

Administrative Accommodation Project Financial Update

Summary

1. The purpose of the report is to consider:-
 - The accounting implications of the abortive costs incurred on the administrative accommodation project, following the decision not to develop the site at Hungate
 - The overall funding position of the administrative accommodation project
 - The creation of a separate item within the Capital Programme to reflect the transfer of the land assembly costs relating to the original Hungate scheme from the £43.804m Administrative Accommodation Budget.

Background

Introduction

2. The case for a new Council headquarters, which is one of the Council's corporate imperatives, remains as compelling as ever. The project makes a significant contribution towards the Council's corporate strategy particularly in the areas of an effective organisation and an inclusive and sustainable city. The accommodation project is integral to the Council's 'More for York' transformation programme and is still on track to achieve a wide range of benefits.
3. It aims to deliver accommodation that is affordable and sustainable, responsive to new environmental legislation, in tune with the climate change agenda that meets the sustainability aspirations of the Council. It will be customer focused through the provision of a customer centre. It will be effective and efficient in its design, construction, subsequent operation and cost in use, incorporating appropriate systems and robust materials and finishes that are easy to manage and maintain. The building will be of a sufficient quality to be flexible and adaptable to respond to the changing needs of the council and stand the test of time. It will be capable of supporting the efficient utilisation of space, new ways of working and the implementation of the Council's Organisational effectiveness Programme.
4. In addition, there are a number of other positive spin offs from the project which include a £1m enhancement of the Council's social services facilities, including a new hydrotherapy pool at Oakland's swimming pool. Premises which are, being retained, will

have over £500k invested in them, and there is the new homeless hostel to replace the facility at Peasholme Green. The St Leonard's complex will also be regenerated with the buildings being converted from offices to a mix of uses that complement the city.

5. The project continues to be affordable and make sound business sense. The project would continue to be viable even if it did not return any revenue savings over the next 30 years because of the costs associated with remaining in our current buildings, the improved asset base and non financial improvements to the way that we work.
6. The body of the report gives a financial update of the following areas in relation to the Administrative accommodation project:-
 - Accounting Implications of abortive costs incurred
 - Current funding position of the Administrative Accommodation Project
 - Removal of the Land Assembly costs from the existing Administrative Accommodation Project.

Accounting Implications of Abortive Costs

7. On 9 September 2008 the decision was made that the original administrative accommodation project to be located at Hungate would no longer progress and consideration was then given to new development options. The new development options focus on the use of external developers to create the new office accommodation building and this is now the preferred method of delivery which is being procured through the EU competitive dialogue procurement process.
8. The procurement exercise is currently progressing and on 23 March 2009 the Council announced publicly that the new administrative accommodation project would be delivered by one of two developers and would involve the refurbishment and extension of existing buildings rather than a total construction from new as had been the proposal at Hungate.
9. Due to the "refurbishment" option as oppose to a "new build" option being pursued in the 2008/09 financial year, this has necessitated, under accounting regulations, that the Authority identify all those costs which are not relevant (also known as abortive costs) to the "new" scheme under development. Costs identified to be abortive are required to be written off as revenue costs and can no longer be funded through receipts or borrowing as intended in the original capital scheme.
10. It is necessary to understand that the administrative accommodation project is expenditure of a capital nature rather than of a revenue nature. The difference between capital expenditure and revenue expenditure is that capital expenditure results in an asset which adds value to a Councils asset base and derives a benefit to the Council for a period of greater than one year. Revenue expenditure can be summarised as the day-to-day costs incurred in running an organisation.
11. The abortive costs, can no longer be treated as capital expenditure, and therefore have to be written off as a revenue cost through the Income & Expenditure Account. Since they are deemed to be revenue costs, they cannot be funded by capital resources and have therefore been funded from a revenue source – the Venture Fund Reserve. This

treatment has been applied to all the abortive costs identified to the end of the 2008/09 financial year.

