

Agenda Item	4.b
Report No	RES/25/22

THE HIGHLAND COUNCIL

Committee: Corporate Resources Committee

Date: 1 December 2022

Report Title: Corporate Capital Monitoring report for Quarter 2 2022/23

Report By: Head of Corporate Finance

1. Purpose/Executive Summary

- 1.1 This report provides Members with the corporate capital monitoring statement for the second quarter of the 2022/23 financial year to 30th September 2022, which presents a summary of the actual spend together with a forecast 2022/23 year end outturn position.
- 1.2 Net spend on capital projects to the end of Q2 2022/23 totalled £62.520m for the General Fund against a net annual budget figure of £158.752m. Net spend on capital projects for the Housing Revenue Account (HRA) totalled £23.146m against a net budget figure of £54.236m.
- 1.3 The forecast net outturn for the General Fund for 2022/23 totals £127.038m and this would give rise to a forecast net underspend against budget of £31.714m. The forecast net outturn for the HRA for 2022/23 totals £52.742m and this would give rise to a forecast net underspend against budget of £1.494m. The forecast underspends are primarily a result of a lack of availability of contractors and materials affecting the construction sector.
- 1.4 The report also highlights how the planned capital expenditure for 2022/23 will be funded, with borrowing accounting for over 70% of total forecast spend.
- 1.5 **Appendix 3** to the report provides Members with the whole life financial overview and risk assessment rating in respect of the Council's major projects in the General Fund Capital Programme.

2. Recommendations

- 2.1 Members are asked to:
 - i. Note the spend for Q2 2022/23, the estimated year end outturn and the funding profile.
 - ii. Note the whole life financial overview and risk assessment rating for the major capital projects.

- iii. Note that the review of the capital programme remains ongoing and an update will be brought to a special meeting of the Council on a date yet to be determined.

3. Implications

- 3.1 Resource - Resource implications are discussed in the report.
- 3.2 Risk - Risk implications to the budget position, and budget assumptions, will be kept under regular review and any project-specific risks identified reported to future Committees. The affordability of the capital programme as a whole is subject to variations in construction industry inflation and changes in interest rates.
- 3.3 Legal - The contents of this report and the annual accounts aim to satisfy the requirement of Sections 6 and 7 of the CIPFA Financial Management Code- 'Monitoring financial performance' and 'External financial reporting'.
- 3.4 There are no specific equality, climate change/Carbon Clever, rural or Gaelic implications arising as a direct result of this report. However, the capital programme will have a major impact on the Council's delivery of net zero targets and so is included as one of the thematic groups in the Council's Net Zero Strategy.

4. General Fund Capital Programme Q2 2022/23

- 4.1 **Appendix 1** provides a summary of the capital programme budgets, spend and income for Q2 of financial year 2022/23, along with the estimated outturn position forecast for the end of the financial year. The actual figures provided reflect the net project expenditure, i.e. project costs incurred, less project-specific income received. The net budget for 2022/23 is £158.752m.
- 4.2 Overall there has been a net expenditure of £62.520m for Q2, which reflects 39% of the annual budget.
- 4.3 The estimated outturn position shows a net expenditure of £127.038m which would result in an estimated underspend against budget of £31.714m. The forecast underspend can be attributed to challenging market conditions, in particular a limited availability of contractors, consultants and materials due to a high volume of work across the construction industry and supply chain constraints. The estimated outturn will continue to be monitored closely.
- 4.4 Individual project spend forms the basis of the capital reports to Strategic Committees and links to those papers are provided below:
 - **Communities & Place Committee:**
https://www.highland.gov.uk/download/meetings/id/80755/item_6_capital_budget_monitoring_report_202223_quarter_2
 - **Housing & Property Committee:**
https://www.highland.gov.uk/download/meetings/id/80780/7_property_capital_monitoring_statement_and_progress_update
 - **Economy & Infrastructure Committee:**
https://www.highland.gov.uk/download/meetings/id/80724/item_7_capital_monitoring_quarter_2_202223

5. Major Capital Projects

5.1 **Appendix 3** provides a summary of the whole life financial position for the Council's major projects to the end of Q2 2022/23. The reporting of major projects provides an estimated outturn over the entire life of each major project, spanning multiple financial years where relevant. The estimated outturn is presented alongside the whole life budget, as per the approved Capital Programme, and the actual expenditure incurred and project-specific income received to date. The estimated outturn will be reviewed on a regular basis and any changes will be reported to future Strategic Committees.

