Agenda Item 11

Capital Programmes Update Report

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Falkirk Council

Title:	**Capital Programmes Update Report**
Meeting:	**Executive**
Date:	**19 October 2021**
Submitted By:	**Director of Corporate & Housing Services**

1. Purpose of Report

1.1 The purpose of this report is to provide an update to Members on the 2021/22 Capital Programmes for Housing and the General Fund.

2. Recommendations

2.1 The Executive is asked to:

(1) note the forecast spend by Services for both the General Fund Services (£61.1m) and Housing Capital Programmes (£45.1m)

(2) note the Prudential Indicators.

3. Background

3.1 The Capital Programmes for Housing and General Fund Services were approved in January 2021 and March 2021 respectively and adjusted following the year end outturn as at 31 March 2021.

3.2 The 2021/22 budgets for both programmes are part of a five year plan and as such there will be movement in spend across the years. The update report to Executive on 24 August 2021 set out a number of risks and uncertainties which could impact on the both the HRA and General Fund capital programmes, both in terms of delays and potential cost increases. These risks and uncertainties remain.

3.3 The August Executive report also noted that Services have projected a high level of capital expenditure for 2021/22 for the General Fund - higher than has been achieved in a number of years. Finance considered it unlikely that this level of spend could be achieved. This remains the case.

4. Considerations

4.1 General Risks and Uncertainties

4.1.1 There is a high risk that spend on the General Fund capital programme will be lower than Services are currently projecting. Some of the reasons behind this are outwith Services control, for example:

- Issues with supply chains
- High levels of staff absence, both internally and externally due to the impact of Covid
- Long lead in times for contract works

4.1.2 The August Executive report highlighted potential cost pressures that could impact on the affordability of the capital programmes. These risks remain and recent press reports on inflationary pressures demonstrate the types of issues impacting costs.

4.1.3 According to their latest ‘State of Trade Survey Q2 2021’ the Federation of Master Builders say that the recovery from the pandemic is being curtailed by a long-lasting crisis in the price and availability of vital building materials and that 80% of their respondents were forced to raise their prices in the past quarter. In addition, it is well documented that there is a shortage of approximately 100,000 drivers in the UK which is having an impact on the transport industry, a factor which also has the potential to push up the cost of goods.

4.1.4 In short, the risk that existing project budgets are no longer sufficient is increasing. Given the financial pressures facing the Council, it is not feasible to simply find the additional funds and therefore it is becoming increasing likely that there will be the need to reduce the scope of the capital programme. This is as much an issue for future years programmes as it is for 21/22.

4.1.5 Previous reports have flagged up that projects which are at an early stage, for example design or costing, are at more risk of cost pressures. Unfortunately for Falkirk Council this makes up a significant proportion of the General Fund capital programme. A number of large construction and infrastructure projects remain in the design or costing stage or are waiting for the return of tenders. Initial indications suggest that the costs for a number of these projects will be well in excess of what is currently included in the budget, albeit this cannot be confirmed at this time. Future reports to Members may require projects to be deferred or put on hold to deal with these issues.

4.1.6 The continuing slippage in the General Fund means that borrowing undertaken in the year will be less than originally anticipated and therefore budgeted for (see section 4.8). Whilst this may result in some short term benefit to the revenue budget, there is a risk that the Council’s investment activity is not appropriately spread across a number of years. This increases the Council's exposure to interest rate risk. In addition, the ongoing slippage increases the Council's exposure to inflationary cost pressures. Both of these risks will impact on the affordability of the Capital Programmes. This in turn could impact on service delivery.

4.2 **Project Specific Risks and Uncertainties**

4.2.1 On 29 September 2021 the Council agreed to the provision of gas installation to a number of villages across the area. That decision will require borrowing of up to £2.8m for the General Fund and £5.5m for Housing. Following the Council decision, work to determine the timescale associated with this spend, including any potential impact on 2021/22, will be undertaken and reported back to Members.

4.2.2 The Scottish Government has recognised a significant anticipated overspend on the Flood Risk Management (FRM) programme and it was subsequently agreed that all Councils would pause schemes which are not legally committed to allow a review to be undertaken. Grangemouth Flood Protection Scheme falls into this group, albeit this does not impact on 2021/22 spend. A data gathering exercise has now been started by COSLA with data to be returned by 1 October 2021. It is unclear how long this process will take and impossible to anticipate what the outcomes will be. Separate dialogue is ongoing between the Scottish Government and Falkirk Council regarding the financing of this major project. Updates will be reported to Members when they become available.

