

**Lancaster City Council**

**Capital Investment Strategy**

**2020 – 2024**

## 1.0 Introduction

1.1 This Strategy has been developed to include all Capital Investments made by the Council particularly around Regeneration, those which deliver a Social Return such as housing, or seek to address the climate emergency as well as those which generate an income or provide for Operational Service Delivery. It covers the period 2020 to 2024 and reflects both the aspirations of Funding the Future and the Medium-Term Financial Strategy (MTFS).

## 2.0 Background

2.1 The Council recognises the longer term need to balance the use of its capital resources to contribute to wider investments that deliver against its Priorities such as regeneration of the local economy and projects that deliver wider social returns such as housing and green energy. The Council is moving towards a more commercial way of operating if it is to achieve its aim of being more financially independent.

2.2 The Council updated its Priorities in January 2020 and they are key to driving its service provision and its capital investment ambitions. The updated priorities are detailed in table 1 below.

Table 1

Lancaster City Council   Priorities Update 2020				
Priorities	A Sustainable District	An Inclusive and Prosperous Local Economy	Healthy and Happy Communities	A Co-operative, Kind and Responsible Council
<b>Themes</b>				
<b>Climate Emergency</b> Taking action to meet the challenges of the climate emergency	<ul style="list-style-type: none"> <li>▶ net zero carbon by 2030 while supporting other individuals, businesses and organisations across the district to reach the same goal</li> <li>▶ moving records and residual waste to landfill and incineration</li> <li>▶ increasing the amount of sustainable energy produced in the district and decreasing the district's energy use</li> <li>▶ transitioning to an accessible and inclusive low carbon and active transport system</li> <li>▶ supporting our communities to be resilient in handling and adapt to the wider effects of climate change</li> <li>▶ increasing the biodiversity of our district</li> </ul>	<ul style="list-style-type: none"> <li>▶ supporting the development of new skills and improved prospects for our residents within an environmentally sustainable local economy</li> <li>▶ advocating for fair employment and just labour markets that increase productivity and reduce income inequality</li> <li>▶ supporting new and existing enterprises in sustainable innovation and the strengthening of local supply networks</li> <li>▶ using our land, property, finance and procurement to benefit local communities and encouraging residents, businesses, organisations and institutions to do the same</li> <li>▶ securing investment and regeneration across the Lancaster and South Cumbria Economic Region</li> </ul>	<ul style="list-style-type: none"> <li>▶ supporting wellbeing and ensuring local communities are engaged, involved and connected</li> <li>▶ addressing health and income inequality, food and fuel poverty, mental health needs, and loneliness</li> <li>▶ focused on early-intervention approaches and involving our communities in service design and delivery</li> <li>▶ (re)developing housing to ensure people of all incomes are comfortable, warm and able to maintain their independence</li> <li>▶ improving access to the arts, culture, leisure and recreation, supporting our thriving arts and culture sector</li> <li>▶ keeping our district's neighbourhoods, parks, beaches and open space clean, well-maintained and safe</li> </ul>	<ul style="list-style-type: none"> <li>▶ listening to our communities and treating everyone with equal respect, being friendly, honest, and empathetic</li> <li>▶ working in partnership with residents, local organisations and partners, recognizing the strengths and skills in our community</li> <li>▶ investing in developing the strengths and skills of our staff and councillors</li> <li>▶ focused on serving our residents, local organisations and district</li> <li>▶ introducing innovative ways of working to improve service delivery and the operations of the council</li> <li>▶ providing value for money and ensuring that we are financially resilient and sustainable</li> </ul>
<b>Community Wealth-Building</b> Building a sustainable and just local economy that benefits people and organisations				
<b>Community Engagement</b> Drawing on the wealth of skills and knowledge in the community and working in partnership				

## 3.0 Strategy Objectives

3.1 The Capital Investment Strategy forms a key part of the Council's overall Corporate Budget Planning and provides a framework for the Council to consider a wide range of capital investments which support the Council's stated Priorities and Outcomes. Key to the strategy is ensuring that robust governance processes are in place, full business case assessments are made and that the associated risks are minimised and so maintains links to other key strategic documents, notably

