use of Capital Receipts Strategy and any loan repayment.
- 5.9. The Council will aim to maximise its capital receipts, where possible, by enhancing the land prior to disposal (e.g., by obtaining planning permission or providing a development plan).

### Tices Meadow

- 5.10. The land known as Tice's Meadow (formerly Farnham Quarry) is a restored sand and gravel site owned and operated by Hanson Aggregates. The site area is approximately 55 hectares and was formally opened in May 2019 and is now subject to a 20-year aftercare and long-term Management Plan, pursuant to the Section 106 Agreement of the extraction permission.
- 5.11. The site has been restored to a nature conservation end use, with permissive public access along the northern boundary. It also afforded the opportunity to incorporate a realignment and enhancement of the River Blackwater by the Environment Agency. The restoration and long-term management is overseen by a Management Group comprising Hanson, Surrey County Council (SCC), Tice's Bird Group, Blackwater Valley Countryside Partnership, and Farnham Residents Association.
- 5.12. Hanson put the site on the market in late 2019 but, despite several bids, the site remains unsold to date. Following a number of meetings with local authority partners it was decided to purchase the site to secure its future as a protected nature reserve for use by the community. The area is heavily used by Rushmoor residents despite the site not being in the Borough.
- 5.13. Longer term there remains the scope to create wider opportunities to link Tice's Meadow with SCC's adjacent lands at Tongham Pools.
- 5.14. Following discussions with Hanson an agreement has been reached allowing SCC to purchase the site for £425,000 including tax and costs with contributions from other local authority partners including the Council. SCC will own the site and will be responsible for its management and liabilities moving forward. The funding package is proposed as follows (note the contributions shown in the table below were based on an assumed purchase value of £475,000):

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Surrey County Council	£250,000
Guildford Borough Council	£50,000
Waverley Borough Council with Farnham Town Council	£75,000
Rushmoor Borough Council	£50,000
Hampshire County Council	£50,000

- 5.15. Cabinet recommends to Council that a contribution of up to £50,000 is made to Surrey County Council for the purchase of Tices Meadow as outlined above; to be funded from anticipated capital receipts. The estimated contribution from Rushmoor based on the lower purchase price of £425,000 is £45,075 (being 10%).

## 6. IMPLICATIONS

### Risks

- 6.1. This report has identified some specific risks around the economic forecast for inflation, the recovery from Covid-19 and the Council's funding from Government. There remains significant uncertainty for 2022/23 and beyond due to the economic outlook, limited information around likely levels of Government funding and support, and the longer-term changes from the review of Relative Needs and Resources and Business Rates Retention.
- 6.2. Covid-19 risks
- Any further restrictions should new variants take hold or infection rates increase.
  - Council Tax & Business Rates collection shortfalls contained within the collection fund but will need to be incorporated into the 2022/23 budget
  - Cost of additional council tax support cases in 2021/22 and impact of scheme going forward, particularly considering the ending of the additional £20 per week Universal Credit payment.
  - Fees and Charges income in 2021/22 and forecasts for 2022/23 with the Government's Sales, Fees and Charges support scheme ending in June 2021.
- 6.3. There are a number of other risks to the Council that have been highlighted within the report including inflationary pressures, interest rates, commercial property performance, and closing the funding gap identified in the February 2021 MTFS ([FIN2106](#)).

### Legal Implications

- 6.4. The Council through its Members has a legal obligation to set a balanced budget and the MTFS provides the information that will inform the approach to be taken in the budget setting process for early 2022 when reports will be taken to Cabinet and Council for approval.



### Financial and Resource Implications

- 6.5. There are not considered to be any financial implications arising directly from this report. However, it is worth noting the indicative MTFS position shows a widening funding gap based on the assumptions made within this report. It is anticipated that significant work on the expenditure and savings plans will enable the funding gap to be reduced. An updated position will be included in the reports to Cabinet and Council in February 2022.

