ISLINGTON

Resources Directorate
7 Newington Barrow Way, London, N7 7EP

Report of: Executive Member for Finance and Performance

Meeting of	Date	Ward(s)
Council	23 September 2021	All

Delete as appropriate	~~Exempt~~	Non-exempt

SUBJECT: FLEXIBLE USE OF CAPITAL RECEIPTS STRATEGY

1. Synopsis

1.1 This is a report to seek the adoption of a Flexible Capital Receipts Strategy as outlined in the 'Proposed Usage' section of this report. This strategy would be required if the council was to go ahead with the proposed additional payments to the Pension Fund to reduce its deficit and make savings over the longer term.

1.2 In December 2017, the Secretary of State announced the continuation of the capital receipts flexibility programme, which provides Local Authorities the freedom to use capital receipts generated from the sale of assets (with the exception of Right to Buy disposals) to fund revenue costs arising from transformational revenue projects that deliver savings.

1.3 Ordinarily only expenditure qualifying as capital may be funded from these capital resources. The additional flexibility therefore provides the council with a potentially valuable resource to invest in schemes which deliver savings or improvements.

1.4 The council currently holds a deficit on its Pension Fund which will ultimately lead to a revenue cost to the council. The early repayment of this deficit will save the council money over a 19 year deficit repayment period. Executive considered a report on the 2^{nd} September 2021 which recommended an approach to Council of utilising Flexible Capital Receipts to repay the deficit. This is attached to this report as Appendix A.

1.5 The Council (General Fund) is expecting £30m of capital receipts in 2021/22, which could be used to make a one-off contribution towards the balance of the Pension Fund deficit. A further £24m of capital receipts is expected by 2023/24, which could be applied for the same purpose.

2. Recommendations

2.1 To note the 'Impact on Prudential Indicators' section of this report.

2.2 To agree to the adoption of a Flexible Capital Receipts Strategy as outlined in the 'Proposed Usage' section of this report.

3. Background

3.1 Before the council can flexibly use capital receipts it must prepare, publish and maintain a flexible use of capital receipts strategy. This must consider the impact of this flexibility on the affordability of borrowing by including updated prudential indicators. Full Council must approve this strategy before any qualifying expenditure is incurred.

3.2 Under the Flexible Capital Receipts guidance, the Secretary of State sets out that individual authorities are best placed to decide which expenditure projects are best to be funded by this method in local areas. The key criteria for expenditure to qualify is that the schemes must be designed to generate ongoing revenue savings in the delivery of public services and/or transform service delivery to reduce costs and/or transform service delivery in a way that reduces costs or demand for services in future years for any of the public sector delivery partners.

4. Proposed Usage

4.1 The proposed usage of the capital receipts is to make additional payments to the council's Pension Fund and therefore minimising deficit recovery payments over the remainder of the 19 year recovery period.

4.2 The Council (General Fund) is expecting £30m of capital receipts in 2021/22, which is proposed to be used to make a one-off contribution towards the balance of the Pension Fund deficit. A further £24m of capital receipts is expected by 2023/24, which could be applied for the same purpose.

4.3 Using these capital receipts to reduce the Pension Fund deficit would reduce the total contribution that the Council would need to make to the Pension Fund, and the number of years over which the Council made these payments. This is illustrated in the table below, but it must be noted these are high-level estimates and the actual performance of the fund will vary so the figures below should be viewed as illustrative only.

	Capital receipt: £30m	Capital receipt: £54m
Total contribution to repay deficit	318	283
Saving against current deficit payment schedule at 2019 valuation (estimated £360m)	**(42)**	**(77)**
Initial capital receipt contribution	30	54
Borrowing cost (19 years - interest @at 1.56%)	9	16
Net saving after cost of borrowing and repayment (£m)	**3**	**7**

5. Impact on Prudential Indicators

5.1 Capital receipts generated are currently used to support the funding of the Council's capital programme. Using the capital receipts for pension fund deficit payments would therefore have a corresponding impact on the amount the Council would need to borrow to fund its planned capital programme.

5.2 The Authorised Borrowing and Operational Borrowing Limit prudential indicators will not be exceeded in 2021/22 as the council now does not expect to externally borrow the amount it had originally budgeted for. The update to future years Prudential Indicators will be factored into the council's budget setting process.

5.3 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 many years into the future. The Section 151 Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable because updated revenue costs of the planned borrowing can be fully met within the 2021/22 revenue budget and MTFS.

6. Implications

Financial Implications

6.1 Utilising borrowing instead of capital receipts will increase the Council's borrowing requirement. This is affordable and will remain within prudential indicators. Amendments to the capital financing of items within the capital programme will be required to accommodate the change.

6.2 If the Council makes any form of additional payment to partially extinguish the deficit, the actuary will not review its rate certificate until the next valuation, meaning the **c**ouncil must continue to pay against its expected contributions until they are revised.

