

Agenda Item	5.b
Report No	RES/02/23

THE HIGHLAND COUNCIL

Committee: Corporate Resources Committee

Date: 22nd February 2023

Report Title: Corporate Capital Monitoring report for Quarter 3 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 third quarter of the 2022/23 financial year to 31st December 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 Q3 2022/23 totalled £90.800m for the General Fund against a net annual budget figure of £157.394m. Net spend on capital projects for the Housing Revenue Account (HRA) totalled £36.479m against a net budget figure of £54.236m.
- 1.3 The forecast net outturn for the General Fund for 2022/23 totals £118.906m and this would give rise to a forecast net underspend against budget of £38.488m. The forecast net outturn for the HRA for 2022/23 totals £48.540m and this would give rise to a forecast net underspend against budget of £5.696m. 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 65% of total forecast spend across the General Fund and HRA.
- 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 Q3 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 Council in March 2023.

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.

4. General Fund Capital Programme Q3 2022/23

- 4.1 **Appendix 1** provides a summary of the capital programme budgets, spend and income for Q3 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 £157.394m.
- 4.2 Overall there has been a net expenditure of £90.800m for Q3, which reflects 58% of the annual budget.
- 4.3 The estimated outturn position shows a net expenditure of £118.906m which would result in an estimated underspend against budget of £38.488m. 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. 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/meetings/committee/139/communities_and_place_committee
 - **Housing & Property Committee:**
https://www.highland.gov.uk/download/meetings/id/81045/item_7_property_capital_monitoring_statement_and_progress_update
 - **Economy & Infrastructure Committee:**
https://www.highland.gov.uk/download/meetings/id/81048/item_5_capital_monitoring_quarter_3_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 Q3 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 are 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 can be viewed via the links provided in section 4.4 above.

6. HRA Capital Programme Q3 2022/23

- 6.1 **Appendix 4** presents the actual spend for Q3 of 2022/23 and the anticipated outturn for the full financial year. The Q3 net spend is £36.479m, equating to 67% of the annual budget of £54.236m. The anticipated net outturn for 2022/23 is £48.540m which would result in a projected net underspend of £5.696m.
- 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 Spring 2023 with further market and construction industry uncertainty exacerbated by the conflict in the Ukraine and the ongoing energy crisis.
- 6.3 The agreed new build development programme includes 490 new homes which will be progressed on site during 2022/23, as well as 45 one-off individual purchases. An estimated 280 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.
- 6.4 The Council remains committed to investing in its HRA properties however due to affordability concerns it was agreed when setting the HRA budget and rents for 2023/24 that a review of the current HRA capital programme would take place during the coming year.

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 £81.616m forecast, amounting to 69% 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 £28.389m forecast, amounting to 58% of forecast capital expenditure. The other major sources of funding include the Scottish Government Grant of £17.000m and the Council's Landbank Fund of £2.170m.
- 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, particularly as the Council's overall debt levels continue to increase.

8. Capital Programme Review

- 8.1 An announcement on the outcome of the bidding process for Phase 3 of the Learning Estate Investment Programme was expected from the Scottish Government in December 2022, however this has been delayed. As the outcome of the bid will have a material impact on the Council's capital expenditure commitment over the next 5 years, a decision has been taken to defer a decision on the wider capital programme review until after the Scottish Government's announcement. An update will be provided to Council in March 2023, along with a proposed capital expenditure budget for 2023/24 for approval.

Designation: Head of Corporate Finance

Date: 10th February 2023

Authors:

Edward Foster - Head of Corporate Finance

Darryl Urquhart - Principal Accountant

Background papers:

