ANNEX 1

INVESTMENT SUB-COMMITTEE – 15th JANUARY 2020

CAPITAL, INVESTMENT AND TREASURY MANAGEMENT STRATEGY (THE STRATEGY) 2021/22 to 2023/24

1. Executive Summary

1.1 The Capital, Investment and Treasury Management Strategy (The Strategy) sets out the over-arching principles and processes by which the capital and investment decisions set out in the capital programme will be prioritised against the Council's key priorities.

1.2 The Strategy considers the funding implications of the capital programme and where borrowing is required. In addition, it sets out how this will be managed along with the policy for managing investments.

1.3 The following appendices are included:

- Appendix A – Investment Property Strategy (including Annexe A and Annexe B)
- Appendix B – Capital Strategy Principles
- Appendix C – Corporate Governance
- Appendix D – Capital Programme 2021/24
- Appendix E – Sources of Capital Funding
- Appendix F – Annual Minimum Revenue Provision Policy Statement 2021/22
- Appendix G – Statement of Investment Beliefs
- Appendix H – Treasury Management Strategy

2. Introduction

2.1 The Council is required to operate a balanced budget which broadly means that income raised during the year will meet planned expenditure. Part of the treasury management operation is to ensure that the cashflow for this is adequately planned, with cash being available when it is needed. Where surplus monies are available these are invested with counterparties or in instruments commensurate with the Council's low risk appetite, providing security and adequate liquidity initially before considering investment return.

2.2 The Strategy is a combined document bringing together previously separate documents; Capital and Investment Strategy, Treasury Management Strategy and Investment Property Strategy. It gives a high-level overview of how capital expenditure, capital financing and other investments contribute to the delivery of the Council's priorities along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style in an attempt to enhance Members' understanding of these rather technical areas.

2.3 The overarching aim of the 2021/22 to 2023/24 Strategy is to provide a framework within which the Council's capital investment plans will be delivered. It has been prepared to cover a three-year time-frame and covers borrowing and investment considerations. This includes the requirements of the Local Government Act 2003 and the CIPFA Treasury Management Code along with the requirements of the CIPFA Prudential Code for Capital Finance in Local Authorities.

2.4 In accordance with IFRS16 all leases will be accounted for as finance leases effective from 1 April 2022. This requires a right of use asset and corresponding lease liability to be shown on the Council's balance sheet. Whilst the accounting arrangements change there is zero impact on the general fund. As this has been deferred any impact will be reflected in the 2021/22 Strategy.

2.5 Capital investment plans are driven by the Council's priorities included within the Strategic Plan, agreed by Strategy and Resources Committee. The plan sets out the Council's priorities, listed below and the actions that are being taken now and into the next four years.

3. Council's priorities

3.1 The Council's key priorities are:

- **Building a better Council –** making the Council financially sustainable and providing residents with the best possible services;
- **Creating the homes, infrastructure and environment we need** – both now and in the future;
- **Supporting economic recovery in Tandridge –** from lockdown to growth that everyone benefits from; and
- **Becoming a greener, more sustainable District –** tackling climate change.

3.2 The above priorities will be achieved by working in partnership with other public-sector agencies and businesses within the District and beyond.

3.3 The priorities reflect the on-going commitment to ensure the Council works to serve the people of Tandridge in all that it does and provides strong leadership for the District. Such leadership is essential if the District is to be able to meet the immediate challenges faced in a way that means it is stronger and able to make the most of opportunities in the future.

3.4 Aligned to the Council's priorities, individual scheme proposals are included within approved capital spending plans or are to be considered for financing over the period of the Strategy

3.5 The Investment Property Strategy (IPS) presents a framework for strategic management of the Council's land and property portfolio, reflecting the Council's key priorities and driving transformational change. It aligns with the Council's strategic priorities and the Council's wider priorities for revenue generation, site acquisition, site development, release of assets for disposal, affordable housing and regeneration within the District.

3.6 The Council is continuing to develop the IPS and this will regularly be refreshed to improve the way in which Property Investment objectives can be delivered. This will enable the Council to accelerate progress and realise benefits within a shorter timeframe, whilst maximising regeneration and investment opportunities. The current **Investment Property Strategy can be found at Appendix A**. A set of overarching principles, which apply to the Council's 2020/21 Strategy, are set out in **Appendix B.**

3.7 The Council's intention in relation to capital investment is to ensure it can make a real and demonstrable impact on the economy of Tandridge by:

- **Regenerating the District**, by attracting and securing significant amounts of external investment to supplement Council resources and deliver an enhanced district-wide regeneration offer;
- **Prioritising the regeneration investment** to develop the local economy and to support job creation and promote local employment within the District.; and

- **Using the regeneration investment to drive up the yield from business rates**. This will provide additional resources which can either be used to support the Council's budget or to pursue opportunities for further investment in Tandridge.

3.8 The Council will also:

- Work with Surrey County Council, Parish Councils, Health, Police and Fire as a co-operative and commissioning District particularly with regard to the integration of health and social care to promote joint investment opportunities, co-location and the release of surplus assets;
- Instigate further transformational approaches to the delivery of services with and by communities and staff, that maximise involvement and delivery at a more local level, working with residents to reset priorities, manage expectations and promote self-help;
- Get the basics right, drive improved business performance with more flexible customer focused ICT systems which enable web-based self-service and instigate new delivery models; and
- Focus on effective service delivery, achieving social value and maximising the impact of the resources invested.

4. Capital Programme Governance

4.1 The Council has specific arrangements for the management of capital expenditure. The principles for governance of the Capital Programme are detailed in **Appendix C.** The separate approval process for the acquisition of investments in property is contained within the Investment Property Strategy.

5. Asset Management & Asset Disposals

5.1 When a capital asset is no longer needed for Council purposes and surplus to requirements, it may be sold so that the proceeds, known as capital receipts, can be used to finance the acquisition of new assets or used to repay debt. The Council does not currently have a land disposal programme for the General Fund. The current policy is to use any surplus land and property which is identified for housing purposes. Therefore, it is unlikely that any significant General Fund capital receipts will be received in the future.

5.2 There are specific regulations about the extent to which capital receipts from sales of Council Houses can be used to finance new capital expenditure. Repayments of capital grants, loans and investments are classified as capital receipts. The Council does not anticipate any General Fund capital receipts in the coming financial year. The estimated capital receipts are set out below:

Table 1: Capital receipts in £ millions

	2019/20 Actual £m	**2020/21 Estimate £m**	**2021/22 Estimate £m**	**2022/23 Estimate £m**	**2023/24 Estimate £m**
HRA Disposals	1,129	1,400	1,400	1,400	1,400
GF Disposals	0	0	0	0	0
Loans repaid	566	318	318	318	318
TOTAL	**1,695**	**1,718**	**1,718**	**1,718**	**1,718**

6. Key Priorities for Capital Investment

6.1 Priority investment areas for 2020/21 onwards will be taken forward subject to the availability of resources and the approval of a full business case.

7. Capital Expenditure and Financing

7.1 Capital expenditure investment is where the Council spends money on physical capital assets, such as property or vehicles, that will be used for more than one year in the delivery of services, and, where appropriate:

- Capital loans to specific service providers e.g. loans to Gryllus Property Ltd and Freedom Leisure;
- Loans and shareholdings in limited companies, joint ventures and other non-financial investments in property; and
- Spending on assets owned by other bodies and providing loans and grants to other bodies to enable them to buy assets.

7.2 The Council capitalises expenditure on the acquisition or creation of a tangible or intangible asset, where the expenditure adds to and not merely maintains the value of the asset. The Council's capital expenditure is the key driver of treasury management activity.

7.3 The capital expenditure prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of the budget cycle. In 2021/22, the Council is planning capital expenditure investment of c£55m, over the medium-term as summarised below:

Table 2: Prudential Indicator: Capital Expenditure in £ millions

	2019/20 Actual £m	**2020/21 Estimate £m**	**2021/22 Estimate £m**	**2022/23 Estimate £m**	**2023/24 Estimate £m**
General Fund services	17.486	6.386	8.514	1.656	1.129
Council Housing (HRA)	8.126	9.275	16.554	7.705	4.025
Commercial activities/non-financial investments*	16.899	0	0	0	0
TOTAL	**42.511**	**15.661**	**25.068**	**9.361**	**5.154**

** Commercial activities/non-financial investments relate to areas such as capital expenditure on investment properties, loans to third parties etc.*

7.4 The main General Fund capital projects include the refurbishment of public conveniences (£0.550m), IT hardware/infrastructure projects (£0.966m), Vehicle Replacement Programme (£0.624m) and Children's Playground Improvements (£0.580m). The Council also plans to incur £4.9m of capital expenditure on the refurbishment of Quadrant House phase 2 as part of the Council's economic development plans. Quadrant House is currently a catalyst for improvement in Caterham and the expenditure is being funded via two Local Enterprise Partnership grants that have been awarded.

7.5 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. Details of the draft Capital Programme 2021/24 are attached at **Appendix D.**

7.6 All capital expenditure must be financed, either from external resources (government grants and other contributions), the Council's own resources (revenue contributions, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiative). The planned financing of the programme is shown below:

Table 3: Financing of Capital Expenditure in £ millions

	2019/20 Actual £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
External resources	1.025	1.550	6.093	0.790	0.460
Internal resources	8.344	10.300	10.894	6.214	4.025
Borrowing	33.142	3.811	8.081	2.357	0.669
TOTAL	**42.511**	**15.661**	**25.068**	**9.361**	**5.154**

7.7 Further details on the various funding sources for funding capital expenditure are set out in **Appendix E**.

8. Capital Financing Requirement

8.1 The Capital Financing Requirement (CFR) measures the Authority's underlying need to borrow. The CFR will increase by the amount of new capital expenditure not immediately financed (e.g. by capital receipts, capital grants/contributions or from revenue) and will reduce by resources set aside for the Minimum Revenue Provision (MRP). The CFR is anticipated to increase by c£3m during 2020/21. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Capital Financing Requirement in £ millions

	31/03/2020 Actual £m	31/03/2021 Estimate £m	31/03/2022 Estimate £m	31/03/2023 Estimate £m	31/03/2024 Estimate £m
General Fund services	23.811	27.276	33.843	33.486	32,840
Council housing (HRA)	61.308	61.308	67.068	68.659	68.759
Commercial activities/non-financial investments	21.619	21.183	16.066	15.844	15.616
TOTAL CFR	**106.738**	**109.767**	**116.977**	**117.989**	**117.215**

Minimum Revenue Provision (MRP)

8.2 The Local Authorities (Capital Finance and Accounting)(England)(Amendment) Regulations 2008 require a local authority to determine each financial year an amount of MRP which it considers to be prudent. The broad aim of MRP is to ensure that debt is repaid over a period reasonably commensurate with that within which the capital expenditure provides a benefit. The Ministry of Housing, Communities and Local Government (MHCLG) recommends that a statement of MRP policy for the forthcoming Financial year is approved by the full Council of the Authority.

