Aberdeenshire Council 2024/25 Budget Appendix 4

CAPITAL PLAN 2024 - 2039

1. What is Capital Expenditure?

1.1. Capital expenditure is money invested by the Council in buildings, land, roads, bridges, and equipment by either acquiring new assets or extending the life of an asset.

1.2. Capital expenditure is money spent on creating or improving assets where the benefits last more than 12 months.

1.3. This kind of spending is different to revenue spending, which covers day-to-day items to run services such as staffing and purchase of services, so it is budgeted for separately.

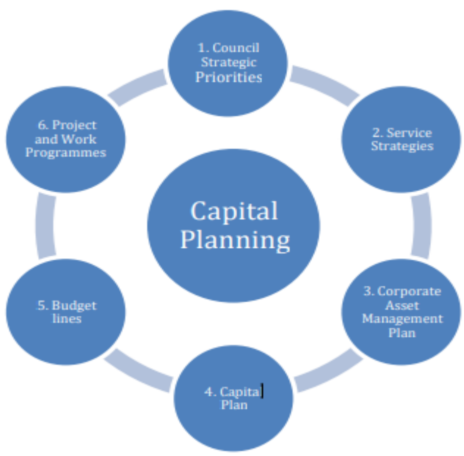
1.4. The Council's Capital Expenditure programme is reflected and budgeted for in the Capital Plan and is updated for agreed changes as the Plan progresses and reported through Policy Committees and Council.

2. The Council's Capital Plan

1.5. The Council strategically manages its operational portfolio, education estate and wider infrastructure and assets through the Capital Plan and is informed by regular condition surveys to establish a rolling programme of improvement, refurbishments and new builds and purchases.

1.6. The Council has an investment property portfolio managed to generate income to stimulate economic activity, whilst contributing income to the revenue budget.

1.7. The long-term financial investment strategy adopted by the Council is viewed as a prerequisite to good asset management and capital planning. An overview of the Council's capital planning process is illustrated below.



1.8. Asset disposal is informed by the Surplus Property Policy which was approved by Business Services Committee in June 2022 with the process overseen by the Council's Asset Disposal Group. Details of progress with Asset Disposals will be reported regularly during the financial year as part of the monitoring process.

1.9. Expenditure reflected within the plan is classified under three headings: -

- **Projects** – construction of a new asset e.g., school
- **Rolling Programmes** – annual funding required to ensure the maintenance and development of an existing asset in line with statutory functions, council priorities and strategies e.g., property lifecycle maintenance. These will continue to be reflected in the capital plan unless a decision is taken to stop the programme.
- **Workstream Programmes** – programme of individual projects that contribute to the delivery of a specific workstream, the overall capital value is usually fixed and delivered over a fixed period e.g. Early Years (1140 hours) programme.

3. How is the Capital Plan Financed?

There are several sources of funding that are used to support the Council's Capital Plan. As the high-level spending plan is over a 15-year period a number of assumptions have to be made based on the information that is available at the time of writing this report. The focus within this paper is on the 5 years of the Medium Term Financial Strategy (MTFS).

a) Capital Grant Funding

The Council receives a Capital Grant from the Scottish Government as part of the Annual Settlement (**Appendix 1**). The level of funding for the 2024/25 financial year as reflected in the Local Government Settlement Letter is as follows:

Funding	**£m**
General Capital Grant	19.695
Cycling Walking and Safer Streets	1.161
Total	20.856

b) Capital Receipts

Capital receipts are income generated from the sale of assets. The Capital Plan assumes £1.750m of capital receipts generated annually over the term of the plan. The assumptions around the deliverability of these will be subject to ongoing review.

c) Developer Contributions

Developer Obligations cover both developer contributions and affordable housing. When a development takes place there is a need for infrastructure and services to accompany it. This can include roads, schools or a wide range of facilities depending on the scale and location of development.

Developer contributions are intended to ensure that developers address any impact on infrastructure created by the development but cannot resolve existing deficiencies.