6.3 The following table sets out the presently agreed contributions together with the actuary's view of what contributions are theoretically required. The Council's deficit recovery plan currently assumes a significant step up in revenue cost in 2026/27. The lower payments in prior years is supplemented by a required additional performance on the pension fund's assets in order to make up the shortfall.

Year	Deficit Lump Sum Agreed £m	Full Theoretical Deficit Lump Sum £m
2020/21	8.2	13.39
2021/22	8.52	13.91
2022/23	8.85	14.45
2023/24	9.2	15.01
2024/25	9.56	15.60
2025/26	9.93	16.21
2026/27	16.84	16.84
Total	**71.1**	**105.41**

Legal Implications

6.4 Local authority pension funds operate under the provisions of the Public Service Pensions Act 2013 and the Local Government Superannuation Act 1972. The Council is the "administering authority" of the Islington Pension Fund (the Fund) under the Local Government Pension Scheme (LGPS). The Council is also one of the "scheme employers" in the Fund.

6.5 The LGPS is:- (1) A defined benefit scheme; and (2) A funded scheme, and the Council has duties to:

6.5.1 Make minimum deficit recovery contributions, based on triennial actuarial valuations, under Regulation 62 of the LGPS Regulations and an actuarially prepared 3 years Rates and Adjustments Certificate (the Certificate), to secure the solvency of the Fund and its long-term cost efficiency; and

6.5.2 Make contributions to the Fund each year under Regulations 16 and 67-71 inclusive.

6.6 The wording and interpretation of the Regulations do not appear to prevent an authority making a prepayment of contributions, and the current Rates and Adjustments certificate allows for contribution over payments to be made. In practice where a prepayment extends beyond the period of the prevailing Rates and Adjustment Certificate (i.e. 31 March 2023 here), the deficit would be re-set at the next valuation to consider the updated funding strategy and experience over the inter-valuation period (i.e. over 2019 – 2022). The impact of the prepayment would then be taken into account in future contribution outcomes arising from that valuation.

6.7 The Council has also sought legal advice from James Goudie QC who has advised that the Council has the legal power to make a beneficial prepayment in respect of its overall deficit (under the General Power of Competence in section 1 of the Localism Act 2011).

6.8 Section 151 of the Local Government Act 1972 states that: "without prejudice to section 111, every local authority shall make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs". Section 111 of the Local Government Act 1972 relates to the subsidiary powers of local authorities.

6.9 The Local Government Act 2003 ("the Act"), section 15(1) requires a local authority "… to have regard (a) to such guidance as the Secretary of State may issue, and (b) to such other guidance as the Secretary of State may by regulations specify …".

6.10 The Statutory Guidance "Statutory Guidance on the Flexible Use of Capital Receipts (updated)" is issued under section 15(1) of the Act and authorities are therefore required to have regard to it.

6.11 The Statutory Guidance defines qualifying expenditure as 'Qualifying expenditure is expenditure on any project that is designed to generate ongoing revenue savings in the delivery of public services and/or transform service delivery to reduce costs and/or transform service delivery in a way that reduces costs or demand for services in future years for any of the public-sector delivery partners. Within this definition, it is for individual local authorities to decide whether or not a project qualifies for the flexibility' and goes on to give examples of qualifying expenditure including: 'Funding the cost-of-service reconfiguration, restructuring or rationalisation (staff or nonstaff), where this leads to ongoing efficiency savings or service transformation'.

6.12 It is the Section 151 Officer's opinion that the approach described within this paper for the Flexible Use of Capital Receipts meets the definition required within the Statutory Guidance.

6.13 Full Council approval is required for the use of the capital receipts.

Environmental Implications

6.14 This report does not have any direct environmental implications.

Resident Impact Assessment

6.15 The Council must, in the exercise of its functions, have due regard to the need to eliminate discrimination, harassment and victimisation, and to advance equality of opportunity, and foster good relations, between those who share a relevant protected characteristic and those who do not share it (section 149 Equality Act 2010). The Council has a duty to have due regard to the need to remove or minimise disadvantages, take steps to meet needs, in particular steps to take account of disabled persons' disabilities, and encourage people to participate in public life. The Council must have due regard to the need to tackle prejudice and promote understanding.

6.16 This report considers options for financial investment and does not have direct policy implications, so a separate RIA is not required for this report.

Conclusion and reasons for recommendations

6.17 The Council is incurring additional costs in relation to holding a pension deficit. The recommendations support the reduction of this deficit in a financially advantageous way to both the General Fund and the Pension Fund. Should the recommendations not be adopted then the Council will continue to stand higher interest costs that it could avoid.

Appendices: Appendix A: Pension Fund Deficit Payments
(Report to Executive 2nd September 2021)

Background papers: None

Final report clearance:

Signed by:

15 September 2021

Executive Member for Finance and Performance	Date

Responsible Officer: Dave Hodgkinson, Corporate Director of Resources (Section 151 Officer)

Report Author: Paul Clarke, Director of Finance

Legal Implications: Peter Fehler, Director of Law and Governance (Monitoring Officer)