5.2 In addition to the presentation of financial information, the report also includes a review of the level of risk associated with each project's **cost, scope and timing**, using a RAG rating system, as follows:

- **Red** – there are major concerns the project will not deliver as intended.
- **Amber** – there is some concern the project will not deliver as intended.
- **Green** – the project is still on track to deliver as intended.

A summary of the key issues is highlighted below:

Cost - almost all projects have been rated red for cost unless they have been procured under fixed price arrangements or are nearing completion. This reflects the high level of inflation currently affecting the economy and the level of uncertainty about how pricing will change in the months and years ahead. Contractors, sub-contractors and suppliers are factoring in additional risk allowances to cover further increases, particularly for projects with a longer construction period. The Highlands also faces a higher cost location factor, particularly when procuring from the central belt.

Timing – global supply chain issues are having a significant impact on lead times to procure materials, contractors, equipment and vehicles. The lead time on some new fleet can be up to 24 months and ICT projects are affected by the global semiconductor chip shortage. The ability to plan ahead is key but is hindered to an extent by the uncertainty around pricing and affordability.

Scope – the knock-on effect of rising prices and lack of availability of resources puts some projects at risk of being unable to deliver their original intended scope. Those rated red are predominantly multi-year infrastructure and property estate upgrade programmes where the level of risk and uncertainty make it very difficult to predict what those programmes will be able to achieve in the years ahead. Should current market conditions fail to improve in the foreseeable future, there will be a significant reduction in the achievable scope of works across the board.

5.3 Given the wider uncertainties around the capital programme a number of projects in their very early stages have been ranked as 'tbc'. For those projects it is very difficult to give a clear assessment at this stage however there is significant cost risk across all of those projects.

5.4 The reporting of major projects to other Strategic Committees has taken place and links to those papers are as provided in section 4.4 above.

6. HRA Capital Programme Q2 2022/23

- 6.1 **Appendix 4** presents the actual spend for Q2 of 2022/23 and the anticipated outturn for the full financial year. The Q2 spend is £23.146m, equating to 43% of the annual budget of £54.236m. The anticipated outturn for 2022/23 is £52.742m which would result in a projected underspend of £1.494m.
- 6.2 The delivery of capital investment contracts is at risk for a number of reasons. With particular regard to housing projects, the construction industry at both a Highland and a national level continues to experience labour and materials shortages. These issues are causing longer lead-in times, higher prices, and price volatility. The unprecedented uncertainty regarding materials, coupled with ongoing resourcing issues, has been demonstrated by no tender returns for some projects and higher than budgeted prices on returned tenders. Industry experts predict little improvement until at least the beginning of 2023 with further market and construction industry uncertainty exacerbated by the conflict in the Ukraine and the ongoing energy crisis.
- 6.3 An estimated 277 new Council house builds are anticipated to be completed by 31 March 2023. These are part-funded through Housing Revenue Account borrowing with grant provided by The Scottish Government supplemented by a contribution from the Council Landbank Fund.

