

## FINANCIAL CODE 2

# CAPITAL BUDGET PREPARATION & MONITORING

### 1. Background

1.1 This Financial Code gives guidance on the overall management of the Capital Investment Strategy including budget preparation, monitoring and funding arrangements.

1.2 The Code provides a definition of capital expenditure and the policy framework for the preparation, monitoring and reporting of the Capital Investment Strategy. It defines the procedures to be adopted by the Chief Financial Officer and other Chief Officers in the development of the Council's Capital Investment Strategy and capital budget monitoring.

1.3 The code also sets out the arrangements for the control of cost and timescale variations from initially agreed plans and sets out the level of authority delegated from Full Council to Service Committees and to Chief Officers.

1.4 In addition to sound financial management and contributing to Best Value, the need for effective arrangements for capital budget preparation and monitoring flows from a number of sources including: -

- Section 95 Local Government (Scotland) Act 1973,
- The Local Government in Scotland Act 2003,
- The CIPFA Prudential Code for Capital Finance in Local Authorities,
- The Council's Financial Regulations,
- The General Accounting Framework & The Prudential Code.

1.5 The Local Government in Scotland Act 2003 sets out that it is the duty of a local authority to determine the maximum amount it can afford to allocate to capital expenditure and that, in discharging this duty, the authority must comply with capital expenditure regulations. The capital expenditure regulations state that councils must comply with the provisions of the *CIPFA Prudential Code for Capital Finance in Local Authorities*.

1.6 The Prudential Code stipulates that councils must be able to demonstrate, on an on-going basis, that capital spending and associated borrowing is affordable, prudent and sustainable and complies with Best Value requirements. The Council meets this requirement by annually approving a series of prudential indicators and ensuring that there are suitable arrangements for monitoring the indicators on an on-going basis. In addition, when considering, agreeing and implementing a capital investment strategy, the Prudential Code requires councils to take account of a variety of factors such as value for money, asset management planning, practicality and achievability.

1.7 The Chief Financial Officer is responsible for reporting to the Council on all relevant matters to be taken into account by the Council when setting prudential indicators and for establishing procedures for the agreement and monitoring of these indicators.

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1.8 To ensure the effective integration of revenue and capital budget planning, and to ensure the affordability of capital investment levels, the Capital Investment Strategy will be agreed alongside the 3 Year Revenue Budget as part of an integrated process. The Chief Financial Officer will continually assess the affordability of the Capital Investment Strategy in terms of the Council's overall Financial Strategy and the likely impact upon the Revenue Account, advising the Council on affordability in light of available revenue resources.

## 2. Definition of Capital Expenditure

2.1 The CIPFA Accounting Code of Practice defines capital expenditure as '*All expenditure on the acquisition, creation or enhancement of fixed assets*'. Examples include, but are not limited to: -

- Acquisition, reclamation, enhancement or laying out of land,
- Acquisition, construction, preparation, enhancement or replacement of roads, buildings and other structures,
- Acquisition, installation or replacement of moveable or immovable plant, machinery, apparatus, vehicles and vessels; and,
- Acquisition, installation or replacement of information and communication technology.

2.2 Enhancement of an asset refers to investment that will significantly lengthen the useful life of the asset; increase the open market value of the asset; or increase the extent to which the asset can or will be used.

2.3 Capital income relates to receipts received on the sale or disposal of a fixed asset (net of the costs of selling/disposal) or the value of grants/contributions received to offset the cost of a new fixed asset.

2.4 Only expenditure and income that meet the above definitions should be recorded against the capital investment strategy. Conversely, all expenditure and income that meet the above definitions must be recorded as capital expenditure, including items where the revenue budget provides the funding source.

2.5 Salary costs are allowable capital expenditure when the post being charged to a capital project makes an identifiable and measurable contribution to the physical development of property, plant and equipment. Any staff costs charged to Capital should comply with the CIPFA Code of Practice and approval should be sought from Finance & Procurement prior to any staff costs being charged.

2.6 Capital project budgets should cover all costs required to bring the asset into operation (including equipment, furniture etc.) and any revenue implications must be clearly identified at the project development stage to encourage the development of projects that reduce running costs and the avoidance/restriction of projects that add to running costs.

2.7 Where expenditure is incurred to ensure a fixed asset maintains (rather than enhances) its previously assessed standard of performance, this must be treated as revenue spending and recognised in the revenue account as it is incurred.

### 3. Development of the Capital Investment Strategy

#### Funding of the Capital Investment Strategy

3.1 To support the development of the Capital Investment Strategy, the Chief Financial Officer will report to the Council on the level of financial resources estimated to be available to support the Capital Investment Strategy in each financial year alongside estimates of ongoing capital commitments based on previous approvals.

