Committee and Date
Cabinet 17th September 2018 Council 20th September 2018

REVISED MINIMUM REVENUE PROVISION STATEMENT 2018/19

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1. Summary

1.1 This Council is required by statute to set aside a minimum revenue provision (MRP) for the repayment of external debt. The calculation of the minimum revenue provision (MRP) is as per the *Local Authority (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414].* In regulation 28, detailed rules are replaced with a simple duty for an Authority to make an amount of MRP which it considers to be "prudent".

1.2 The legislation recommends that before the start of each financial year the Council prepares a statement of its policy on making MRP in respect of that financial year and submits it to the Full Council for approval. If it is proposed to vary the terms of the original statement during the year, a revised statement should be put to Council at that time. The MRP Policy Statement was last revised for 2016/17 and was approved by members in February 2016 as part of the Treasury Strategy 2016/17. This revised policy was retained by the Council for the 2017/18 and 2018/19 financial years and approved by members as part of the 2017/18 and 2018/19 Treasury Strategy reports in February 2017 and 2018 respectively.

1.3 Shropshire Council's Treasury advisor, Link Asset Services (LAS), has recently undertaken a review of the Authority's Minimum Revenue Provision (MRP).

1.4 The brief for the review was to advise the Authority on how it can profile MRP for the repayment of its underlying debt liability, in line with the life of assets associated with that debt, to achieve short to medium term benefit to the General Fund and assist with easing current budgetary pressures, whilst ensuring that the provision provided remains prudent and compliant with the statutory guidance for MRP.

1.5 The review was limited to options for supported borrowing and PFI.

2. Recommendations

Members are asked:

2.1 To consider all the options modelled for the revision of the calculation of MRP charges in relation to supported borrowing.

2.2 To approve the use of Option C3 (use a 45-year annuity method and apply Adjustment A from 2018/19) to calculate MRP charges in relation to supported borrowing.

2.3 To approve that the £2.217m saving generated in 2018/19, be ringfenced to fund the Digital Transformation Programme.

REPORT

3. Risk Assessment and Opportunities Appraisal

3.1 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998.

3.2 There are no direct environmental, equalities or climate change consequences arising from this report.

3.3 Compliance with the Local Authority (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414] ensures that the Council is managing the risk of not providing an adequate and prudent budget for repaying external debt.

4. Financial Implications

4.1 The financial implications arising from the Revised MRP Statement 2018/19 are detailed in sections 6 and 7 of this report. Changes to the MRP Policy are producing budgetary savings over a five year period and it is proposed that total savings of £9.25m can be delivered over this period, with a £1.85m saving each financial year.

5. Minimum Revenue Provision

5.1 The Council is required by statute to set aside a minimum revenue provision (MRP) for the provision to repay external debt. The calculation of the minimum revenue provision (MRP) is as per the *Local Authority (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414].* In the regulation 28, detailed rules are replaced with a simple duty for an authority to make an amount of MRP which it considers to be "prudent".

5.2 The broad aim of a prudent provision is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by

Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant. The guidance includes four options (and there are two alternatives under Option three) for the calculation of a prudent provision.

5.3 There is no requirement to charge MRP where the Capital Financing Requirement (CFR) is nil or negative at the end of the preceding financial years. There is also no requirement to charge MRP on the Housing Revenue Account share of the CFR.

5.4 The legislation recommends that before the start of each financial year the Council prepares a statement of its policy on making MRP in respect of that financial year and submits it to the Full Council for approval. If it is proposed to vary the terms of the original statement during the year, a revised statement should be put to Council at that time.

5.5 Members approved the MRP Statement for 2018/19 in February 2018 as part of the Treasury Strategy for 2018/19.

5.6 The Council's current MRP policy introduced in 2016/17 is as follows:

- The provision for Supported Borrowing is calculated on the basis of the average remaining asset life of the assets financed from previous supported borrowing on a straight line (equal instalments) basis over 45 years.
- For all unsupported borrowing from 1 April 2008, MRP will be based on the estimated life of the assets (Option 3), on a straight-line basis (equal instalments).
- For assets under on-balance sheet PFI contracts and finance leases, the annual principal payment amount in the PFI or finance lease model is used as the MRP payment amount, with no additional charges above those within the contract.
- There is no mandatory requirement to make provision in the HRA for annual MRP payments. However, the Council will make annual voluntary provision for debt repayment in the HRA based on affordable levels in the HRA against the need for investment and delivering services in the HRA. The annual level of provision will be determined annually as part of the closure of the HRA.
- Where the Council has made capital loans to third parties financed from the Council's balances, the annual repayments of principal amounts are treated as capital receipts and set aside in the Capital Adjustment Account in place of a revenue MRP charge.