4.3 **General Fund Services Capital Programme**

4.3.1 The forecast for the General Fund Services Capital Programme is c£61.1m against a revised budget of £66.9m; a potential further underspend of c£5.8m. A summary of the 2021/22 outturn position is shown in Appendix 1. The forecast variance is analysed in the following table:

	£'m
Revised Capital Budget	**66.863**
Forecast	61.092
Forecast Variance 2021/22 - Underspend	**(5.771)**
Variance due to:	
Saving in Energy Efficiency Street Lighting	(1.180)
Slippage	(5.359)
Externally funded projects	0.768
Forecast Variance 2021/22	**(5.771)**

4.3.2 As reported to the Executive in August, the Council has never spent more than £35m on capital investment in any of the last five years. It must be stated that this suggests that the Council will be extremely unlikely to deliver investment of c£61m in 2021/22. The forecasts provided by the Services suggest a high level of optimism bias and Members should be aware that a much lower level of investment is likely.

4.3.3 The forecasted underspend for the General Fund Capital Programme has increased by c£5m from the figure reported to the Executive in August. The movement of c£5m is analysed in the following table:

	£'m
Underspend reported to August 2021 Executive	(0.796)
Projected underspend per table 4.3.1	(5.771)
Movement in Forecast Variance 2021/22	**(4.975)**
Breakdown of Movement:	
Projects funded from External Sources	0.330
Planning Obligations	0.007
Slippage (see paragraph 4.3.5)	(5.312)
Movement in Forecast Variance 2021/22	**(4.975)**

4.3.4 The increase in externally funded projects is due to the Government grants for the Play Parks Renewal Fund (£147k) and the Nature Restoration Fund (£183k).

4.3.5 There have been delays in some projects which have increased the Slippage for the Capital Programme. The main reasons for the increases in Slippage are as follows:

Project	£'m	Comments
Falkirk to Denny Cycleway	(1.230)	Bridge piers inspection led to delays
C116 Waterslap Rd (Road Safety)	(1.777)	Project under review due to other higher priority schemes
HQ/AC & Back Offices	(1.846)	Delays due to project specification
Front Facing Offices	(0.459)	Linked to the new HQ/AC project
Net Increase in Slippage	**(5.312)**	

4.3.6 For the Falkirk to Denny Cycleway project a further inspection of bridges is required to determine if they are fit for purpose. This work could impact on the specification of the project.

4.4 **Resources – General Fund Services**

4.4.1 The overall forecast for resources is c£5.8m less than the revised budget and has reduced by c£5m from the figure reported to the August Executive. The majority of this movement will be in borrowing, along with a decrease in anticipated capital receipts of c£0.6m. An increase in external grant income of £0.3m from the Government will be received for specific projects as per paragraph 4.3.4.

4.4.2 The projected level of expenditure would require borrowing of c£24m. However, as outlined in paragraph 4.3.2 it is unlikely that this level of spend and borrowing will be required in 2021/22. A much lower level of borrowing for the General Fund has therefore been built into borrowing projections for the year.

4.5 **Housing Capital Programme**

4.5.1 The approved 2021/22 budget is £53.5m, with a forecast of £45.1m. This represents a potential underspend of £8.4m.

4.5.2 A summary of the Housing Investment programme is included in Appendix 2. The main movements in forecast expenditure since the August Executive total £5.6m and are detailed below:

- A reduction of £6m in the projected door and window replacement expenditure due to a legal challenge delaying the award of the contract. The contract has now been awarded and a programme of surveys is underway. Installation is expected to commence from January 2022.

- The consequences of Covid and limitations on available trade resources has impacted on the performance of contractors delivering the electrical upgrading programme. A reduction of £0.8m is now projected for this programme.

- As previously reported, the installation of Air Source Heating has been delayed due to land ownership rights. This matter has now been resolved and a revised programme of work is now being developed by the contractor. A further reduction of £1.2m in projected spend is now anticipated this year.

- The projected spend for new build housing has been reduced by £0.7m to allow more detailed analysis of tender returns in relation to the development at Oakbank Polmont.

4.5.3 The above reductions in expenditure have been offset in part by increased labour and material costs of £1.2m for the estate improvement works. Additionally, buyback expenditure is anticipated to be higher by £1.9m to reflect the increased market prices for properties.