https://www.highland.gov.uk/download/meetings/id/81043/item_5_housing_revenue_account_hra_capital_monitoring_report_to_31_december_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 31ST DECEMBER 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	1,947	378	0	378	695	(100)	595	(1,352)	(1,352)	0
SCHOOLS	46,472	20,960	(1,420)	19,540	35,609	(1,731)	33,878	(12,594)	(12,594)	0
HEALTH & SOCIAL CARE PROGRAMME	5,419	286	(4)	282	1,023	(4)	1,019	(4,400)	(4,400)	0
ICT	4,172	3,908	0	3,908	4,172	0	4,172	0	0	0
ROADS AND BRIDGES	34,518	19,944	(928)	19,016	29,656	(3,053)	26,603	(7,915)	(7,917)	2
ACTIVE TRAVEL	1,981	2,078	(1,518)	560	3,802	(2,853)	949	(1,032)	(1,027)	(5)
LIGHTING, CCTV & RADIO MASTS	2,402	1,072	0	1,072	1,765	(520)	1,245	(1,157)	(1,157)	0
FLOOD PREVENTION	7,623	5,159	(108)	5,051	7,098	(108)	6,990	(633)	(633)	0
WASTE MANAGEMENT	7,841	6,696	0	6,696	7,662	0	7,662	(179)	(179)	0
FERRIES AND HARBOURS	19,116	19,901	(83)	19,818	40,274	(23,505)	16,769	(2,347)	(2,347)	0
BEREAVEMENT SERVICES	2,282	309	0	309	819	(82)	737	(1,545)	(1,545)	0
COMMUNITY SPACES	386	347	(381)	(34)	954	(381)	573	187	187	0
PUBLIC CONVENIENCES	330	72	(60)	12	713	(293)	420	90	90	0
STRATEGIC ASSET MANAGEMENT	13,631	5,862	(222)	5,640	9,583	0	9,583	(4,048)	(4,048)	0
VEHICLES & PLANT	4,883	1,547	(97)	1,450	2,060	(145)	1,915	(2,968)	(2,968)	0
PLANNING & DEVELOPMENT	1,650	10,096	(7,648)	2,448	15,864	(14,973)	891	(759)	(1,063)	304
CAPITAL CONTRIBUTIONS	800	4,806	(2,373)	2,433	7,841	(7,841)	0	(800)	(800)	0
CAPITAL DISCRETIONARY FUND	79	9	0	9	79	0	79	0	0	0
SELF FUNDING PROJECTS	(1,758)	1,525	(563)	962	2,210	(1,004)	1,206	2,964	2,964	0
HOUSING (NON HRA)	3,620	1,510	(260)	1,250	3,866	(246)	3,620	0	0	0
OVERALL TOTAL	157,394	106,465	(15,665)	90,800	175,745	(56,839)	118,906	(38,488)	(38,789)	301

FUNDING OF CAPITAL EXPENDITURE - 1ST APRIL 2022 TO 31ST DECEMBER 2022

SERVICE: GENERAL FUND

	2022/23 Budget	2022/23 Actual Net	2022/23 Estimated	2022/23 Variance	2022/23 Acceleration /	2022/23 Overspend /
	(incl. carry forward from prior year)	Year to Date	Outturn	Est Outturn v Budget	(Slippage)	(Underspend)
	£000	£000	£000	£000	£000	£000
Funding						
General Capital Grant	36,726	29,933	36,726	0	0	0
Capital Receipts	564	564	564	0	0	0
Borrowing	120,104	60,303	81,616	(38,488)	(38,789)	301
TOTAL FUNDING	157,394	90,800	118,906	(38,488)	(38,789)	301