7. Funding of the Capital Programme

- 7.1 **Appendix 2** presents how the General Fund capital expenditure expected to be incurred in 2022/23 will be funded. Borrowing continues to be the largest source of funding with £90.152m forecast, amounting to 71% of forecast capital expenditure. The General Capital Grant (which includes specific elements in relation to flood and roads/bridge infrastructure schemes) is expected to be £36.726m.
- 7.2 **Appendix 5** presents how the HRA capital expenditure expected to be incurred in 2022/23 will be funded. Borrowing continues to be the largest source of funding with £34.278m forecast, amounting to 65% of forecast capital expenditure. The other major sources of funding include the Scottish Government Grant of £16.000m and Landbank sales of £2.056m.
- 7.3 The level of borrowing required to support capital investment presents an ongoing challenge to the Council's financial sustainability. The repayment of borrowing (principal and interest) that is used to fund capital expenditure incurred today creates a future revenue budget commitment for up to 60 years. Rising interest rates will continue to add additional strain on future revenue budgets.

8. Capital Programme Review

- 8.1 As highlighted at the meeting of Council in October 2022, the review of the capital programme remains ongoing. This includes consideration of the affordability envelope in which the future capital programme must operate, especially given the ongoing revenue budget challenges. Rising construction prices coupled with rising interest rates results in a significant increase to the total payback on capital projects funded by borrowing. Estimations suggest the total payback has more than doubled when compared to the position from 12 months ago, rendering the current capital programme unaffordable given the revenue budget context. Further information regarding the review of the capital

programme will be reported at a Special meeting of the full Council – at a date yet to be determined.

Designation: Head of Corporate Finance

Date: 11th November 2022

Authors:

Edward Foster - Head of Corporate Finance

Darryl Urquhart - Principal Accountant

Background papers:

https://www.highland.gov.uk/download/meetings/id/80778/item_5_housing_revenue_account_hra_capital_monitoring_report_to_30_september_2022

https://www.highland.gov.uk/download/meetings/id/79295/9_medium_term_financial_plan_-_capital_strategy_and_capital_programme_to_203637

MONITORING OF CAPITAL EXPENDITURE - 1ST APRIL 2022 TO 30TH SEPTEMBER 2022

SERVICE: GENERAL FUND

Project Description	BUDGET	ACTUAL			ESTIMATES			VARIANCE		
	2022/23 Budget (incl. carry forward from prior year)	2022/23 Actual Expenditure	2022/23 Actual Income	2022/23 Actual Net Year to Date	2022/23 Estimated Expenditure	2022/23 Estimated Income	2022/23 Estimated Outturn	2022/23 Variance Estimate v Budget	2022/23 Acceleration / (Slippage)	2022/23 Overspend / (Underspend)
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
COMMUNITY AND LEISURE FACILITIES	1,856	310	(114)	196	755	(114)	641	(1,215)	(1,215)	0
SCHOOLS	45,948	13,843	(25)	13,818	38,691	(337)	38,354	(7,594)	(7,594)	0
HEALTH & SOCIAL CARE PROGRAMME	7,303	104	(4)	100	903	0	903	(6,400)	(6,400)	0
ICT	4,172	3,305	0	3,305	4,172	0	4,172	0	0	0
ROADS AND BRIDGES	34,518	13,105	(535)	12,570	29,282	(2,871)	26,411	(8,107)	(8,112)	5
ACTIVE TRAVEL	2,001	1,008	(465)	543	3,529	(2,789)	740	(1,261)	(1,267)	6
LIGHTING, CCTV & RADIO MASTS	2,402	854	0	854	1,965	(20)	1,945	(457)	(457)	0
FLOOD PREVENTION	7,623	3,562	(108)	3,454	7,110	(108)	7,002	(621)	(621)	0
WASTE MANAGEMENT	7,841	5,358	0	5,358	7,993	0	7,993	152	152	0
FERRIES AND HARBOURS	19,116	12,467	(83)	12,384	40,139	(23,370)	16,769	(2,347)	(2,347)	0
BEREAVEMENT SERVICES	2,282	119	0	119	1,044	0	1,044	(1,238)	(1,238)	0
COMMUNITY SPACES	477	127	(167)	(40)	644	(167)	477	0	0	0
PUBLIC CONVENIENCES	330	39	(60)	(21)	603	(210)	393	63	63	0
STRATEGIC ASSET MANAGEMENT	14,234	3,061	0	3,061	10,283	0	10,283	(3,951)	(3,951)	0
VEHICLES & PLANT	4,883	1,541	(80)	1,461	4,883	0	4,883	0	0	0
PLANNING & DEVELOPMENT	1,650	7,092	(4,942)	2,150	10,579	(9,915)	664	(986)	(1,289)	303
CAPITAL CONTRIBUTIONS	800	2,702	(748)	1,954	7,841	(7,841)	0	(800)	(800)	0
CAPITAL DISCRETIONARY FUND	79	9	0	9	79	0	79	0	0	0
SELF FUNDING PROJECTS	(2,383)	1,115	(563)	552	2,210	(1,004)	1,206	3,589	3,589	0
HOUSING (NON HRA)	3,620	939	(246)	693	3,679	(600)	3,079	(541)	(541)	0
OVERALL TOTAL	158,752	70,660	(8,140)	62,520	176,384	(49,346)	127,038	(31,714)	(32,028)	314