8.3 The guidance issued gives four options for making MRP which the Secretary of State considers prudent provision. The option chosen can be altered annually.

8.4 The Council's MRP policy is to follow the Asset Life Method. The Asset Life - annuity method allows MRP to increase gradually over the asset life, which better reflects the profile of the Council's borrowing requirement for its previous commercial activities. The Asset Life – equal instalments instalment method provides MRP in equal instalments and is applied to the Council's non-commercial activities. The Council's full minimum revenue provision policy statement is attached at **Appendix F.**

8.5 Borrowing is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is MRP. Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP repayments are as follows:

Table 5: Replacement of debt finance in £ millions

	2019/20 Actual £m	2020/21 Estimate £m	2021/22 Budget £m	2022/23 Budget £m	2023/24 Budget £m
Minimum Revenue Provision	0.162	0.782	0.871	1.344	1.443

8.6 There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made.

9. Treasury Management

9.1 The capital expenditure plans are set out in Section 7. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. 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 income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

Current portfolio position

9.2 The overall treasury management portfolio as at 31 March 2020 is shown below for both investment and borrowing:

Table 6: Current Investment Portfolio in £ millions

	2019/20 Actual 31/03/2020 £m	2019/20 Actual 31/03/2020 %
Notice Accounts & Cash Plus Funds	4.0	0.8
Money Market Funds	10.9	0.7
Short-term Deposits	0	0
CCLA Property Fund	4.2	4.4
Funding Circle	1.8	3.9
Schroders Bond Fund	2.5	4.9
UBS Multi-Asset Fund	2.5	5.5
CCLA Diversification Fund	1.8	3.7
Total Treasury Investments	**27.7**	**2.5**
Long-term PWLB loans (HRA)	61.2	2.7
Long-term PWLB loans (GF)	43.4	2.6
Total Borrowing	**104.6**	**2.7**
Net Borrowing	**76.9**	

9.3 As a result of decisions taken in the past, the Council has borrowing of £105m at an average interest rate of 2.7 % and treasury investments totalling £27.7m at an average rate of 2.5% at 31st March 2020.

Borrowing Strategy

9.4 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need, (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure (internal borrowing). This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

9.5 Against this background and the risks within the economic forecast, caution will be adopted with the 2021/22 treasury operations. The Chief Finance Officer (s151) will monitor interest rates in financial markets, in conjunction with Link, our Treasury advisers and adopt a pragmatic approach to changing circumstances. These changes will be reported to the appropriate decision-making body at the next available opportunity.

PWLB Consultation

9.6 In March 2020 the government launched a consultation on revised lending terms and guidance to prevent Local Authorities from using PWLB loans to buy commercial assets with the primary aim of generating yield.

9.7 The government issued new lending terms following this consultation which applies to all loans from 26th November 2020. As it is impossible to 'reliably link particular loans to specific spending' the restriction applies to the whole capital programme. This means the PWLB will not lend to a Local Authority that plans to buy investment primarily for yield anywhere in its capital plans.

9.8 The Council's expenditure plans included in **Table 2** reflect these new restrictions which do not impact the Council as there is no intention to buy investment assets primarily for yield over next three years.

Prudential borrowing

9.9 The Council will investigate opportunities to resource capital projects using prudential borrowing where plans are sustainable, affordable and prudent. A full business case will be required to ensure, sufficient revenue returns are generated to cover all the costs of borrowing. This will be especially important when undertaking property acquisitions under the Investment Property Strategy where, in addition, a revenue income stream is required to support the revenue budget. Strategy and Resources Committee will review the detailed capital expenditure plans before resources are committed to ensure affordability.

Table 7: Prudential Indicator: Forecast Gross External Debt and the Capital Financing Requirement in £ millions

	31.3.2020 Actual £m	**31.3.2021 Estimate £m**	**31.3.2022 Estimate £m**	**31.3.2023 Estimate £m**	**31.3.2024 Estimate £m**
HRA Debt	61.2	61.2	66.8	68.3	68.3
General Fund External Debt	43.4	43.4	43.4	43.4	43.4
Other Long-Term Liabilities	0	0	0	0	0
Total Debt	**104.6**	**104.6**	**110.2**	**111.7**	**111.7**
Capital Financing Requirement	106.7	109.8	117.0	118.0	117.2
CFR not funded by Borrowing	2.1	5.2	6.8	6.3	5.5

9.10 Statutory guidance is that to ensure that over the medium-term debt will only be for a capital purpose, external debt should remain below the CFR, except in the short-term. As can be seen from **Table 7,** the Council expects to comply with this.

Borrowing in advance of need

9.11 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved CFR estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Affordable borrowing limit

9.12 The Prudential Code requires the Council to set two limits on its total external debt, as set out in the table below. The limits have been adjusted as required for growth and slippage in the capital strategy. The limits are:

9.13 **Authorised Limit for External Debt.** This is the limit prescribed by section 3(1) of the Local Government Act 2003 representing the maximum level of borrowing which the Council may incur. It reflects the level of external debt which, while not desired, could be afforded in the short-term, but may not be sustainable in the longer term.

9.14 **Operational Boundary.** This is the limit which external debt is not normally expected to exceed. In most cases this would be a similar figure to the CFR but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing from other cash resources. The boundary is based on current debt plus anticipated net financing need for future years.

Table 8: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2020/21 limit £m	**2021/22 limit £m**	**2022/23 limit £m**	**2023/24 limit £m**
Authorised limit – borrowing	150	150	150	150
Authorised limit – leases	0	0	0	0
Authorised limit – total external debt	150	150	150	150
Operational boundary – borrowing	140	140	140	140
Operational boundary – leases	0	0	0	0
Operational boundary – total external debt	140	140	140	140

Prospects for interest rates

9.15 The Council has appointed Link Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates.

Maturity structure of borrowing

9.16 Managing the profile of when debt matures is essential for ensuring that the Council is not exposed to large fixed rate sums falling due for re-financing within a short period, and thus potentially exposing the Council to additional cost. The table below sets out current upper limits for debt maturity.

Table 9: Debt Maturity Profile in %

Debt Maturity Profile Limits	Actual as at 31/03/20	Upper Limit 2021/22
	%	%
Under 1 year	4	15
1 to 2 years	2	15
2 to 5 years	9	25
5 years to 10 years	25	50
More than 10 years	11	50
Over 20 years	49	50
Total	**100%**	

9.17 In the event that there is a much sharper rise in long and short-term rates than currently forecast, then the balance of the loan portfolio will be re-visited with a view to taking on longer term fixed rate borrowing in anticipation of future rate rises.

<u>Investment strategy</u>

Treasury Investments

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

9.19 The Council's policy on treasury investments is **to prioritise security and liquidity over yield**, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other Local Authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both short-term and medium-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

The Council's Statement of Investment Beliefs can be found in **Appendix G.**

Table 10: Treasury management investments in £millions

	31/03/20 Actual £m	31/03/21 Estimate £m	31/03/22 Estimate £m	31/03/23 Estimate £m	31/03/24 Estimate £m
Short Term Investments	8.5	8.0	8.0	8.0	8.0
Medium Term investments	5.1	5.1	5.1	5.1	5.1
Long Term Investments	28.1	28.1	28.1	28.1	28.1
TOTAL	**41.7**	**41.2**	**41.2**	**41.2**	**41.2**

9.20 Further details on treasury investments are contained within **Appendix H** the Treasury Management Strategy.

9.21 Governance- Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Chief Finance Officer (s151) and staff, who must act in line with the Treasury Management Strategy approved by Council. Regular reports on treasury management activity are presented to the Investment Sub-Committee.

Service Investments-Loans and Shares

9.22 Loans- the Council makes investments to assist local public services; including making loans to local service providers, local small businesses to promote economic growth and the Council's subsidiaries that provide services. 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 generate a profit after all costs.

9.23 Security- the main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. To limit this risk, and ensure that total exposure to service loans remains proportionate to the size of the Authority, upper limits on the outstanding loans to each category of borrower have been set as follows:

Table 11: Loans for service purposes in £ millions

Category of borrower	31.3.2021 Forecast			2021/22
	Balance owing	Loss allowance	Net figure in accounts	Approved Limit
Subsidiaries	15.070	0	15.070	19.3
Suppliers	1.350	0	1.350	2.6
TOTAL	**16.420**	**0**	**16.420**	**21.9**

9.24 Accounting standards require the Authority to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Authority's Statement of Accounts from 2018/19 onwards are shown net of this loss allowance. However, the Authority makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.

9.25 Risk assessment- The Council assesses the risks of loans prior to arrangement. The loan to the supplier is partly secured on a fixed asset and the balance is secured against a cash deposit.

Shares

9.26 Security- One of the risks of investing in shares is that they fall in value meaning that the initial outlay may not be recovered. To limit this risk, upper limits on the sum invested in each category of shares have been set as follows:

Table 12: Shares held for service purposes in £ millions

Category of company	31.3.2021 Forecast			2021/22
	Amounts invested £m	Gains or losses £m	Value in accounts £m	Approved Limit £m
Subsidiaries	5.253	0	5.253	11.000
TOTAL	**5.253**	**0**	**5.253**	**11.000**

9.27 The Council currently has one Service Loan to a supplier (Freedom Leisure - £2.225m) who provides the Council's outsourced leisure services. The other loan £15.070m is with the Council's subsidiary Gryllus Property Ltd. The Council has created an Income Equalisation Reserve with an initial balance of £150,000 to finance any diminution in value of the investment and loan to Gryllus or any non-repayment of the Freedom Leisure Loan in future years. The reserves will also be used to smooth income from the investment property portfolio due to voids or non-payments. The 2020/21 budget allows for a further contribution of £250,000 to this reserve with additional annual contributions of £100,000 currently budgeted for in the MTFS. The provision for loss will be reviewed annually.