12. The approved budget of £43.804m remains the same and includes the abortive costs, however the funding position has changed. Originally the project was to be funded by capital receipts and borrowing alone, with the early year revenue deficit being funded from the Venture Fund reserve. However due to the abortive costs being of a revenue nature, the Venture Fund reserve has also been used to fund £1.092m of the £43.804m budget. This is detailed later in the report at paragraphs 17 to 35.
13. The expenditure incurred on the administrative accommodation project since 2005 has been reviewed in accordance with accounting regulations to accurately identify those costs which are directly attributable to bringing the asset into working condition for its intended use, and those which are not (abortive costs).
14. For the purpose of analysing the costs incurred, the expenditure is broken down into 7 discrete areas - Land Assembly, Hungate Design & Construction, Property Exit Strategy, Facilities Management, ICT, User/Change Management and the Project Management team. When reviewing costs in the context of accounting regulations, it has been deemed that the expenditure incurred on 5 of the discrete areas relate to costs which are still directly attributable to bringing the administrative accommodation building into being.
15. The areas of expenditure where abortive costs have occurred are in design & construction and also in the project management team. To identify the expenditure deemed under accounting regulation to be abortive, all documentation in the form of invoices, orders, internal memo's etc have been examined by relevant personnel involved in the project.
16. The actual costs identified to be abortive since 2005 totals £1.092m. It should be noted that the following assumptions have been made in ascertaining which costs are deemed to be abortive:-
 - a. the abortive costs focus on the external costs associated with the construction and design work stream
 - b. the invoices for the actual external works have been analysed to identify the construction and design costs which are abortive
 - c. the internal recharges in the construction and design work stream that have been deemed to be abortive are based on the percentage of the external abortive costs in each given year.
 - d. the abortive costs in the project management work stream, which are all internal recharges, have been based on the percentage of abortive costs identified in each year for the construction and design work stream.
17. The abortive cost of £1.092m is broken down over the financial years 2005/06, 2006/07, 2007/08 and 2008/09 in table 1 below. The design and construction of the original Hungate scheme would have become more detailed as the project progressed and the table below reflects the increase in abortive costs each year. In the year 08/09 the costs decrease as a result of the original project at Hungate no longer proceeding.

Area of Expenditure	2005/06	2006/07	2007/08	Prior Year Adj	2008/09	Total
	Expenditure	Expenditure	Expenditure	Total Expenditure	Expenditure	Expenditure
	£000	£000	£000	£000	£000	£000
Project Management	17	1	13	31	6	37
Hungate Construction	0	2	539	541	514	1,055
Total	17	3	552	572	520	1,092

Table 1 - breakdown of abortive costs

18. In the Statement of Accounts for 2008/09, £520k costs for 2008/09 have been charged to the Income & Expenditure Account and funded through the Venture Fund. The £520k costs are written out through the Statement of Movement in the General Fund balance and charged to the Venture Fund. This process is outlined in further detail within the Statement of Accounts as part of the note to the Core Statements on Exceptional Items
19. Costs of £572k relating to expenditure incurred prior to 2008/09, have also been funded by the Venture Fund. Within the Statement of Accounts, this is presented as a Prior Year Adjustment and is explained as part of the note to the Core Statements on Restated Comparative Figures for 2007/08. Further technical accounting adjustments have been made to remove these costs from the Council's Balance Sheet.
20. The Pre-Audit Statement of Accounts were approved by Audit & Governance Committee on 29 June 2009. The Audit Commission will review the Statement of Accounts including the treatment of costs relating to the Administrative Accommodation Project and report their findings back to the Audit & Governance Committee by 30th September 2009.

Funding Position of the Administrative Accommodation project

21. The Administrative Accommodation project is of a capital nature and can therefore be funded from capital resources in the form of capital receipts and prudential borrowing. In addition, there is an option for the costs to be funded from reserves or revenue contributions.
22. Table 2 below shows the headline funding position of the resources used to support the Administrative Accommodation project reported to the Executive on 17 June 2008 compared with the current proposed funding position.