6. Evaluation of Options for Revising MRP Policy

6.1 The options for the calculation of a prudent Provision are detailed in Appendix A to this report. The Council is proposing to revise the calculation basis for part of its debt from 2018/19. Up to 2016/17, the Council policy for debt supported by the Government through the Revenue Support Grant system, has been calculated on the basis of expected useful life of the asset on a straight-line basis.

6.2 Option 3a - Asset Life Method - Equal Instalment Method - will continue to be used for unsupported borrowing and specific treatment for PFI assets and assets held under finance leases and long-term capital loans.

Supported Borrowing

6.3 The following options were considered for revision of the MRP calculation associated with supported borrowing.

- Option A: Apply a 2% (50-year) straight-line method from 2018/19.
- Option B1: Apply a 45-year annuity method from 2018/19
- Option B2: Apply a 50-year annuity method from 2018/19.
- Option C1: Use the current 2.22% (45-year) straight-line method and apply Adjustment A from 2018/19
- Option C2: Use a 2% (50-year) straight-line method from and apply Adjustment A from 2018/19.
- Option C3: Use a 45-year annuity method and apply Adjustment A from 2018/19.
- Option C4: Use a 50-year annuity method and apply Adjustment A from 2018/19.

6.4 The various alternative approaches are summarised below and more detail of the options are contained in Appendix A.

Option A: 2% 50 Year Straight Line From 2018/19

6.5 Option A produces a saving in MRP charges up to Year 40 of £18.998m but an increased liability in years 41 to 50 of £18.998m. This change in policy would generate savings of £0.475m and £1.900m in 2018/19 and 2019/20 to 2022/23 respectively, compared to the current calculation basis.

6.6 In February 2016 Council approved a proposal to calculate MRP for supported borrowing by linking MRP to the average remaining useful life of the assets it was used to finance. This is in accordance with the general principle of achieving a prudent approach set out in the guidance, that MRP charges should reflect the economic benefit the Council gets from using the asset to deliver services over its useful life. This ensures the Council Tax payers are being charged each year in line with asset usage and prevents current taxpayers meeting the cost of future usage or future Council Tax payers being burdened with “debt” and the costs of that debt, relating to assets that are no longer in use.

6.7 An analysis of the average remaining asset life of the assets financed from previous supported borrowing, determined the average remaining life to be around 45 years and this has been used as the basis of the existing calculation.

6.8 Extending this estimated life to 50 years would result in a longer repayment period and would oppose the MRP guidance which recommends that whatever period is chosen at the outset must remain as the chosen life.

6.9 Additionally, this approach would not be appropriate as it would extend the repayment period to longer than the life of the assets, as the asset lives have been reviewed and it is believed that 45 years is still appropriate.

6.10 Therefore, this option has been dismissed as a viable option.

Option B1: 45 Year Annuity Basis From 2018/19

6.11 Option B1 produces a saving in MRP charges up to Year 25 of £28.619m but an increased liability in years 26 to 50 of £28.619m. This change in policy would generate savings of £2.162m and £7.953m in 2018/19 and 2019/20 to 2022/23 respectively, compared to the current calculation basis.

6.12 The annuity calculation method results in lower MRP payments in the early years, but higher payments in later years. This method has the advantage of linking MRP to the flow of benefits from an asset where these are expected to increase in later years.

6.13 CIPFA puts forward the following reasons for using the annuity method in CIPFA's "The Practitioner's Guide to Capital Finance in Local Government" (2008) which states:

- The annuity method provides a fairer charge than equal instalments as it takes account of the time value of money, whereby paying £100 in 10 year's time, is less of a burden than paying £100 now.
- The schedule of charges produced by the annuity method results in a consistent charge over an asset's life, taking into account the real value of the amounts when they fall due.
- The annuity method is a prudent basis for providing for assets that provide a steady flow of benefits over their useful life.

