Finance and Resources Committee

10.00am, Thursday, 5 March 2020

Capital Strategy 2020-30 – Annual Report

Item number	
Executive/routine	
Wards	
Council Commitments	

1. Recommendations

1.1 To note the Capital Strategy, as set out in Appendix 1, and refer to full Council for approval;

1.2 To note the potential implications of International Financial Reporting Standard (IFRS) 16 – Leases on future iterations of the Capital Strategy; and

1.3 To note that the Council has set an ambitious target for Edinburgh to be a Carbon Neutral city by 2030 which will inform all future capital budget considerations.

Stephen S. Moir

Executive Director of Resources

Contact: Liam MacDonald, Senior Accountant,

Finance Division, Resources Directorate

E-mail: Liam.MacDonald@edinburgh.gov.uk | Tel: 0131 469 3174

Report

Capital Strategy 2020-30 – Annual Report

2. Executive Summary

2.1 This report sets out the proposed capital strategy, which provides a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the infrastructure and provision of services for the benefit of Edinburgh communities and citizens.

3. Background

3.1 Local authorities are required by regulation to have regard to the Prudential Code when carrying out their duties under Part 7 of the Local Government in Scotland Act 2003. The Prudential Code was revised by CIPFA in 2017. A key element of the revised code is that local authorities should have a long-term capital strategy in place that sets out the long-term context in which capital and revenue decisions are made.

Capital Budget Strategy 2020-30

3.2 The Capital Budget Strategy 2020-30 is a separate report which was presented to Finance and Resources Committee on 14 February 2020. It details priorities for council capital investment over the medium to long-term and sets out a plan on how they could be funded. Priorities put forward for additional funding included the Wave 4 schools programme, additional infrastructure required due to population growth and demography as well as increased investment in the Council's existing estate.

3.3 At its meeting on 20 February 2020 Council approved the Capital Budget Strategy 2020-30. The approved Capital Budget Strategy 2020-30 will deliver a total programme of capital expenditure of £2,324.786m to 2029/30.

3.4 This report sets out the Council's capital strategy and builds upon the capital strategy annual report approved by Council on 14 March 2019.

4. Main report

4.1 In order to deliver Council priorities and for the city to grow in a sustainable way, the Council needs to invest in its existing assets as well as creating new ones. The capital strategy gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services. It also provides an overview of how associated risk is managed and the implications for future financial sustainability.

4.2 The capital strategy is a high-level document, which brings together a number of other key Council strategies. It should be read in conjunction with the following plans and policies

- Programme for the Capital: Council Business Plan for 2017/22
- 2050 Edinburgh City Vision
- Council Sustainability Programme Short Window Improvement Plan
- Local Development Plan
- Local Development Plan Action Programme
- Capital Budget Strategy 2020-30
- Annual Treasury Management Strategy 2020/21 (on same agenda)
- Housing Revenue Account Budget Strategy 2019-24
- Corporate Asset Strategy
- Property and Asset Management Strategy
- Transport Asset Management Plan

4.3 In addition to the statutory background, Edinburgh and the Council's role and the Council's Vision and Corporate Strategy, the capital strategy covers the following areas;

- Capital Expenditure and Financing (the Council's capital expenditure plans, and the corresponding financing requirement);
- Treasury Management (how the Council keeps sufficient but not excessive cash to meet the Council's spending needs, while managing risks involved);
- Other investments and long-term liabilities (the Council's non-treasury investments and other liabilities); and
- Knowledge and Skills (the professional skills and knowledge contained within the Council's accounting, treasury and property teams, as supplemented by external advisers).

4.4 The Council will need to adhere to International Financial Report Standard (IFRS) 16 - Leases from the start of financial year 2020/21, with information also prepared for a disclosure note in the 2019/20 Annual Accounts.

4.5 The introduction of IFRS 16 within the Accounts will have a significant impact on the balance sheet from its introduction in 2020/21. This will subsequently have an impact on the Capital Financing Requirement (CFR) as from the 2020/21 financial year. Therefore, it should be expected to see an increase in the CFR in future years.

4.6 The full capital strategy is included in Appendix 1.

5. Next Steps

5.1 This report will be referred to full Council for approval of the capital strategy. The strategy will be updated on an annual basis, with this being the second iteration.

6. Financial impact

6.1 There are no direct financial implications arising from this report. The implications of the expenditure and investment plans contained in the strategy were considered at the Council's budget setting meeting on 20 February 2020.

7. Stakeholder/Community Impact

7.1 The capital strategy is a high-level document which brings together a number of other Council strategies, each of which is the result of appropriate community engagement.

7.2 Approval of the capital strategy, ensures the Council continues to have regard to the Prudential Code when carrying out their duties under Part 7 of the Local Government in Scotland Act 2003.

7.3 There are no sustainability impacts directly arising from this report.

8. Background reading/external references

8.1 Capital Investment Programme 2009-2019, Policy and Strategy Committee, 4 November 2008

8.2 Local Development Plan Action Programme, January 2019

8.3 Capital Investment Programme 2019/20 to 2023/24, Finance and Resources Committee, 1 February 2019, as amended by the Council's budget meeting of 21 February 2019

8.4 Corporate Asset Strategy, Corporate Policy and Strategy Committee, 12 May 2015

8.5 Property and Asset Management Strategy, Finance and Resources Committee, September 2015

8.6 Transport Asset Management Plan (TAMP), Transport and Environment Committee, 6 December 2018

8.7 Update on Short Window Improvement Plan, Policy and Sustainability Committee, 25 October 2019

8.8 Capital Budget Strategy 2020 – 2030, Finance and Resources Committee, 14 February 2020

8.9 Council's Change Strategy – Planning for Change and Delivering Services 2020/23, Finance and Resources Committee, 14 February 2020

8.10 Housing Revenue Account Budget Strategy 2019-24, Finance and Resource Committee, 14 February 2020

8.11 Treasury Management Strategy 2020-21, Finance and Resources Committee, 5 March 2020

Appendices

Appendix 1: Detailed Capital Strategy 2020-30

Appendix 1: Capital Strategy 2020-30

1. Introduction

1.1 The Capital Strategy for City of Edinburgh Council provides a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the infrastructure and provision of services for the benefit of Edinburgh communities and citizens.

1.2 The Strategy takes a long-term view and covers the period from 2020 to 2030.

1.3 The Council Change Strategy: Planning for Change and Delivering Services 2019-23 reported to Finance and Resources Committee on 10 October 2019 set out the intention to set a policy-based budget through the lenses of poverty, well-being and sustainability with key messages for this year's budget approach linked to these important issues.

