Appendix 5a

REPORT

of the

DIRECTOR OF RESOURCES

to the

EXECUTIVE

on

8 FEBRUARY 2021

MINIMUM REVENUE PROVISION POLICY REVIEW

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1. Purpose

1.1 In 2020 the Council commissioned Link Asset Services to review the Council's existing Minimum Revenue Provision (MRP) Policy. The resulting review identified matters pertinent to the Council's MRP, which may appropriately be taken into account when formulating a revised MRP Policy.

1.2 This Paper has been produced in order to provide the necessary information to enable the Council to consider varying their MRP Policy.

2. Minimum Revenue Provision (MRP) for reduction of outstanding capital debt liability

2.1 The Local Government Act 2003 requires the Council to make a prudent annual revenue charge, termed a Minimum Revenue Provision (MRP), which serves to reduce the amount of outstanding capital debt liability that has arisen from earlier unfinanced capital expenditure.

2.2 The legislation specified originally that MRP should be charged at an annual rate of 4%, applied to the outstanding capital debt liability at the end of the previous financial year. However, mainly due to the length of time over which such charges stretched, and perceived inflexibility, statutory requirements were varied in 2008, whereby in future MRP should represent a prudent annual provision related broadly to the life of assets or other capital expenditures which cause the capital debt liability to increase.

2.3 It is for each local authority to determine itself each year an amount of MRP which it considers to be prudent. For the purposes of exercising this discretion, statute requires authorities to have regard to the MRP Guidance issued by the Secretary of State. The Guidance is not intended to represent requirements that must be adhered to. It represents recommendations for determining how the term "prudent provision" might appropriately be interpreted, whilst leaving scope for local authorities to consider an approach that is considered most appropriate for their individual circumstances.

2.4 The Guidance recommends that an annual MRP Policy should be determined before the commencement of each financial year by the full Council, whilst recognising that it may be appropriate to vary it during the currency of any financial year.

3. Alternative Options for a Revised Future MRP liability

3.1 Adjustment A

3.1.1 The statutory conditions that require an annual MRP charge were revised with effect from 1st April 2004 when the present system of local authority capital finance was introduced. Prior to this, MRP was charged under terms governed by the Local Government and Housing Act 1989 (The 1989 Act).

3.1.2 The revised MRP assessment provisions were related to a different method of assessing a local authority's capital debt liability. Under the 1989 Act, the annual amount of MRP was a stipulated percentage of an assessed "Adjusted Credit Ceiling (ACC)". The manner of assessing the ACC was set out in statute, but was not subject to any form of balancing with the amount of capital debt liability signified by the certified Statement of Accounts (Consolidated Balance Sheet).

3.1.3 The revised Statutory MRP assessment provisions effective from 1st April 2004 changed the perceived shortcomings of the ACC, and its link to a system of borrowing "credit approvals" by relating future MRP to 4% of the capital debt liability signified by the Consolidated Balance Sheet. The new measure of capital debt was termed the Capital Financing Requirement (CFR).

3.1.4 Additionally, the Government also considered it necessary to make provision for any variation that existed between the amount of an authority's closing ACC, and their CFR, in order to avoid any increase in MRP revenue costs arising under the revised capital control arrangements. The amount of any difference between these two forms of measuring capital debt liability was termed "Adjustment A".

3.1.5 The procedure for assessing Adjustment A is governed by Regulations issued in 2003, in conjunction with guidance contained within the Prudential Code. The identification of all relevant factors to be included is extremely important, as Adjustment A will normally represent a statutorily supported amount of ongoing revenue expenditure saving. It effectively relates to an amount of actual capital debt liability that will never be charged to revenue unless an authority determines to offset the saving by making an additional voluntary MRP.

3.1.6 The review carried out by Link Group has identified certain items that were not included within the Council's assessment of their CFR, which would have the effect of increasing the Council's Adjustment A, and in turn result in the identification of excess MRP charges that have been made since 2004, namely:-

a) An amount of £1.681m, relating to premiums outstanding, was excluded from what are termed "deferred charges", and in turn not included within the CFR. A letter from the appropriate Government Department indicated that premiums were a capital debt item.

b) Long term debtors of £0.917m were also excluded (mainly in respect of Blackpool FC, Lancashire County Enterprises and the principal element of mortgage loans).

c) Transferred Debt - the Council was a participant authority in an earlier Local Government Reorganisation, under which assets were transferred to them. The outstanding debt liability in respect of these assets was determined by statute to be represented by an amount of borrowing which continued to be managed by a separate Designated Authority.

3.1.7 There was no provision at the time for the transferred debt to be included within the Council's ACC. The Council's capital debt liability, as signified by the Consolidated Balance Sheet, increased in order to reflect the asset transfer, whilst their ACC remained at an unaltered level. Consequently, the manner in which statute provided for Adjustment A to be calculated should have resulted in the amount of transferred debt outstanding at 31st March 2004 (£32.145m) being included within the Adjustment A calculation.

3.1.8 Collectively, these three factors result in an upward revision of the Council's Adjustment A of £34.743m, which in turn reduces the amount of future year MRP liability under the statutory and subsequent prudential MRP arrangements. Essentially, this is not a discretionary adjustment provided that it is in compliance with proper Adjustment A calculation procedures. The statutory provision that governs Adjustment A, with specific provision for ignoring any known errors or exclusions in/from the ACC, effectively removes any need to consider whether the manner in which Adjustment A operates might otherwise meet with tests of prudence.