9.28 Risk assessment- The investment in shares totalling £5.253m is within the Council's subsidiary Gryllus Property Ltd. The Authority assesses the risk of loss before entering into and whilst holding shares by assessing the current and future return achievable and the level of security provided by the assets of the company, and the level of control which the Council can exert over the strategy of the company. Gryllus is 100% owned and controlled by the Council. The Council also takes independent financial advice on investments. The Income Equalisation Reserves will help mitigate the risk of any loss of income from the Council's investments allowing time to formulate plans to address any longer-term reductions in income.

9.29 Liquidity- The funding of long term investments in the Council's subsidiary are financed by fixed long-term borrowing, so that there is no short or medium-term risk to the liquidity of the Council, which would require the Council to be forced to liquidate its asset in the company.

9.30 Non-specified Investments- Shares are the only investment type that the Authority has identified that meets the definition of a non-specified investment in the government guidance. The limits above on share investments are therefore also the Authority's upper limits on non-specified investments. The Authority has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

9.31 Governance- Decisions on service investments are agreed by Executive Leadership Team led by the Chief Executive in consultation with the Chief Finance Officer and must meet the criteria and limits laid down in the Investment Property Strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

10. Property Investment

10.1 With Central Government financial support for local public services declining, the Council invests in commercial and residential property principally within the local area in pursuit of primarily economic development objectives and also lends to its subsidiary Gryllus Property Ltd.

Table 13: Property held for socio economic and/or development purposes in £ millions

Property		**Actual**	**31/03/2020 Actual**	
	Year of Purchase	**Purchase cost £m**	**Gains or (losses) £m**	**Value in accounts £m**
Redstone House	1975/76	0.120	0.387	0.507
Linden House	2018/19	4.434	0.155	4.589
Village Health Cub	2018/19	0.860	0.076	0.936
Quadrant House	2019/20	15.495	-	15.495
TOTAL		**20.909**	**0.618**	**21.527**

10.2 Security- In accordance with government guidance, the Authority considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.

10.3 A fair value assessment of the Authority's investment property portfolio has been made within the past 12 months, and the underlying assets provide security for capital investment. Should the 2020/21 year-end accounts preparation and audit process value these properties below their purchase cost, then an updated investment strategy will be presented to full council detailing the impact of the loss on the security of investments and any revenue consequences arising therefrom.

10.4 Risk assessment**-** The Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include near-term and longer-term risks, e.g. vacancies, fall in capital value, etc. These risks are managed by ensuring leases are with tenants of good financial standing and there is considerable before break clauses apply and the properties are of good quality in good locations. A varied portfolio will be acquired in diverse sectors thus spreading the risk. The Authority assesses the risk of loss before entering into and whilst holding property investments through independent advice sought from advisers. The Council has a risk matrix for assessing the quality of the investment to measure the suitability and risk of the investment, this is contained within the Investment Property Strategy. To further mitigate risk, a provision will be set aside from rental income to mitigate the risks of voids and only properties with a significant period before the next break clause.

10.5 Liquidity- Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice and can take a considerable period to sell in certain market conditions. The funding of long term investments in the Council's subsidiary are financed by fixed long term borrowing, so that there is no short or medium-term risk to the liquidity of the Council, which would require the Council to be forced to liquidate its asset and suffer a loss nor impact upon the Council's provision of services. As these long-term investments are matched by long-term borrowing, it will not be necessary to access the invested funds in an emergency. Investments in property are not undertaken unless they are secure over the medium term and the target rate of return significantly exceeds the annual cost of borrowing.

10.6 The Council's strategy for these property investments is covered by the Investment Property Strategy.

10.7 Governance- Decisions on property investments are made by the Chief Executive and Strategy and Resources Committee in line with the criteria and limits approved by Council in the Investment Property Strategy. Property acquisitions are also capital expenditure and purchases will therefore also be approved as part of the capital programme.

10.8 Further details on commercial property investments and limits on their use are set out in the Investment Property Strategy.

11. Liabilities

11.1 The Council is committed to making future payments to cover its pension fund deficit (valued at £50.9m). This is revalued on a triennial basis, with the next valuation due in 2022. Payments are made based on a calculated contribution rate.

11.2 Governance- Decisions on incurring new discretional liabilities are taken by Executive Leadership Team in consultation with the Section 151 Officer. The risk of liabilities crystallising and requiring payment is monitored by Finance and reported as and when they are identified as part of regular financial monitoring.

11.3 Loan Commitments and Financial Guarantees

Although not strictly counted as investments, since no money has changed hands yet, loan commitments and financial guarantees carry similar risks. The Council has given no further formal loan commitments or guarantees to Gryllus Property Limited, Freedom Leisure or any other organisation. However, the Council would consider any request for funding from its Gryllus Property Limited if required, subject to a suitable business case.

12. Proportionality

12.1 The Authority does not plan to be dependent on profit generating investment activity to achieve a balanced revenue budget. **Table 14** below shows the extent to which the expenditure planned to meet the service delivery objectives and/or place making role of the Authority is dependent on achieving the expected net profit from investments over the lifecycle of the MTFS. Should it fail to achieve the expected net profit, the Authority's contingency plans for continuing to provide these services will be to set side rental income in an income equalisation reserve and income will only be released from the reserve when earned. Income will only be used to support expenditure initiatives which by nature represent one-off spending or are easily curtailed. Income from rental income will not be used to support statutory responsibilities.

Table 14: Proportionality of Investments

	2019/20 Actual £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
Net Revenue Stream	11.860	10.600	10.446	10.232	10.576
Investment rental income	0.746	0.742	0.905	0.914	0.923
Proportion	6.3%	7.0%	8.7%	8.9%	8.7%

13. Revenue Budget Implications

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

Table 15: Prudential Indicator: Proportion of financing costs to net revenue stream

	2019/20 Actual £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
Net revenue stream	11.860	10.600	10.446	10.232	10.576
General Fund-Financing costs	(0.268)	0.357	0.406	0.880	0.979
Proportion of General Fund net revenue stream	(2.3%)	3.40%	3.9%	8.6%	9.3%

13.2 Sustainability- 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 Section 151 Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable.

14. Knowledge, Skills, Capacity and Culture

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

14.2 Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Link Asset Services as Treasury advisers and employs property advisers to carry out valuations and advise on property purchases. This approach is more cost effective than employing such staff directly and ensures that the Council has access to knowledge and skills commensurate with its risk appetite. Senior staff maintain their skills and knowledge up to date by attending technical briefings, circulars from Treasury advisers and CIPFA treasury workshops. The Council also provides training for Councillors who are involved with Treasury matters.

APPENDIX A

INVESTMENT PROPERTY STRATEGY 2021/2022

Introduction

1. The Investment Property Strategy forms part of the Council's overall Capital, Investment & Treasury Management Strategy and is included with the fund performance monitoring and reporting procedures.

2. The returns from property investment will contribute positively towards the achievement of savings targets *and budgets* to enable the continued delivery and investment in key frontline services and/or the bolstering of financial reserves whilst achieving a balanced budget.

3. The Investment Property Strategy aims to provide a robust and viable framework for the acquisition of property towards the pursuance of redevelopment and regeneration opportunities that can deliver positive returns and/or significant benefits to our residents, businesses and communities.

4. The strategy is to set out how the investment property portfolio will be managed and covers the following matters:

    - Objectives and strategic priorities for Investment Property;
    - Governance and performance reporting arrangements;
    - Risks;
    - Portfolio Mix;
    - Funding, Performance monitoring and Financial Indicators for Investment Property;
    - Investment evaluation criteria;
    - Acquisition procedure; and
    - Disposal Procedure

Background

5. The Local Government Act 2003 (the Act) and supporting regulations requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code and MHCLG Investment Guidance (the Guidance) to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

6. The Local Government Act 1972 – Section 120 of the Local Government Act 1972 empowers Local Authorities to acquire by agreement "any land whether situated inside or outside their area for the purpose of any of their functions under this or any other enactment, or for the benefit, improvement or development of their area".

7. The Localism Act 2011 – Part 1, Section 1 of the Localism Act 2011. Local Authorities are allowed to confer powers for a commercial purpose or for the benefit of the Authority, its area or residents.

Government Guidance

8. In February 2018 the Secretary of State issued new guidance on Local Government Investments (the Guidance) which widened the definition of an investment to include all the financial assets of a Local Authority as well as non-financial assets held primarily or partially to generate a profit.

9. The Guidance requires the Investment Property Strategy to be approved by Full Council on an annual basis and sets out the disclosure and reporting requirements. Any midyear material changes will also be subject to Full Council approval. Further CIPFA guidance issued in November 2019 reinforces the need for a comprehensive Investment Property Strategy.

10. In November 2020 *HM Treasury published their conclusions from the consultation regarding the use of monies lent by the Public Works Loan Board (PWLB).* “In recent years a minority of Local Authorities have borrowed substantial sums from the PWLB to buy investment property with the primary aim of generating yield.

11. *New guidelines have been brought in for PWLB borrowing which mean that borrowing for yield purposes only will not be possible without using other sources of finance, which would almost certainly mean increased costs for the Council. Borrowing for yield through the PWLB will exclude the Council from all other future PWLB borrowing whatever the purpose. This would cause significant problems and increase costs, in particular for the funding of affordable housing development and essential works through the Housing Revenue Account. Other sources of finance are unlikely to be at such competitive levels.*

Objectives and Strategic priorities for the Property Investment Portfolio

12. The objective of the Investment Property Strategy is to establish a framework for the identification of property investments which, if acquired, would either provide the Council with a positive rental return and capital growth or provide significant regeneration and/or development opportunities for the District. When making investments the Strategy & Resources Committee will have regard not only to the potential for positive rental returns and capital growth but also to the likely economic, social and environmental benefits for the residents and businesses of the Council.

13. *The Council has considered the potential outcome of the HM Treasury consultation through 2020. Mindful of the economic climate, organisational attitude to risk and the Council’s financial position. It anticipated the outcome of the Consultation and has recently moved away from acquisitions of commercial property for yield*

14. *The Investment Evaluation Criteria* ***(Annexe A)*** *and the Acquisition and Disposal Procedure* ***(Annexe B)*** *remain applicable as they cover good practice of all property purchase circumstances.*

15. In delivering the strategy over the next year the following main priorities are to be used to guide the growth of the investment property portfolio:

    a) A major driver for acquisition of new investment property will be economic benefit for the residents of the Council either through protection of commercial space or employment generation/protection; and
    b) Properties that have a development potential will also be considered for their long-term benefits.