1.4 The climate emergency has led to the Council setting a new and ambitious target to be carbon neutral by 2030 within a legal context for Scotland being carbon neutral by 2045. This has already led to some significant strategic decisions in respect of the City Development Plan Choices document, the City Mobility Plan and specific investment programmes such as the plan to design and build Currie High School to Passivhaus certified standard.

1.5 The Council is being supported by the Edinburgh Centre for Carbon Innovation to develop a carbon scenario tool that will augment current business case analysis of major Council projects and capital investment. This strategy will continue to be review on the basis of this work and wider needs to deliver the 2030 zero carbon target.

1.6 Explicitly adopting these policy priorities as a focus for the development of the Council's capital budget is a helpful development of the Council's wider Change Strategy.

1.7 These policy priorities have also been adopted within the Capital Strategy 2020-30.

2. Statutory Background

2.1 Local authorities are required by regulation to have regard to the Prudential Code when carrying out their duties under Part 7 of the Local Government in Scotland Act 2003. The Prudential Code was revised by CIPFA in 2017. A key element of the revised code is that local authorities should have a long-term capital strategy in place that sets out the long-term context in which capital and revenue decisions are made.

3. Edinburgh and the Council's Role

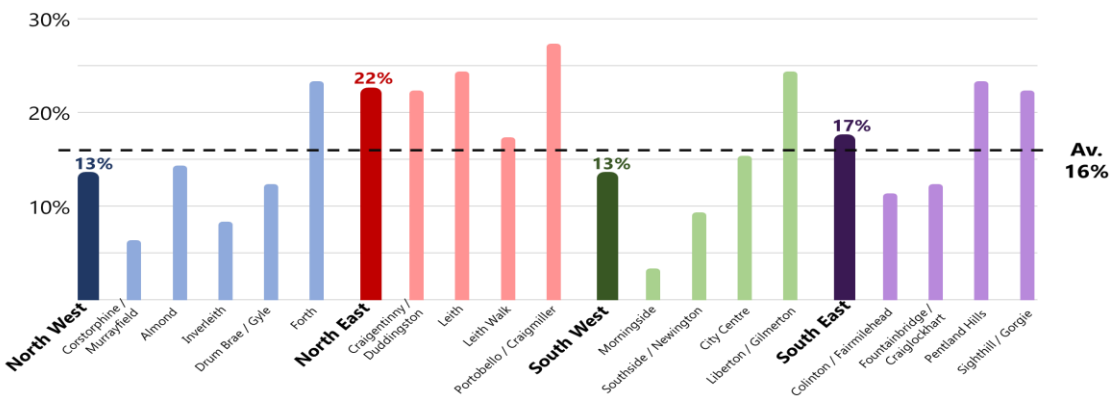
3.1 Edinburgh is one of the best cities in the world in which to live, work and study. We live in a city full of vibrancy and opportunity and, as a council, we are working hard to ensure that all residents can share in our success. We will keep investing in the things that support and sustain growth while confronting the challenges that come with it.

3.2 Edinburgh has seen significant population growth, with a 12.2% increase between 2006 to 2016, compared to a national rise of 5.3%. In 2021 it is forecast that the number of people aged 65 and over will overtake the number of people aged under 18. In comparison to 2018, by 2023 there will be 4,000 more children in our schools and our total population will have increased by 23,000 people.

3.3 This growth will place further demand on a range of frontline services, as such, the Council's budget framework continues to provide additional annual sums in respect of growing numbers of school pupils, at-risk children, older people and those with physical and/or learning disabilities.

3.4 A growing population is one of the most visible signs of the city's economic success. However, not all of our citizens share in that success and alongside our affluent areas, the city contains some of the most deprived communities in Scotland. We know that over 80,000 of our citizens, including almost 1 in 4 of our children, live in poverty and an increasing number of our citizens, even some in work, rely on foodbanks. This cannot be allowed to continue.

3.5 Working together as a city, we have a responsibility to act and a legal duty to end Child Poverty by 2030. More than that we have an opportunity to improve this position. We believe that much lower rates of poverty in Edinburgh can be achieved.



3.6 Narrowing these gaps and allowing all residents to share in the city's success therefore forms a key strand of the City Vision.

3.7 Responding to the global climate crisis is a central part of our plan for the future. We want to be a carbon-neutral city by 2030.

4. City of Edinburgh Council's Vision and Corporate Strategy

Programme for the Capital: Council Business Plan for 2017/22

4.1 The Programme for the Capital: Council Business Plan for 2017/22 describes the Council's commitments to the city, the strategic aims and outcomes, the challenges, how success will be measured and the future of the organisation. The plan sets out overlapping strategic themes common to the work of all service areas. The strategic aims set out below are underpinned by the 52 commitments to the city.

- Deliver an economy for all;
- Build for a future Edinburgh;
- Deliver a sustainable future;
- Deliver for our children and families; and
- Deliver a Council that works for all.

4.2 To deliver the vision and strategic aims, the Administration has set out 20 associated outcomes, these are shown in the diagram below. These outcomes link to the 52 commitments to the city which will be prioritised over the duration of the plan and into the future.

4.3 A new Council Performance Framework 2017-22 has been revised to support the implementation of the Council Business Plan 2017-22.

4.4 The framework will be reviewed annually and will include refreshing the measures, actions and milestones to ensure that the data collected is useful in terms of being able to measure performance and delivery.

2050 Edinburgh City Vision

4.5 In the autumn of 2016 the City of Edinburgh Council launched a major conversation about the future of a city and a society, inviting Edinburgh to talk about its aspirations, plans, and concerns, for the first time in a generation: Edinburgh's City Vision for 2050.

4.6 During the first year of stakeholder and public engagement on the development of a long-term vision for Edinburgh, the Council engaged with thousands of people of all ages and identified four important themes that were obviously relevant to participants. These themes are

- *An Inspired City* - Edinburgh is a city that inspires the world and we will continue to treasure, and grow, our unique culture and heritage. The Edinburgh of 2050 will be a city renowned for its creativity and ingenuity, building on its reputation as a premier destination for culture, education and innovation.
- *A Thriving City* - The skills of our people and our global industries have been the driver of our success over the past thirty years. In 2050, Edinburgh will be a place of opportunity and ambition, where innovators and entrepreneurs can achieve prosperity and success.
- *A Connected City* - Connections are at the core of how a city is lived in and how its people interact with each other. In 2050, Edinburgh will be a city built around shared spaces which create opportunities for understanding, for friendship, and for the exchange of ideas.
- *A Fair City* - A great city commits to sharing success and improving the wellbeing and life experience of all its citizens. In 2050, Edinburgh will be a city without barriers to achievement and where a good quality of life is a basic requirement enjoyed by all.