3.2 Estimated funding available to support the Capital Investment Strategy will reflect a combination of the following: -

- **Borrowing** – Borrowing undertaken on a prudential basis to support capital investment. Members will determine the level of borrowing to be undertaken and will receive advice from the Chief Financial Officer on the level of borrowing that is prudent, affordable and sustainable,
- **General Capital Grant** – Non-ring-fenced funding provided by the Scottish Government to support capital investment,
- **Other Grants** – funding provided by the Scottish Government and/or other bodies to support individual projects and therefore ring-fenced for that purpose,
- **Capital Receipts** – Funding generated through the sale of fixed assets (excluding vehicles which are used to support vehicle replacement). In conjunction with the Property, Estates & Programmes Manager, the Chief Financial Officer will determine the estimated value of asset sale receipts obtainable over the period of the Capital Investment Strategy,
- **Use of Revenue Funding and Reserves** – Funding from resources held in reserves, including the Capital Fund, and revenue funding to support capital investment (CFCR).

#### Allocation of Funding Within the Capital Investment Strategy

3.3 Full Council, as part of budget setting in February each year, determines the overall level of capital investment and the strategic direction of the Capital Investment Strategy by agreeing funding allocations to Strategic Projects and Asset Class Programmes within a 10 year planning period. Full Council will also receive a mid-year report on the progression of the Capital Investment Strategy to provide an opportunity for any required revisions to the agreed Strategy.

3.4 Strategic Projects – these are projects that are of significant strategic significance to the Council as a whole and/or projects whose funding requirements exceed the levels that could realistically be accommodated within Asset Class allocations.

All Strategic Projects must follow the Council's approved *Gateway Process* which has been developed to align with the HM Treasury "Guide to Developing the Project Business Case – Better Business Cases" and recognised best practice. The business case must demonstrate the Strategic, Economic, Commercial, Financial and Management case for the project, ensuring alignment with the Council Plan and that any revenue consequences of the project have been fully considered. Only when a strategic project has progressed to the appropriate stage (Gateway 3) of the approved process will it be included in the Capital Investment Strategy.

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**3.5 Asset Classes** – Full Council allocates funding to Service Committees (Economy & Infrastructure Committee for all asset classes except the Digital/ICT Asset Class which is overseen by the Enabling & Customer Services Committee) to be used to fund upgrades, replacements, and enhancements of existing assets and some new builds. It is essential that Service Committees have a degree of certainty regarding funding allocations for at least a 3-year period to allow medium term investment programmes to be effectively developed and to support projects that span more than one financial year.

The funding allocated by Full Council for each Asset Class is then allocated to projects and programmes by the relevant Service Committee (Economy & Infrastructure Committee for all asset classes except the Digital/ICT Asset Class which is overseen by the Enabling & Customer Services Committee) who will annually agree detailed allocations within a rolling 3-year programme. Budgets for individual projects within Asset Classes must be reported to Service Committees for approval at the beginning of each financial year, and by no later than June each year. Any individual project over £250K (including where it is within an overall programme of works) must be detailed and reported separately as part of the Asset Class Programme.

To ensure that funding allocations to asset classes are fully and effectively utilised, the development of detailed capital investment programmes within each asset class will be supported by: -

- The use of an appropriate (to that asset class) scoring/prioritisation system to ensure that funding is allocated to support the achievement of identified priorities and fully recognises the revenue consequences (including running cost savings) of competing projects.
- A focus on spend to save opportunities whenever possible
- The use of 'reserve lists'/over-commitment in the spending plans to ensure that, where delays occur against approved projects, there is an ability to effectively utilise the released funding.
- A key focus on project delivery arrangements to ensure that projects are delivered in line with appropriate outputs, budgets and timescales; and
- Clear arrangements for the control of variations from agreed programmes and clarity on the level of delegated authority provided to officers to approve works and incur costs.

The detail of the above arrangements should be agreed by the Economy & Infrastructure Committee (Enabling & Customer Services Committee for Digital/ICT) taking into consideration the nature of the capital projects being undertaken within each asset class.

**3.6** The agreement of Full Council to the Capital Investment Strategy, and subsequent agreement of Asset Class Programmes by the Economy & Infrastructure Committee and the Enabling & Customer Services Committee, provides Chief Officers with approval to incur expenditure on the individual capital projects contained therein up to the amounts identified, and to the timeframes presented and agreed.

### **Spend to Save Capital Projects**

**3.7** It is important that the allocation of funding to Strategic projects and asset classes within the Capital Investment Strategy fully takes into account future revenue implications of capital projects and seeks to reduce costs where possible. In addition, specific Spend to Save Capital Projects can be agreed outwith/beyond the Capital Investment Strategy where specifically agreed by Full Council or Enabling & Customer Services on a spend to save basis.

