Appendix 15 Review of the Minimum Revenue Policy (MRP)

1. Introduction

1.1 The repayment and management of debt is frequently reviewed, to assess value for money and appropriateness, based on the current financial circumstances of the Council. The Council has posted underspends in the last 4 years to build up a capital financing reserve.

1.2 As the Council becomes more self sufficient, it also has to manage significant growth in demand led services, it is now more prudent to use annual income sources to support the direct cost of services.

1.3 The review of the Minimum Revenue Provision has identified that significant revenue funding can be used to support front line services without a significant impact on the lifetime costs of managing debt. The change in approach reflects a change in circumstances, and the opportunity to change the approach to financing debt has been made possible through prudent use of balances to date.

2. Background

2.1 Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, requires local authorities to charge to their revenue account for each financial year a Minimum amount to finance the cost of capital expenditure. Commonly referred to as MRP (Minimum Revenue Provision).

2.2 ***Duty to make revenue provision***

27.*—(1) During the financial year beginning on 1st April 2004 and every subsequent financial year, a local authority—*

(a) shall charge to a revenue account a minimum amount ("minimum revenue provision") for that financial year; and

(b) may charge to a revenue account any amount in addition to the minimum revenue provision,

in respect of the financing of capital expenditure incurred by the local authority in that year or in any financial year prior to that year.

2.3 The current policy, which has been applied since 2009, is as follows:

(a) **Supported Capital Expenditure** (applied to capital expenditure, pre 2008, which is supported by the Government through the Revenue Support Grant system). Revenue provision is charged at 4% of the previous year's Supported Capital Financing Requirement (CFR). i.e., the balance of capital expenditure still to be financed.

(b) **Unsupported Capital Expenditure** (applies to capital expenditure, post 2008, under the Prudential system for which no government support is being given and is therefore self-financed). Revenue provision is made over the estimated life of the asset on a straight line basis.

2.4 The Council has the option under its current policy to apply the annuity method instead. This results in a consistent charge to Revenue for assets that provide a steady flow of benefits over their useful lives. It is appropriate to set the annuity rate at estimated inflation. The percentage chosen corresponds with the Monetary Policy Committee's inflation target rate of 2%. MRP will increase by this percentage each year. This reflects the time value of money and can therefore be considered to be fairer on Council Tax payers as it produces a consistent charge as measured in real terms.

2.5 Once set at 2% the rate would not be adjusted annually on the basis of actual CPI as this could result in significant fluctuations in the amount of MRP charged in any one year. However, should a significant and sustained divergence develop between the actual rate of CPI and the target rate or the MPC's target for CPI be amended at any stage then it would be appropriate for the Council to reflect this in an adjusted annuity rate for new unfinanced capital expenditure.

2.6 CIPFA's Practitioners' Guide to Capital Finance in Local Government supports the use of the Annuity method on the basis that the MRP charge to Revenue takes account of the time value of money.

3. Supported Capital Expenditure

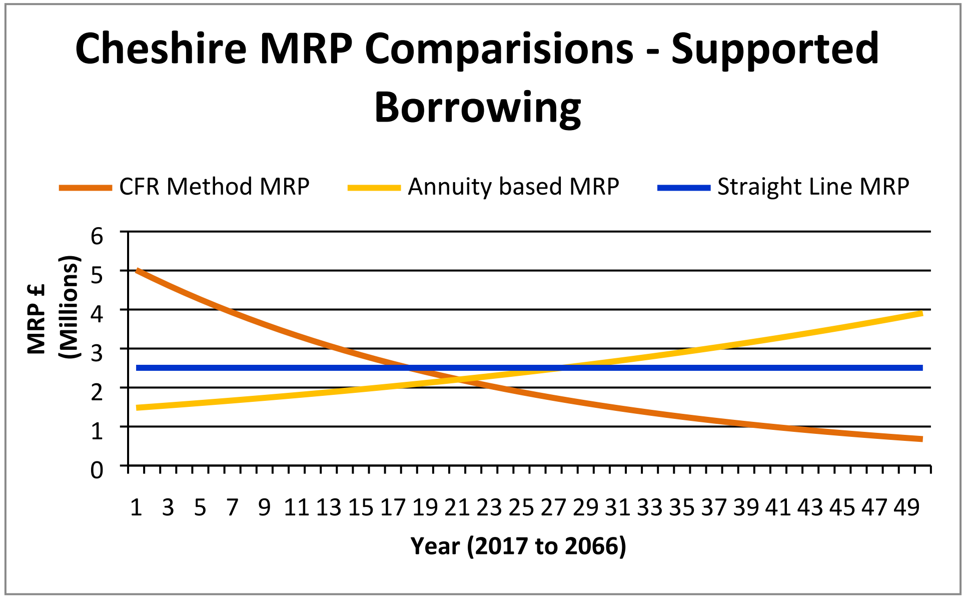
3.1 Consideration has been given to adopting an Annuity based calculation for MRP on the supported capital expenditure element of the CFR.

3.2 Under the 2% Inflation based Annuity method this element of the CFR would be fully financed in 50 years' time. This method can also be considered to be more prudent than the current methodology as it fully finances the capital expenditure over the given period of years.

3.3 Under the currently used CFR Method, MRP falls by 4% each year, giving the Council an inbuilt budgetary easing. In the 2% Annuity method outlined above, MRP rises by 2% each year, giving the Council an inbuilt budgetary pressure each year which would need to be reflected in the MTFS .