- Corporate Plan/ Priorities/ Plan 2030
- Funding the Future
- Medium Term Financial Strategy
- Capital Strategy
- Treasury Management Strategy
- Minimum Revenue Provision Policy
- Asset Management Plan

3.2 The key objectives of the Strategy are therefore to:

- Clearly articulate the Council's intentions in relation to the various forms of investment in terms of its objectives, scale and timing.
- Consider proposals which requires long term capital investment in line with the Council's priorities, outcomes and financial objectives.
- Give emphasis to proposals which support sustainable physical and economic regeneration and those that provide a social return contributing to the wider financial and economic resilience of the district or address the climate emergency.
- Develop a governance framework that enables the Council to be agile and respond in a timely fashion to commercial market opportunities.

#### **4.0 Types of Capital Investment**

4.1 Examples of the areas in which the Council may wish to undertake capital investments are detailed below. However, investments should not be solely limited to these definitions but should be flexible enough to enable delivery of the Council's priorities and outcomes.

##### Regeneration

4.2 To make investments for the benefit, improvement, or development of the area, through balanced acquisition, retention, and management of good quality investments, whilst delivering regeneration outcomes through:

- Development and regeneration in our town centres.
- Job creation - successful creation of new jobs or retention of jobs with fair and decent working conditions (i.e. fair work charter) within the District,
- Business rate growth,
- Preventing Local Market failure, and.
- Opportunities that have strategic importance, such as those that will improve key sectors, key locations, or address issues such as deprivation and child poverty.

##### Delivering a Social Return

4.3 This classification is broad to enable support for a wider range of investments, but it may include areas such as housing, for example

- Acquisitions of existing residential properties, to provide good quality housing in the private sector rental sector.
- Maintain the Council's objective to be an effective and responsible landlord ensuring that good quality housing options remain for the District's residents.
- Retrofitting properties acquired to an agreed defined standard both in terms of quality and thermal efficiency.

##### Address the Climate Emergency

4.4 This includes support of schemes which examine

- How we use and create energy, such as installation of solar panels, or investment in larger scale solar energy facilities'
- How we work, such as supporting agile working to reduce our carbon footprint, or the increased electrification of our vehicle fleet
- How we reduce waste both within the Council and across the wider District

##### Operational Investments

4.5 These are capital investments that sustain the day to day operational delivery of the Council's services, which underpin a broad range of Council priorities, such as,

- Upgrades or replacement of key information and communication systems,
- Invest to save proposals which provide short-term funding to services to help services become more efficient and effective.