Local Development Plan and Action Programme

4.7 As the city works towards these objectives, it is also predicted to grow. Its plans for development are set out its Local Development Plan The Local Development Plan Action Programme sets out the new infrastructure that is required to accommodate this growth.

4.8 To deliver the 2050 vision and for the city to grow in a sustainable way, the Council needs to invest in its existing assets as well as creating or acquiring new ones. This Capital Strategy for City of Edinburgh Council provides a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the infrastructure and provision of services for the benefit of Edinburgh communities and citizens. It also provides an overview of how associated risk is managed and the implications for future financial sustainability.

Other Key Plans and Policies

4.9 As well as the strategies, plans and policies outlined above, the capital strategy should be read in conjunction with the following plans and policies for additional background;

- Capital Budget Strategy 2020-30
- Treasury Management Strategy 2020-21
- Housing Revenue Account (HRA) Budget Strategy (2020-2030)
- Council's Change Strategy: Planning for Change and Delivery Services 2020-2023 – Progress Update
- Council's Change Strategy 2020/23: Risks and Reserves
- Corporate Asset Strategy
- Transport Asset Management Plan (TAMP)

5. Capital Expenditure and Financing

Capital Expenditure

5.1 Capital expenditure is where the Council spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are not capitalised and are charged to revenue in year.

5.2 The Council's policy on capitalisation complies with the accounting requirements for local authorities and is set out in its Audited Annual Accounts.

5.3 The capital programme was previously based on the ten-year capital plan originally set out in 2008 (Capital Investment Programme 2009-19), which was subsequently rolled forward on an indicative basis on broadly similar terms.

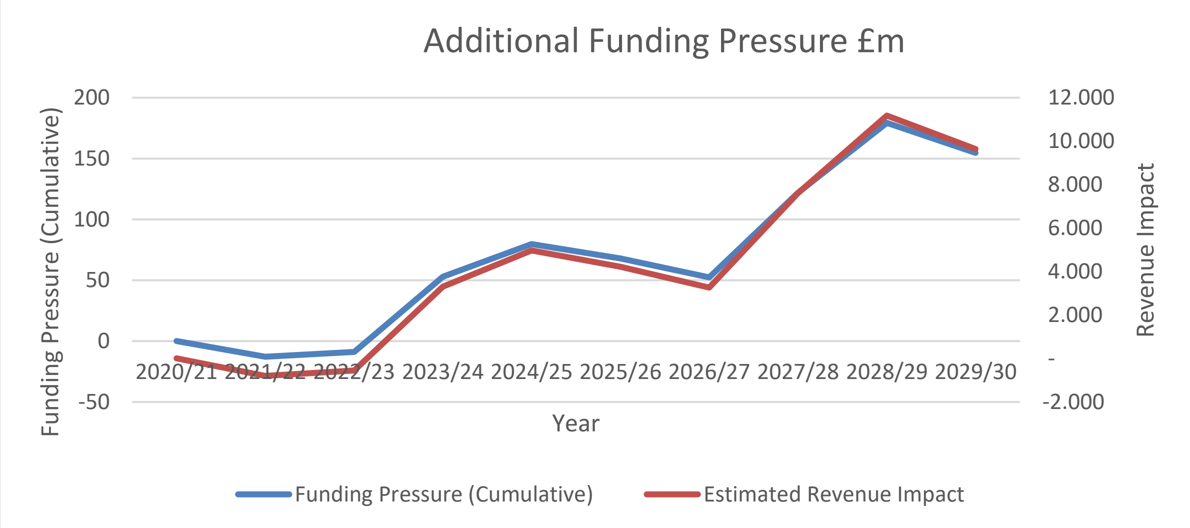
5.4 The Capital Investment Programme 2009-19 has now been superseded by the Capital Budget Strategy 2020-30, which was reported to Finance and Resources Committee on 14 February 2020 and approved at the Council's budget meeting of 20 February 2020. This Capital Budget Strategy will be subject to annual review and will form part of the annual budget setting.

5.5 This Capital Budget Strategy 2020-30 set out additional capital expenditure of £556.748m, offset by additional income of £226.437m, resulting in a requirement of £330.311m in loans fund advances. The loans charges associated with this over a 30-year period would be a principal amount of £330.311m and interest of £288.985m, resulting in a total cost of £619.296m based on an assumed loans fund interest rate of 4.5%. This represents an annual cost of £20.643m.

5.6 Revenue budget planning assumptions mean that that costs associated with £78m of the loans fund advances will be met from savings initiatives and £43m can be met from Council Tax. This was contingent on the Council approving a balanced medium-term revenue budget on 20 February 2020. It is also assumed that £41m will come from services for investment in schools. A further £12.564m will be funded through the fleet review and third-party grants and £1.145m from temporary accommodation savings for the house share scheme.

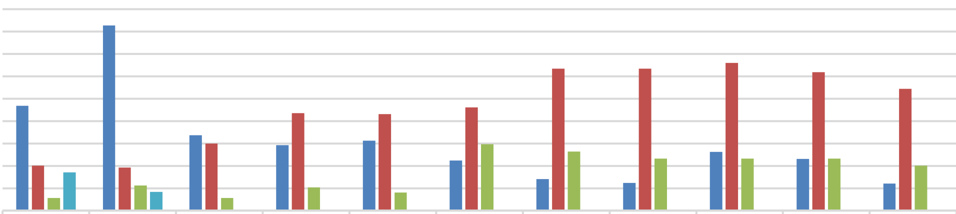
5.7 The remaining £154.602m is currently unfunded and will require the Council to find additional revenue savings in future years, or lead to projects having to be removed from the capital investment programme before they commence. The graph below sets out the funding pressure;

Chart 1: Estimates of Additional Funding Pressure in £ millions



5.8 In the period 2020/30, the Council is planning capital expenditure of £4,838.855m. Whilst the later years are only indicative at present, they are summarised below:

Chart 2: Prudential Indicator: Estimates of Capital Expenditure in £ millions



	2019/20 Forecast	2020/21 Budget	2021/22 Budget	2022/23 Budget	2023/24 Budget	2024/25 Budget	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
General Fund Services	234.399	413.661	168.227	146.451	155.992	111.983	70.060	61.892	130.983	115.767	60.358
HRA - Council Housing	100.679	96.468	149.982	217.371	215.537	230.887	317.233	316.873	330.170	309.312	271.837
On-lending	28.448	56.139	28.413	52.040	40.575	148.029	132.216	116.231	116.231	116.231	100.206
PPP and Similar Assets	85.091	41.500	-	-	-	-	-	-	-	-	-

General Fund Services HRA - Council Housing On-lending PPP and Similar Assets

5.9 Significant General Fund capital projects through the 2020-30 strategy include[1]:

- Wave 4 Schools - £280.834m
- Asset Management Works - £203.270m

- Infrastructure for Population Growth - £166.000m
- Trams to Newhaven - £174.734m

- Investment in Carriageways and Footways - £122.631m
- New Schools and Extensions - £96.502m

[1] Values are those included in the Council's Capital Investment Programme and do not recognise any external funding which has not yet been received, including funding from the Edinburgh and South East Scotland City Deal.

- St James Infrastructure Assets and Picardy Place - £62.900m
- Millerhill Waste Facility - £29.520m
- North Bridge Structural Works - £12.602m

5.10 In addition to the existing programme and additional priorities, we are developing a funding strategy to deliver City Centre Transformation and the wider City Mobility Plan. This analysis does not include provision for these and a separate funding strategy is being developed. Should these projects and funding strategy be approved, this strategy will be amended to reflect Council decisions.

Housing Revenue Account

5.11 The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately.

5.12 The Housing Revenue Account (HRA) Budget Strategy (2020-2030) sets out planned capital investment of £910.245m over the next five years, rising to £2,457.997m over 10 years to deliver tenant priorities, including building new homes, modernising existing homes and help tenants reduce their cost of living. This is summarised in the table below:

Table 1: HRA Five Year Capital Investment Programme and Ten-Year Investment Strategy

Programme Heading	1	2	3	4	5	5 Year	6 to 10	10 Year
	2020/21	2021/22	2022/23	2023/24	2024/25	Total	2025/26 to 2029/30	Total
	£m	£m	£m	£m	£m	£m	£m	£m
New Homes Development*	35.890	97.156	170.677	169.287	183.688	656.698	1,190.595	**1,847.293**
New Homes Land Costs	12.000	8.200	6.500	-	-	26.700	106.220	**132.920**
Tenant's Homes	19.030	16.457	10.693	10.836	11.059	68.075	57.880	**125.955**
External Fabric and Estates	29.548	28.169	29.501	35.414	36.140	158.772	190.730	**349.502**
Total Expenditure	**96.468**	**149.982**	**217.371**	**215.537**	**230.887**	**910.245**	**1,545.425**	**2,455.670**
Prudential Borrowing	23.346	94.916	116.650	136.322	53.807	425.041	789.540	**1,214.581**
Capital Financed from Current Revenue	3.656	3.013	3.121	3.229	3.238	16.257	14.000	**30.257**
Capital Receipts	3.150	6.722	11.340	9.805	6.638	37.655	11.500	**49.155**
Receipts from LLPs*	47.374	28.413	52.040	40.575	148.029	316.431	581.115	**897.546**
Scottish Government Subsidy (Mid-Market)	5.962	3.938	-	-	-	9.900	-	**9.900**
Scottish Government Subsidy (Social)	12.980	12.980	34.220	25.606	19.175	104.961	149.270	**254.231**
Total Funding	**96.468**	**149.982**	**217.371**	**215.537**	**230.887**	**910.245**	**1,545.425**	**2,455.670**

**The budget for new build housing includes the upfront capital costs for the Council led development of all 10,000 affordable homes, including homes for mid-market and affordable market that will be purchased by the Council's new LLPs. This has no impact on the HRA as interest payments are deferred until the homes are purchased. £76m of the £898m anticipated receipts from LLPs by year ten is for homes already under construction and due to complete in the next two years. Please note these receipts go beyond current approved levels of on-lending, approval will be sought to expand the programme in future years.*

5.13 This investment aims to deliver Council commitments on affordable housing and net zero carbon by 2030. Capital investment will be accompanied by improvements in how we deliver housing services to increase customer satisfaction. The Strategy is aimed at reducing tenants cost of living, with below inflation rent increases and service charges frozen for the fifth year in a row.

5.14 The HRA Budget Strategy 2020-2030 will also enable wider area improvements; including the regeneration of Granton Waterfront, Pennywell, Craigmillar, Meadowbank, Fountainbridge, Powderhall and Wester Hailes.

Housing Limited Liability Partnerships

5.15 The Council also uses general fund resources to increase the provision of affordable housing in the city, through lending to arms' length limited liability partnerships under the National Housing Trust and Edinburgh Living initiatives with £900.555m provided in the 10-year strategy. These projects are self-financing because of income from affordable rents. However, it should be noted that at present the City of Edinburgh Council only has consent to borrow from the Scottish Government for Edinburgh Living LLPs up to 2023-24 for a total of £248.000m.

Identifying Capital Priorities

5.16 For new projects to be added to the Council's capital programme. Asset Investment Groups, within each directorate identify their investment priorities and develop business cases supporting those priorities. These priorities are then scored against a set series of prioritisation criteria agreed by the Council's Asset Management Board.

5.17 The Asset Management Board, which is an officer group chaired by the Executive Director of Resources, appraises all business cases and recommends investment priorities to the Corporate Leadership Team of the Council and then to the Finance and Resources Committee, ahead of the full Council budget setting meeting each year. Smaller ad-hoc projects may be added through the year following appropriate approval of project business cases, including those through executive committees or via the full Council itself.