    Investments will be mainly focussed within the District boundary. It is not considered that there will many opportunities for properties outside the District over the next three years of the Investment Property Strategy which will align with the Council’s priorities

16. Investment relating to the Investment Property Strategy will be directed towards:-

Regeneration and Development Opportunities

Investment which can facilitate/generate regeneration or economic development benefits as well as positive financial returns for the Council. Financial returns for the Council may come in the form of increased business rates or New Homes Bonus where the Investment is within the District.

The Contributions from Regeneration and Development Investments will include positive financial returns for the Council and may also include the following:

- Regeneration benefits for the area including employment opportunities;
- Economic benefits for the area;
- Social value improvements e.g. place-making, public realm space, pride in one's local area and surroundings; and
- Environmental improvements e.g. demolition or refurbishment of old, inefficient and/or vacant/unsightly properties.

Economic, social and environmental benefits collectively make up the strategic value of an asset, and collectively, they can drive inward private investment and prosperity for an area.

Governance and Performance

17. The Strategy and Resources Committee will be responsible for approving the strategic priorities and the arrangements set out in this policy. There will be an annual report to the Committee that will set out performance over the previous year and plans for the next.

18. Operational management, including acquisitions is to be delegated to officers acting within Financial Regulation 17 of the Council Constitution

    a) The Chief Executive, in consultation with Members as per Standing Order 46 of the Council's Constitution (Part B)[1], has delegated authority for acquisitions up to £10m; and
    b) The Committee process will be used for acquisitions above £10m

19. The Council recognises that investing in land and properties is a specialist and potentially complex area. The Council will require the services of professional property, legal and financial advisers, where appropriate, in order to access specialist skills and resources to inform the decision-making process associated with the strategy.

20. The Executive Head of Communities shall lead on potential purchases and development opportunities that meet the pre-determined selection criteria contained within the strategy. The criteria to evaluate potential acquisitions is attached as **Annexe A**. The Asset Management team will identify opportunities based on the selection criteria, will co-ordinate all necessary due diligence in accordance with the Acquisition Procedure **(Annexe B),** and will present a business case for challenge and scrutiny to the relevant Committee or Chief Executive as required under Financial Regulation 17.

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[1] Standing Order 46 prescribes that: (i) if the Council is in a state of no overall control (i.e. where no single political group or a coalition of groups has an absolute majority of seats) such consultation shall be with the Leaders, or their nominated representatives, of political groups comprising ten or more Councillors; or
(ii) if a single political group or a coalition of groups forming the Administration has an absolute majority of seats, such consultation shall be solely with the Leader(s) of the Council or his / her / their nominated representative(s).

21. CIPFA Guidance requires that elected members and officers involved in the investment decision-making process have appropriate capacity, skills and information to enable them to take informed decisions as to whether to enter into a specific investment. In addition, it places a duty on the council to ensure that advisors negotiating deals on behalf of the Council are aware of the core principles of the prudential framework and the regulatory regime in which the council operates.

22. The Council recognises that it is responsible for property investment decisions at all times and will ensure that undue reliance is not placed upon our external service providers.

23. The Executive Head of Communities is to be accountable for the performance of the investment property portfolio and will be charged with making recommendations to the Chief Executive for acquisitions.

24. Disposal of investment property assets are to be undertaken in accordance with the Council's Financial Regulations and delegated Authorities. The Executive Head of Communities will make recommendations to the Strategy & Resources Committee and in accordance with officer delegated powers.

25. The Strategy and Resources Committee delegates the Freehold Disposal of assets in the General Fund worth less than £250,000 to the Chief Executive, in consultation with Members as per Standing Order 46 of the Council's Constitution (Part B)[2] . Leasehold disposals of General Fund assets of up to 16 years and with an annual rental valuation of up to £75,000 are also delegated to the Chief Executive, in consultation with Members as per Standing Order 46 of the Council's Constitution (Part B)[3].

Risk Assessment

26. Property investment has its own specific risks, set our below:

   a) **Property Risks –** the property market is cyclical and is affected by the wider economic environment. There are also property risks that are specific to a building due to its location, condition and quality of the tenants. Mitigation proposed in this policy for these risks include diversifying the portfolio (portfolio mix) to include investments that perform during different cycles of the economic cycle. The evaluation criteria, diversity of location, due diligence tests, approval processes and accountability for implementation are also proposed to address property specific risks;

   b) **Financial Risks –** the primary financial risks are borrowing levels, interest rate movement, ongoing ability to service debts, the general investment market conditions and its effect on rental income. Proposals have included the creation of a fully owned subsidiary property investment company, Gryllus Property Ltd and a funding strategy that allocates debt and all associated costs to the investment property portfolio so that the net revenue benefits to the Council is transparent and can be benchmarked; and

   c) **Corporate Risks –** effective delivery of the Strategy requires staff with the requisite expertise, effective arrangements for asset management and the recognition of the reputational risks that can come from inappropriate tenants and from legal and environmental breaches. In accordance with the Statement of Investment beliefs as we

[2] As per footnote 1 on the previous page
[3] As per footnote 1 on the previous page

are investing public money we will be sensitive to the ethical considerations of local residents.

27. The Council assesses the risk of loss before entering into and whilst holding property. The approach is laid out in **Annexe A** – Investment Evaluation Criteria.

Liquidity

28. Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice and can take a considerable period to sell in certain market conditions. The funding of long-term investments is financed by fixed long term borrowing, so that there is no short or medium-term risk to the liquidity of the Council, which would require the Council to be forced to liquidate its asset and suffer a loss nor impact upon the Council's provision of services. As these long-term investments are matched by long-term borrowing, it will not be necessary to access the invested funds in an emergency. Investments in property are not undertaken unless they are secure over the medium-term, have additional socio- economic benefits and the target rate of return significantly exceeds the annual cost of borrowing.

Portfolio Mix

29. The medium and long-term aims of this Strategy have been adjusted following the publication of the HM Treasury consultation to:

    a) Acquire properties mainly within the District in areas with strong sustainable economic activity i.e. areas with the environmental and business activities capable of providing an economy whereby capital and rental growth over the mid to long term was possible;
    b) When making investments the Strategy and Resources Committee will have regard to other economic and social benefits for the residents of Tandridge; and
    c) Achieve a balanced portfolio where **after 6 (was 4) years** no single class of property, ie retail, industrial, office and leisure is larger than 60% and none smaller than 10%, other than retail or leisure.

Contribution

30. The Council has previously invested in commercial property with the intention of making a surplus that will be spent on local services and for socio- economic benefits. The portfolio is at an early stage of development.

31. **Table 1** shows the properties currently held by Tandridge District Council for Investment Purposes, by type.

Property by Type	Type	Value in Accounts 31st March 2020 £m
Offices	Offices	20.591
Leisure	Leisure	0.936
Total		**21.527**

32. Investments held under Gryllus Holdings are reported separately.

33. Income from Investment Property

	31st March 2020 £m	31st March 2021(forecast) £m
Income	0.746	0.742

Funding and Financial Performance of the portfolio

34. The Council will fund investment property acquisitions by utilising the most appropriate and efficient funding strategy available at the time of purchase. The Council has the option of utilising long-term prudential borrowing, capital receipts or reserves. Financing decisions will link to the Council's Capital & Investment Strategy and Treasury Management Strategy.

35. All new acquisitions are to achieve an appropriate positive return net of borrowing and other costs associated with the acquisition. *Properties purchased for redevelopment, refurbishment or regeneration may not provide an immediate positive return. These will be assessed through a comprehensive business case and considered by Strategy & Resources Committee*

36. Separate accounts are to be kept for income and expenditure in connection with investment property and are to be included in the Annual Report to the Strategy & Resources Committee.

37. Key Indicators have been adopted to monitor performance of the portfolio. Performance will be reported against the following indicators along with a property market narrative:

- **Total Return** – the annual increase in capital value plus income expressed as a percentage of the previous year's capital value (adjusted to include purchases);
- **Effective Return** – total return receivable less costs expressed as a percentage of the previous year's capital value;
- **Growth in Asset Value** – Percentage increase per year;
- **Income Growth** – Percentage increase in gross income per year; and
- **Vacancy Rate –** Expressed as a percentage and number of vacant units compared with total number of units. This will also be expressed in terms of lost rental. Void periods are factored into financial appraisals as part of the assessment criteria.

	2019/20
Total Return	6.42%
Effective Return	3.31%
Growth in Asset Value	281%
Income Growth	407**%**
Vacancy Rate	No Vacant buildings. Quadrant House is 33% vacant

38. In addition to property specific performance indicators are quantitative indicators that will be reported within the Council's Capital & Investment Strategy and Treasury Management Strategy to allow Councillors and the Public to assess a local authority's total risk exposure as a result of property investment decisions.

39. The operating cost of the Council's internal Strategic Asset Management Team excluding the Housing Development Specialists is projected to be c£145k for the year 2020/21, (£c£202k - 2019/20). The costs reflect the cost of managing the Council's entire property portfolio and *functions*, not just the assets acquired under this Investment Property Strategy. Additional costs may be incurred as a result of the purchase of Investment Properties. Any such costs will be factored into the financial appraisals as part of the purchase assessment to ensure that anticipated net rates of return are achieved.

Investment Property Strategy - Annexe A

Investment Evaluation Criteria

40. As with other forms of investment at the most basic level, property investment is a trade-off between risk and return. A traditional well diversified property portfolio (spread across different property sectors and geographical areas) will deliver long-term rental and capital growth with relatively low risk.

41. Prime property in the target region covered by this strategy will typically provide an initial yield of between 5 –7% with the additional prospect of capital growth leading to a higher total return to the Council. Equivalent /Income yields over longer periods will also be reported.

42. The four main commercial property sectors will be included (industrial, office, retail and leisure) and in turn, these will be additionally diversified on criteria including location, the lease term and lot size. This will assist in protecting the councils overall risk return profile should an individual property investment cease to be income producing (for example, it is undergoing refurbishment or awaiting a new tenant). Residential and mixed used sites will be considered using similar criteria albeit for residential investments lease terms and repairing obligations are likely to be very different. Regeneration opportunities and potential development sites will be considered using additional criteria, including if a development appraisal shows strong potential or if there is strong asset management potential.

