Minimum Revenue Provision – Revised Policy Statement

Summary

Local authorities are required to prepare an annual Minimum Revenue Provision (MRP) Statement as part of the Treasury Management Strategy. This report sets out a proposed change to the policy for 2016/17, in respect of unfunded capital expenditure incurred before 1 April 2008. This change will require Full Council approval.

It is proposed to change the MRP policy for pre 2008 debt from a 4% reducing balance basis to a straight line basis over 50 years from 1 April 2016 as a prudent basis over which to repay debt:

- The approach has a beneficial impact on the Council's overall budget position with an initial saving in 2016/17 of £3.564m and a saving of £15.8m over the first 5 years;
- Moving to a straight-line basis will ensure that all debt is paid-off over this period; unlike the existing method whereby where £30m or 18% of debt remains un-provided for;
- This is in line with the estimated average age of this group of assets;
- There is sufficient capacity in the capital programme to maintain the assets going forward to ensure that they will continue to be operational for at least another 50 years;
- The straight-line basis provides consistency and certainty for forward planning within the MTP in respect of pre-2008 unfunded capital expenditure fixed at £3.6m per annum.

Recommendation

Agree a change to the MRP policy from a reducing balance basis to a straight line basis over 50 years from 1 April 2016.

Minimum Revenue Provision (MRP)

Background

The Council has a duty to make an annual revenue provision in respect of the financing of unfunded capital expenditure. The rules around the MRP are covered by statue and regulations[1]. The guidance sets out that the aim is to ensure that debt is repaid over a period that is reasonably commensurate with the period over which the capital expenditure provides benefits, and it provides a number of options (not exhaustive) by which this could be achieved:

(i) The regulatory method – this is the old system of determining MRP.This includes making a MRP of 4% of the outstanding debt, amended by Adjustment A (the difference between the credit ceiling and the Capital Financing Requirement on 1st April 2004).

(ii) The CFR method – a simplification of the above and involved setting MRP equal to 4% Capital Financing Requirement at the end of preceding financial year.

(iii) The asset life method – this method requires MRP to be charged over the asset life using equal instalments or annuity calculation. The asset life is determined in the year MRP commences and is not subsequently revised.

(iv) The depreciation method – this requires depreciation accounting to be followed, including impairment should the asset last for a shorter life than originally set.

[1] The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 and the DCLG document, Capital Finance Guidance on Minimum Revenue Provision (February 2012)

While Councils are required to have regard to the guidance, they are allowed to set their own policy outside of the options given if it can be demonstrated that this would be prudent. It is for the Council to determine that such provision is prudent.

Current MRP Policy
For unfunded capital expenditure incurred **before** 1st April 2008 the Council currently adopts the Option 1 the 'Regulatory Method'. For unfunded capital expenditure incurred **after** 1st April 2008 MRP is currently based on Option 3, the asset life method.

As at 1 April 2016, the Council had an outstanding capital financing requirement on unfunded capital expenditure incurred prior to 1 April 2008 of £180.462m. Under the current policy the total MRP charge to the General Fund budget in 2016-17 is expected to be approximately £7.599m of which £7.173m is in relation to debt incurred prior to 1 April 2008.

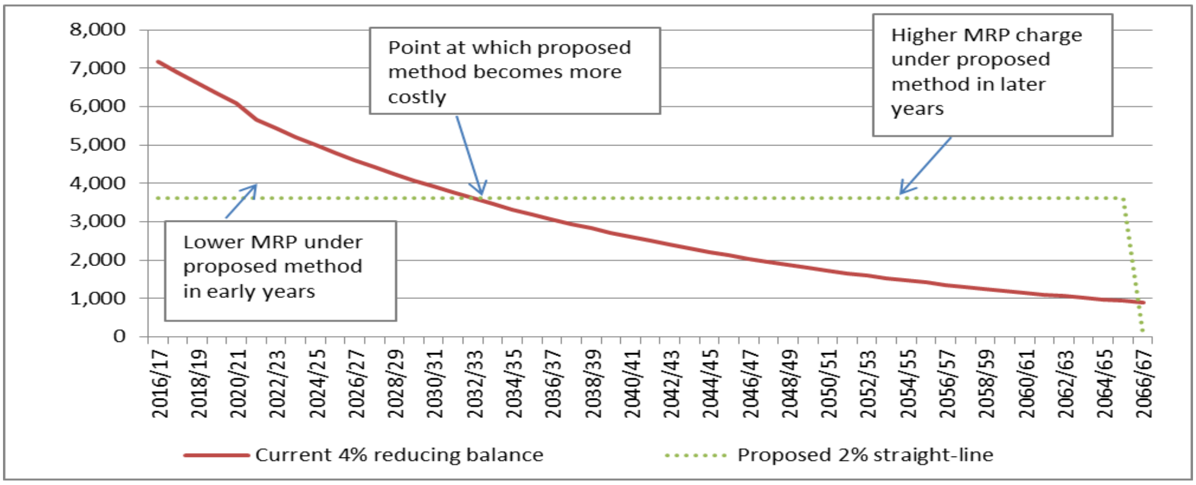
The purpose of this report is to propose an amendment to the policy for unfunded capital expenditure incurred **before** 1 April 2008.