6.14 To adopt the annuity calculation method, the Council would need to recognise and be comfortable with the fact that using this method would increase MRP in later years and therefore may impact upon its ability to afford further capital expenditure financed by borrowing in the future. This is considered a viable option.

Option B2: 50 Year Annuity Basis From 2018/19

6.15 Option B2 produces a saving in MRP charges up to Year 25 of £43.659m but an increased liability in years 26 to 50 of £43.659m. This change in policy would generate savings of £2.585m and £9.765m in 2018/19 and 2019/20 to 2022/23 respectively, compared to the current calculation basis.

6.16 Whilst the use of the annuity basis would be a viable option, this option has been dismissed due to the increase in payment profile in excess of the useful asset lives.

Option C: Use Adjustment A From 2018/19 Onwards

6.17 When the Council revised its MRP Policy in December 2016 and elected to adopt the Asset Life method to calculate MRP charges in relation to supported borrowing, it was also decided to revise the calculation of the Capital Financing Requirement (CFR). From 2009/10 to 2015/16 the Council determined CFR used for the supported borrowing MRP calculation by adjusting for Adjustment A (the variance between the credit ceiling and the CFR as at 1st April 2004).

6.18 When the MRP Policy was revised it was no longer considered appropriate to adjust CFR by Adjustment A on the basis that it was not in line with the remaining asset life of the assets linked to the borrowing and not in line with the repayment profile of the Council's existing external debt.

6.19 However, Adjustment A continues to be a legitimate part of the MRP calculation under the 2003 Regulations (Regulation 28) and can therefore continue to be used to reduce the supported borrowing CFR for MRP purposes.

6.20 The following options model MRP charges utilising Adjustment A with a value of £4.446m.

Option C1: Adjustment A with Existing 2.22% (45 Years) Straight Line From 2018/19

6.21 Option C1 produces an overall saving in MRP charges £4.446m and savings are realised in every year of the repayment period. This option produces a saving in MRP charges up to Year 40 of £22.703m but an increased liability in years 41 to 45 of £18.257m. This change in policy would generate savings of £0.103m and £0.414m in 2018/19 and 2019/20 to 2022/23 respectively, compared to the current calculation basis.

6.22 This is considered an appropriate option for consideration, however has been declined in order that the Council delivers a fairer and more consistent charge as per the annuity method.

Option C2: Adjustment A With 2% (50 Years) Straight Line From 2018/19

6.23 Option C2 produces an overall saving in MRP charges £4.446m. This option produces a saving in MRP charges up to Year 25 of £22.703m but an increased liability in years 26 to 50 of £18.257m. This change in policy would generate savings of £0.568m and £2.270m in 2018/19 and 2019/20 to 2022/23 respectively, compared to the current calculation basis.

6.24 This option has been dismissed due to the increase in asset life not being appropriate and the intention to move to an annuity approach.

Option C3: Adjustment A With 45 Years Annuity Approach From 2018/19

6.25 Option C3 produces an overall saving in MRP charges £4.446m. This option produces a saving in MRP charges up to Year 25 of £30.555m but an increased liability in years 26 to 50 of £26.109m. This change in policy would generate savings of £2.217m and £8.186m in 2018/19 and 2019/20 to 2022/23 respectively, compared to the current calculation basis.

6.26 This is considered a viable option as it maintains the payback period so that it is in line with the asset lives and it adopts the fairer annuity approach.

Option C4: Adjustment A With 50 Years Annuity Approach From 2018/19

6.27 Option C4 produces an overall saving in MRP charges £4.446m. This option produces a saving in MRP charges up to Year 25 of £45.254m but an increased liability in years 26 to 50 of £40.808m. This change in policy would generate savings of £2.629m and £9.957m in 2018/19 and 2019/20 to 2022/23 respectively, compared to the current calculation basis.

6.28 This option has been dismissed due to the extension in payment profile over the useful asset lives.

6.29 The results clearly show that all the options would generate savings over the next 25 years when compared to the current methodology. However, these options would effectively reprofile the debt repayment over the same or a longer period, and so the Council's MRP liability is significantly increased with all the options considered over the 26 to 50-year period.