43. The following Criteria are to be used to make decisions on acquiring new property investment properties:

    a. **Location** – Property is categorised as prime, secondary or tertiary in terms of its location desirability. For example, a shop located in the best trading position in the town would be prime, where as a unit on a peripheral neighbourhood shopping parade would be considered tertiary;
    b. **Tenant covenant** – the financial strength of a tenant determines the security of the property is rental income. A financially weak tenant increases the likelihood that the property will fall vacant. The minimum acceptable financial strength for any given tenant will be determined through financial appraisal of company accounts and the use of appropriate methods of risk assessment and credit scoring. To minimise management and risk, the preference will be for single occupancy investments wherever possible;
    c. **Lease terms** – the lease is to be free from unencumbered/onerous terms. The lease must have mechanisms for the rent to be periodically reviewed to take into account inflation and upward market movement;
    d. **Occupational lease length** – the lease term will determine the duration of the tenant's contractual obligation to pay rent. The most attractive investments offer a long lease with a strong tenant covenant. The lease term will reflect any tenant break clause;
    e. **Building quality** – a brand-new or recently refurbished building will not usually require capital expenditure for at least 15 years. This is attractive for income investors requiring long-term rental income with a minimum of ongoing capital expenditure;
    f. **Tenure and Title** anything less than a freehold acquisition will need to be appropriately reflected in the price. The legal title is required to be clean and free from any onerous conditions.;
    g. **Tenant repairing obligations**. – Under a full repairing and insuring lease (FRI), the tenant is responsible for the building's interior and exterior maintenance/repair. The obligation is limited to the building's interior under an internal repairing and insuring lease (IRI). The preference will be to favour FRI terms (or FRI by way of

service charge i.e. all costs relating to occupation repairs are born by the tenants administered through a service charge; and

h. **Lot size –** to maintain portfolio balance the preference will be for no single property to exceed *£25 million* for a single let property.

In addition, it must -

a. Have passed a **building and plant survey**;
b. Show a **positive return** after making allowance for financing costs, borrowing repayments and other associated costs;
c. Be supported by an Independent **RICS Red Book Valuation; and**
d. Be accompanied by a **full business case report** prepared by the Head of Strategic Asset Management and other officers where relevant.

Each potential property investment will undergo a quantitative and qualitative appraisal and risk assessment to establish portfolio suitability and the legal and financial implications of the purchase.

All due diligence findings will be included in the reporting procedure. The business case is to include reference to all areas above, the financial modelling, a risk assessment matrix and Strengths, Weaknesses, Opportunities and Threats (SWOT) analysis.

An investment opportunity that does not meet the minimum criteria and investment criteria may have separate investment or regeneration benefits and therefore may be considered separately under the regeneration and development stream of the strategy.

For a regeneration or development opportunity to be considered by the Council it must:

a. Deliver a rate of return commensurate with the deemed level of risk associated with the investment. The financial returns from regeneration activities may be capital rather than revenue. If the returns are capital all the full costs will be capitalised; and
b. Be accompanied by a full business case prepared by the Executive Head of Communities and other officers where relevant.

Some of the above criteria may be relaxed if the property is of strategic value to the Council and has gained Strategy & Resources Committee Approval. Strategic Value may be seen where a property is close to significant Council land ownership, a property gives economic benefits through Council ownership and or there are opportunities to change the use in accordance with Council priorities.

Investment Property Strategy - Annexe B

Acquisition Procedure

44. Acquisition of new investment properties is to follow the following process:

<table>
<tr><th>Activity</th><th>Acquisition Stage and Timeline Guide</th></tr>
<tr><td>a) Property identified as a potential investment by Asset Management or by Agents
b) Property to be discussed with in house Legal team for initial review
c) Executive Head of Communities to notify Chief Executive and the Investment Property Group (includes Head of Legal & Head of Finance) of potentially suitable property and summarise to seek views
d) If possible, obtain desktop valuation from suitably qualified and experienced Valuer
e) Review the valuation against the cost of Borrowing with Finance
f) Finance to undertake search of tenant to ascertain the tenant’s current financial status
g) Finance to produce initial financial appraisal</td><td>Initial Review
2 to 3 weeks</td></tr>
<tr><td>h) Make offer for property, subject where appropriate to any of the following:
• Contract
• Approval by Chief Executive, or relevant Committee
• RICS Red Book valuation carried out by external Registered Valuer (independent of introducing Agent)
• Searches
• Legal due diligence to include receipt and analysis of all leases to determine landlord’s financial obligations
• Disclosure of freehold title and review to ensure clear of any onerous restrictions.
• Pre-acquisition survey by chartered building surveyor to include, if appropriate, structural, mechanical and electrical survey
• Internal inspection
• Valid Energy Performance Certificate
• Disability Discrimination Assessment if appropriate
• Environmental desktop study if search suggests one is appropriate
• Asbestos Survey if appropriate
• Resolution of any TUPE transfer implications
• VAT
• Insurance requirements
• Tax implications</td><td>Under Offer
3 to 4 weeks</td></tr>
</table>

If offer accepted: i) Instruct legal services to deal with contract documentation, searches and legal due diligence j) Instruct valuation k) Instruct surveys l) If appropriate based on any of the above, propose adjustment to purchase price to reflect the monetary value of any issues discovered.	
m) Complete any outstanding surveys/ M&E reports and resolve all contractual matters before exchange n) Complete TDC Strategic Asset Management Acquisition Checklist o) Complete full Business Case for approval in accordance with Financial Regulation 17. p) Following agreement of terms and before instructing exchange of contract prepare Record of Officer Delegated Decision Notice and advise Leader of the Opposition and Ward Councillors if located in the District prior to publication date q) Arrange for transfer of funds r) Arrange Insurance Cover s) Exchange Contracts, if not simultaneous with Completion	Exchange 1-2 weeks
t) Complete purchase. All Documents and Management handed over to Asset Management to take forward as appropriate.	Completion 1 day

45. Newly purchased property acquired under this strategy would be added to the existing portfolio. The Asset Management Team would undertake management to maintain and improve the performance of an investment property; or additional specialist resources may need to be brought in as required.

Disposal Procedure

46. Properties will be considered for sale based on their performance and fit for the portfolio.

47. Any property considered for sale should be appropriately marketed. If an off-market approach is made and considered the property would not be sold unless the price offered is in excess of an independent Red Book Valuation to support such a decision

48. A property will be disposed of in accordance with the Financial Regulations of the Council's Constitution and in line with the Delegated Authority provisions in place. The Executive Head of Communities will make recommendations to the Strategy & Resources Committee and in accordance with officer delegated powers.

CAPITAL STRATEGY PRINCIPLES

Executive Leadership Team led by the Chief Executive lead the strategic direction of capital investment for the Council.

All schemes already approved in the 2020/24 Continuing Capital Programme or contractually committed will be supported and sufficient resources will be provided to enable them to proceed or complete. These schemes are presented in Appendix E, Current Capital Priorities.

A capital project sponsor for a new bid must also be able to demonstrate that a rigorous process of options appraisal has been followed, requiring evidence of need, cost, risk, outcomes and methods of financing. Capital investment proposals which will result in a revenue cost saving, income generation or efficiency are encouraged. The Executive Leadership Team has a clear role in ensuring that all the key questions have been asked at the initiation stage of a project.

All capital investment decisions will be made with reference to Council objectives and regional strategies and, only after a positive contribution to one or more of the objectives has been demonstrated, is a project to be considered for resource allocation. There will be no ring-fencing of capital receipts to specific projects. Any in year Capital scheme approvals will be included in the current Capital Programme and reported to the relevant Committee.

The Capital Strategy will support the implementation of the approved Investment Property Strategy by the allocation of resources and facilitating the introduction of activities required to promote the objectives of the strategy.

For the purposes of preparing the Capital Programme for 2021/22, an assumption has been made that any funding relating to slippage in capital projects at the end of 2020/21 will be carried forward into 2021/22 to fund the completion of the projects. However, carry forward of slippage will not be automatic; a robust business case and spending profile will need to be made for any carry forward funds. Where an underspend occurs, this will be returned to the Council Capital resources and will be used to fund new capital priorities. Funding for any overspends will be taken from the Council’s uncommitted capital resources.

As well as using traditional funding mechanisms to finance capital schemes, the Council will also consider the use of new initiatives and develop these options if it is considered financially advantageous in the context of the Council achieving its capital investment objectives.

The Council is conscious that the Government could in the future introduce a range of grant funding opportunities for which bids must be submitted at short notice, some of which may have a matched funding requirement. The Council will respond as it considers appropriate to bidding opportunities, ensuring that bids are submitted which align with its objectives and capital investment priorities and that matched funding requirements are considered on a scheme by scheme basis with resource requirements prioritised accordingly.

The Council will work in a collaborative manner with Surrey County Council, Surrey Police & NHS.

Regard will be given during the appraisal process to ensure that the Council’s capital investment priorities are achieved. The Capital Programme 2020-2024 set out at Appendix F reflects the Council’s current Strategies and Priorities.

APPENDIX C

CORPORATE GOVERNANCE

Executive Leadership Team

Executive Leadership Team (ELT), which comprises the Executive Heads of each Department lead by the Chief Executive, is the officer body for Capital Investment development and planning and is charged with bringing forward funded capital expenditure plans for approval by the Strategy and Resources Committee. The Committee considers capital expenditure and funding plans, monitors performance through a series of regular capital monitoring reports and recommends the annual Capital Programme to Council for approval.

All capital investment will be commissioned on the recommendation of the ELT which will enable any expenditure and it's funding to be aligned with the Council's Key Capital Priorities and funding sources. Partners, from both the public and private sector will be at regional and local levels as well as at a District level.

Approval of Capital Investment

Within the Council, a concept for a potential capital project will originate from, or at least be 'owned' by the Executive Head. The 'owner' should prepare or direct the preparation of a Strategic Business Case (SBC) for the proposed project. The Strategic Business Case outlining the initial idea or 'concept' for a project should be submitted to ELT for consideration.

If ELT is satisfied that the proposal meets investment criteria, it will be given approval to progress to Stage 2 of the process – the completion of an Outline Business Case (OBC).