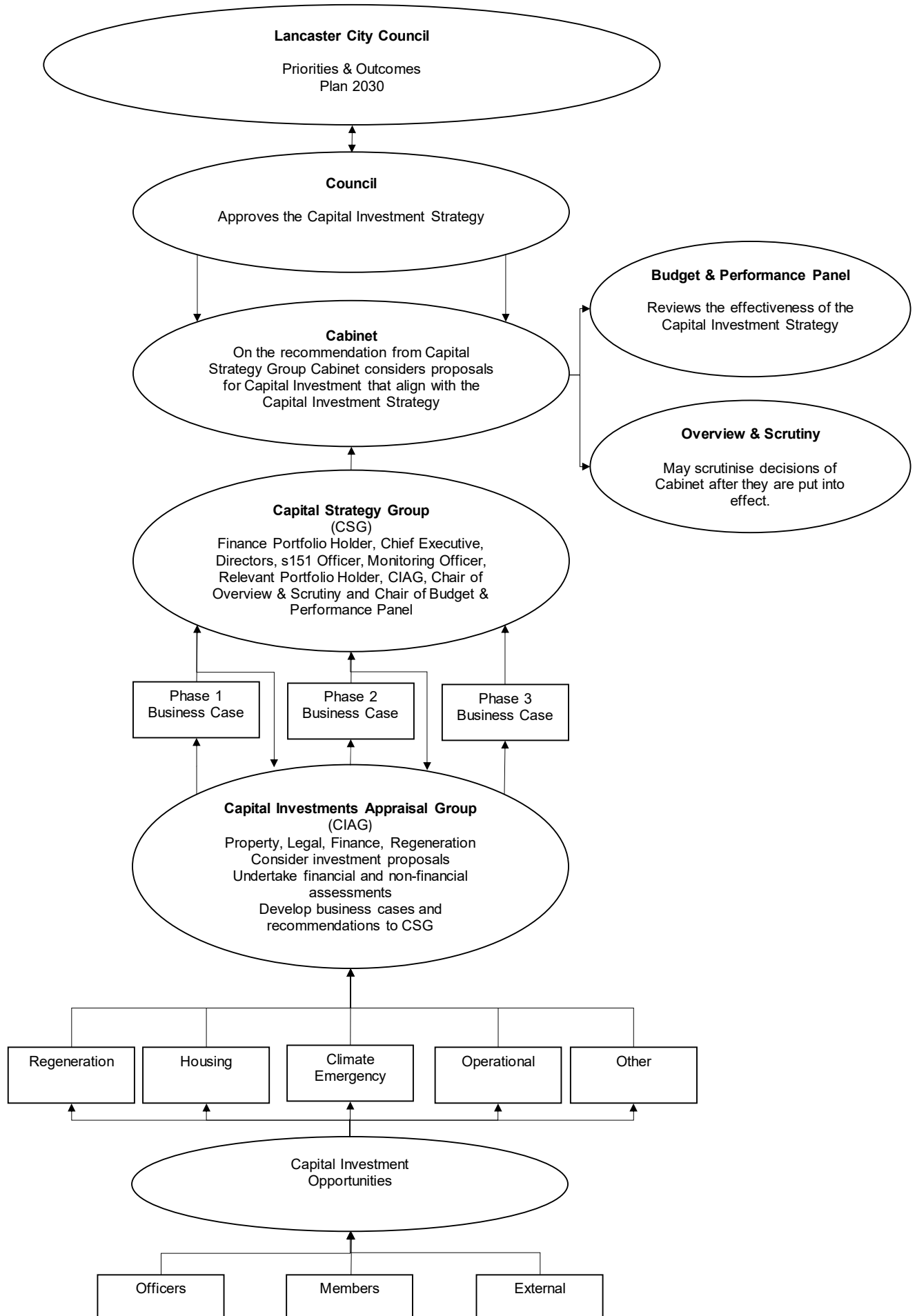
##### Other Investment Types

4.6 These are investments which may not easily fall into one of the previous categories, but which the Council may wish to consider such as those that provide a commercial yield or return.

## **5.0 Decision Making Process and Governance Arrangements**

- 5.1 This Strategy is to be agreed by the Council and sets the parameters within which Capital Investment activity will take place. These parameters are designed to ensure that investments are ethical, that all risks are assessed and managed and that effective due diligence takes place in establishing the financial business case and show links to Corporate Priorities.
- 5.2 The Council has agreed the financial threshold for a key decision is £250,000. The Council has delegated amounts in excess of this limit to the Leader and to officers to facilitate the daily activities of the Council. The delegation to the Leader will be exercised by Cabinet, which will be the decision-making body for all decisions.
- 5.3 In order to deliver the Capital Investment Strategy, as well as its other aspirations, a Capital Strategy Group (CSG) has been constituted with representation from Cabinet, Executive, Capital Investments Appraisal Group (CIAG) and the Chairs of both Budget & Performance Panel (B&PP) and Overview & Scrutiny (O&S). Early involvement of scrutiny at the pre-decision stage adds value by informing a decision rather than an after-the-event critique under the traditional process. CSG's terms of reference are included at appendix 4 to this strategy
- 5.4 The CSG, has the responsibility for overseeing the development of this capital investment strategy, considering each investment proposal, and making appropriate recommendations to Cabinet. CSG along with B&PP will subsequently monitor the performance of the investments against agreed benchmarks.
- 5.5 Cabinet will ultimately consider each proposal and the recommendations presented by CSG and may accept the proposal or instruct CSG and CIAG to undertake further work.
- 5.6 Capital investment proposals may be brought forward from many sources both internal and external. On submission of a Strategic Outline Business Case each proposal will be considered by (CIAG) and will be subjected to a detailed review which will include:
- Financial and legal due diligence including gross and net return calculations and scenario analyses
  - Risk Assessment Matrix
  - Outcomes Matrix
  - Consideration of Full Business Case
- Further details of these key aspects are provided at section 6 below
- 5.7 At each phase of the due diligence process CIAG will present to CSG a business case making appropriate recommendations and may request authority to incur additional expenditure.
- 5.8 A summary of the Decision-Making Process is given in table 2 below