### Equalities Impact Implications

- 6.6. None

## 7. CONCLUSIONS

- 7.1. The Medium-Term Financial Strategy will be updated over the coming weeks and months to ensure it provides the framework for managing the Council's financial position and helps to ensure that resources are available to deliver against the Council Plan.
- 7.2. Whilst the Council has delivered a number of budget and efficiency savings in previous years, the Council will need to review adequacy and composition of the Cost Reduction and Efficiency Programme (CREP) on an on-going basis. It is likely that the Council will need to identify further budget and efficiency savings over and above those already within the MTFS and identified as part of the CREP process.
- 7.3. The Council does face a significant financial challenge over the medium term, particularly given the uncertainty set out in this report regarding Covid-19 and the Government's proposed changes to local government funding from April 2022 (although these reforms may be delayed).
- 7.4. The Council will need to ensure the adequate reserves are maintained over the medium term to mitigate the risks identified in this report. However, the use of reserves to deal with changes in the financial standing of the Council on an ongoing basis is not a long-term or sustainable plan. It does, however, enable the Council to mitigate against short-term changes, whilst allowing the Council to plan and implement effectively over the medium-term.

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### Revised HM Treasury PWLB Guidance – August 2021

#### Defining activity

25. **Service delivery** is expenditure on assets that form part of the authority's public service delivery. This consists of activity that would normally be captured in the following areas in the MHCLG Capital Outturn Return (COR): education, highways & transport, social care, public health, culture & related services, environmental & regulatory services, police, fire & rescue services, and central services.
26. The COR is not an exhaustive list and the section 151 officer can categorise similar items of expenditure as service delivery, even if they are not normally captured in the COR. For example, the climate change costs section of the COR normally only includes capital costs associated with waste reduction schemes, but many local authorities have wider expenditure to meet climate change related policy objectives (such as renewable energy developments) which would also be categorised as service delivery. An asset that is held primarily to generate an income which is used to support wider service spending, but serves no direct policy purpose, **should not** be categorised as service delivery.
27. **Housing** is activity normally captured in the HRA and General Fund housing sections of the COR, or housing delivered through a local authority housing company. This is given separately from 'service delivery' because of the relative concentration of cross-subsidy and other innovative financing arrangements in housing projects.
28. Housing can include all spending on delivering new homes, maintaining or improving existing homes, and purchasing built homes to deliver housing services. This is the case irrespective of the financial arrangements of the housing project or housing delivery. However, the government expects that the location and value of any housing expenditure be appropriate to meet the local authority's housing needs.
29. **Regeneration** involves direct investments in assets to generate additional social or economic benefits. Regeneration projects would usually have one or more of the following characteristics:
  - a. the project is addressing an economic or social market failure by providing services, facilities, or other amenities that are of value to local people and would not otherwise be provided by the private sector
  - b. the local authority is making a significant investment in the asset beyond the purchase price: developing the assets to improve them and/or change their use, or otherwise making a significant financial investment
  - c. the project involves or generates significant additional activity that would not otherwise happen without the local authority's intervention, creating jobs and/or social or economic value

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30. While some parts of a regeneration project may generate rental income, these rents should be **recycled within the project or applied to related regeneration projects**, rather than being applied to wider services.
31. **Preventative action** is a special category which involves direct financial support to local companies or acquiring assets as a way to protect jobs, prevent social or economic decline. This type of activity is distinct from regeneration, as it is only preserving existing activity as opposed to creating additional activity, but is not an 'investment assets bought primarily for yield' as yield is not the primary motive of the activity.
32. This type of action would have all of the following characteristics:
  - a. the intervention **prevents a negative outcome**, such as by buying and conserving assets of community value that would otherwise fall into disrepair, or providing support to maintain economic activity that would otherwise cease
  - b. there is no realistic **prospect of support** from a source other than the local authority
  - c. the local authority has an **exit strategy**, and does not propose to hold the investment for longer than is necessary to achieve the objectives that justified the intervention
  - d. the intervention takes the form of grants, loans, sale and leaseback, equity injections, or other forms of business support that generate a **balance sheet asset**.
33. This category can also be used for taking up rights issuances of new shares, where a local authority jointly owns a company with private investors, as described in paragraph 19, where it does not better fall into one of the alternative categories.
34. This category is distinct from routine repairs, maintenance and preventative activities which would normally be captured in the MHCLG Capital Outturn Return (COR) (such as expenditure on flood defences, repair or maintenance work to existing council-owned assets etc.) which should be included in the service delivery category.
35. The government does not anticipate that local authorities would spend significant sums on preventative action. Local authorities that are considering such action should ensure that they have assessed the compliance of the proposed action with all relevant subsidy control provisions in domestic and international law. The government is not responsible for ensuring that local authorities meet this requirement.
36. **Treasury management**, unlike the other categories listed, is not a type of capital expenditure. However, treasury management includes the refinancing or extending of existing debt from any source, the externalisation of internal borrowing or borrowing to manage cashflow within year, which local authorities often finance through PWLB borrowing or other capital resources.

