Appendix 4 – Proposed Report to County Council - Addition to Capital & Asset Strategy 2018/19

1 Background

1.1 The County Council in February approved the Integrated Plan including the Council's Treasury Management Strategy and its Capital and Asset Strategy. In February, MHCLG issued new statutory guidance on local authority investments, that requires additional disclosures on some investments and the setting of a self – assessed limit on non-treasury investments, which include loans made by a local authority to one of its wholly-owned companies or associates, to a joint venture, or to a third party. More detailed guidance, including from CIPFA, is still awaited.

1.2 Local Authorities are required to comply with this revised Statutory Guidance from 1 April 2018. Authorities are also required to reflect this in Treasury Management and Investment Strategies approved by Full Council, covering both Treasury and non-Treasury investments. However, as full guidance on the new requirements is not yet available, MHCLG accepted that it was not practical to include these requirements in authorities' Investment and Treasury Management Strategies approved for 2018/19. They have confirmed that any amendments resulting from the guidance must be included when the Strategies are next brought to Council for approval. Where Local Authorities currently prepare a Capital Strategy in line with the Prudential Code, and a Treasury Management Strategy in line with the Treasury Management Code, the disclosures required by the new Investment Guidance can be incorporated into these documents as opposed to a separate Investment Strategy. The Investment Strategy is a new requirement which for Hertfordshire County Council has largely been met in the Capital and Asset Strategy (part D of the 2018/19 Integrated Plan).

1.3 Revised Strategies including these disclosures will therefore be brought to Council for approval as required, once full guidance is available. Officers currently plan to make the necessary revisions in the Capital and Asset Management Strategy, although this will be subject to the detailed guidance. The existing content of the Treasury Management Strategy and its prudential indicators are unchanged, apart from changes to the Capital Programme, as set out below.

1.4 This report details the proposed limit and disclosure relating to non-treasury investments, including loan arrangements to Herts Living Limited (HLL) by the County Council arising from the Joint Venture for property development. Subject to final guidance, it is proposed that the following wording be added to a revised Capital Strategy. Cabinet are asked to recommend that County Council agree an upper limit of £50m on non-treasury investments in 2018/19.

2 Proposed Addition to Capital & Asset Strategy

2.1 The aim of the proposed Joint Venture (JV) property development model is to create a greater return to the County Council (enhanced capital receipts) on land currently owned by the County Council but declared surplus to requirements, whilst also working in partnership to deliver housing within Hertfordshire. The County Council must receive best consideration reasonably obtainable for the land (this is to meet the Council's duty under section 123 of the Local Government Act 1972). The

JV model requires HLL to invest equity (matched by the Preferred Bidder) into the JV. It is intended that the required equity will be provided via loan from the County Council to HLL (or loan note from HLL to the Council), repayable upon receipt to HLL of any subsequent disposal of land receipts and profit. Loan transactions will be "other investment" i.e. non treasury loans, required to be treated as capital expenditure as they are loans for capital purposes. It is possible that loan notes may not fall under these requirements: this is being confirmed with our external advisers.

2.2 As set out in the report to Cabinet there are a number of routes whereby land can be transferred to the JV. Depending on the route for land transfer, there may be a need for the County Council to provide a loan to HLL for the full sum of the best consideration, rather than just for the required equity. This would occur when land is transferred to HLL rather than direct to the JV. In these circumstances there would be a part re-payment of the loan/loan notes when the land is transferred to the JV with the balance being repaid when the developed properties are sold.

2.3 Some further loans may be made to HLL, to cover operational costs – as these will be service loans financing revenue costs these will not be capital expenditure. Similar loans may be made to other subsidiaries or entities.

2.4 As the arrangements set out above are likely to fall within the definition of non-Treasury investment, the revised Capital Strategy will set a self –assessed limit for such loans. To cover all potential loan requirements, an upper limit of **£50m** for 2018/19 is proposed. This is deemed proportionate: although it is 6% of net revenue budget, some of the initial capital receipts could be held to cover any non-repayment of loans.

2.5 An allowed "expected credit loss" model for loans and receivables, as set out in International Financial Reporting Standard (IFRS) 9 *Financial Instruments* as adopted by proper practices, will be used to measure the credit risk of the Council's loan portfolio.

2.6 Credit risk will be managed by the Council's oversight of management information from the JV and HLL, which will signal any emerging issues and allow mitigating action to be taken.

2.7 Where the transactions count as expenditure for capital purposes, they will add to the agreed Capital Programme. It is proposed that they are funded from the gross capital receipt received for the land being developed, and so will not increase the need to borrow. These variations will be reported to Cabinet within the Finance Monitor.