

Item: 12

Policy and Resources Committee: 19 February 2019.

Former Papdale Halls of Residence.

Report by Head of Finance.

1. Purpose of Report

To consider the funding source of costs associated with demolition of the former Papdale Halls of Residence.

2. Recommendations

The Committee is invited to note:

2.1.

That, on 6 September 2018, the Asset Management Sub-committee resolved that, subject to additional resources being made available, demolition of the former Papdale Halls of Residence building be progressed through the annual corporate property asset maintenance programme.

2.2.

That the demolition cost of the former Papdale Halls of Residence building has been estimated at up to £2,500,000.

2.3.

That, on 11 December 2018, the Council resolved that the funding source relating to the cost of demolition of the former Papdale Halls of Residence be referred back to the Policy and Resources Committee for further consideration.

2.4.

The potential funding sources to meet the cost of demolition of the former Papdale Halls of Residence, detailed in section 4 of this report.

It is recommended:

2.5.

That the budget estimate of £2,500,000 in respect of the cost of demolition of the former Papdale Halls of Residence be established as a balance within the Repairs and Renewals Fund, comprising the following contributions:

- Insurance Fund – £1,021,000.
- Renewables, Redevelopment and Regeneration Fund – £250,000.
- General Fund Repairs and Renewals – £459,000.
- Care Facility Fund – £420,000.
- Non-Earmarked General Fund Balances – £350,000.

2.6.

That powers be delegated to the Head of Finance to substitute General Capital Grant for the funding sources identified in paragraph 2.5 above, should it be possible to capitalise some, or all, of the expenditure associated with demolition of the former Papdale Halls of Residence.

2.7.

That any unutilised funding from the contributions set out in paragraph 2.5 above be returned to the Renewables, Redevelopment and Regeneration Fund.

3. Background

3.1.

At its meeting held on 6 September 2018, when considering options for the disposal of the former Papdale Halls of Residence, the Asset Management Sub-committee resolved that, subject to additional resources being made available, demolition of the former Papdale Halls of Residence building be progressed through the annual corporate property asset maintenance programme.

3.2.

At its meeting held on 27 November 2018, when considering options for funding demolition of the former Papdale Halls of Residence the Policy and Resources Committee recommended:

- That powers be delegated to the Head of Finance to make a contribution of up to £2,500,000 from the Strategic Reserve Fund to the corporate property asset maintenance programme for General Fund services to fund the demolition cost of the former Papdale Halls of Residence.
- That powers be delegated to the Head of Finance to substitute General Capital Grant for Strategic Reserve Fund funding, should it be possible to capitalise some, or all the expenditure associated with demolition of the former Papdale Halls of Residence.
- That any proceeds from disposal of the future site be credited to the Strategic Reserve Fund to offset the contribution made towards demolition costs of the former Papdale Halls of Residence.

3.3.

On 11 December 2018, when considering the recommendations above, the Council resolved that the funding source relating to costs associated with demolition of the former Papdale Halls of Residence be referred back to the Policy and Resources Committee for further consideration.

4. Options Analysis

4.1.

The use of the Strategic Reserve Fund to cover the cost of demolition has been questioned because the former Papdale Halls of Residence has always been utilised in the provision of General Fund services and the feeling is that it would be unfair to now burden the Strategic Reserve Fund with the cost of cleaning up the site.

4.2.

The principal difficulty with funding demolition of the former Papdale Halls is that it was not addressed as part of the Schools Investment Programme where it could have been treated as part of the overall capital project and the cost spread over the life of the new buildings. The sitting tenant and the asbestos content of the buildings were largely responsible for exclusion of the demolition from the Schools Investment Programme. Consequently, demolition will not now create or contribute to a new capital asset with the result that most of the cost will require to be treated as a revenue expense and any “capital” element would be restricted to any increase in the value of the site as a result of the demolition.

4.3.

The previous recommendation to fund the cost of demolition from the Strategic Reserve Fund was arrived at only after other obvious routes to fund the works had been discounted. Use of the Strategic Reserve Fund was not selected because there was a natural fit but because the other options were all constrained by available resource or prior commitment. The options are reconsidered below with a view to identifying revenue funding of £2,500,000 from General Fund sources.

4.4.

Option 1 – a re-provisioning of earmarked balances held on the General Fund.

4.4.1.

When the Committee considered the earmarked sums in February 2018 there was general satisfaction with the level of earmarked balances and the reasons for holding these sums, however with demolition of the former Papdale Halls an immediate priority for funding, a re-prioritisation of some of the balances could be undertaken.

4.4.2.

One of the earmarked balances held is the Insurance Fund which has a balance of £1,021,000. This fund was set aside with the intention of the Council undertaking more self-insurance and carrying a greater level of risk through the ability to draw from the Insurance Fund in the event of a claim. The Council carried out a successful tendering exercise early in 2018 to renew its insurance and achieved significant savings on premiums to the extent that the attractiveness of the Council carrying more risk has diminished. The balance on the Insurance Fund could therefore be utilised.

4.4.3.

The Renewables, Redevelopment and Regeneration Fund currently has an uncommitted balance of £658,000. If this fund were to be fully depleted, this would remove the most obvious source of funding for the St Margaret's Hope Conservation Area Regeneration scheme and other possible regeneration projects that require match funding. A contribution of £250,000 however would still leave a balance for future projects of £408,000.

4.4.4.

Within the Repairs and Renewals Fund is a General Fund Services repairs and renewals balance of £929,000. A contribution from this balance of up to £459,000 would still leave a balance of £470,000 towards funding repairs to General Fund properties.