The OBC builds on the SBC providing more detailed information including the benefits that could be realised focusing on the links to the Council's Capital Investment Priorities and the proposed outcomes and may include several options to deliver the proposed benefits. The OBC will be submitted to the ELT for consideration, and if it is satisfied with the proposal will give guidance for the development of a preferred option.

Stage 3 of the process entails the completion of a Final Business Case (FBC) which will then be submitted to the ELT for final consideration. Again, building on the OBC, the FBC will contain evidence of a:

- Full option appraisal;
- Detailed financial analysis of all costs/income including how the project is financially sustainable and that any adverse revenue implications can be dealt with within existing budgets;
- Robust delivery plan including how the chosen option delivers the highest impact in achieving the required outcomes with identified key project milestones enabling progress review. Included within the delivery plan should be proposed consultation arrangements, value for money assessment equality and environmental impact assessments;
- Risk assessment and that appropriate actions to negate these risks have been identified;
- Full exit strategy where the project involves a disposal; and
- Method of procurement that represents value for money.

Depending on the circumstances of the bid for resources, ELT has the discretion to vary the three-stage review process and omit one or more of the stages. Once Final Business Cases have been agreed, these bids will be prioritised against agreed criteria

The results of this process will be presented to Members each year as part of the capital budget setting process, or during the year if projects come forward outside the normal timeframe.

Service Challenge & Review, Efficient Use of Assets

With regard to the review of operational assets, the Asset Management Team and services continue to work closely with service managers alongside wider public and third sector partners to ensure that portfolios are best fit for purpose and efficient usage is maximised.

The Chief Executive and ELT will oversee any acquisition and disposal of land and property assets and monitors the progress of any corporate disposals and performance of the investment portfolio.

In terms of acquisition of property there is a specific process for this under Financial Regulation 17 to enable proposals to progress in year. Details of this are set out in the Investment Property Strategy.

Performance Monitoring of Capital Programme

The capital expenditure investment approach above is supported by a strong programme management process to ensure a coordinated corporate approach. This will ensure that investments are planned, managed and delivered prudently.

ELT has a remit to review the financial performance of the capital programme and it receives a monthly monitoring report. In addition, financial monitoring reports will be considered by Service Committees periodically throughout the year, together with a capital outturn report. Issues that have been considered and agreed at ELT can be reported to Service Committees as necessary via the regular financial monitoring reports.

The undertaking of the detailed annual review of the capital programme provides the opportunity to review all schemes or focus on specific areas of concern.

Where a potential cost overrun has been identified, ELT will explore possible solutions in detail. It will also consider any underspending or identified surplus resources which can be added to the central pool of resources. ELT may also suggest a reallocation of resources to other projects.

Where there is a delay in the commitment of programme/project resources, the ELT will require project managers to report the reasons for the delay and consider whether it would be appropriate to recommend the decommissioning of the project and the reallocation of un-ring-fenced resources to other projects.

APPENDIX D

CAPITAL PROGRAMME 2021/24

Proposed Capital Programme	2021/22	2022/23	2023/24	Total 2021-24
Housing HRA				
Structural Works	835,000	855,000	830,000	2,520,000
Modernisation & Improvements	439,000	732,000	511,000	1,682,000
Energy Efficiency Works	550,500	559,500	546,000	1,656,000
Service Renewals	685,000	712,500	695,000	2,092,500
Void Works	425,000	425,000	425,000	1,275,000
Health & Safety	190,000	190,000	180,000	560,000
Adaptations for the Disabled	250,000	250,000	250,000	750,000
Essential Structural Works	185,000	185,000	185,000	555,000
Communal Services	30,000	30,000	30,000	90,000
Council House Building	12,700,000	3,705,200	301,200	16,706,400
Housing Management Software	0	0	0	0
HRA IT Hardware/infrastructure/Projects	264,200	60,600	72,200	397,000
TOTAL HRA	**16,553,700**	**7,704,800**	**4,025,400**	**28,283,900**
Housing GF				
Disabled Facilities Grant	460,000	460,000	460,000	1,380,000
Housing Enabling - General	0	0	0	0
Total- Housing GF	**460,000**	**460,000**	**460,000**	**1,380,000**
Community Services				
Children's Playground Improvements	300,900	179,200	99,500	579,600
Parks, Pavilions & Open Spaces	202,800	114,200	114,500	431,500
Grange Meadow access works	250,000	0	0	250,000
Vehicle Fleet Renewals	450,800	167,900	5,000	623,700
Collection / Containerisation	0	0	0	0
Car Park Equipment/Maintenance	34,800	34,900	35,000	104,700
Ellice Road Car Park Decking	0	0	0	0
Public Conveniences	550,000	0	0	550,000
Litter Bins	8,200	8,300	8,400	24,900
Roads&Paths at St.Mary's Church Cemetery	0	0	0	0
Land Drainage	13,700	10,000	10,000	33,700
Plant & Machinery Replacement Programme	8,000	8,000	10,000	26,000
Waste Vehicles	0	0	0	0
Garden Waste Bins	25,000	25,000	25,000	75,000
Recycling, food waste and refuse bins	90,000	90,000	90,000	270,000
Playground Improvements (Match Funding Pot)	20,000	0	0	20,000
Environmental Health Database contributon	0	0	0	0
Total- Community Services	**1,954,200**	**637,500**	**397,400**	**2,989,100**
Resources				
Council Offices Major Works Programme	0	0	0	0
Customer First/IT	0	0	0	0
IT - Hardware/infrastructure/Customer First Projects	466,600	228,000	271,500	966,100
Investment & Development Fund	0	0	0	0
Quadrant House	4,900,000	0	0	4,900,000
Land / Asset Development	0	0	0	0
Total- Resources	**5,366,600**	**228,000**	**271,500**	**5,866,100**
Planning Policy				
Capital Contributions from CIL	733,000	330,000	0	1,063,000
Total-Planning Policy	**733,000**	**330,000**	**0**	**1,063,000**
TOTAL GENERAL FUND	**8,513,800**	**1,655,500**	**1,128,900**	**11,298,200**
Total Capital Programme	**25,067,500**	**9,360,300**	**5,154,300**	**39,582,100**

APPENDIX E

SOURCES OF CAPITAL FUNDING

External Resources

External resources from Central Government and other public-sector bodies can be split into two categories:

Un ring-fenced – resources which are delivered through grant that can be utilised on any project (albeit that there may be an expectation of use for a specific purpose). This now encompasses the vast majority of Government grant funding.

Ring-fenced – resources which are ring-fenced to particular areas and therefore have restricted uses. e.g. Disabled Facilities Grant

Where there is a requirement to make an application to an external agency for external funding and, when appropriate, to commit Council resources as matched funding to any bid for external resources, a business case must be presented to the Executive Leadership Team for approval.

Internal Resources

Capital Receipts

Section 9 (1) of the Local Government Act 2003 defines a capital receipt as ''a sum received by the authority in respect of the disposal by it of an interest in a capital asset''.
Section 9 (2) of the Act defines a capital asset as ''an asset is a capital asset if, at the time of the disposal, expenditure on the acquisition of the asset would be capital expenditure''. Following the 2015 Spending Review, the MHCLG published statutory guidance on the flexible use of capital receipts for a three-year period covering 2016/17 to 2018/19. The guidance allows Local Authorities to use capital receipts to offset the revenue cost of transformational projects which are expected to deliver future ongoing revenue savings. As part of 2018/19 Provisional Local Government Finance Settlement, the Secretary of State announced an extension of this flexibility for a further three years to 2022.

In 2020/21 the Council intends to use £139,000 of 'flexible' capital receipts to fund transformation costs.

In 2020/21, the Council intends to use up to £1.5m of general fund capital receipts to fund elements of Capital Programme.

In general capital receipts arising from the disposal of housing assets and for which account is made in the Housing Revenue Account (HRA), are governed by the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. In summary the regulations require that receipts arising from:

Right to Buy (and similar) sales may be retained to cover the cost of transacting the sales and to cover the debt on the properties sold, but a proportion of the remainder must be surrendered to Central Government;

However, exemptions from the regulations were published in 2012 which enable the Council to use Housing Capital receipts to part finance the replacement of homes for rent sold under the renewed Right to Buy, including purchasing, remodelling and new build

HRA disposals may be retained in full provided they are spent on affordable housing, regeneration or the paying of housing debt.

Ring-fencing of Capital Receipts

The Council will not ring-fence or earmark capital receipts to specific projects, projects will be considered on the costs and benefits of the individual project.

Capital Receipts will be retained to support the Capital Programme as a corporate resource.

Availability of Capital Receipts

In considering the 2021 to 2024 capital programme, and given the position regarding capital receipts, a prudent approach has been taken and there has been no assumption of any additional capital receipts to finance new expenditure over and above those already known amounts underpinning the programme.

No additional general fund capital receipts have been anticipated. However as advised above, the Council anticipates using up to £1.639m of capital receipts in 2020/21 to support projects.

The level of receipts upon which the programme relies to fund existing and new commitments has in the past been affected by the property market which has impacted on the:

i) Ability of the Council to sell assets within the timescale anticipated.

ii) Level of receipt actually generated, which has sometimes been less than originally expected.

Monitoring of capital receipts is undertaken through the ELT and the Corporate Property Board (CPB); follow-up actions are initiated to address any comments raised.

<u>Revenue Contributions</u>

A service or the Council may wish to offer some of its revenue budget or reserves to support the financing of a capital project.

<u>Leasing</u>

Some of the assets used by the Council are financed by a lease arrangement, for example vehicles. With the advent of Prudential Borrowing this source of financing is less attractive. As it is usually generally a more expensive form of borrowing and there are usually costs which arise when vehicles, plant and equipment is returned in poor condition. Therefore, it is the Councils policy not to lease unless it can be demonstrated that leasing will offer value for money, when options are appraised.

<u>Section 106 Agreements</u>

In considering an application for planning permission, the Council may seek to secure benefits to an area or restrict uses or activities related to a proposed development through the negotiation of a ‘planning obligation’ with the developer. Such obligations, authorised by Section 106 of the Town and Country Planning Act 1990, generally either improve the quality of the development, or overcome difficulties which would otherwise result in planning permission being refused. A planning obligation must be:

i) Necessary to make the development acceptable in planning terms;

ii) Directly related to the development; and

iii) Fairly and reasonably related in scale and kind to the development.