Capital Financing

5.18 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing, Public Private Partnerships and similar instruments). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

Capital Financing	2018/19 Actual	2019/20 Forecast	2020/21 Budget	2021/22 Budget	2022/23 Budget	2023/24 Budget	2024/25 Budget	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
Grants	122.376	140.405	143.342	88.831	130.260	110.681	212.204	214.178	191.495	191.995	192.495	172.722
Asset Sales	26.534	50.496	6.150	9.722	14.340	12.805	9.638	16.989	5.000	5.000	5.000	14.508
Capital Fund	7.482	6.311	14.195	-	12.805	-	-	-	-	-	-	-
Supported Borrowing	48.518	23.000	69.262	30.241	37.921	37.529	28.538	7.100	7.100	7.100	7.100	27.100
On-Lending	-	-	56.139	28.413	52.040	40.575	148.029	132.216	116.231	116.231	116.231	100.206
Other External Income	7.938	4.617	6.297	10.012	3.106	3.273	12.038	18.619	23.964	7.701	4.065	0.756
PPP and similar arrangements	-	85.091	41.500	-	-	-	-	-	-	-	-	-
Loans Fund Advances - Self-Financed	53.855	138.697	270.883	179.403	165.391	207.241	80.452	130.407	151.206	249.357	216.419	117.109
Total	**266.703**	**448.617**	**607.768**	**346.622**	**415.862**	**412.104**	**490.899**	**519.509**	**494.996**	**577.384**	**541.310**	**432.401**

5.19 The grants total above doesn't include external funding where the timing of that funding is uncertain. This includes Sustrans funding for Active Travel.

5.20 To become carbon neutral by 2030, the city will need to tackle its largest sources of carbon emissions. The transport sector is one such significant source and road transport accounts for 68% of total transport emissions. Investing in active travel infrastructure provides the city's residents, visitors and businesses a means of transport that is low carbon and can efficiently move people and goods around the city. Active travel not only has a lower carbon footprint than private vehicles, it is also better for the city's air quality.

5.21 After rent or mortgages, people in Edinburgh spend more per week on transport than anything else. Providing high quality active travel infrastructure can make walking and cycling a realistic and appealing option for many who currently do not feel safe choosing to travel in this way. With the cost of accessing a bike far lower than for accessing a car, good active travel infrastructure can provide a low cost travel option for people to get around the city.

The image below shows George IV Bridge with Meadows to George Street implemented:

Loans Fund Review and Policy

5.22 The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 require the statutory loans fund to be administered in accordance with the 2016 Regulations, proper accounting practices and prudent financial management. The Council operates a consolidated loans fund under the terms of these Regulations. Capital payments made by services are financed by capital advances from the loans fund.

5.23 Apart from advances in relation to Edinburgh Living LLPs, all advances from the loans fund in the current year have a repayment profile set out using Option 1, the statutory method. All capital advances from the loans fund are repaid using the previous hybrid annuity structure with fixed principal repayments. The Council operates the loans fund to manage historic debt and the balance therefore represents historic borrowing for capital spend.

5.24 A Loans Fund Review was carried out in 2019/20 with the objective to explore options which could re-profile loans fund repayments in order to assist with delivery of a prudent, sustainable and deliverable medium-term revenue budget strategy, whilst ensuring that the provision remains prudent and appropriate to the benefits that are provided to the community from the associated expenditure.

5.25 The review was reported to Finance and Resources Committee on 14 February 2020. This report revised the Loans Fund debt charge repayment periods, based on a prudent financial management strategy.

5.26 The depreciation policy of the Council had generally set a higher useful life period than the average loan repayment periods, which repaid the advances over a shorter period than the actual use of the asset. The report recommended using an average life of 30 years for General Fund repayments which is more in line with the depreciation policy.

5.27 For the Housing Revenue Account (HRA) it was recommended to use an average life of 30 years for non-component spend. Component spend will remain on an average 20-year life, due to the nature of the expenditure, e.g. replacement of kitchens, bathrooms, heating systems, etc.

5.28 The Council had applied the average loans pool rate each year to calculate loan repayments for historic debt based on interest incurred and loans fund advances made. This ranged from 10% in 1996/97 to 4.63% in 2018/19. Taking into account the level of expenditure in each year, the average loans fund borrowing rate over this period is 5.8% and it was recommended that this interest rate was used to calculate loans fund charges for advances made during this period. Going forward, for new advances, the pool rate for the year will be used.

5.29 As a result of the Loans Fund Review, the repayments for both historical and new capital advances (with the exception of those detailed below) will be calculated using option 3 – the Asset Life method.

5.30 For capital advances relating to loans to the Edinburgh Living LLPs and capital advances for the “Trams to Newhaven” project, all advances from the loans fund in the current year have a repayment profile set out using Option 4 – the funding/income method and these capital advances will be repaid using an annuity structure with fixed interest rate and principal repayments.

5.31 The business cases brought forward for other projects involving major capital expenditure funded by borrowing will consider the appropriate repayment method depending on the structure of the business case.

International Financial Reporting Standard (IFRS) 16 - Leases

5.32 The Council will need to adhere to IFRS 16 from the start of financial year 2020/21, with information also prepared for a disclosure note in the 2019/20 Annual Accounts.

5.33 The objective of IFRS 16 is to report information that represents lease transactions and provides a basis for users of financial statements to assess the amount, timing and uncertainty of cash flows arising from leases.

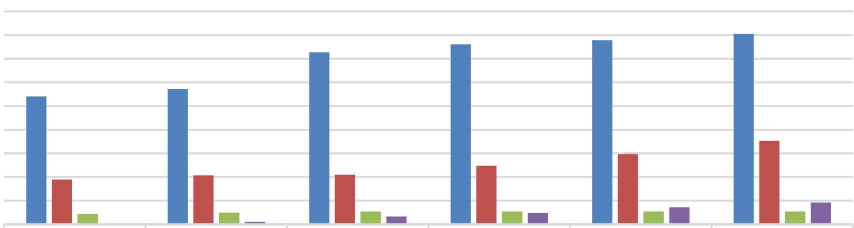
5.34 IFRS 16 introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments.

5.35 The introduction of IFRS 16 within the Accounts will have a significant impact on the balance sheet from its introduction in 2020/21. This will subsequently have an impact on the Capital Financing Requirement (CFR) as from the 2020/21 financial year. Therefore, it should be expected to see an increase in the CFR in future years.

Capital Financing Requirement

5.36 The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with loans fund repayments and capital receipts used to replace debt. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Chart 3: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions



	2018/19 Actual	2019/20 Forecast	2020/21 Budget	2021/22 Budget	2022/23 Budget	2023/24 Budget
General Fund Services	1,079	1,146	1,453	1,520	1,556	1,610
HRA - Council Housing	377	413	418	495	592	706
NHT LLPs	87	99	108	108	108	108
Edinburgh Living LLPs	3	19	66	94	145	183

Asset Management

5.37 To ensure that capital assets continue to be of long-term use, the Council has asset management strategy in place. This was set out in 2015 with two documents; the Corporate Asset Strategy approved by Corporate Policy and Strategy Committee in May 2015, and the subsequent Property and Asset Management Strategy reported to Finance and Resources Committee in September 2015. The Asset Management Strategy sets out the objective to create a credible, focused and sustainable delivery organisation for property and facilities management; provide a fit for purpose, right-sized and safe estate; provide an appropriate level of service at an acceptable and efficient cost; and act in a commercial manner in pursuit of maximising value for the Council.