Table 2: Decision Making Process



## **Financial Due Diligence**

- 6.1 In financial terms yield is used to describe a certain amount earned on an asset or investment, over a period. It is expressed annually as a percentage based on the value of the asset or investment.
- 6.2 An example of the yield calculator and supporting Cashflow analysis is included at appendix 1 to this strategy. It covers total costs of acquisition, all expenses associated with holding the asset including the cost of borrowing and a provision for repayment of the borrowing, known as Minimum Revenue Provision and any current and potential income streams. The appendix details the level of rigor that will be adopted in completing the financial due diligence and the importance of ensuring not only that the information is complete and accurate but also that a number of different scenarios are presented to reflect a range of social and economic conditions.
- 6.3 Where possible the results from the cashflow and return calculations will be compared to industry benchmark data to provide context and enable reasoned consideration.

## **Risk Assessment Matrix**

- 6.4 The risk assessment matrix is included as appendix 2 to this strategy. It will ensure that every potential investment is scored against several factors which reflect the relative risks and mitigations of each investment. Each of the risk factors will be weighted and scores will be assigned according to pre-agreed definitions of what constitutes low and high risk. Every proposition would have to achieve a minimum score to satisfy the requirement to minimise the risk to the Council.
- 6.4 The majority of factors will be assessed on a five-point scale (set out in appendix 2) from excellent to poor; these are summarised in the following paragraphs. Paragraph 6.5 deals specifically with those proposals in which the Council will not invest on ethical grounds.

### Exclusions

- 6.5 There are a number of activities that the Council would not want to support, on ethical grounds, with respect to capital investments. The list below, which will be reviewed, outlines those sectors in which the Council will not invest:

- Tobacco production
- Animal exploitation
- Armaments
- Environmentally damaging practices
- Bookmakers
- Human Rights Abuse / Oppressive regimes
- Pornography

### Investment Location

- 6.6 Several local authorities have made significant financial investments outside of their boundaries as this provides an increase in the opportunities for acquiring good yields. Whilst this strategy is not focused on commercial yields it must be recognised that the Lancaster City Council boundaries are relatively small and so the opportunities for certain types of investments may not be readily available. It is recommended that where possible the Council focusses its efforts on investments inside the Council boundary but where this is not possible that the investment boundary be extended to include South Cumbria and North Lancashire.
- 6.7 Both the Government and the Chartered Institute of Public Finance & Accountancy (CIPFA) have expressed concerns about commercial property investments and the perceived speculative investments by Councils in pursuit of returns. This strategy seeks to promote capital investments that are clearly aligned with the Council's priorities particularly around projects that provide long term support for local businesses through regeneration and those that are able to deliver a social return such as housing or to help address the climate emergency.

### Portfolio Strategy

- 6.8 There are seven recognised types of property investment. These are retail, industrial, commercial, food and beverage, private sector housing, green technology and other. In order to ensure that the authority is not over exposed to any one sector, a limit of 30% exposure, both in terms of property value and rental income, will be set. No future investments will be considered where they take the portfolio exposure over these limits.

### Location - Micro

- 6.9 This factor is designed to assess the quality of the individual location regarding current use. This will change according to the sector. For example, excellent links for a retail proposal would cover footfall where a central city centre location might be deemed excellent whereas for an industrial location, proximity to transport links might be assessed as more important. As there is a degree of subjectivity to this assessment, the proposal will be scored by the Capital Strategy Group.

### Tenant Covenant

- 6.10 This is an assessment of the financial strength of the tenant which will be undertaken using a recognised credit referencing agency. The assessment will be objective as it will use the search agency's independent risk scoring.

### Building Quality

- 6.11 This factor is designed to assess the quality of the building. A building which is new or recently refurbished scoring highly. As there is a degree of subjectivity to this assessment, the proposal will be scored by the CSG. Any refurbishment costs to improve the scoring would be factored into the financial assessment.