As such, therefore, the Council may in some instances receive funds to enable it to undertake works arising from these planning obligations. Examples of the use of planning obligations are the:

i) Provision of affordable housing.

ii) Improvement to community facilities - Public open space/play areas, educational facilities.

iii) Improved transport facilities.

iv) Public art.

v) Renewable energy measures.

vi) Specific measures to mitigate impact on a local area - parking restrictions, landscaping or noise insulation.

The use of any Section 106 funding will be presented to the ELT for review.

Community Infrastructure Levy

The Community Infrastructure Levy (CIL) is a planning charge based on legislation that came into force on 6 April 2010. When adopted, a CIL levy allows the Council to raise contributions from new development to help pay for infrastructure that is needed to support planned growth. CIL contributions can be used to supplement other funding streams and can wholly or partly fund a variety of strategic infrastructure projects ranging from transport, green infrastructure, flood defences, education and health, subject to pooling restrictions.

Where a CIL charging schedule is in place, it largely replaces Section 106 Obligations in delivering strategic infrastructure. However, S106 would still be used for affordable housing and site development-related infrastructure requirements that are deemed necessary to make a development acceptable. Some developments would pay both Section 106 and CIL, but they would fund different types of infrastructure. Contributions may also be sought for Section 278 of the Highways Act where modifications are required to the highways network.

UK Municipal Bonds Agency Plc formerly Local Capital Finance Company

The Local Government Association (LGA) has now set up the Local Capital Finance Company (formerly known as the UK Municipal Bonds Agency) the aim of which is to seek to provide Councils with a cheaper source of long term borrowing and to introduce sector owned diversity into the Local Government lending market. The Council will keep under review the availability and cost of funds from the Company as an alternative source of finance with a view to borrowing at an appropriate time if terms are preferential.

Borrowing

The Council will investigate opportunities to resource capital projects using prudential borrowing where plans are sustainable, affordable and prudent. Full appraisal will take place to ensure that, where appropriate, sufficient revenue returns are generated to cover the cost of borrowing. This will be especially important when undertaking property acquisitions under the Investment Property Strategy where, in addition, a revenue income stream is required to support the revenue budget.

Where it is considered that Prudential Borrowing is the appropriate method of funding it will require additional revenue budget to finance the interest and minimum revenue provision.

Strategy and Resources Committee will review the detailed capital expenditure plans before allocations of resources are committed to ensure that the costs of prudential borrowing are understood and affordable.

The Council is able to take advantage of the Public Works Loans Board (PWLB) certainty rate, whereby there is a 20 basis points discount on standard loans from the PWLB under the prudential borrowing regime for authorities which provide improved information on their long term borrowing and associated capital spending plans. The obvious benefit to the Council of the certainty rate is reflected in reduced Treasury Management borrowing costs in relation to any PWLB borrowing undertaken.

APPENDIX F

ANNUAL MINIMUM REVENUE PROVISION POLICY STATEMENT 2021/22

Where the Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum previous to 2017/18. The Local Government Act 2003 requires the Council to have regard to the Department for Housing, Communities and Local Government's Guidance on Minimum Revenue Provision (the CLG Guidance) most recently issued in 2018.

The broad aim of the MHCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by revenue grant, reasonably commensurate with the period implicit in the determination of that grant.

MHCLG regulations have been issued which require the Full Council to approve the MRP Statement in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision.

The Council's MRP policy will be Asset Life Method. This basis is subject to review and changes in line with the Councils Treasury Management Strategy and approved Prudential Indicators which are revised annually.

Capital expenditure incurred during 2021/22 will be fully subject to a MRP charge from 2022/23 onwards or in the financial year after the asset becomes operational whichever is the latest. This ensures that MRP is only charged to the first, full operational year of the asset's life.

The Council is recommended to approve the following MRP Statement:-

For all unsupported borrowing (General Fund) the MRP Policy will be; Asset Life Method.

Under this method MRP will be based on the estimated life of the assets, in accordance with the regulations. This option provides for a reduction in the borrowing need over approximately the asset's life.

STATEMENT OF INVESTMENT BELIEFS

Assets

There are 3 pools of assets which have different objectives and constraints -

- *Short-term Pool*: short-term cash management, representing monies that need to be available for immediate funding needs of the Council, typically up to a period of 1 year.

- *Medium-term Pool*: where funds are not immediately required but may be required over a 1 to 5 year period. These investments will achieve a return of approximately cash base rate plus 2% as an indicative target.

- *Strategic Investment Pool*: where funds can be invested for the long term (greater than 3 years), to deliver returns in real terms, aiming to achieve additional revenue to support front line services of the council. These investments will seek to achieve the prevailing consumer price inflation (CPI) rate plus 3%.

Aims

The 3 pools have different aims. In the list above –

- *Short-term pool:* represents short-term liquid assets, which are invested to provide immediate liquidity. To manage risk, these assets are held in a way that achieves a measure of diversification. Where appropriate and after member input, the officers will from time to time investigate whether there is any possibility to move some of these funds into the medium term pool in the search for additional returns.

- *Medium-term pool:* is aimed at preserving the value of the funds in real terms in the medium term, assumed to be 1 to 5 years. Pure equity investment would generally not be an appropriate form of investment for the medium-term pool, but balanced portfolios incorporating an equity element may be appropriate.

- *Strategic Investment pool:* is aimed at preserving the value of funds in real terms in the medium to long term, while achieving revenue well in excess of the borrowing costs for the council. These investments will mainly be financed through external borrowing. Such investments may be very long term in nature and it is recognised that liquidity will be restricted. Timing of purchases and disposals is vital to preserve fund value.

Key beliefs

<u>The aims for each pool are the key drivers for asset allocation</u>

Of the three pools of assets referred to above:

- *The Short-term pool* is roughly matched to immediate or very short-term cash requirements. Therefore, the nominal value and liquidity must be preserved.

- *Medium-term pool* has no specifically defined liabilities. The prime aim is capital preservation in real terms to achieve an enhanced return over 1–5 years.

- *Strategic Investment pool* represents long-term assets and any investment strategy must seek at least to maintain the value of these assets after allowing for inflation, as well as to generate revenue in excess of the loan interest cost plus the minimum revenue provision (MRP). It is acknowledged that this cannot be achieved without accepting some risk. Where there is some conflict between any of these aims, the need to generate income exceeding the loan rate plus Minimum Revenue Provision (MRP) for the specific investment will be paramount.

Asset allocation is the main driver of performance

We believe that the performance of investment markets is the dominant aspect of investment.

Attempting to "time" markets is rarely successful as market timing introduces risk, without the expectation of return, so variations in asset allocation will be driven by other considerations rather than tactical return generation. These considerations as determined in the over-arching Treasury Management Strategy includes factors such as; credit risk, counter-party strength, security, liquidity and yield as well as interest rate risk and inflation. Asset allocation in multiple classes will also be a factor.

Costs matter and need to be managed in order to achieve value for money

Costs can materially impact the long-term value of the investment portfolio and are an important component in assessing different investment strategies and the managers appointed to invest Council assets. This does not necessarily imply that costs need to be minimised: there are often circumstances when paying extra costs will be more than compensated by rewards.

Careful management of costs is important in achieving the highest quality of returns on all our portfolios.

Investment decisions should reflect wider stakeholder views

Our stakeholders, including local residents, expect the Council to follow the highest ethical standards in all its activities. Strategy & Resources Committee members will therefore act in accordance with the Committee on Standards in Public Life's seven principles of public life, namely selflessness, integrity, objectivity, accountability, openness, honesty and leadership. We expect the investment professionals we deal with to act in a similar manner.

We are always conscious that we are investing public money and we will be sensitive to the ethical considerations of local residents.

Investment goals and performance measures need to be clearly articulated to ensure accountability

A key measure of success is the delivery of investment performance. It is important that the investment goal and the performance measures used are clearly set out to ensure full accountability, in accordance with the aims of each pool, which are respectively liquidity, capital preservation in capital terms and capital preservation in real terms with yields in excess of borrowing costs including MRP as appropriate.

Risk is multi-faceted and complex

The only investment opportunities that provide no "risk" in the sense of no possibility of unexpected negative outcomes are those that will provide negative inflation-adjusted returns. It is therefore necessary to accept some risk if positive inflation-adjusted returns are to be achieved.

A selection of appropriate performance measures will allow visibility that adequate compensation for risk taken has been achieved.

A long-term investment horizon is an advantage and a responsibility

The long-term horizon for the Strategic Investment pool brings with it the responsibility to take an appropriately long-term approach to assessing the success or otherwise of investment strategies and the advisers hired to implement our strategies.

The Strategic Investment pool and (to a lesser extent) medium-term pool have long to medium horizons which provide additional investment opportunity. This potentially allows the acceptance of less liquidity on a portion of assets. This may include extended periods of underperformance due to the long term nature of investments in the context of the aims described above.

The Strategic Investment pool will mainly invest in property

Given the constraints that apply to Local Councils, most of the Strategic Investment pool will be invested in property.

The first priority for investment will be property within the District boundary, a secondary priority will be for property outside of the District as long as this is within accepted guidelines for Local Council property investments.

When making investments the Strategy & Resources Committee will have regard to other economic and social benefits for the residents of Tandridge District.

Investment strategies and complexity need to be consistent with the governance resources available

One of the most significant constraints on investment strategy is the level of governance resources available. The complexity of strategies employed needs to be consistent with the resources available to manage them. In practice, this will normally mean that simple solutions will be preferred to complex ones unless there is a compelling reason to contemplate the complexity: this will normally be driven by a conviction that there are significant additional returns to be achieved and obtaining suitable outside professional advice to support this conviction.

What funds are available for investing?

In determining the allocation of funds to each of the 3 pools (short, medium-term and Strategic Investment pool), the Strategy & Resources Committee will, on a regular basis, consider relevant budgets, cash flow forecasts and other medium term financial projections. The main allocation will be the annual budget setting process.

Allocation of funds on this basis will normally be reviewed on at least, an annual basis, to tie in with relevant financial projections and quarterly reports from external investment advisers.

In terms of the allocation process for the medium-term pool, the Strategy & Resources Committee will have the authority to select investments in line with our investment beliefs. For investments through Gryllus, these will be in accordance with the company's individual investment objectives as an entity.