FUNDING OF CAPITAL EXPENDITURE - 1ST APRIL 2022 TO 30TH SEPTEMBER 2022

SERVICE: GENERAL FUND

Funding	2022/23 Budget (incl. carry forward from prior year)	2022/23 Actual Net Year to Date	2022/23 Estimated Outturn	2022/23 Variance Est Outturn v Budget	2022/23 Acceleration / (Slippage)	2022/23 Overspend / (Underspend)
	£000	£000	£000	£000	£000	£000
General Capital Grant	36,726	18,691	36,726	0	0	0
Capital Receipts	160	160	160	0	0	0
Borrowing	121,866	43,669	90,152	(31,714)	(32,028)	314
TOTAL FUNDING	158,752	62,520	127,038	(31,714)	(32,028)	314

CAPITAL MAJOR PROJECT WHOLE LIFE REPORTING

CORPORATE RESOURCES COMMITTEE

Project Description	WHOLE LIFE BUDGET TO 2036/37			ACTUALS TO DATE			FORECAST TO END OF PROJECT			PROJECT ASSESSMENT			COMMENTS
	LIFE BUDGET EXPENDITURE	LIFE BUDGET INCOME	LIFE BUDGET NET	ACTUAL EXPENDITURE TO DATE	ACTUAL INCOME TO DATE	ACTUAL NET TO DATE	FORECAST EXPENDITURE	FORECAST INCOME	FORECAST NET	COST	TIMING	SCOPE	COMMENTS
	£000	£000	£000	£000	£000	£000	£000	£000	£000				
ICT Transformation (incl. Carefirst Management Information Systems Replacement)	50,368		50,368	7,520	-99	7,421	50,467	-99	50,368	R	R	R	An options appraisal for the future of the Data Centre may result in a change to the scope for future years. Also we are dependent on global supply and pricing of ICT equipment which could have a negative impact on cost and timing and therefore risk does exist given the current uncertainty affecting the economy.
Landfill Restoration Programme	9,302		9,302	7,156		7,156	9,302		9,302	R	G	G	The landfill restoration programmes profiled spend includes £72k in 22/23, £1.1m in 23/24 and £1m in 24/25, this is reflected in the overall forecast expenditure. However rising costs may impact on these forecasts. Some restoration cost may be delayed if capacity in Seater is used for authorised landfilling beyond 2025.
Residual Waste Management Facility - Longman Project	13,102		13,102	12,539		12,539	14,028		14,028	R	G	G	The Inverness WTS project is on course to be completed in Nov 2022, the forecast outturn remains £14.028m.
Vehicle & Plant Purchases (incl. Large Goods Vehs)	38,906		38,906	5,284	-2,000	3,284	40,906	-2,000	38,906	R	R	G	We are experiencing increased costs across all areas of vehicles and plant. The availability of materials and components used in manufacturing processes, the impact of inflation, Brexit and Covid, all affect the price and availability of vehicles and plant. The lead in time between ordering and delivery of a large goods vehicle is in the region of 18 months. We will keep the fleet replacement programme under review and monitor the impact of vehicle availability and cost (market and running costs) and any changes to the way Roads and Waste services operate in relation to their fleet requirements.
Road Structural Capital Works	119,266		119,266	17,109	-1,271	15,838	119,266		119,266	R	R	R	This budget includes various capital works related to the road asset which will be impacted by the rising cost of materials and labour, linked to inflation. Programmes will be adjusted to take account of the cost increases which may result in a reduction of renewal of assets in certain cases.
Road Surface Dressing Capital	36,140		36,140	5,874		5,874	36,140		36,140	R	R	R	The surface dressing programme budget will be impacted by the rising cost of materials and labour, linked to inflation. Programmes will be adjusted to take account of the cost increases which may result in a reduction or adjustment of programmed works.
Bridges, Retaining Walls & Culverts	8,141		8,141	641	-8	633	8,141		8,141	R	R	R	Because this is a rolling programme of projects, inflation can be managed by reducing the rate/number of projects progressed to maintain spend within budget.
Timber Extraction (STTS - Strategic Timber Transport Scheme)	19,921	-13,346	6,575	11,936	-8,251	3,685	19,921	-13,346	6,575	R	R	R	£200k outstanding commitments at Oct 2022. (But please note part of our commitment is £17k per year in ongoing rental charges for emergency propping at two bridges. Repair schemes are not yet developed. The full commitment to repair these bridges two would be circa £800k.)
The Inverness West Link	41,735	-3,362	38,373	42,469	-1,698	40,771	43,100	-3,362	39,738	A	A	A	This is a series of annual programmes which is largely dependent on annual funding awards. Programmes will be defined once level of funding is confirmed and will take account of pricing at that point in time.