Due to the uncertainty of the timing on payment of these it is not prudent to include large sums of development contributions being received at the same time as the assets are being constructed. This means the Council is required to either use the General Capital Grant or borrowing to fund the construction until the contributions are received.

d) External Funding

Several projects and programmes are successful in attracting external matched funding from agencies such as Visit Scotland *(£0.256m),* NESTRANS *(£2.678m),* the Transport Road Safety Fund *(£0.6m),* as well as funding through Levelling Up *(£7.053m).* The Peterhead Community Campus Project has been awarded revenue funding from Scottish Futures Trust and is reflected in the revenue budget in later years. These funds are usually time limited and with very strict and specific conditions for their use.

e) Borrowing

The balance of funding required to finance the capital plan is borrowed and the ongoing cost of this borrowing must be met from the Council's Loans Fund Charges revenue budget. This is explained in more detail below.

4. The Capital Plan 2024/25 to 2038/39

1.10. The level of borrowing required to support capital investments presents an ongoing challenge to the Council's financial sustainability. The repayment of borrowing used to fund capital expenditure incurred today, creates a future revenue budget commitment over the entirety of the anticipated life span of the new asset. For long life assets such as schools or similar assets, the repayment of borrowing for these projects will create a revenue budget commitment for up to 50 years.

1.11. Therefore, in setting the revenue budget the Council must consider the revenue implications of the Capital Plan for current and future years and balance this against ensuring sufficient capital investment to deliver the Council's priorities and the Council Plan.

1.12. A review of the Capital Plan was undertaken during 2023/24 with a view to ensuring that the Plan was prudent, affordable, and sustainable in the current economic climate. The outcome of that review demonstrated that the Capital Plan was no longer affordable in its existing format and changes were required.

1.13. To maintain the continued affordability of borrowing, it is essential to contemplate a constraining element. A borrowing cap at 8.5% on the maximum borrowing (financing) cost, (excluding PFI/PPP/finance lease payments), as a percentage of our net revenue streams to 2038/39 is considered prudent.

1.14. The cap-setting procedure enables the Council to flexibly align its borrowing requirements with forecasted interest rates and increases to income streams and make necessary adjustments to the capital plan.

1.15. Establishing the capital budget has involved a collaborative effort, wherein Services have given priority to projects, including those legally obligated, to ensure that the overall budget remains within the agreed-upon affordability limits. Those changes have been incorporated into the Capital Plan presented today.

1.16. The Capital Plan is still an ambitious one and will necessitate an increase in new prudential borrowing and result in increased revenue resources being required to support the higher borrowing costs. With increasing demands for revenue resources in future years, the potential future costs of borrowing have been quantified, in 2028/29 this is currently estimated to be £57m, and limits agreed to ensure that the impact on the revenue budget is contained within the MTFS.

1.17. The proposed capital plan continues to reflect significant investment in the infrastructure of Aberdeenshire including progressing Peterhead Community Campus, Levelling Up projects at Peterhead (Cultural Quarter) and Macduff (Aquarium) and improvements to bridges, schools and Live Life Aberdeenshire facilities as part of the IF2 programme.

1.18. **Appendix 4A and 4B** provides details of the five-year period 2024/25 through to 2028/29 and indicative high level spend and funding estimates that fall within the affordability limits set out in the MTFS and this report for the period 2029/30 through to 2038/39.

1.19. To present total costs for the same project within individual lines in the Capital Plan, it is recommended to action the following two virements:

Public Toilets at Glenshee Ski Centre - a virement of £0.150m from Lifecycle Maintenance line to Glenshee Toilets Upgrade line is required to reflect previously agreed funding streams for the completion of works that are being funded predominantly from third party grants.

Fraserburgh Lighthouse Museum – a virement has been accounted for transferring budget of £0.226m from the Development of Industrial Portfolio & Factory Units line to the Fraserburgh Lighthouse Museum line to part fund the works that are required following the damage caused by Storm Arwen.

1.20. Additional capital funding of £0.850m is reflected for the Stonehaven Flood Scheme. Although completed and operational, direct project costs have increased due to forecast valuations for compensation events being settled during financial year 2023/24. The timing of the compensation claims is out with the Council's control.

5. Prudential Borrowing

5.1 In setting the Capital Plan, the Council must adhere to CIPFA’s (Chartered Institute of Public Finance and Accountancy) Prudential Code for Capital Finance in Local Authorities, which requires the Council to set an Annual Treasury Management Strategy demonstrating the affordability and sustainability of the financing of the Capital Plan. The Treasury Management and Borrowing Strategy for 2024/25 is included in **Appendices 5 and 5A.**

5.2 As outlined in the MTFS and Treasury Management Strategy, it's essential to assess and limit spending within agreed parameters to ensure the long-term sustainability and affordability of the general services capital plan.