4.6 **Resources – Housing**

4.6.1 The Housing Investment Programme forecast (£45.1m) will be funded by borrowing of £39.7m, New Build grant of £2.9m, Buy Back grant of £2.4m and the Travelling Persons site grant of £0.07m. The borrowing is £7.6m less than budget due to the net slippage reported in section 4.5.1.

4.7 **Prudential Indicators**

4.7.1 A series of Prudential Indicators are used to demonstrate that capital spending plans are affordable, prudent and sustainable. They are approved by Members each year as part of the Budget process. There are eight indicators for the Council as a whole and three for Housing only. Appendix 3 sets out the indicators for 2021/22.

4.7.2 Members will be aware that there is an option for local authorities to take a loans fund principal repayment holiday in 2021/22. This means that no principal repayment of debt would be made to the loans fund in 2021/22 and that only interest on debt would be repaid. At this stage, the prudential indicators have been calculated based on what the repayments would be if the holiday was not taken. This is consistent with the approach taken to calculate the budgeted prudential indicators and allows easier comparison with prior years.

4.8 **Capital Investment Plans & Treasury Management**

4.8.1 Capital Investment plans and Treasury Management are intrinsically linked. The 2021/22 Treasury Strategy Report to Council in May 2021 detailed the estimated long term borrowing requirement for 2021/22. However, as the capital outturn projections change, these in turn impact on the borrowing requirement.

4.8.2 Section 4.3 provides an update on the projected expenditure in the Capital Programme which forms the main basis of the borrowing requirement. Section 4.3 also sets out concerns that Services will not achieve the level of spend included in their projections. This concern comes from consideration of past expenditure levels compounded with the risks and uncertainties set out in section 4.1. However, it should be noted that spend could be pushed up due to higher costs, with fewer projects being delivered.

4.8.3 Service projections would result in borrowing for the Capital Programme, net of capital receipts, of £74.3m. However, given the concerns set out in Section 4.3, this figure has been reduced to £53.8m. This will continue to be closely monitored and updated as required. The details are set out in the table below.

	Forecast in August £'m	**Forecast £'m**	**Variance £'m**
Capital Programmes Net of Capital Receipts	63.3	53.8	(9.5)
Service Repayments of Debt	(21.7)	(21.7)	-
Replacement of Long Term Borrowing	2.0	2.0	-
Replacement of Short Term Borrowing	41.0	36.0	(5.0)
Total Long Term Borrowing Requirement	**84.6**	**70.1**	**(14.5)**

4.8.4 The reduction in borrowing for the capital programme is due to the projected slippage in the General Fund and Housing Capital Programmes. The reduction in replacement of short term borrowing is because some of the borrowing will not now be repaid until early 2022/23.

4.8.5 At this point in the financial year, it is assumed that borrowing repaid in 2021/22 will be replaced by further borrowing. However, the Council does not borrow before it needs to. The Council is carrying large cash balances, with no borrowing likely to be required until November/December 2021.

5. Consultation

5.1 All Services have been consulted on this report. There is no requirement to carry out further consultation on this report. The Capital Planning and Review Working Group meets approximately once a month and projections against projects, as well as any factors impacting on the whole capital programme are discussed. However, Services must advise Finance of any slippage on forecast expenditure as soon as it is identified. The projections for spend are provided directly by Services. Services may be required to provide detailed explanations for slippage against these projections, in line with the processes previously agreed.

6. Implications

Financial

6.1 The projected outturn of the 2021/22 capital programme will be closely monitored and the impact on the revenue budget estimated as part of the revenue financial updates to Executive. Services are asked to ensure that Finance are regularly informed of any material changes to their projects and projections to ensure all information reported to Members is as accurate as possible. However, there will doubtless be further slippage, in large part due to the risks and uncertainties set out in section 4.1 of this report.

6.2 It is crucial that there are robust projections of capital spend in the year. Not only does this indicate whether investment will be delivered, but it will impact on the Council’s borrowing in any given year and the subsequent projections for loan charges.

6.3 Future capital programme budgets will be adjusted to take account of projects which have slipped or been rescheduled for the General Fund Services and Housing Capital Programmes. There is a risk that rising prices will require a recalibration of the Capital Programmes going forward. This will be kept under review and reported to Members if necessary.

Resources

6.4 There are no direct resource implications as a result of the recommendations in this report.

Legal

6.5 There are no legal implications arising from the report recommendations.

Risk

6.6 The most significant risks and uncertainties are set out in section 4.1 of this report. Services are asked to provide regular updates on the status of their projects to the Capital Planning and Review Working Group. However, there are difficulties in getting robust updates across all projects. In part this is due to the uncertainties in the wider economy. However, delays in implementation of the new structure for the Place Directorate and availability of staff, may result in some short term risk to project delivery and monitoring.