### Lease Term

- 6.12 This factor is designed to measure the longevity of the income to the council with longer lease terms scoring more highly. The assessment will be based on a Weighted Average Unexpired Lease Term (WAULT) calculation and as such is objective.

### Tenants Repairing Obligation

- 6.13 This factor is designed to determine the authority's responsibility and liability for property repairs with a higher score attributable to those properties where all responsibilities are passed to the leaseholder. This is an objective assessment which will be made by the Monitoring Officer or nominated representative.

### Rent Review Mechanisms

- 6.14 This factor is designed to determine the robustness of the rent review process where more regular rent reviews based on open market rental values scoring more highly. As this will be specified in the lease, the assessment will be made by the Monitoring Officer, or nominated representative.

### Occupational Demand

- 6.15 This factor is designed to determine demand for the property. It will usually be determined by external advice and will be assessed by the Capital Strategy Group.

### Management Intensity

- 6.16 This factor measures the number of tenants that the Council will deal with for each property with lower number of tenants, and therefore less complexity, scoring more highly. This is an objective criteria and will be assessed by the Monitoring Officer or nominated representative based on the number of leases issued.

### Liquidity

- 6.17 This factor considers the attractiveness of the property to other investors if the Council was to seek to dispose of the property. As it is a partially subjective assessment, the authority will seek independent external advice which will be assessed by the Capital Strategy Group.

### Tenure

- 6.18 This factor considers the tenure of the property with freehold and long leaseholds scoring more highly. This is an objective criterion which will be clear from the property deeds and as such the assessment will be made by the Monitoring Officer or nominated representative.

- 6.19 **Environmental Impact**  
To consider if the proposed investment can provide secondary sources of green energy through installation of solar panels etc. This would be a subjective criterion through consideration of external advice.
- 6.20 **Asset Management**  
Is the investment capable of sustaining additional sources of income, or efficiencies through effective asset management. This would be a subjective criterion through consideration of the views of the Property Services team.

***Outcomes Matrix***

- 6.21 The outcomes matrix is included as appendix 3 to this strategy. This provides an analysis of any outcomes and impacts that will be delivered by the capital investment. Outcomes should be reconcilable to the Council's Corporate Plan and Priorities and be measurable both before and after the investment so that the benefits accruing can readily be identified, reported, and monitored.
- 6.22 It is important that Members are aware that there may be an inverse relationship between the finance and outcomes tests. The Council may choose to accept investments that provide a lower yield where the investment can deliver significant positive outcomes in respect of its priorities.

**Appendices**

- |             |   |
|-------------|---|
| Appendix 1: | Financial Yield Calculator                  |
| Appendix 2: | Risk Matrix                                 |
| Appendix 3: | Outcomes Matrix                             |
| Appendix 4: | Capital Strategy Group – Terms of Reference |