**3.8** Spend to Save Projects should be linked to the delivery of revenue savings/income generation

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and the savings identified must be sufficient to fully offset the cost of the resultant increase in loan charges from the additional borrowing. Any proposals should be put forward through the agreed template and adhere to the spend to save policy. All spend to save proposals should be presented to the Capital Investment Programme Board for challenge and scrutiny prior to being presented to Full Council or the Enabling & Customer Services Committee for approval.

3.9 Savings identified from any proposal approved on a spend to save basis will be removed from the revenue budgets identified in line with the template and will be made available to Members to be included in the budget setting process.

## **4. Variations to the Capital Investment Strategy / Plans**

4.1 The oversight and management of the delivery of the Capital Investment Strategy is delegated to the Economy & Infrastructure Committee. To support the Economy & Infrastructure Committee to effectively undertake this role, and to avoid unnecessary delays, Full Council determines parameters within which the Economy & Infrastructure Committee may make changes to approved funding allocations without seeking the prior approval of Full Council. Any required changes beyond these parameters (as set out below) require the prior approval of Full Council before being progressed.

4.2 Variations may include: -

- Changes to the overall level of capital investment spending
- Increases, underspends and/or overspends against approved budgets
- The virement/transfer of funding between Strategic Projects and AssetClasses.
- Changes to the timing/profile of approved project costs (ie.the acceleration or slippage of funding between years)

4.3 All variations agreed by the Economy & Infrastructure Committee under the arrangements set out below will be subsequently reported to the Enabling & Customer Services Committee or Full Council. Any changes to the arrangements below will be subject to the prior approval of Full Council.

### 4.4 Variations to Overall Capital Investment Strategy

The Economy & Infrastructure Committee has delegated authority to increase overall capital spending (beyond the levels approved at the start of each year by Full Council) by up to 5% each year for the first 3 years of the Capital Investment Strategy. Such changes will be subject to the approval of the Chief Financial Officer (to ensure affordability within the 10 Year Investment Strategy and the agreed loan charges budget), and subsequent reporting to Enabling & Customer Services Committee or Full Council.

The inclusion of any new Strategic Projects within the capital investment strategy requires the approval of Full Council.

### 4.5 Variations to Strategic Projects Budgets

The Economy & Infrastructure Committee has delegated authority to increase individual Strategic Project budgets (beyond the levels approved at the start of each year by Full Council) by 5% of the total project budget (or £0.5M, whichever is the greater). Such changes will be subject to the approval of the Chief Financial Officer (to ensure affordability within the 10 Year Investment Strategy and the agreed loan charges budget) and subsequent reporting to Enabling & Customer Services Committee or Full Council.



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Any accumulation of changes to Strategic Project budgets must be within the Variation to Overall Capital Investment Strategy parameters at 4.4 above. Any proposal beyond this level will be subject to the prior approval of Full Council.

### 4.6 Virement Between Approved Project/Asset Class Budgets

The Economy & Infrastructure Committee also has delegated authority to vire funding (from the levels approved at the start of each year by Full Council) between Strategic Projects and/or Asset Classes by 10% (or £1M whichever is the greater) with subsequent reporting to the Enabling & Customer Services Committee or Full Council. Any virement outwith these parameters would require the approval of Full Council. This provides the Economy & Infrastructure Committee with the flexibility to manage project and asset class variances without requiring to increase the overall level of capital spending.

### 4.7 Changes to the Timing/Profile of Project/Asset Class Costs (Acceleration & Slippage)

Where it is identified that net spending on a project or asset class is likely to vary from the agreed annual profile (i.e. variation to timing of spend but not to total project/asset class costs), the Economy & Infrastructure Committee may pull forward/accelerate or slip/push back up to 10% (or £250k, whichever is the greater) of the following year's allocation on the basis that the following year's allocation will be reduced or increased accordingly. Any proposal to accelerate/slip funding beyond this level will be subject to the prior approval of Enabling & Customer Services Committee or Full Council.

Any accumulation of changes must be within the Variation to Overall Capital Investment Strategy parameters at 4.4 above. Any proposal beyond this level will also be subject to the prior approval of Full Council.

### 4.8 Variations Within Asset Class Allocations

Total funding for each of the Asset Classes is determined by Full Council. How that funding is then prioritised, and details of the projects to be included in each Asset Class Programme, are then determined by Economy & Infrastructure Committee (with the exception of Digital/ICT Asset Class which is determined by Enabling & Customer Services Committee). These committee will take advice from other Committees as appropriate (particularly for the Schools asset class that is heavily influenced by the School Estate Strategy).

Budgets for individual projects within Asset Classes must be reported to the Economy & Infrastructure Committee (Enabling and Customer Services Committee for Digital/ICT) for approval at the beginning of each financial year, and by no later than June each year. Any individual project over £250K (including where this is within an overall programme of works) must be detailed and reported separately as part of the Asset Class Plans.