6.7 There is a risk that the cost of those projects which have slipped or been rescheduled beyond 2021/22 may increase because of construction inflation, in part driven by supply shortages. This will continue to be monitored and reported to Members.

Equalities

6.8 The recommendations in this report do not require an equality and poverty impact assessment to be carried out. However, such assessments should be carried out for each project within the capital programme.

Sustainability/Environmental Impact

6.9 The recommendations in this report do not require a sustainability assessment. However, many of the projects within the capital programme will have an impact on sustainability and/or the environment and will have impact assessments.

6.10 Moving forward, it is important that the Council continues to develop clear linkages between sustainability and capital investment, ensuring that sustainability is embedded in decision making. The capital bid process is being updated for the 2022/23 budget and the profile of sustainability and environmental impacts within project bids has been raised to help inform decision making. Moving forward, projects will be required to demonstrate how carbon reduction can be achieved or carbon emissions offset in line with the Council’s declared climate emergency and its work to achieve net zero emissions by 2030.

7. Conclusions

7.1 The projected outturn by Services for the 2021/22 for the General Fund is £61.1m which is £5.8m lower than budget. The outturn for the 2021/22 Housing capital programme is £45.1m, which is £8.5m less than budget.

7.2 There is a high level of risk around deliverability and affordability of the capital programme for 2021/22, as set out in section 4.1 of this report. Further consideration will be given to how best to assess and report on these risks at individual project level.

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Appendices
Appendix 1 - General Fund Forecast 2021/22
Appendix 2 - Housing Forecast 2021/22
Appendix 3 - Prudential Indicators 2021/22

List of Background Papers:

The following papers were relied on in the preparation of this report in terms of the Local Government (Scotland) Act 1973:

Five Year Capital Programme 2021/22 to 2025/26 – Council 11 March 2021

Housing Investment Programme 2021/22 to 2025/26 – Council 20 January 2021

Appendix 1

2021/22 CAPITAL PROGRAMME

GENERAL PROGRAMME - SUMMARY

FORECAST 2021/22

APR 2021 TO SEP 2021

EXPENDITURE	2021/22 REVISED BUDGET	2021/22 FORECAST	2021/22 FORECAST VARIANCE
SERVICE INVESTMENT PLANS	**£000**	**£000**	**£000**
CHILDREN'S SERVICES	15,345	15,345	0
DEV - DESIGN, ROADS & TRANSPORT	24,789	20,779	(4,010)
DEV - PLANNING & ECONOMIC DEVELOPMENT	5,772	6,316	544
DEV - ENVIRONMENTAL SERVICES	3,567	3,567	0
ADULT SERVICES (SOCIAL WORK)	1,332	1,332	0
CORPORATE & HOUSING SERVICES	15,206	12,901	(2,305)
COMMUNITY TRUST	852	852	0
TOTAL EXPENDITURE 2021/22	**66,863**	**61,092**	**(5,771)**

RESOURCES	2021/22 REVISED BUDGET	2021/22 FORECAST	2021/22 FORECAST VARIANCE
FALKIRK COUNCIL BORROWING	24,931	23,977	(954)
SCOTTISH GOVERNMENT BLOCK GRANTS	23,816	23,816	0
SCOTTISH GOVERNMENT SPECIFIC GRANTS	7,794	8,124	330
CAPITAL RECEIPTS - SALES	1,415	830	(585)
EXTERNAL FUNDING	3,107	3,545	438
RESERVES (DMR, CFCR and R&R)	800	800	0
SLIPPAGE ALLOWANCE	5,000	0	(5,000)
TOTAL RESOURCES 2021/22	**66,863**	**61,092**	**(5,771)**

Appendix 2

2021/22 CAPITAL PROGRAMME

HOUSING INVESTMENT PROGRAMME - SUMMARY

FORECAST 2021/22

APR 2021 TO SEP 2021

EXPENDITURE	2021/22 REVISED BUDGET	2021/22 FORECAST	2021/22 FORECAST VARIANCE
HOUSING INVESTMENT PLANS	**£000**	**£000**	**£000**
ELEMENTAL IMPROVEMENTS	23,350	15,300	(8,050)
ENERGY EFFICIENCY	7,900	6,000	(1,900)
ESTATE IMPROVEMENTS	1,800	3,000	1,200
OTHER PRIORITY AREAS	1,800	1,800	0
HEALTH & SAFETY	1,650	1,650	0
NEW BUILD HOUSING	10,500	8,875	(1,625)
PROPERTY BUY BACKS	6,000	7,900	1,900
LHS INITIATIVES & OTHER WORKS	571	571	0
TOTAL EXPENDITURE 2021/22	**53,571**	**45,096**	**(8,475)**