5.38 The Council's Change Strategy - Planning for Change and Delivery Services 2020/23 – Progress Update outlines our aims for a 21st Century Estate. We have more greenspace than any other UK city and two UNESCO World Heritage Sites. We also have a fantastic network of community buildings which are a highly valued part of the social fabric of Edinburgh. Over the last few years we have reduced the number of buildings we use but still spend £100m a year running the ones we still own.

5.39 Resources like offices and depots can be shared across the public sector. We'll be able to identify sites for new housing, release capital for investment, reduce costs and carbon emissions. This will be overseen by a Land and Property Commission and supported by the Scottish Government. Three years ago we had 16 depots and yards spread all over the city. Today we have 10 and by 2023 we want this to reduce to three consolidated fit-for-purpose facilities. This will release land for housing and development and make our services more efficient and effective.

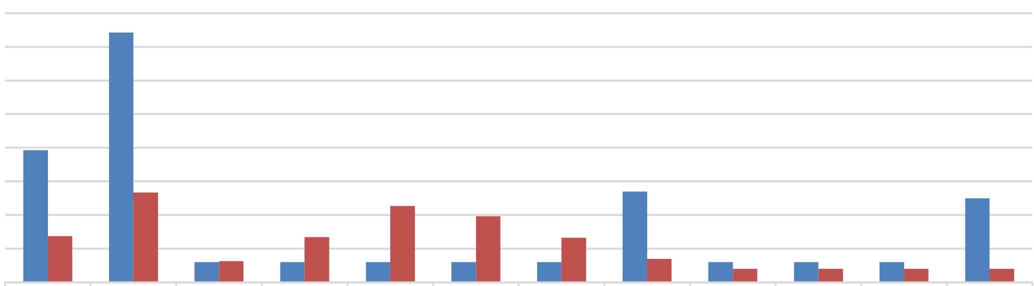
5.40 We are developing a new Estate Strategy examining all aspects of how we run and maintain our buildings and land. We have committed £153m of additional investment in our estate. This will hugely improve the condition, safety and accessibility of our buildings. We are investigating energy generation, insulation and energy saving measures in some of our older buildings which will be done in an ethical, sustainable way contributing to our carbon target and saving money in the long term.

5.41 We are developing our Learning Estate with 10 new or replacement primary schools and seven replacement secondary schools over the next 10 years. Queensferry High School will be opening after Easter 2020. As a part of our environmental commitments, as many of our renewals and new builds as possible will conform to Passivhaus standards in line with the 2030 City Plan. The latest update on our Communities and Families Learning Estate went to Finance and Resources Committee on 10 October 2019.

Asset Disposals

5.42 When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. Repayments of capital grants also generate capital receipts. The Council expects to receive £99.152m of capital receipts in the HRA and General Fund in the years 2020/21 to 2029/30 as follows:

Chart 4: Capital receipts in £ millions



	2018/19 Actual	2019/20 Forecast	2020/21 Budget	2021/22 Budget	2022/23 Budget	2023/24 Budget	2024/25 Budget	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
General Fund	19.659	37.143	3.000	3.000	3.000	3.000	3.000	13.489	3.000	3.000	3.000	12.508
HRA	6.875	13.353	3.150	6.722	11.340	9.805	6.638	3.500	2.000	2.000	2.000	2.000

6. Treasury Management

Treasury Management

6.1 Treasury management's role is to keep sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent and holds cash reserves, at least in the short-term. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

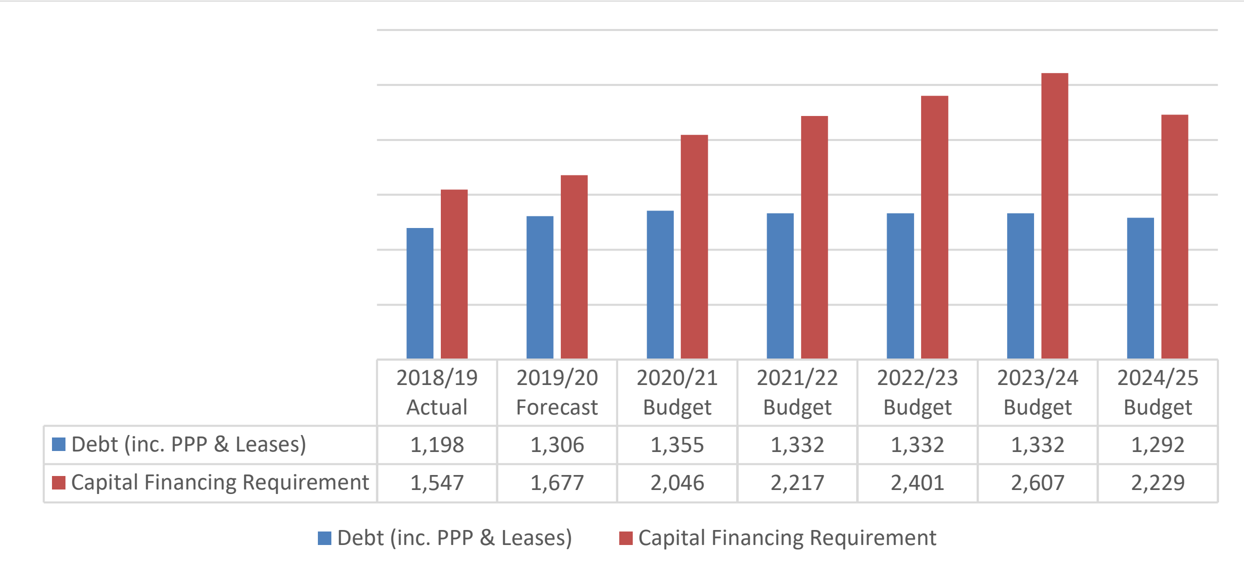
6.2 Due to past borrowing undertaken, at January 2020 the Council currently had £1,311m borrowing at an average interest rate of 4.66%. This excludes £60m of borrowing which the Council has committed to draw down from PBB in 2020. It also includes over £100m funded internally through cash investments. We also held c. £232m treasury investments at an average rate of 0.82%.