5.3 The level of prudential borrowing that will be required to support the Capital Plan over next five years totals over £236m, with new borrowing of just under £56 million expected in 2024/25.

5.4 The Council’s Capital Financing Requirement (CFR) is a prudential indicator that measures the Council indebtedness and so its underlying need to borrow. The Council currently has an under borrowed position now of approximately £120m. This represents the capital expenditure incurred historically by the Council but has yet to be financed. Currently this position is being managed through utilising internal resources. If internal resources diminish, then this gap will require to be met through increased borrowing and could result in the 8.5% cap being achieved sooner than anticipated. Any changes to this under borrowed position will impact on the estimated borrowing requirements highlighted in the figure above.

5.5 The revenue budget resources to fund loans charges are shown in paragraph 6.6 below. Decisions to increase future capital borrowing will require permanent increases, funded by savings within the revenue budget or the generation of additional income, in the loans charges budget to repay additional capital borrowing.

6. Affordability

6.1 In accordance with CIPFA's Prudential Code the Council's S95 Officer is required to have full regard for affordability, sustainability and prudence when making recommendations about the Council's future capital programme. Such consideration includes the level of long-term revenue commitments. The Council considers the affordability of capital investment and the impact on revenue forecasts when formulating its capital plan.

6.2 Capital expenditure plays a key role in delivering the Council's long-term priorities as it can be targeted in creative and innovative ways. However, capital is not unlimited or "free money" – the Council's capital funding decisions can have significant revenue implications. Based on interest rates at time of writing, every £10m of prudential borrowing costs will incur approximately £0.6m per annum in revenue financing costs (including repayment of the principal) for 40 years, assuming an asset life of 40 years. For Information Technology projects the revenue costs are much higher per annum as the life of the asset is shorter. This is in addition to any ongoing maintenance and running costs associated with the capital investment. The more revenue that is tied up to repay borrowing, the less is available within the revenue budget to support service delivery, and this should be considered when setting the revenue budget.

6.3 The proposed Capital Plan includes borrowing of £55.964m in 2024/25, and a further £180m between 2025/26 and 2028/29. Ensuring borrowing remains sustainable and affordable in the short to medium term necessitates monitoring of overall borrowing requirements and interest rate movements.

	2024/25 £m	**2025/26 £m**	**2026/27 £m**	**2027/28 £m**	**2028/29 £m**	**Total £m**
Planned Capital Expenditure	**95.613**	**118.546**	**93.853**	**45.799**	**48.111**	**401.922**
Funding Sources						
Scottish Government						
General Capital Grant	19.695	19.695	19.695	19.695	19.695	98.475
Specific – Cycling & Walking	1.161	1.161	1.161	1.161	1.161	5.805
Other Grants from Scottish Government	4.240	5.351	0.100	0.100	0.100	9.891
Other Funding						
Levelling Up Funding (UKG)	7.053	12.432	-	-	-	19.485
Nestrans	2.528	-	-	-	-	2.528
Other Contributions	1.141	1.597	5.038	1.882	4.189	13.847
Capital Receipts	1.750	1.750	1.750	1.750	1.750	8.750
PFI / PPP Funded	2.081	1.687	0.837	0.960	1.257	6.822
Cash and Borrowing	55.964	74.873	65.272	20.251	19.959	236.319
Total	**95.613**	**118.546**	**93.853**	**45.799**	**48.111**	**401.922**

6.4 The cost of borrowing is a material inclusion in the Council's revenue budget and therefore this budget line (Capital Financing Charges & Interest on Revenue Balances) is subject to the same scrutiny as all other budgets. The proposal within today's Budget reports is that almost £41 million is required to support the Council's borrowing requirements for 2024/25 with a further £208 million required to support a high-level indicative capital investment plan over the next 4 financial years (in 2028/29, the cost of borrowing is estimated to be £57m).

6.5 The estimated increase in borrowing costs is due to the quantum of borrowing required to fund the proposed capital plan across the next five financial years, with the assumption that interest rates will fall below 5%. There is no other provision for significant interest rate rises in future years and is reflected as a risk within the Councils Budget Risk Register.