Funding Position	14-Jun-08	08-Sep-09
	£m	£m
Capital Receipts	15.066	13.679
Borrowing	28.738	29.033
Venture Fund Reserve		1.092
Total Funding	43.804	43.804
Venture Fund revenue reserve to fund Early Years Deficit	2.094	1.692
Total Capital & Revenue Funding	45.898	45.496
Decrease		-0.402

Table 2 – Headline Funding Position

23. The Administrative Accommodation project remains at £43.804m, however the funding position has changed due to the abortive costs, £1.092m, being funded by the Venture Fund revenue reserve in accordance with accounting regulations and the change in the capital receipts position. Previously, in the Executive report 17 June 2008, £2.094m was available from the Venture Fund revenue reserve to the Administrative Accommodation project to fund the early years revenue deficit. The abortive costs of £1.092m have been funded from the Venture Fund revenue reserve and there is therefore an increased call of £0.690m on the Venture Fund reserve to £2.784m to support the overall Administrative Accommodation project.
24. The additional use of £0.690m Venture Fund revenue reserve, results in a fall in the overall level of capital funding for the administrative accommodation project of £1.092m. An indirect saving of £0.402m, as seen in Table 2 above – a comparison between £45.898m and £45.496m. This saving is as a result of the change in the timings and changes in the sources of funding used. Part of the Venture Fund revenue reserve, £1.092m, has been used in 08/09 and therefore even though capital receipts have fallen in future years so has the requirement for the need to borrow. The reduction in borrowing and the use of the Venture Fund revenue reserve in 08/09 reduces the early years revenue deficit and therefore overall cost to the Council.
25. It should be noted that the borrowing and capital receipts position will oscillate over time in accordance with market / environmental conditions and therefore the funding requirement – the need to borrow in relation to the amount of capital receipts received – will continue to fluctuate.
26. The following paragraphs explain in more detail the reasons for the changes in the funding requirement, the profile of capital receipts and Venture Fund revenue reserve, the changes in the affordability indicators – NPV Savings and Early years deficit and the borrowing requirement.
27. The funding position of the Administrative Accommodation project was last reported in detail to Executive on 17 June 2008. Table 3 below shows the change in use of resources over the last 14 months and the reasons for those changes.

Date		Capital Receipts	Borrowing	Venture Fund Reserve	Total Funding
		£m	£m	£m	£m
17-Jun-08	Funding Position at Executive 17 June 08	15.066	28.738		43.804
9-Sep-08	Position same as June 2008	15.066	28.738		43.804
14-Apr-09	Fall in originally estimated capital receipts of £1.22m but increase of £1m from contribution of sale of Hungate Land Borrowing fluctuates in line with a fixed budget of 43.8m and the position of capital receipts	14.944	28.860		43.804
8-Sep-09	Fall in originally estimated capital receipts of £265k and fall of £1m from estimated contribution of sale of Hungate Land	13.679	29.033	1.092	43.804

Borrowing fluctuates in line with a fixed budget of 43.8m and the position of capital receipts				
Venture Fund revenue reserve contribution to finance abortive costs				

Table 3 –Change in the funding of the Administrative Accommodation Project

28. The Administrative Accommodation project is mainly funded from borrowing and capital receipts, with additional funding being used from the Venture Fund reserve in relation to abortive costs. Capital receipts available to fund the project are anticipated to result from the sale of the properties which will be surplus to requirement as a result of rationalisation when the new administrative accommodation development is completed. These forecast receipts are therefore earmarked specifically to the funding of the scheme.
29. Capital receipts are currently estimated at £13.679m with the remainder of the overall capital funding coming from prudential borrowing £29.033m and the Venture Fund revenue reserve of £1.092m. This has changed from the original assumption as detailed in table 3 above. The capital receipts realised will fluctuate with regards to when the sale of surplus properties occur and the value of them on the market at a given time. As a result, and in order for the overall funding of the scheme to remain in balance, the levels of prudential borrowing will fluctuate accordingly. Table 4 below shows the current forecast capital receipts profile:

	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12	2012/13	Total
	£m	£m	£m	£m	£m	£m	£m	£m
TOTAL	7.027	0	0.780	1.180	2.280	0.750	1.662	13.679