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	50,368		50,368	8,123	-99	8,024	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	7,163		7,163	9,302		9,302	R	G	G	The landfill restoration programmes profiled spend includes £160k in 22/23, £1,012m in 23/24 and £1.0m 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. Spend in 22/23 has been increased to accommodate SEPA requirements to provide additional leachate management activities at Seater via the installation of temporary capping (brought forward from 23/24 forecast spend).
Residual Waste Management Facility - Longman Project	13,102		13,102	13,809		13,809	14,028		14,028	R	G	G	The Inverness WTS project forecast outturn remains £14,028m.
Vehicle & Plant Purchases (incl. Large Goods Vehs)	38,906		38,906	5,290	-2,017	3,273	40,923	-2,017	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	119,366		119,366	19,732	-1,271	18,461	119,366		119,366	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	7,043		7,043	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	870	-8	862	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	13,088	-8,644	4,444	19,921	-13,346	6,575	R	R	R	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.
The Inverness West Link	41,735	-3,362	38,373	42,791	-1,698	41,093	43,100	-3,362	39,738	A	A	A	Developer contributions to fund future expenditure. Cost is Amber as majority of work completed.
Inshes Roundabout	8,638	-1,801	6,837	2,231	-399	1,832	9,500	-2,000	7,500	R	A	A	Planning application will be lodged in 2022/23.
A890 Stromeferry Rockface Stabilisation	6,351		6,351	4,326		4,326	6,351		6,351	R	A	A	Works to repair debris flow.
B863 Invercoe Bridge, Lochaber	10,604		10,604	6,073		6,073	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 will increase costs.
Naver Bridge	7,113		7,113	876		876	8,101		8,101	R	A	A	Design contract (value = £400k) in place - about to commence detailed design stage. Red status on price is due to a number of project and design risks, including inflation.
Active Travel Transformation (Highland)	11,550		11,550	1		1	11,550		11,550	R	R	R	Programme of works being drawn up for approval.
Structural Lighting Works	8,690		8,690	3,124	-527	2,597	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. There are significant material cost increases which create a budget pressure.
Caol FPW	12,854	-14	12,840	12,064	-524	11,560	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	27,949	-4,704	23,245	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	9,685	-7,378	2,307	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	37,432	-1,000	36,432	37,883	-3,101	34,782	G	G	G	New building operational from October 2020, phase 2 works completed in 2022.
Inverness High School	16,789		16,789	16,929		16,929	16,929		16,929	A	G	G	Works complete.
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	14,868	-2,084	12,784	13,822		13,822	14,868	-2,084	12,784	G	R	G	New building to be operational in February 2023.
Train 3-18 Campus - LEIP Phase 1	69,400	-800	69,400	4,897	-800	4,097	69,400	-800	68,600	G	G	G	Construction work underway, to be complete in December 2024. Budget previously revised to reflect increased project costs.
Broadford Primary - LEIP Phase 2	14,193	-599	13,594	632	-604	28	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Nairn Academy - LEIP Phase 2	42,165	-25	42,140	1,378	-20	1,358	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Beauly Primary School	12,000		12,000	646		646	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Charleston Academy	16,011	-164	15,847	351		351	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Culloden Academy	19,218	-1,001	18,217	5,814		5,814	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Dunvegan Primary School	12,250	-250	12,000	711	-250	461	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
Park Primary School	13,000		13,000	154		154	TBC	TBC	TBC	R	TBC	TBC	Design in progress.
St Clements School	13,000		13,000	81		81	TBC	TBC	TBC	R	TBC	TBC	Design in progress.

Project Description	Actual Net Year to Date £000	Revised Net Budget £000	Year End Estimated Net Outturn £000	Year End Net Variance £000	(Slippage)/Acceleration Net £000	Anticipated Year End (Under)/Over £000
Capital Programme 2022/23						
Equipment and Adaptations	725	1,440	1,037	(403)	(502)	99
Major Component Replacement	2,112	1,878	2,772	894	790	105
Heating/Energy Efficiency	3,264	9,281	4,632	(4,649)	(4,657)	8
External Fabric (Major Component Replacement)	3,487	6,859	4,836	(2,023)	(2,214)	190
External Fabric (Environmental Improvements)	623	1,466	733	(733)	(755)	22
Healthy, Safe and Secure	652	552	867	315	315	0
Retentions	1		1	1	1	0
Total 2022/23 Programme	10,864	21,476	14,878	(6,598)	(7,022)	424
Insurance Works	7					
Total 2022/23 Programme	10,871	21,476	14,878	(6,598)	(7,022)	424
Council House Building Capital Programme						
New Council House Buildings	19,607	29,508	26,662	(2,846)	(3,335)	489
Individual House Purchases	6,001	3,252	7,000	3,748	3,748	0
Total Council Building Programme	25,608	32,760	33,662	902	413	489
OVERALL TOTAL	36,479	54,236	48,540	(5,696)	(6,609)	913

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	29	0	30	30
RHI Income	60	0	65	65
Sale of LIFT Properties	536	0	536	536
Government Grant	8,242	17,000	17,000	0
Landbank	600	2,500	2,170	(330)
Evergreen Infrastructure Loan Fund	0	1,413	350	(1,063)
Borrowing	27,012	33,323	28,389	(4,934)
GROSS FUNDING	36,479	54,236	48,540	(5,696)