6.6 The ratio of capital financing costs to the total revenue streams (Revenue Support Grant, Business Rates and Council Tax) available to the Council are shown in the table below. For 2024/25, the costs are budgeted at almost £41 million. On a provisional basis the revenue costs of borrowing to fund the Capital Plan from year 2 to 5 have been included within the 5-year Revenue Budget report. This demonstrates the proportion of revenue funds that will be required to deliver the Capital Plan as proposed.

	Total Revenue Streams (£m)	Capital Financing Charges (£m)	Capital Financing as a % of Revenue Streams
2024/25	753.000	40.827	5.4%
2025/26	754.000	46.549	6.2%
2026/27	754.000	50.646	6.7%
2027/28	754.000	54.380	7.2%
2028/29	755.000	57.022	7.6%

Capital Financing costs (excluding PFI/PPP) as a % Total Revenue Streams

6.7 The increasing ratio percentage in the above table shows the increasing cost of our borrowing, the proposed cap will ensure that that the borrowing incurred to meet our capital investment requirements is not to the detriment of service delivery. Capital financing (excluding PFI/PPP) as a % of net revenue streams is expected to reach 8.2% by 2031/32.

6.8 Should any of the above funding streams vary from the predictions reflected in the Capital Plan for future years this may require the associated borrowing levels, phasing and prioritisation of projects within the Capital Plan to be revisited.

6.9 Capital planning is led by the Capital Plan Group (CPG) and is a key element of Aberdeenshire Council's strategic framework. The CPG is chaired by Head of

Property & Facilities Management with membership comprising senior officers from all Services and reports to the Strategic Leadership Team (SLT).

6.10 This approach ensures that capital investment and expenditure is consistent with Council priorities. The CPG also co-ordinates, challenges and assesses bids for inclusion in the capital programme and makes recommendations to SLT and Committees for decision.

7. Risks

7.1 Capital projects by their very nature contain a degree of risk around deliverability. The effect of slippage and cost control across all budget lines within the capital plan, in year and across financial years, will be managed and considered when preparing future years programmes of work and the impact that would have on borrowing requirements. Full costs of individual projects will be captured and reported on a regular basis to Committee and then to Council. The capital investment planned for the next 15 years is lower than that planned in previous years acknowledging both the need to be affordable and deliverable.

7.2 Following a period of sustained inflationary pressures fueled by unprecedented global events, it appears that in later half of 2023/24, we have returned to a more typical economic cycle. Construction inflation is expected to persist, albeit likely at historical levels. The cumulative effect of the past three years is that we have now established a new normal of price levels, approximately 35% to 45% higher within this period. Consequently, funding and affordability considerations must be based on these escalated costs. Additionally, it's crucial to consider the current Bank of England base rate, which stands at 5.25%, significantly higher than the 0.10% observed in late 2021. This disparity will directly influence borrowing, affordability, and the life cycle costs associated with construction projects.

7.3 The borrowing proposals contained within the Capital Plan include an element of risk based on three factors:

- **Cash Flow**: during this financial year 7% of the Capital Plan was spent after 3 months, 25% after 6 months and 32% after 8 months, therefore the use of the Council's cash balances which average over £27 million per day is an acceptable source of funding given the spend profile of the Capital Plan and acknowledging all other financial commitments the Council has to meet day to day.

- **Debt Maturity**: when existing debt matures it must be repaid and this is factored into the cash flow management. Cash flow is forecast and managed on a daily basis to ensure that sufficient cash is available to meet all expenditure commitments. In 2024/25 there are £25.2 million of long term loans due to mature and this has been factored into the budget assumptions stated above.

- **Interest rates**: the Council can borrow on a fixed basis for a long-term period (one year or more) or on a temporary basis (for less than one year). During this financial year new long-term borrowing taken have ranged from rates of 4.19% to 4.90%. Temporary loan rates are currently within the range of 5.55% to 6.00%. Uncertainty in the financial markets and interest rates could result in any adverse movements impacting on the Loans Fund budget and the Council's ability to deliver the Capital Plan.

7.4 To mitigate the borrowing risks, the experienced treasury officers within Finance will continue to work within the Council's approved Treasury Strategy and manage the Council's cash flow position with advice taken when required from the Council's external advisers.