**Investment**

Criteria	Criteria Description	Maximum Weighted Score	Score to Apply to Each Column:					WEIGHTED SCORE	Comments supporting assessment	Actions taken to reduce risk and change to assessment	Consequences of actions to taken to reduce risk (eg. reduced yield)	
			5	4	3	2	1					
Portfolio Strategy Context	Does the acquisition take the exposure of the whole portfolio to over 30% in either of the six sectors: retail, industrial, commercial, food and beverage, private sector housing, green technology and other		YES	Proposal to be scored using risk matrix below.					100	To be confirmed	Review of council portfolio % value/income/floor area	Informs decision
			NO	Over exposure to one of the six sectors. Proposal can not proceed without a review of existing portfolio to ensure that Council is not over exposed to any one sector.						The purchase does not form more than 30% ownership in sector	As above	Informs decision
Location: Micro	Quality of the individual situation of the property within the macro location with regard to property use (i.e.. sector). Refer to separate sector definition sheet.	20	Excellent links x	Good links	Reasonable links	Poor links, but prospects of improvement	Location with limited benefit	100				
Tenant Covenant	Financial rating provided by Dun & Bradstreet	20	Excellent financial covenant	Strong financial covenant	Good financial covenant x	Poor but improving financial covenant	Poor financial covenant	60				
Building Quality	Quality of the building compared to its market sector. Refer to separate sector definition sheet.	15	New, modern or recently refurbished x	Good quality, no spend required for 20+ years	Good quality but spend required in 10-20 years	Spend required in 5-10 years	Tired, Spend required in next 5 years	75				
EPC	fact	5	A/B x	C	D	E	F/G	25				
Lease Term	Unexpired lease terms, WAULT	15	Greater than 15 years x	Between 10 and 15 years	Between 6 and 10 years	Between 2 and 6 years	Under 2 years	75				
Tenants Repairing Obligations	Tenants repairing obligations	10	Full repairing and insuring (Effective FRI) x	Full repairing and insuring - partially recoverable	Internal repairing	Internal repairing - partial recovery	Landlord responsible	50				
Rent Review	Rent review mechanisms	10	Fixed uplift + OMRV x	OMRV but no near comparable	CPI/RPI	Caps and Cuff review	No proper review mechanism	50				
Occupational Demand	Anticipated level of demand from other occupier if tenant(s) was (were) to vacate	15	Demand from many tenants x	Demand from a few tenants, but low number of competing buildings	Reasonable prospect of securing new tenants	Poor demand	Niche / limited demand	75				
Management Intensity	Complexity and cost of managing the property	15	1-2 tenants x	3 -5 Tenants	5 - 9 tenants	10 - 15 tenants	16 plus tenants	75				
Liquidity	The degree to which the property can be quickly sold in the market without affecting the price	15	Lot size and sector attractive to investors x	Lot size not attractive to investors but sector is	Lots size attractive to investors but sector is not	Generally unattractive	Attractive to niche investors only	75				
Tenure	Freehold / Leasehold. Consideration of any ground rent obligations	10	Freehold x	Long leasehold 125+ years / peppercorn ground rent	Lease between 100 and 125 years / peppercorn ground rent	Lease between 50 and 100 years	Lease less than 50 years and/or high ground rent	50				
Environmental Impact	Opportunities for secondary sources of green energy	10	Excellent x	Good	Acceptable	Marginal	Poor	50				
Asset Management	Opportunities for additional sources of income, or efficiencies through effective asset management	10	Excellent x	Good	Acceptable	Marginal	Poor	50				
<b>Weighted Score (810 Max Sum)</b>								<b>810</b>				

**Outcomes**

Proposed Capital Investment:

**Outcomes and Impact Matrix**

Council Priority

Success Factors:

**Outcomes:**

*The likely achieved short-term and medium-term effects from the capital investment*

Measures: before  
Measures: after

**Impact**

*The likely longer-term effects produced, directly or indirectly, from the commercial investment*

Measures: before and after

**Social Value Outcomes**

This matrix should capture all the non-financial benefits accruing from the potential capital investment. Reference should be made to the Council's 'Ambitions' Corporate Plan and any other strategic plan arising from the Ambitions plan (eg. Economic Growth strategy). This matrix should provide a good level of clarity on additional benefits that may accrue such as business rates, impact on a high street frontage, detail on any social impact such as employment and how this would be measured.

# Capital Strategy Group: Terms of Reference

## Role

1. The Capital Strategy Group (CSG) is a Member and officer working group with a clear remit to be the Council's advisory body on the Council's Capital Investment Strategy.
2. The Capital Investment Strategy has clear priority areas of work which although distinct from one another should be considered in an integrated manner when forming and delivering the Council's capital programme and related areas:
3. The types of Capital Investments which may be considered when forming the capital programme.
  - a) **Regeneration** - Investments for the benefit, improvement, or development of the area, through balanced acquisition, retention, and management of good quality investments, whilst delivering regeneration outcomes.
  - b) **Investments Delivering a Social Return** - This classification is broad to enable support for a wider range of investments, but it may include areas such as provision of private sector housing and retrofitting properties acquired to an agreed defined standard both in terms of quality and thermal efficiency.
  - c) **Investments that address the Climate Emergency** – Examples of these types of investments may include installation of solar panels, investment in larger scale solar energy facilities', supporting agile working to reduce our carbon footprint, and the increased electrification of our vehicle fleet.
  - d) **Operational Investments** - Investments that sustain the day to day operational delivery of the Councils services which underpin a broad range of Council priorities.
  - e) **Other Investments** - Investments which may not easily fall into the previous categories, but which the Council may wish to consider such as those that provide a commercial yield or return.