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37. The government recognises the benefits of having ready access to the PWLB for refinancing. The PWLB will therefore lend for this purpose even if the local authority is planning activity that makes them otherwise ineligible for PWLB support. Authorities which intend to borrow for refinancing or the externalisation of internal borrowing whilst planning activity that makes them otherwise ineligible for PWLB support should make this clear on the electronic template when applying to borrow from the PWLB.
38. Local authorities must not pursue a deliberate strategy of using private borrowing or internal borrowing to support investment in an asset that the PWLB would not support and then refinancing or externalising this with PWLB loans.
39. For the purposes of these lending arrangements, activity that should be included in the treasury management section of the Certainty Rate return are the refinancing or extending of existing debt from any source, and the externalisation of internal borrowing. Other treasury management investments, such as inflation-proofing cash balances, in compliance with CIPFA's Treasury Management in the Public Services code of practice are outside the scope of the PWLB lending terms and should not be included in the Certainty Rate return.
40. Under the Prudential Framework local authorities cannot borrow or invest for speculative purposes. Financial investments should be made for security, liquidity, and yield in that order, meaning local authorities should always pick safe investments over riskier investments with higher returns. Therefore, while it is accepted that authorities might borrow in advance of capital expenditure, this must be for prudent financial management and not for the purpose of securing yield.
41. The government and CIPFA are clear that borrowing to invest for yield is not permitted under the Prudential Framework.
42. Investments in commercial property or speculative financial instruments are not considered treasury management.
43. **Investment assets bought primarily for yield** are assets that serve no direct policy purpose but is held primarily to generate an income. An 'investment asset' could be a capital or property asset, or interest or right that generates a balance sheet asset (such as, but not limited to a loan, sale and leaseback agreement). As it has been 'bought primarily for yield', the investment asset would serve no direct policy purpose linked to the authority's core functions, but has been acquired primarily because it would generate an income stream for the authority, which would most often (but not exclusively) be used to support wider service spending. If a local authority is planning to acquire investment assets bought primarily for yield in any of the following three years, the authority will be unable to borrow from the PWLB to finance any expenditure in its capital plan.

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44. These investment assets bought primarily for yield would usually have one or more of the following characteristics:
- a. buying land or existing buildings to let out at **market rate**
  - b. buying land or buildings which were previously operated on a commercial basis which is then continued by the local authority without any **additional investment or modification**
  - c. buying land or existing buildings other than housing which **generate income and are intended to be held indefinitely**, rather than until the achievement of some meaningful trigger such as the completion of land assembly
  - d. buying a **speculative investment asset** (including both financial and non-financial assets) that generates yield **without a direct policy purpose**
45. If a local authority is planning to acquire investment assets bought primarily for yield in any of the following three years, the authority will be unable to borrow from the PWLB to finance any expenditure in its capital plan. Local authorities cannot use the receipts from selling existing primarily for yield assets to acquire new primarily for yield assets. Local authorities can use the receipts from selling existing primarily for yield assets to finance other capital expenditure in service delivery, regeneration, housing and preventative action.
46. Where an authority has committed to a transaction which would be categorised as investment assets bought primarily for yield but **commenced or was contractually agreed prior to 26 November 2020**, this will not affect access to the PWLB. Where an authority decides to proceed with a new investment asset bought primarily for yield transaction despite these lending terms, they will not be able to access the PWLB in that financial year and the PWLB **cannot** be used to refinance this transaction at any point in the future.
47. This does not prevent capital expenditure to maintain existing commercial properties, or in order to increase their value where the local authority is planning to sell the property.