Table 4 – capital receipts profile

30. The finance costs of the prudential borrowing are calculated over 60 years and are to be funded from budgets previously allocated to the rental and running costs of accommodation buildings that will no longer be required after the move into the new office accommodation building scheduled at the end of 2012. The existing rental and running costs budgets will not become available until after 2012 and therefore the finance costs resulting from prudential borrowing, the early years revenue deficit, will initially be funded from the Venture Fund revenue reserve, until such time as ongoing revenue budgets become available.
31. In addition to the Venture Fund reserve supporting the finance costs for prudential borrowing, the early years deficit, the reserve has also been used to finance the abortive costs at £1.092 in 08/09. The use of the Venture Fund reserve has always been available to the Administrative Accommodation project to fund the early years revenue deficit and due to the abortive costs being of a revenue nature and not capital, it is also being utilised to fund the abortive costs. Table 5 below shows the current forecast of the venture fund reserve to fund the Administrative Accommodation project. If the capital receipts are not realised as expected, there maybe an additional call on the Venture Fund to finance additional prudential borrowing prior to this date.

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	Total
	£m	£m	£m	£m	£m	£m	£m
Early Years deficit			0.034	0.524	1.109	0.025	1.692
Abortive costs	1.092						1.092
Total	1.092		0.034	0.524	1.109	0.025	2.784

Table 5 – Venture Fund reserve profile

32. There are currently sufficient funds forecast for the Venture Fund reserve to support the early years revenue deficit and the abortive costs, which total £2.784m. When future savings are made on the administrative accommodation project from lower rental and maintenance cost being required, it will be possible to replenish the Venture Fund reserve.
33. In accordance with the finance model the repayment to the Venture Fund reserve of the principal amount only will commence in 2013/14 and complete in 2018/19. Interest will not be repaid to the Venture fund reserve on the principal sum used. It is important to note that the current budgets for rental and maintenance of present accommodation buildings must be redirected for the purpose of the Administrative Accommodation project early years revenue deficit, otherwise the project is not sustainable.
34. The early years revenue deficit figure, along with the NPV of savings figure for the project, were reported to the Executive on 17 June 2008 as being the affordability indicators of the £43.8m Administrative Accommodation project. The NPV of Savings was £4.768m and the early years revenue deficit £2.094m. Table 6 below shows the movement in the NPV savings and early years deficit over the last 14 months.

Date		NPV of Savings £m	Early Years Deficit £m
17-Jun-08	NPV Saving & Early Years Deficit approved at Executive 17 June 2009	4.768	2.094
9-Sep-08	Position same as June 2008	4.768	2.094
14-Apr-09	4 main assumptions have been revised: 1. Repairs and maintenance costs have been included in the original base case model to comply with DDA and to maintain fabric for Health & Safety matters, 2. Current values for revenue costs, R&M, disposals and dilapidations have been updated in the model, 3. Valuation of buildings that are owned at year 30 have been inflated by 2.5% per annum in conjunction with Property Services, 4. Capital receipt values and timings have been changed in accordance with forecast.	5.842	1.970
8-Sep-09	2 main assumptions have been revised: 1. Capital receipt values and timings have been changed in accordance with forecast, 2 The Venture Fund reserve has been used to fund the Abortive costs	5.141	1.692

Table 6 – Change in the NPV of Savings and Early years deficit

35. Table 6 shows that the NPV saving currently stands at £5.141m and the early years revenue deficit stands at £1.692m. The early years revenue deficit will be funded from the Venture Fund revenue reserve, along with the abortive costs of £1.092m.
36. The capital budget of £43.8m, for monitoring purposes, will continue to include the £1.092m of abortive costs, even though they are of a revenue nature. The Council has

made the statement that all costs relating to the administration accommodation project will remain at £43.8m. To continue to include the abortive costs within the capital budget of £43.8m and monitor against this, is more straight-forward, rather than complicate matters in terms of accounting treatment of revenue and capital costs.