4.4.5.

The Care Facility Fund within the Repairs and Renewals Fund was set aside to provide for the soft furnishings, curtains and wall coverings in the new care facilities. The build contract for the replacement St Peter's House facility includes all fittings and furnishing. Accordingly, the fund balance of £420,000 could be applied to demolition of the former Papdale Halls of Residence.

4.4.6.

In summary, a total reallocation of earmarked balances of £2,150,000 could be achieved towards the total cost estimate of £2,500,000.

4.5.

Option 2 – a contribution from the non-earmarked General Fund balance.

4.5.1.

With this Fund having a balance of £4,787,000 as at 31 March 2018, a contribution to meet the full cost of demolition would cause the General Fund balance to drop significantly below the agreed target of 5% of the Council's net budgeted expenditure. A contribution of up to £350,000 from non-earmarked General Fund balances would, assuming no further draw at year end, reduce the fund balance to 5% of the Council's net budgeted expenditure.

4.6.

Option 3 – the annual corporate property asset maintenance programme for General Fund services

4.6.1.

This programme has a total available budget of £1,676,500 for 2018 to 2019. If the contribution was sourced from this revenue budget over two or even three financial years, there would be an inability to deliver the planned and most of the reactive maintenance required on the Council's property estate.

4.6.2.

If the required level of expenditure on the demolition had been at a relatively low level this would have been the recommended funding source. A contribution of £100,000 from the corporate property asset maintenance programme for General Fund services will put pressure on the budget but the demolition will also remove a cost pressure from this budget.

4.7.

Option 4 – utilise some of the Council's General Capital Grant if it is allowable to classify the value enhancing expenditure as capital.

4.7.1.

Without clearance from the External Auditors or any indication of what the value of the site may be after demolition and remediation, it is not possible to assess what, if any, General Capital Grant may be utilised.

4.7.2.

The level of General Capital Grant that the Council will receive in 2019 to 2020 will increase to £7,447,000 as the Scottish Government is due to repay £150,000,000 of capital to Local Government in that year.

4.8.

Option 5 – a contribution from the Strategic Reserve Fund, which was valued at £232,000,000 as at 31 March 2018.

4.8.1.

The Strategic Reserve Fund managed fund investments have not performed as well as expected over the past year but would still be expected to be able to accommodate the demolition costs within the available headroom above the Strategic Reserve Fund floor.

4.8.2.

Proceeds from the site disposal could also be returned to the Strategic Reserve Fund to reduce the cost to the Fund.

4.9.

Taking all of the above options into account and the rationale for the referral back to this Committee at the General Meeting, the recommended funding source is a combination of Options 1 and 2.

5. Corporate Governance

This report relates to the Council complying with its governance and financial processes and procedures and therefore does not directly support and contribute to improved outcomes for communities as outlined in the Council Plan and the Local Outcomes Improvement Plan.

6. Financial Implications

6.1.

The land and buildings of the former Papdale Halls of Residence, and surrounding area, is held on the General Fund. The former Papdale Halls is recorded in the Asset Register as a surplus property with a land component valued at £327,000 and a building component valued at Nil (based on the fact it is scheduled for demolition). The Nursery is valued separately as an operational building at a total value of £200,000, comprising a land component of £50,000 and a building component of £150,000.

6.2.

The building component of the Nursery will be written down to Nil when the tenant vacates the building. This revaluation will be accounted for as a charge to General Fund Services through the Income and Expenditure Account.

6.3.

It was previously reported to the Asset Management Sub-committee that the rental income generated from leasing the Nursery does not cover the upkeep of the property, including the cost of providing utilities. With the building in a poor state of repair the Head of Finance is exploring whether the building may be exempted from Council Tax as a below tolerable standard dwelling.

6.4.

The proposed demolition of the former Papdale Halls has been provisionally estimated at a cost of up to £2,500,000. It is questionable whether any of the expenditure on demolition and site clearance would be capital in nature. However, discussion with the Scottish Government's Head of Local Authority Accounting has revealed a possibility that may allow capitalisation of some of the expenditure which would allow the cost to be spread over more than one financial year and funded either through borrowing or the application of General Capital Grant. This accounting treatment is being explored with the Council's External Auditor. The default position is however that the cost of demolition will require to be funded from existing revenue resources, be that a current revenue budget, or a contribution from reserves and charged as a revenue expense in the year in which the expenditure is incurred.

6.5.

On the basis that the annual corporate property asset maintenance programme for General Fund services, with a total available budget of £1,457,600 for 2018 to 2019, is unable to accommodate a project of this scale without significant detriment to both planned and reactive works, a contribution from this budget has not been recommended on this occasion.

6.6.

A contribution of £2,500,000 from the non-earmarked element of General Fund balances would reduce the Council's contingency balance to a very low level and would not therefore be recommended. A more modest contribution however, together with reprioritisation of some earmarked balances could provide a budget to cover the estimated cost of demolishing the former Papdale Halls as follows:

	£
Insurance Fund	1,021,000
Renewable, Re-development and Regeneration Fund	250,000
General Fund Repairs and Renewals	459,000
Care Facility	420,000
Non Earmarked Balances	350,000
	2,500,000

6.7.

To minimise the cost to the Council of the remediation of the site, the Council should endeavour to ensure that it maximises the disposal value of the development site once it has been cleared for future development.

7. Legal Aspects

There are no legal implications arising directly from the recommendations of this report.

8. Contact Officer

Gareth Waterson, Head of Finance, extension 2103, Email gareth.waterson@orkney.gov.uk