Borrowing Strategy

6.3 The Council's main objective when borrowing is to achieve a low but certain cost of finance while, where possible, managing the Council's future interest rate risk. The current strategy is to balance reducing investments to fund capital expenditure in the short term while managing the Council's longer-term interest rate risk by securing borrowing for future capital expenditure as the delivery becomes more certain.

6.4 Projected levels of the Council's total outstanding debt (which comprises borrowing, PFI liabilities, leases are shown below, compared with the capital financing requirement as summarised in the chart below:

Chart 5: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions



	2018/19 Actual	2019/20 Forecast	2020/21 Budget	2021/22 Budget	2022/23 Budget	2023/24 Budget	2024/25 Budget
Debt (inc. PPP & Leases)	1,198	1,306	1,355	1,332	1,332	1,332	1,292
Capital Financing Requirement	1,547	1,677	2,046	2,217	2,401	2,607	2,229

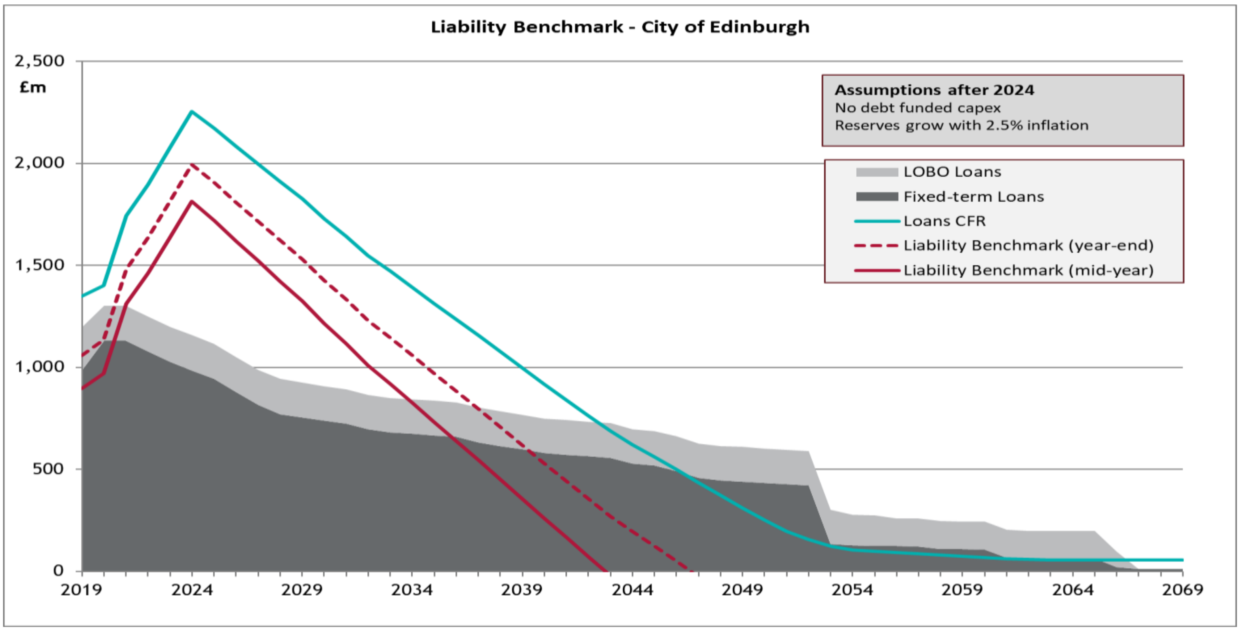
6.5 Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from Chart 4, the Council expects to comply with this in the medium term.

Liability Benchmarking

6.6 To compare the Council's actual borrowing against its predicted underlying need to borrow, a liability benchmark has been calculated using the Council's loans and Capital Financing Requirement less its core underlying cash investments.

6.7 The chart below shows the projection of the Council's benchmark produced by the Council's Treasury Advisors:

Chart 6: Liability Benchmark in £ millions



6.8 The chart shows that the Council is projected to be significantly under its liability benchmark over the period. This shows that the Council will require to undertake additional borrowing in the latter years to fund this.

Affordable Borrowing Limit

6.9 The Council sets an affordable borrowing limit (also termed the authorised limit for external debt) each year. A lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 3: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2018/19 Limit	2019/20 Limit	2020/21 Limit	2021/22 Limit	2022/23 Limit	2023/24 Limit
Authorised Limit – Borrowing	1,595	1,682	1,949	2,112	2,267	2,422
Authorised Limit – PFI and Leases	201	281	317	313	309	305
Authorised Limit – Total External Debt	**1,796**	**1,963**	**2,266**	**2,425**	**2,576**	**2,727**
Operational Boundary – Borrowing	1,231	1,446	1,768	1,929	2,127	2,322
Operational Boundary – PFI and Leases	202	281	317	313	309	305
Operational Boundary – Total External Debt	**1,433**	**1,727**	**2,085**	**2,242**	**2,436**	**2,627**

Investment Strategy

6.10 Treasury investments arise from receiving cash before it is paid out again and through reserves and other fund balances. For nearly 7 years from December 2012, the Council did not draw down any external PWLB or market borrowing, The strategy over this period was to fund the Council's borrowing requirement by reducing the Council's temporary investments. The new borrowing undertaken in 2019/20 to de-risk the core funding for the "Trams to Newhaven" project gave the Council additional temporary cash balances. This was used to add duration to the cash fund, significantly increasing its average weighted life. As the cash is spent on the project and other significant capital expenditure is undertaken in 2020/21, the scope for investing for longer periods will be constrained again.

6.11 The Council's cash investments are pooled with the sterling cash of Lothian Pension Fund and other associated organisations and invested together. The investment policy for treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Additional liquidity is provided using Money Market Funds. Investments made for service reasons are not generally considered to be part of normal treasury management activity

6.12 Further details on treasury investments are in Appendix 5 of the Annual Treasury Management Strategy report.

6.13 Decisions on treasury management investment and borrowing are made daily and are therefore delegated by the Council to the Head of Finance and relevant staff, who must act in line with the Treasury Management Policy Statement approved by the Council on the recommendations of the Finance and Resources Committee. Semi-annual reports on treasury management activity are presented to Council. The Governance, Risk and Best Value Committee is responsible for scrutinising treasury management decisions.