Inshes Roundabout	8,638	-1,801	6,837	2,189	-399	1,790	9,500	-2,000	7,500	R	A	A	Developer contributions to fund future expenditure. Cost is Amber as majority of work completed. Stopping up Order for Beechwood Access to E & I November 22. Planning application will be lodged in 2022.
A890 Stromeferry Rockface Stabilisation	6,351		6,351	4,244		4,244	6,351		6,351	R	A	A	Works to repair small debris flow AA18 Autumn 22. Annual inspection Autumn 22.
B863 Invercoe Bridge, Lochaber	10,604		10,604	5,206		5,206	6,806		6,806	A	G	G	Construction contract (value = £5.5M) in place and work underway. Due for completion March 2023. Cost is amber as this is a lump sum contract with an inflation clause. There is also scope for compensation events that may increase costs. Note that budget increased due to award of Local Bridge Maintenance Funding - any excess unspent on Invercoe will be used to fund other bridges projects.
Naver Bridge	7,113		7,113	779		779	8,101		8,101	R	A	A	Design contract (value = £400k) in place - about to commence detailed design stage. Tender for construction contract Dec 2022, est. start on site May 2023, est. completion Dec 2024. Red status on price is due to a number of project and design risks, including inflation.
Active Travel Transformation (Highland)	11,550		11,550				11,550		11,550	R	R	R	Project Officer recruitment underway, initial AT capital programme to be produced and agreed at future strategic committee.
Structural Lighting Works	8,690		8,690	2,961	-527	2,434	10,017		10,017	R	R	R	This budget includes the rolling programme of replacement of end of life assets within the control of the lighting section to include lighting columns, underground cabling, traffic signals, pedestrian crossings. The reduction in budget is a significant pressure and risks having to turn off/cut down failed lighting columns or sections of lights, traffic signals and pedestrian crossings. There are also significant material cost increases which create another major budget pressure.
Caol FPW	12,854	-14	12,840	10,643	-524	10,119	13,404	-524	12,880	A	G	G	Works underway completion Summer 23. This is a lump sum contract and remains on target for completion cost. £500k extra income received to cover Scottish Water instructed changes.
Uig Ferry Terminal and Link Span	63,994	-38,399	25,595	20,653	-4,704	15,949	63,994	-38,399	25,595	R	A	A	Contract awarded July 2021. Construction works ongoing. Completion programmed for November 2023. Capital spend to be repaid from future income stream.
Inverness Castle	35,905	-20,350	15,555	7,581	-5,753	1,828	35,905	-20,350	15,555	A	G	G	Contract let, on programme, estimated completion Spring 2025. Fixed price contract currently on track.
Alness Academy	37,883	-3,101	34,782	37,417	-1,000	36,417	37,883	-3,101	34,782	G	G	G	New building operational from October 2020. phase 2 works completed in 2022.
Charleston Academy	16,011	-164	15,847	329		329	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Culloden Academy	19,218	-1,001	18,217	5,315		5,315	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Inverness High School	16,789		16,789	16,564		16,564	16,789		16,789	G	G	G	Works complete.
Naim Academy - LEIP	42,165	-25	42,140	853	-20	833	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Merkinch Primary	20,269	-1,000	19,269	20,017		20,017	20,269	-1,000	19,269	G	G	G	New building operational from October 2020.
Ness Castle Primary Ph 1	14,868	-2,084	12,784	12,887		12,887	14,868	-2,084	12,784	R	R	G	New building to be operational in January 2023.
Park Primary School	13,000		13,000	35		35	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
St Clements School	13,000		13,000	72		72	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Beaully Primary School	12,000		12,000	199		199	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Dunvegan Primary School	12,250	-250	12,000	280	-250	30	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Broadford Primary - new school - LEIP	14,193	-5	14,188	148	-10	138	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Tain 3-18 Campus - LEIP	65,000		65,000	4,281		4,281	TBC	TBC	TBC	G	G	G	Construction work underway; to be complete in December 2024