Risk Management

We will be proactive in looking at risk including assessing this in terms of the risk framework set out in both the Asset (Capital) Investment and the Treasury Management Strategy. These strategies will be approved annually by Council and will be updated as necessary to cover risk including credit risk, counter-party risk, timing risks around purchasing and disposing of strategic assets; and the over-riding public sector investment principle of security and liquidity over yield.

Counter parties will only be selected with acceptable credit ratings from the three main rating agencies: Fitch Ratings Ltd, Moody’s Investor Service inc and Standard and Poor’s Financial Services LLC.

In respect of actual investment performance and having taken any external advice considered appropriate, the Council will monitor and review performance benchmarks relevant to each investment pool and in accordance with the recommended CIPFA Investment Code of Practice.

The Council will approve an annual Treasury Management Strategy (TMS) which will be approved annually by Council and incorporated within the Budget and Medium Term Financial Strategy (MTFS).

TREASURY MANAGEMENT STRATEGY

The Council holds significant invested funds, representing income received in advance of expenditure, balances and reserves. During the first half of the current financial year, the Council's average investment balance has been around £25m-30m and the cash flow projections shows this pattern is expected to continue in the forthcoming year. Investments are made with reference to the core balance, future cash flow requirements and the outlook for interest rates.

The Council's investment policy has regard to the MHCLG's Guidance on Local Government Investments ("the Investment Guidance") and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, and then return.

In accordance with the above guidance and to minimise the risk to investments, the Council applies minimum acceptable credit criteria to generate a list of highly creditworthy counterparties which will provide security of investments, enable diversification and minimise risk. The key ratings used to monitor counterparties are the Short-Term and Long-Term ratings.

An investment time limit has to be set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment. For the year 2020/21, the proposed limit of investments for over 1 year is £14m.

The Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to assess continually and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors and monitor changes in market variables and pricing with the credit ratings in order to generate optimal returns.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector to establish the most robust scrutiny process on the suitability of potential investment counterparties.

The primary principle governing the Council’s treasury investment criteria is the **security of its investments, closely followed by liquidity (i.e. repayment of money) and then finally the actual return on the investment.** These factors in that order are a key consideration. After this main principle, the Council will ensure that:

(i) It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security and monitoring their security; and

(ii) It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

The Chief Finance Officer (s151) will use the services of the Council's Treasury management adviser currently, Link Asset Services, to provide advice on an up to date counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. We are also better engaging with our advisers and meeting with them much more regularly in the future, particularly when there is a significant borrowing or investment decision to be made.

The Council takes into account the following relevant matters when proposing counterparties:

- (i) the financial position and jurisdiction of the institution;
- (ii) the market pricing of credit default swaps for the institution;
- (iii) any implicit or explicit Government support for the institution;
- (iv) the use of two of the major credit rating agencies external short and long-term credit ratings to assess creditworthiness;
- (v) Sovereign ratings to select counterparties from only the most creditworthy countries; and
- (vi) core Tier 1 capital ratios.

NB- Definition of Credit Default Swap – CDS are a financial instrument for swapping the risk of debt default. Credit default swaps may be used for emerging market bonds, mortgage-backed securities, corporate bonds and local government bond. The buyer of a credit default swap pays a premium for effectively insuring against a debt default.

The MHCLG Guidance on Local Government Investments made under section 15(1) of the Local Government Act 2003, places restrictions on Local authorities in relation to investments. Investments fall in to one of the three categories; Specified Investments, Loans and Non-Specified Investments

A <u>specified investment</u> is defined as an investment which satisfies all of the conditions below:

- (i) the investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling;
- (ii) the investment is not a long-term investment. This means that the local authority has a contractual right to repayment within 12 months, either because that is the expiry term of the investment or through a non-conditional option;
- (iii) the making of the investment is not defined as capital expenditure under Regulation 25 of the Capital Finance regulations (2013); and
- (iv) the investment is made with a body or in an investment scheme of high credit quality; or with the UK Government, a UK Local Authority or parish/community council.

<u>Loans</u>- Authorities may provide loans to local enterprises, local charities, wholly owned companies and joint ventures as part of a wider strategy for delivering economic growth and delivering services for the Council.

A <u>non-specified investment</u> is any investment that is not a loan and does not meet the criteria to be treated as a specified investment. These principally relates to non–financial investments which an Authority holds primarily or partially to generate a profit.

Credit Rating of Treasury Management Investments

The criteria for providing a pool of high quality short, medium and long-term, cash based investment counterparties along with the time and monetary limits for institutions on the Council's counterparty list are in the table below. The Council defines the following as being of “high credit quality” for making specified investments, subject to the monetary and time limits shown.

High Credit Quality	Individual Monetary limit(1)	Aggregate Monetary Limit	Fitch Credit rating(3)
UK Central Government	No Limit	No Limit	Not applicable
UK Local Authorities including PCC’s	£2m each	LT: £8m	Not applicable
Banks(1) operating in the UK(2)	£2m each	LT: £8m ST: None	LT:A- ST: F1
Overseas Banks (subject to Sovereign Rating AA-)	£2m each	£8m	LT:A- ST: F1
UK building societies with an asset base > £1bn	£2m each		LT: BBB+ ST:F1
UK building societies with an asset base < £1bn	£1m each		LT: A- ST:F1
Money Market Funds	£4m each		ST: AAA
Ultra Short Dated Bond Fund	£4m each		ST: AAA
Pooled Funds(4)			
Bond Funds without credit ratings	£4m each	£8m	Not applicable
Property Funds without credit ratings	£4m each	£4m	Not applicable
Multi Asset Funds	£4m each	£8m	Not applicable
Long Term Loans to small business ranked no lower than average risk by independent credit analysis	£100,000	£6m	Not applicable
Company shares to participate in the UK Municipal Bonds Agency	£10,000	£10,000	Not applicable

1 banks within the same group ownership are treated as one bank for limit purposes
2 where the bank is used as a reserve account the criteria will exclude consideration of the long-term credit rating
3 Minimum Credit rating required, is expressed as a Fitch rating or the equivalent S&P or Moodys ratings etc
4 The Council has placed an overall limit on pooled funds of £16m

The majority of the Council’s investments will be made for relatively short periods and in highly credit rated investments, giving priority to security and liquidity ahead of yield. In order that the Council is not at risk of a large single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £2 million or £4 million per pooled fund. A group of banks under the same ownership will be treated as a single organisation for limit purposes.

Money market Funds and Pooled Funds

Money market funds are pooled investment vehicles consisting of instruments similar to those used by the Council. They have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager.

Funds that offer same-day liquidity and a constant net asset value will be used as an alternative to instant access call accounts, while funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

<u>Risk assessment and credit ratings</u>

The Council uses long-term credit ratings from at least two of the main credit rating agencies to assess the risk of investment default. The lowest available credit rating will be used to determine credit quality.

Long-term ratings are expressed on a scale from AAA (the highest quality) through to D (indicating default). Ratings of BBB- and above are described as investment grade, while ratings of BB+ and below are described as speculative grade. The Council's credit rating criteria are set to ensure that it is unlikely that the Council will hold speculative grade investments directly, despite the risk of repeated downgrades. The Council may invest in bond funds that hold speculative grade bonds themselves, giving the Council an indirect exposure, but the risk is mitigated by the high level of diversification and the expert fund management.

Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made;
- any existing investments that can be recalled or sold at no cost will be; and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

<u>Other information on the security of investments</u>

The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the above criteria.

If these restrictions mean that insufficient commercial organisations of "high credit quality" are available to invest the Council's cash balances, then the surplus will be deposited with Money Market Funds, the UK Government, via the Debt Management Office for example, or with other local authorities. This will cause a reduction in the level of investment income earned but will protect the principal sum invested.

<u>Foreign countries</u>

Investments in foreign countries will be limited to those that hold an AAA or AA+ sovereign credit rating from two of the three major credit rating agencies, and to a maximum of £2 million per foreign country. Investments in countries whose lowest sovereign rating is not AAA will be limited to one year's duration. No country limit will apply to investments in the UK, irrespective of the sovereign credit rating.

Overseas subsidiaries of foreign banking groups will normally be assessed according to the country of domicile of the parent organisation. However, Santander UK plc (a subsidiary of Spain's Banco Santander) will be classed as a UK bank due to its substantial UK franchises and the arms-length nature of the parent-subsidiary relationships.

Sovereign credit rating criteria and foreign country limits will not apply to investments in multilateral development banks (e.g. the European Investment Bank and the World Bank) or other supranational organisations (e.g. the European Union).

Liquidity management

The Council uses financial systems to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Decisions on long-term investments are set by reference to the Council's Medium-Term Financial Strategy and cash flow forecast.

Interest rate exposures

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as net principal borrowed will be:

	2020/21 £m	2021/22 £m	2022/23 £m
Upper limit on fixed interest rate exposures	215	285	285
Upper limit on variable interest rate exposures	50	60	60

Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Instruments that mature during the financial year are classed as variable rate.

Risk Implications - principal sums invested for periods longer than 364 days

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The recommendation for the upper limit of principal sums maturing beyond the year end is £16m, as shown below:

	2020/21	2021/22	2022/23
Limit on principal invested beyond year end	£16m	£16m	£16m

Investment training

The needs of the Council's treasury management staff for training in investment management are assessed annually as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change. Staff regularly attend training courses, seminars and conferences provided by treasury management advisors and CIPFA. A regular programme for the training of Members responsible for Treasury Management is being provided.

Other Financial Policies

Charging interest to the Housing Revenue Account (HRA)- Following the reform of housing finance, the Council is free to adopt its own policy on sharing interest costs and income between the General Fund and HRA. The CIPFA Code recommends that Authorities state their policy on this matter each year in their treasury management strategy.

The Council is required to notionally split each of its existing long-term loans into General Fund and HRA pools. Any new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account.

Transfers between the General Fund and HRA will be made at the Authority's average short-term interest rate on investments, adjusted for credit risk.

Financial Derivatives- In the absence of any explicit legal power to do so, the Authority will not use standalone financial derivatives (such as swaps, forwards, futures and options). Derivatives embedded into loans and investments, including pooled funds and forward starting transactions, may be used, and the risks that they present will be managed in line with the overall treasury risk management strategy.

Markets in Financial Instruments Directive- The Authority has registered as a professional client with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Chief Finance Officer (Section 151 Officer) believes this to be the most appropriate status.

Business models- Under the new IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.