### 4.9 Chief Officer Delegations

In recognition of the need to progress capital projects effectively and without unnecessary delays, there is a requirement for Chief Officers to have a level of flexibility to vary budgets within agreed parameters.

The Economy & Infrastructure Committee (Enabling & Customer Services Committee for Digital/ICT) is responsible for clearly setting out the arrangements and parameters for any officer variations to the Capital Investment Strategy. In line with the approach outlined above for Service Committee delegations, these arrangements should cover each of: -

- The acceleration or slippage of funding for Strategic Projects

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- Underspends and/or overspends against budgets approved for each individual project within the Asset Classes,
- The acceleration or slippage of funding between years for each project within the Asset Classes,
- The virement/transfer of funding, on either a temporary or permanent basis, between projects within the AssetClass.

The agreed Officer delegations from Service Committees is attached at Appendix 1 (*note that current approved delegations will remain unchanged at this stage but will be subject to potential change following further review*).

Any planned variation to individual project budgets in excess of the authorisation limits indicated at Appendix 1 must be reported to the relevant Service Committee for agreement.

### Expedited Procedures

In exceptional circumstances when there is an urgent need for a decision to accelerate/approve additional funding for a project, the Executive Director, with written agreement of the Chair and Vice Chair of the relevant service committee and the Chief Financial Officer, may approve this so long as it is within the delegated committee limits indicated above. Any decisions taken in this manner must be retrospectively reported to the next available meeting of the relevant service committee.

## 5. Capital Monitoring and Reporting

### 5.1 Responsibilities of Chief Financial Officer

The Financial Regulations state that the Chief Financial Officer is responsible for advising the Council on all financial matters as well as monitoring and reporting on its financial performance and overall financial position.

As part of this, the Chief Financial Officer will maintain appropriate financial models that:-

- Monitor capital expenditure and income patterns over the life of capital projects,
- Forecast capital expenditure and income for agreed capital projects,
- Continually assesses the impact of capital investment levels upon the Council's revenue account and affordability in terms of the Council's overall Financial Strategy.

The Chief Financial Officer is also responsible for producing quarterly (as a minimum) summary monitoring reports on the financial progress of the overall Capital Investment Strategy for presentation to the Enabling & Customer Services Committee.

The Chief Financial Officer will also ensure that financial monitoring appendices are provided to the Executive Director Economy & Infrastructure to support the quarterly (as a minimum) reports to the Economy & Infrastructure Committee demonstrating progress and performance against agreed delivery timescales and budgets for the all projects and asset classes within the Capital Investment Strategy.

### 5.2 Responsibilities of Executive Director Economy & Infrastructure

The Executive Director Economy & Infrastructure is responsible for the management and delivery of the Capital Investment Strategy and for securing best value for expenditure incurred, with the objective of achieving the policies of the Council at minimum cost. The arrangements, procedures and systems under their control should ensure the Council's affairs are conducted without waste or extravagance and with full regard for probity and propriety.

All procurement activity in relation to the capital projects should be conducted in line with the

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Council's Procurement Standing Orders. An adequate allowance for the time taken to perform a robust and legally compliant tender process should be built into overall project timescales.

The Executive Director Economy & Infrastructure is fully accountable for their project managers in terms of monitoring and controlling capital budgets.

The approval of the Capital Investment Strategy by Full Council, and the Asset Class Plans agreed by the Economy & Infrastructure Committee (Enabling & Customer Services Committee for Digital/ICT only) each year, provide officers with authority to incur expenditure for the agreed purpose and up to the agreed budget level. Capital expenditure may only be incurred on projects/programmes of work approved through the relevant committee and only to the amounts of the approved funding allocations, considering the flexibility arrangements detailed in section 4 above.

The Executive Director Economy & Infrastructure is required to produce quarterly reports (as a minimum) for the Economy & Infrastructure Committee demonstrating progress and performance against agreed delivery timescales and budgets for the all projects and asset classes within the Capital Investment Strategy.

These reports will be supported by a financial appendix, provided by the Chief Financial Officer, showing:-

- Projected expenditure vs budget for the current year,
- Projected expenditure vs budget over the life of the project,
- Actual expenditure to date (in year and over the life of the project),
- Projected variance from the approved budget (in year and over the life of the project).

Any project within an overall works programme with a total project spend of over £250K must be reported separately.

### 5.3 Responsibilities of Executive Director Enabling & Customer Services

The Executive Director Enabling & Customer Services is responsible for the overview and delivery of the Digital/ICT asset class and is required to produce quarterly monitoring reports (as a minimum) for the Enabling & Customer Services Committee demonstrating progress and performance against agreed delivery timescales and budgets for projects within the Digital/ICT asset class.

A summary of the progress of the Digital/ICT asset class will also be reflected within the quarterly monitoring reports on the progress of the overall Capital Investment Strategy produced by the Executive Director Economy & Infrastructure as set out under section 5.2 above.