Review of MRP
It is not possible to allocate the Council's outstanding pre 2008 debt to specific assets. The review of MRP policy has therefore considered the period over which capital expenditure on the largest block of assets Schools, provides benefit, by looking at a sample of 40 schools revalued in 2015/16. The calculation of the revised MRP has then been undertaken in line with the DCLG guidance on the equal instalment method issued in 2012.

The review has concluded that a 50 year life or 2% straight-line basis is a prudent basis over which to repay debt:

- This is in line with the estimated average age of this group of assets
- There is sufficient capacity in the capital programme to maintain the assets going forward to ensure that they will continue to be operational for at least another 50 years
- Moving to a straight-line basis will ensure that all debt is paid-off over this period; unlike the existing method whereby where £30m or 18% of debt remains un-provided for (see below);
- The approach has a beneficial impact on the Council's overall budget position in the first fifteen years of implementation
- The straight-line basis provides consistency and certainty for forward planning within the MRP in respect of pre-2008 unfunded capital expenditure fixed at £3.6m per annum.
- This approach is consistent with the approach taken by other Local Authorities who have reviewed their MRP provisions.
- The change to MRP policy will result in a permanent reduction in the budget from the current MTP budget of approx. £3.7m. Although the proposed change results in a higher charge in later years, the modelling in later years does not take account of the time value of money.

The graph below models the proposed change moving from the current 4% reducing balance to 2% straight-line from 1 April 2016.



The table below summarises the impact of the proposed change.

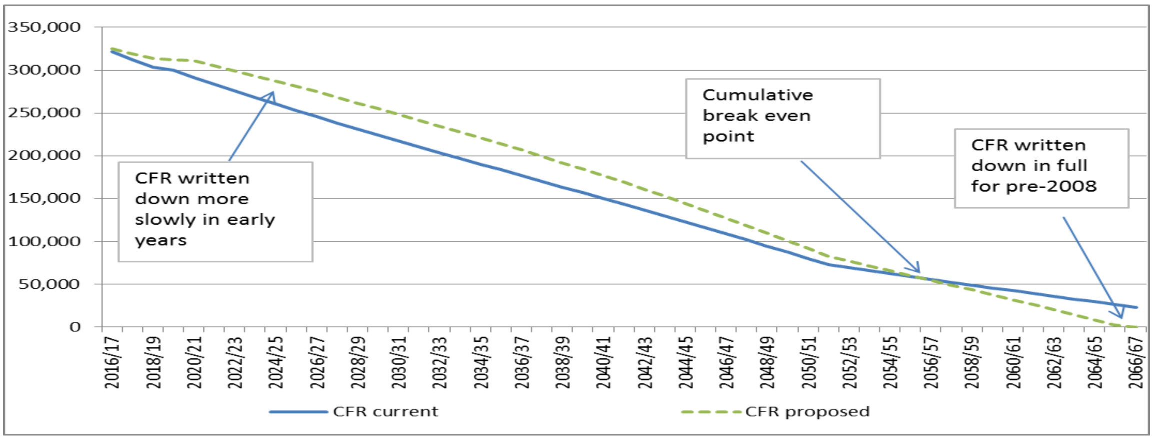
	Impact of change in MRP policy
Remaining CFR on unfunded capital expenditure incurred prior to 1 April 2008	£180.462m
MRP in respect of pre-2008 debt on current policy	£7.173m
Revised MRP charge 50 year straight line from 2016	£3.609m
Budget reduction from current budget	-£3.564m
Saving over 5 years from proposed revised policy	-£15.8m
Saving over 10 years from proposed revised policy	-£24.5m
Year at which method becomes more costly than 4% reducing balance	2033/34

Recommendation
The recommended option is to change the MRP basis to straight line over 50 years from 1 April 2016. This:

- Reflects a prudent estimate of the period of time over which benefit is obtained from the asset.
- Has the most beneficial impact on the Council's overall budget position in the first fifteen years of implementation.

Impact on the Capital Financing Requirement ('CFR')
The CFR is the total amount of capital expenditure that has not yet been financed from resources such as capital grants, capital receipts or MRP, and represents the total amount of prudential borrowing. The CFR is written down more slowly under the proposed straight line method (as annual MRP is lower) until 2056-57 (the cumulative break even point), at which point the annual charge is greater than the existing method.

The graph shows the entire capital financing requirement including the EfW financing and other post 2008 unfinanced capital expenditure as at 1 April 2016 but excluding any activity during 2016/17.



Overall the change to MRP has only a small impact on the CFR. Using the straight line basis ensures that the CFR is written down in full within the specified timeframe which is considered a more prudent approach overall. In contrast, by year 50, the 4% reducing balance method still has approx. 18% or (£30 m) of the total debt from day one, still to write down.

Resource implications

The impact of this change would be a saving to the General Fund in 2016/17 of £3.564m and a saving of £15.8m over the first 5 years. Over 50 years there is an increase in the charge to the General Fund but this does not take into account the time-value of money.