## Composition of CSG

4. The group will consist of the following Members and officers. Where representatives are not able to attend, a suitable alternative will attend in their place.

### Standing Membership

- Cabinet Finance Portfolio Lead
- Chief Executive
- Overview and Scrutiny Chair
- Budget and Performance Panel Chair
- Relevant Cabinet Portfolio Holder
- Relevant Director
- Section 151 Officer
- Governance Lead
- Capital Investment Appraisal Group

### Additional representation as and when required may include

- Capital Strategy Officer Lead
- Asset Management Officer Lead
- Property Services Lead
- Regeneration/ Economic Growth Lead
- ICT Representation
- Programme Manager

## Frequency of Meetings

5. The CSG will meet monthly by routine but may also meet on an ad-hoc basis as required as and when key proposals come forward. Routine meetings will be co-ordinated so that they inform monitoring processes to Cabinet and Budget and Performance Panel.

## Remit

6. CSG's remit is to support the delivery of wider Council policies through its contribute to the development and oversight of the Council's capital programme. This will include assessing initial proposals and business cases through to delivering the programme and assessing its effectiveness in respect of corporate priorities.
7. *With respect to Capital Investment Strategy*
  - a) To keep the Capital Investment Strategy document under review ensuring that it reflects the Council's capital investment priorities and review the Strategy as part of the MTFS update.
  - b) To ensure that the Capital Strategy is informed by and consistent with the Corporate Plan and associated strategies, the Asset Management Plan and Property Investment Strategy.

### *With respect to the Capital Programme*

- c) To consider and score all bids to the capital programme and make accept/ develop/ reject recommendations to Cabinet.
- d) Consider all proposals in accordance with the matrices set out in the Capital Investment Strategy and make recommendations to Cabinet with respect to any agreed proposals having regard to the scrutiny process
- e) To monitor the progress of each scheme within the capital programme in terms of progress to date, expenditure, and delivery of outcomes including those classified within the development pool.
- f) To review all completed schemes with respect to outcomes and impact as well as lessons learned
- g) To monitor the resources available to support the Capital Programme and ensure that, at all times, it remains affordable, sustainable and prudent.
- h) To maintain the capital bid and scoring assessment framework

### *With respect to the Asset Management Plan*

- i) Own and ensure the development of the Asset Management Plan and long-term property strategy, ensuring that it is line with Council Plan / MTFS objectives
- j) To undertake annual review of property holding to ensure that all property is utilised appropriately and consider any capital expenditure/ receipt proposals associated with maintaining, updating, transferring, or disposing of property assets

Each of the above areas of work are covered by the Capital Strategy and Capital Investment Strategy, which are the Council's overarching documents which aim to ensure that Council's capital investments priorities reflect Council priorities and are supported by a long term financing plan.

## Decision Making

8. The CSG is a Member and Officer working group and as such is only advisory and does not have any formal decision-making authority. Following consideration of each business case it may make recommendations to budget holders in relation to due diligence costs and other matters. It may also make final recommendations to Cabinet regarding each proposal. It also ensures that necessary consultation is carried out with Cabinet, relevant Portfolio Holders, Management Board, and relevant Directors as part of the decision-making process. Any proposal that is outside the approved budget and policy framework will be referred to Cabinet or Council in accordance with the Constitution.

## The role of Scrutiny Committee Members

9. The Chairs of both Budget & Performance Panel and Overview & Scrutiny form part of CSG. The early involvement of scrutiny at the pre-decision stage will allow them to add value by informing a decision rather than an after-the-event critique under the traditional process. This intention and their active involvement do not remove or negate the right to call in any decision made by Cabinet in this area.

## **Key Outcomes**

10. The key outcomes from the CSG are:

- a) An effective Capital Programme optimising the capital investment resources within the Council Plan.
- b) Strategic property management ensuring full optimisation of Council property assets, maximising income and return and reducing expenditure where possible but ensuring assets are well maintained.
- c) Enhanced long term planning of capital investment, better use and management of property assets, and accountability.
- d) The integration of the Capital Investment Strategy in line with Council priorities as set out in the Council Plan.