37. Finally, the Council will be able to borrow the required funds for the project on the basis of the Local Government Act 2003 Statutory Instrument 3146 – the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 – and also amendments to that Act brought about by the Local Government Act 2007 No. 573 and the Local Government Act 2008 No. 414, along with the CIPFA Prudential Code. The Prudential Code for Capital Finance in Local Authorities (the Code) has been developed as a professional code of practice to support local authorities in taking capital investment decisions.
38. The Local Government Act 2003 and the Code guidance are there to ensure that the Capital Investment Plans of Local authorities are affordable, prudent and sustainable. Borrowing is taken in accordance with the Council's capital financing requirement which is the Authorities overall need to borrow for the whole capital programme. In accordance with the Treasury Management Borrowing Strategy borrowing is undertaken when interest rates are most favourable, but ensuring that risk is spread so that borrowing does not occur at one point in time or for the same length of time. Borrowing can therefore occur in advance of need or be delayed (if there are sufficient cash resources available in the Council). It should be noted that under these regulations it is not possible to borrow for individual projects on a separate basis. The whole of the capital programme is considered together and the interest rate attributable to all projects is the consolidated rate of interest.
39. The majority of the Council's borrowing is taken from the Public Works Loans Board (PWLB), which is part of the Government's Debt Management Officer. Borrowing can occur at any time in accordance with the prudential code and the Local Government Act 2003 (and amendments). In the current market environment, even though the Bank of England base rate is at 0.5%, current borrowing rates are continually fluctuating around 4.5% out to 50 years and this is the level which finance costs have been calculated at from the commencement of this project.

Removal of the Land Assembly Costs from the Administrative Accommodation budget of £43.804m

40. The update report on the Council Headquarters that went to Executive on 21 July 2009 stated in the financial comments at paragraph 32 that, "The budget for the accommodation project is £43.804m as reported to Executive in June 2008. This includes the construction budget of £32m and incorporates the expenditure that has been incurred to date. All costs associated with the assemble of the land at the Hungate site will be recovered from the sale of the site"
41. The following paragraphs explain:
 - a. the need to remove the original Land Assembly costs from the Administrative Accommodation project (when the project was to be sighted at Hungate) to a capital scheme in their own right,
 - a. how these costs will be funded
 - b. that the overall Administration Accommodation budget will remain at £43.804m

42. The Administrative Accommodation budget is broken down into 7 discrete areas - Land Assembly, Hungate Design & Construction, Property Exit Strategy, Facilities Management, ICT, User/Change Management and the project management team. The £43.804m capital budget is distributed between these discrete areas and the Land Assembly budget stands at £3.54m. The costs charged to the Land Assembly budget relate specifically to the clearing of the Hungate site. The Hungate site was the original proposed location for the Administration Accommodation building but the Hungate site is no longer required as part of the project.
43. The current Administrative Accommodation solution - where the Council is undergoing a procurement process - has identified 2 new potential sites to relocate the Administrative Accommodation building. Therefore the costs associated with the clearing of the Hungate site do not contribute to the Administration Accommodation project.
44. The Land Assembly costs which contribute to the development and relocation of the homeless hostel to Peasholme and to the overall clearing of the Hungate site will create a viable asset i.e. development land at Hungate.
45. It is therefore proposed to remove the Land Assembly costs, at £3.54m, from the overall Administration Accommodation project and include it in the capital programme as a scheme in its own right. These costs will be funded from the capital receipt that would be received from the sale of the Hungate site. The budget for the Administrative Accommodation project remains at £43.804 million.
46. It should be noted that if the Council finds an alternative use for the Hungate site and it is not sold, then the alternative scheme must give consideration to the sale of an alternative asset to either fund the existing costs associated with the clearing of the Hungate site or find an alternative source of funding.

Options for: Removal of the Land Assembly Costs budget from the Administrative Accommodation budget of £43.804m

47. There are two options:
 - a. To remove the land assembly costs of £3.54m from the budget of £43.804m (as they no longer form part of the Administrative Accommodation project) into a separate capital programme scheme
 - b. Not to remove the land assembly costs
48. If the land assembly costs are removed from the project then there are 3 funding options:
 - a. Fund the land assembly costs from the sale of the Hungate site in the current market environment, receive a lower capital receipt than expected and fund the difference from long term prudential borrowing
 - b. Fund the land assembly costs from the sale of the Hungate site when the property market recovers, receive the expected estimated capital receipt of £3.54m and cover the short term shortfall in the interim by prudential borrowing.
 - c. Use the Hungate site for a future Council development and fund the land assembly costs from alternative identified funding.