RESOURCES	2021/22 REVISED BUDGET	2021/22 FORECAST	2021/22 FORECAST VARIANCE
BUDGETED PRUDENTIAL BORROWING	47,300	39,725	(7,575)
SCOTTISH GOVERNMENT - NEW BUILD	3,800	2,900	(900)
SCOTTISH GOVERNMENT - BUY BACK	2,400	2,400	0
OTHER / MISC.	71	71	0
TOTAL RESOURCES 2021/22	**53,571**	**45,096**	**(8,475)**

APPENDIX 3

PRUDENTIAL CODE INDICATORS
FALKIRK COUNCIL [including TIF]

PRUDENTIAL INDICATOR		BUDGET 2021/22	FORECAST 2021/22	COMMENTS
1.	Ratio of Financing Costs to Net Revenue Stream	3.4%	3.0%	Shows how much of the Council's income is committed to repaying debt arising from Capital investment.
2.	Gross Borrowing Gross External Borrowing Accounting Adjustment – Finance Lease Liabilities Capital Financing Requirement (includes Housing) Accounting Adjustment – Finance Lease Liabilities	**£'m** 396.9 76.4 **473.3** 422.4 83.5 **505.9**	**£'m** 334.8 76.4 **411.2** 379.4 83.5 **462.9**	This is a key Prudential Indicator which shows that over the medium-term external borrowing will only be for a capital purpose. These figures are based on the projections of capital expenditure provided by Services. The capital financing requirement reflects the underlying need to borrow to finance assets. It should be noted that the sums included as "Accounting Adjustment – Finance Lease Liabilities," are not an increase in borrowing or need to borrow, they are merely a presentational requirement of International Financial Reporting Standards (IFRS).
3.	Capital Expenditure GF TIF	**£'m** 32.9 14.5 **47.4**	**£'m** 61.1 8.3 **69.4**	Simply the approved 2021/22 Capital Programme and the 2021/22 forecast spend. Note that the General Fund forecast takes account of prior year slippage, projects rescheduled beyond 2021/22 and added projects which are fully funded from additional contributions. Note: the original budget figure excluded any additional borrowing approved at the budget meeting in March 2021 and slippage from 2019/20.

APPENDIX 3

PRUDENTIAL INDICATOR		**BUDGET 2021/22**	**FORECAST 2021/22**	**COMMENTS**
4.	Capital Financing Requirement (excludes Housing)	**£'m** 272.1	**£'m** 243.9	The Capital Financing Requirement reflects the underlying need to borrow for Capital Investment for the General Fund and TIF.
5.	Authorised Limit (AL) for External Debt:- Borrowing Accounting Adjustment - Finance Lease Liabilities	**£'m** 438.6 76.4 515.0	**£'m** 438.6 76.4 515.0	This sets the maximum level of External Debt, based on capital investment plans and allowing some headroom over the Operational Boundary (see 6) for exceptional circumstances.
6.	Operational Boundary (OB) for External Debt:- Borrowing Accounting Adjustment – Finance Lease Liabilities	**£'m** 433.6 76.4 510.0	**£'m** 433.6 76.4 510.0	This is set at a lower level than the Authorised Limit and is a robust estimate of the External Debt level arising from Capital Investment and Treasury Management activities.
7.	Actual External Debt	£'m N/A		This is an actual rather than estimated Indicator and will be reported when outturns become available.
8.	CIPFA Code of Practice for Treasury Management in the Public Services	The Treasury Management Code is designed to ensure prudence in treasury operations.		

APPENDIX 3

PRUDENTIAL CODE INDICATORS
HOUSING ONLY

PRUDENTIAL INDICATOR		BUDGET 2021/22	FORECAST 2021/22	COMMENTS
1.	Ratio of Financing Costs to Net Revenue Stream	21%	20%	Shows how much of the Council's HRA income is committed to repaying debt arising from capital investment.
2.	Capital Expenditure	£53.5m	£45.1m	Simply the approved and forecast capital expenditure.
3.	Capital Financing Requirement	£233.8m	£218.9m	The Capital Financing Requirement reflects the underlying need to borrow for Housing Capital Investment.