7. Other Investments and Long-term Liabilities

Investments

7.1 The Council makes investments to assist local public services, including making loans to and buying share in Council's subsidiaries that assist in the delivery of Council priorities. Examples include investments in the Edinburgh International Conference Centre, the EDI Group, Edinburgh Living LLPs and Energy for Edinburgh. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to break even after all costs.

7.2 Decisions on service investments are made by the relevant Executive Director or Head of Service, in accordance with the scheme of delegation, in consultation with the Head of Finance and are approved by the relevant executive committee of the Council. Most loans and share purchases are capital expenditure and purchases will therefore also be approved as part of the capital programme.

Commercial Activities

7.3 The Council retains a commercial property investment portfolio for city development purposes, but also derives financial gain from this activity. The investment portfolio consists of over 1,130 assets and is forecast to produce a rental income of c. £15m per annum. The portfolio is estimated to have a value of c. £230m.

7.4 With economic development being the main objective, the Council accepts higher risk on commercial investment that with treasury investments. The principal risk exposures include voids and falls in capital value. In order to minimise the liability to the Council the portfolio is actively managed on a commercial basis.

7.5 Decisions on commercial investments are made by the Executive Director of Resources in line with the criteria and limits set by the Council as part of the Scheme of Delegation and Financial Regulations, and directly through the Finance and Resources Committee, where appropriate. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme.

7.6 The council also has commercial activities in Edinburgh International Conference Centre and the EDI group. The commercial activities in the EDI group are in the process of being wound down in accordance EDI transition strategy approved by Council on 31 May 2018.

Integration with Wider Financial Strategy

7.7 It is recognised that the Council's capital resources are limited. Borrowing carried out for investment must be repaid from increasingly limited revenue budgets. The Capital Budget Strategy can only be funded if the Council is able to balance its revenue budget over the medium to long term to comply with the terms of the Prudential Code.

7.8 This strategy should be read in parallel with the Council's Change Strategy - Planning for Change and Delivery Services 2020/23 – Progress Update as the revenue impact of additional capital expenditure needs to be contained within a balanced medium-term revenue budget.

Risks and Reserves

7.9 The Council undertakes an annual review of its risks and reserves in the context of setting the revenue and capital budgets. The most recent update, Council's Change Strategy 2020/23: Risks and Reserves, was reported to the Finance and Resources Committee on 14 February 2020 and set out a number of risks (and associated mitigating actions), including potential cost pressures around demographic-led demand, pay awards and the impacts of other legislative changes, as well as the level of future funding settlements and delivery of approved savings.

7.10 The Council has a reserves strategy aligned to the risks it faces. In addition to maintaining unallocated reserves at a level equal to 1% of gross revenue expenditure, a number of specific statutory and other reserves are maintained.

7.11 The external auditor's report, City of Edinburgh Council - 2018/19 Annual Audit Report to the Council and the Controller of Audit noted that overall reserve levels, taking into account both sums earmarked for specific purposes and the unallocated General Fund balance, were assessed to be adequate based upon the risks the Council faces.

Revenue Budget Implications of Capital Strategy

7.12 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and loans fund repayments are charged to revenue, offset by any investment income receivable. The net annual charge as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general grants.

Table 4: Prudential Indicator: Proportion of financing costs to net revenue stream

	2018/19 Actual	2019/20 Forecast	2020/21 Budget	2021/22 Budget	2022/23 Budget	2023/24 Budget
Financing costs (£m) – General Fund Services	107,521	108,230	103,708	100,356	99,669	100,424
Proportion of net General Fund revenue stream	11.16%	10.93%	10.48%	10.05%	9.88%	9.96%
Financing costs (£m) – Housing Revenue Account	39,171	38,887	36,683	39,493	43,055	46,248
Proportion of net HRA revenue stream	37.29%	38.30%	35.57%	37.13%	38.91%	39.46%

7.13 In addition to financing costs, the Council makes provision for all running costs and lifecycle maintenance of assets in its revenue budget planning process. Before inclusion in the capital programme, a business case is created for every new project which sets out the revenue implications and how they will be funded.

7.14 Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The implications of capital expenditure have been built into the Council’s long-term financial planning assumptions to ensure that the proposed capital programme is prudent, affordable and sustainable.

8. Knowledge and Skills

8.1 The council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions.

8.2 The Finance function, within the Council’s Resources Directorate, has qualified accountants working throughout the Division. The accountancy function is an accredited employer with regard to Continuing Professional Development (CPD) with the following accountancy bodies: CIPFA, CIMA, and ACCA. This accreditation is assessed externally every 3 years.

8.3 The accounting function has been externally assessed as being a Best Practice Employer with regard to training by CIPFA in recognition of the continuing development opportunities provided to staff.

8.4 Benchmarking information (2018) shows that the Council has an above average number of qualified staff compared with other local authorities across the UK with over 66% of staff being qualified or part-qualified. Support is provided for those engaged in study for accounting, treasury and insurance qualifications. The CPD assessment undertaken by CIMA examines the provision of training and guidance available to staff on ethical issues including whistleblowing and money laundering legislation.

8.5 As well as finance qualifications, the Treasury Team hold a range of Treasury, Investment and Banking qualifications including the CIPFA/ACT Certificate in International Treasury Management – Public Finance and the Investment Management Certificate. The team also has a wide range of knowledge and experience in investment instruments as well as debt and other funding structures.

8.6 The Property function, within the Council's Resources Directorate, through which the property investment portfolio is managed, has RICS qualified surveyors working across the Division, the majority of which are also members of the Registered Valuers scheme.

8.7 In addition, use is made of external advisers and consultants that are specialists in their field, when specialist technical advice is required. This approach is more cost effective that employing such staff directly and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

9. Conclusion

9.1 The Capital Strategy is a reporting requirement introduced by the 2017 edition of the CIPFA Prudential Code, with the first iteration published in March 2019.

9.2 The Capital Strategy takes account of the City of Edinburgh Council's Vision and Corporate Strategy whilst considering any new investment within the context of growing in a sustainable way.

9.3 To deliver the Council's Vision, Corporate Strategy and for the city to grow in a sustainable way, the Council needs to invest in its existing assets as well as creating or acquiring new ones.

9.4 This Capital Strategy for City of Edinburgh Council provides a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the infrastructure and provision of services for the benefit of Edinburgh communities and citizens. It also provides an overview of how associated risk is managed and the implications for future financial sustainability.