6.30 In the medium term, i.e. 1 to 5 years, the various options produce MRP savings ranging from £2.375m (Option A) to £12.587m (Option C4).

7. Conclusions

7.1 As discussed previously under the relevant options it would not be reasonable for the Council to revise the remaining asset life of the assets financed from previous supported borrowing from 45 to 50 years, however, it would be prudent to revise the calculation from a straight line methodology to an annuity basis. Additionally, it would be sensible to consider adjusting the CFR calculation by reintroducing the use of Adjustment A in the calculation.

7.2 Taking all these points into consideration, it would be advisable for Council to consider adopting Option C3 for the calculation of MRP charges related to supported borrowing. Option C3 would generate the following relatively consistent MRP savings in the medium term:

- £2.217m in 2018/19.
- £2.150m in 2019/20.
- £2.083m in 2020/21.

- £1.941m in 2021/22.
- £1.867m in 2022/23.

7.3 Given that the savings level diminishes over the five-year period, it is proposed that a consistent level of saving is taken over the 5 year period in order that growth does not need to be built into the budget strategy for the remaining 4 years of the period to reduce down the saving. Therefore, a base budget saving of £1.85m will be taken each year of the five year period giving total savings of £9.25m.

7.4 The saving of £2.217m that will be generated in 2018/19 has not been reflected in the monitoring position for 2018/19. It is intended however that this saving is ringfenced to fund the Digital Transformation Project (DTP). Funding of the DTP was planned to come from capital funding, however there was always a gap of funding that would be bridged by undertaking prudential borrowing. It is therefore proposed that the MRP saving in 2018/19 is redirected to the DTP project so that we can avoid undertaking borrowing and incurring revenue costs of paying back the borrowing.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information) Treasury Strategy 2009/10 - Council 27th February 2009 Treasury Strategy 2016/17 - Council February 2016 Treasury Strategy 2018/19 - Council February 2018
Cabinet Member (Portfolio Holder) David Minnery, Portfolio Holder for Finance
Local Member N/A
Appendices Appendix A: Summary of Options Modelled for the Calculation of MRP Charges Associated with Supported Borrowing

APPENDIX A

SUMMARY OF OPTIONS MODELLED FOR THE CALCULATION OF MRP CHARGES ASSOCIATED WITH SUPPORTED BORROWING

Years	Current Basis	Option A		Option B1		Option B2		Option C1		Option C2		Option C3		Option C4	
	MRP £'000s	MRP £'000s	Difference £'000s	MRP £'000s	Difference £'000s	MRP £'000s	Difference £'000s	MRP £'000s	Difference £'000s	MRP £'000s	Difference £'000s	MRP £'000s	Difference £'000s	MRP £'000s	Difference £'000s
2016/17															
2017/18															
2018/19	4,559	4,084	(475)	2,397	(2,162)	1,975	(2,585)	4,456	(103)	3,992	(568)	2,343	(2,217)	1,930	(2,629)
Years 2 To 5	18,238	16,338	(1,900)	10,285	(7,953)	8,473	(9,765)	17,824	(414)	15,967	(2,270)	10,051	(8,186)	8,280	(9,957)
Years 6 To 10	22,797	20,422	(2,375)	14,574	(8,223)	12,006	(10,791)	22,280	(517)	19,959	(2,838)	14,243	(8,554)	11,734	(11,063)
Years 11 To 25	68,391	61,267	(7,124)	58,111	(10,280)	47,873	(20,518)	66,840	(1,551)	59,878	(8,514)	56,793	(11,598)	46,787	(21,604)
Years 26 To 40	68,391	61,267	(7,124)	88,191	19,800	72,653	4,262	66,840	(1,551)	59,878	(8,514)	86,191	17,800	71,005	2,614
Years 41 To 48	13,678	32,676	18,998	22,498	8,819	53,076	39,398	13,368	(310)	31,935	18,257	21,987	8,309	51,872	38,194
Total	**196,055**	**196,055**	**0**	**196,055**	**0**	**196,055**	**0**	**191,609**	**(4,446)**	**191,609**	**(4,446)**	**191,609**	**(4,446)**	**191,609**	**(4,446)**