3.4 Another option would be to use a straight line method and would result in the same amount of MRP being charged to revenue each year.

3.5 The impact on these three alternative methods on the revenue budget over the 50 year period is shown in the following chart.



Current CFR Method – £5m charge in 2017/18, which reduces year on year until it, is fully repaid in Year 50 (2066).

Annuity based MRP – MRP of £1.5m charged in 2017/18 rising to £4m in Year 50.

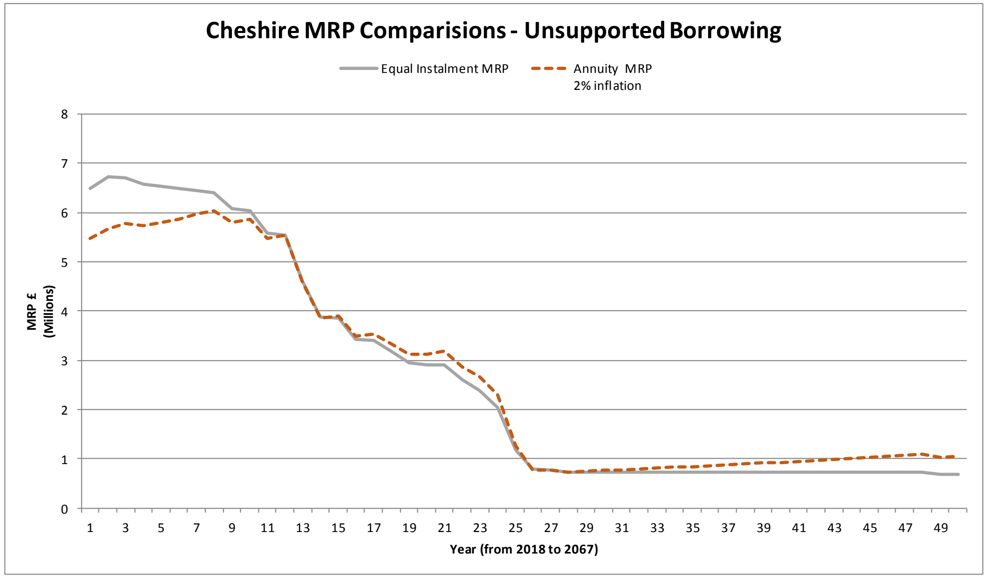
Straight Line MRP – Consistent charge of £2.5m charged each year.

4. Unsupported Capital Expenditure

4.1 Consideration has been given to assessing the impact of adopting the Annuity method for the element of unsupported capital expenditure. The unsupported borrowing element of the CFR under the current methodology as at 31st March 2017 was £133m.

4.2 The Council's existing 2017/18 budget for MRP on unsupported capital expenditure up to 31st March 2017 using its current methodology would need to be £6.3m. Using the equivalent Inflation based calculations the MRP requirement would be £5.5m, resulting in a £0.7m saving on the revenue budget in 2017/18.

4.3 The same amount of MRP will be due to be paid over the 50 year period; the following chart demonstrates the spread of payments.



5. Unsupported Capital Expenditure – Retrospective application of annuity method

5.1 By applying the retrospective recalculation of its MRP on unsupported borrowing, this would provide an opportunity to charge a lesser amount to the revenue budget in the current financial year, and realise a budget saving of £1.9m (for the retrospective application) plus an in year saving of £0.7m, £2.6m in total.

5.2 **Summary of financial implications**

Supported borrowing	**Annuity**
2017/18 saving	£3.5m
2018/19 saving	£3.3m
2019/20 saving	£3.1m
2020/21 saving	£2.9m

Unsupported Borrowing	**Annuity applied retrospectively**
2017/18 saving	£0.7m + retrospective £1.9m **Total saving = £2.6m**
2018/19 saving	£0.7m
2019/20 saving	£0.7m
2020/21 saving	£0.6m

N.B. The figures quoted in this report are based on the 2017-20 Approved Capital Programme, subsequent additions to the capital programme to be funded by borrowing, will increase the charge for the unsupported borrowing element of MRP.

6. Recommendation

6.1 Following liaison with the Council's treasury management advisors, Arlingclose and discussion with Grant Thornton, the Council's external auditors, the Section 151 Officer is now recommending that the Council revise the approach to calculating the Minimum Revenue Provision (MRP) and implement the annuity method retrospectively for both the supported and unsupported elements of borrowing.

6.2 This revised approach delivers revenue savings in the short term but does not alter the overall liability for the financing of the capital programme. As the charts demonstrate, this proposal increases future years MRP charges in cash terms. However, the Council will seek to mitigate these future pressures through its longer term financial strategies andthe capital financing budget will be adjusted to reflect both the MRP changes and available capital resources, including the use of anticipated capital receipts.

6.3 This proposal is in accordance with the Capital Financing Regulations and an allowable option within our MRP policy. Grant Thornton have confirmed that they are comfortable with these decisions as lawful and that they do not cause an issue from a VfM perspective.

6.4 This recommendation has been formulated after careful consideration of the options available to the Council and after taking advice from the Council's treasury management advisors, and its external auditor. It has been reached with full regard to and is compliant with the Local Authorities (Capital Finance and Accounting)(England) Regulations 2003 (as amended). Accordingly it is considered to be a lawful and reasonable approach in all the circumstances.