Project Description	Actual Net Year to Date	Revised Net Budget	Year End Estimated Net Outturn	Year End Net Variance	(Slippage)/Acceleration Net	Anticipated Year End (Under)/Over
	£000	£000	£000	£000	£000	£000
Capital Programme 2022/23						
Equipment and Adaptations	502	1,440	1,440	0	0	
Major Component Replacement	1,782	1,878	1,678	(200)	(200)	
Heating/Energy Efficiency	2,039	9,281	6,432	(2,849)	(2,849)	
External Fabric (Major Component Replacement)	2,005	6,859	5,805	(1,054)	(1,054)	
External Fabric (Environmental Improvements)	649	1,466	1,466	0	0	
Healthy, Safe and Secure	406	552	797	245	245	
Retentions	1		1	1	1	
Total 2022/23 Programme	7,384	21,476	17,619	(3,857)	(3,857)	0
Insurance Works	1					
Total 2022/23 Programme	7,385	21,476	17,619	(3,857)	(3,857)	0
Council House Building Capital Programme						
New Council House Buildings	12,649	29,508	30,573	1,065	605	460
Individual House Purchases	3,112	3,252	4,550	1,298	1,298	
Total Council Building Programme	15,761	32,760	35,123	2,363	1,903	460
OVERALL TOTAL	23,146	54,236	52,742	(1,494)	(1,954)	460

Funding	Actual Net Year to Date	Revised Net Budget	Year End Estimated Net Outturn	Year End Net Variance
	£000	£000	£000	£000
Investment Programme				
Useable Capital Receipts	8	0	8	8
RHI Income	36	0	50	50
Sale of LIFT Properties	0	0	0	0
Government Grant	4,189	17,000	16,000	(1,000)
Landbank	504	2,500	2,056	(444)
Evergreen Infrastructure Loan Fund	0	1,413	350	(1,063)
Contribution to Individual Property/VDLF	0		0	0
Borrowing	18,409	33,323	34,278	955
Capital from Current Revenue			0	
GROSS FUNDING	23,146	54,236	52,742	(1,494)