49. The most viable option is to remove the land assembly costs from the administrative accommodation project, as the costs associated with the clearing of the Hungate site no longer contribute to the Administration Accommodation project, and therefore include them as a separate scheme within the capital programme. The funding will be delivered from the sale of the Hungate site at the most opportune time, option (b) paragraph 44.

Corporate Priorities

50. The Administrative Accommodation project makes a significant contribution towards the Councils corporate strategy particularly in the areas of an effective organisation and an inclusive and sustainable city. The Administrative Accommodation project is approved as part of the capital programme. The capital programme is decided through a formal process, using a Capital Resource Allocation Model (CRAM). CRAM is a tool used for allocating the Council's scarce capital resources to schemes that meet corporate priorities. The CRAM evaluates scheme submissions to the capital programme against key corporate objectives and national government priorities.

Implications

51. **Financial Implications** - The financial implications are considered in the main body of the report.
52. **Human Resources Implications** - There are no HR implications as a result of this report
53. **Equalities Implications** - There are no equalities implications as a result of this report
54. **Legal Implications** - There are no legal implications as a result of this report
55. **Crime and Disorder** - There are no crime and disorder implications as a result of this report
56. **Information Technology** - There are no information technology implications as a result of this report
57. **Property** - The property implications of this paper are included in the main body of the report.

Risk Management

58. The risks associated with this project are detailed in the Corporate Risk Register, of which the top 10 risks were reported to the Administrative Accommodation Project Board on 24 April 2009.

Recommendations

59. **Accounting Implications of Abortive Costs**
That the Executive notes the abortive costs of £1.092m included in the overall budget of £43.804m have been written off directly to the Income and Expenditure Account and funded from reserves as part of the preparation of the 2008/09 Statement of Accounts. These costs will however remain within the budget allocation of £43.804 m
60. **Funding Position of the Administrative Accommodation project**
That the Executive notes:

- a. the overall funding position of the administrative accommodation project which is estimated to use a combination of capital receipts, reserves and borrowing as the sources of funding used to support the £43.8m budget.
 - b. the overall funding position will continue to fluctuate in relation to timing and value of capital receipts and impact borrowing accordingly. The Administrative Accommodation project remains viable in accordance with the affordability indicators, with the NPV savings remaining positive and the Venture Fund revenue reserve being sufficient to cover the early years revenue deficit and the abortive costs paid to date, paragraphs 25 to 27.
61. That the Executive recommends to Council the increased use of the Venture Fund revenue reserve of £0.69m, to £2.784m, to support the early years revenue deficit, whilst noting that in the future the Administrative Accommodation project will replenish the Venture Fund revenue reserve with the amount used, paragraphs 17-20 and 27-30 refer.
62. Reason: to enable the effective management and monitoring of the Council's capital programme to ensure the continuation of a balanced capital programme as required by the Local Government Act 2003.
63. **Removal of the Land Assembly Costs budget from the Administrative Accommodation budget of £43.8m**
That the Executive recommends to Council the removal of the land assembly costs of £3.54m, which creates a viable asset – the development land at Hungate, from the Administrative Accommodation project of £43.804m, into a separate capital programme scheme, option (a) paragraph 43. The funding will be realised from the sale of the Hungate site at the most opportune time, option (b) paragraph 44.
64. Reason: to enable the effective management and monitoring of the Council's capital programme and to ensure the continuation of a balanced capital programme as required by the Local Government Act 2003.

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Specialist Implications Officer(s) *List information for all*
Implication ie Financial *Implication ie Legal*
 Name Name
 Title Title
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Wards Affected: All

For further information please contact the author of the report

Background Papers:

Hungate Ad-hoc Scrutiny Review Committee – 10th March 2009

Administrative Accommodation Review – Executive 17 June 2008

Council Headquarters – Update Report - Executive 21st July 2009

Pre-Audit Statement of Accounts 2008