3.1.9 With regard to the MRP saving that results from the revised Adjustment A calculation for years 2004/05 – 2018/19, this represents a gross savings potential of £20.8m. Link Group calculations of the annual amount of saving (at 4% until 2007/08, and at 2% thereafter) have additionally taken into account the additional MRP liability that would have arisen had the higher Adjustment A operated from the 2004/05 financial year. This produces a net minimum aggregate potential savings amount of £12.647m, which is available to the Council as a means of reducing what would otherwise be a future year's prudent amount of MRP.

3.1.10 Further savings may arise from the higher amount of Adjustment A in each future financial year including 2019/20 and 2020/21 and are currently being reviewed.

3.2 <u>Amounts Voluntarily Set Aside</u>

3.2.1 The Manner in which MRP is to be assessed was varied in 2007, whereby subsequent annual MRP liability is required to reflect a prudent provision. In order to assist with the determination of what might represent a prudent provision, statute requires local authorities to have regard to MRP Guidance. The Guidance contains a number of recommendations, whilst also providing for local discretion to be exercised

3.2.2 One of the recommended principles of the original Guidance was to recognise that "authorities may in any year make additional voluntary revenue provision", combined with an option to make an appropriate reduction for such voluntary contributions when determining a subsequent year's prudent amount of MRP.

3.2.3 Link Group has carried out an analysis of all such revenue contributions made by the Council between years 2004/05 – 2014/15, and identified an aggregate total amount of £13.054m. After applying the same philosophy of adjusting this amount to reflect the higher MRP charge that would have arisen had these contributions not been made, a further potential savings benefit of £11.161m is available to set against the MRP liability that would otherwise arise with effect from the 2020/21 financial year.

3.2.4 The cumulative aggregate MRP minimum saving identified from Adjustment A and voluntary revenue contributions is £23.808m.

4. Exercising the MRP Savings option

4.1 The amount of £23.808m is now available to the Council as a means of reducing what would otherwise represent a future years MRP liability. In practice, this means that the whole, or a proportion, of what would otherwise be the annual charge may be alleviated. It will be for the Council itself to consider whether, and the extent to which, any saving amount is realised. The one statutory condition is that it is not possible in any year to obtain such relief that is greater than the charge that would otherwise be made. The aggregate savings amount will therefore be available to the Council over a number of years.

4.2 The statutory MRP Guidance recommends that MRP Policies/strategies may be varied at any time. It will be for the Council to determine when they wish to implement the first tranche of potential saving, and its extent.

5. Capital Receipts

5.1 Capital receipts may either be applied to finance capital expenditure, or set aside in order to reduce the Council's capital debt liability. The setting aside of capital receipts has the effect of reducing the outstanding amount of Capital debt liability, as signified by a reduction in the CFR.

5.2 Since the assessment of MRP was changed to reflect the life of new assets acquired/constructed etc., a reduction to the CFR no longer has an automatic effect upon MRP liability. It is therefore possible for the Council to determine, as part of its MRP Policy, that the amount by which the CFR is reduced may be reflected in an equivalent reduction to the amount of MRP liability that would otherwise have been charged. In terms of prudence, such a determination would reflect the fact that the outstanding capital debt liability is consistently reduced each year by the amount of MRP.

6. Recommendations

1. To recommend that the Council approves the revised Minimum Revenue Provision Policy 2020/21 set out within Appendix 5b to the Executive this report.

2. To recommend to the Council that in approving the revised Minimum Revenue Provision Policy Council endorses the following amendments which had been included in the document:

i. The Council has accepted the principle that any capital receipts which it determines in future should be set aside in order to reduce the outstanding amount of capital debt liability may, if desired, be taken to represent a debt liability reduction that has been made in lieu of a corresponding amount of prudent provision that would otherwise have been made in a particular financial year. Any such setting aside of capital receipts will not, however, apply to those capital receipts which represent the repayment of loan principal amounts in respect of loans made in earlier financial years which have been treated as capital expenditure, but not subjected to an Minimum Revenue Provision charge.

ii. The policy changes reflected above will in future be represented as a new local Option for the ongoing determination of an amount of Minimum Revenue Provision which is considered each year to be prudent.

iii. In respect of new capital debt liability incurred after 1st April 2008, the Authority's Policy continues to adopt the principles outlined in Option 3 (asset life method) that are exemplified in the Minimum Revenue Provision Guidance, whereby the liability will be charged over a period that is reasonably commensurate with that over which the new capital expenditure is estimated to provide a benefit to the Authority.

iv. Any credit arrangements or expenditure treated as capital expenditure under Direction or Regulation will either have Minimum Revenue Provision determined under Option 3, or otherwise related to the estimated life of the underlying asset. For example, a loan granted to a third party towards "capital expenditure" will, where Minimum Revenue Provision is considered to be necessary, be related to the life of the asset towards which the financial assistance is being provided.

v. Whether any charges are appropriate for this type of activity after taking account of the different powers available to it.

vi. Minimum Revenue Provision will not be charged (voluntarily) on any Part II (Housing Revenue Account related) housing debt.

vii. Minimum Revenue Provision will not be charged on loans made to wholly owned subsidiaries or other third parties where such loans are treated as capital expenditure in cases where there are satisfactory and supportable repayment obligations attached to those loans. Unlike other types of capital receipt, the capital receipts that will arise from these repayments will be set aside generally or specifically to reduce the outstanding amount of capital debt liability in respect of these loans. The anticipated receipts will be kept under review on an annual basis in order to ensure that the deferment of Minimum Revenue Provision remains prudent.

viii. Following the identification of savings in respect of financial years 2004/05 – 2018/19, totalling £23.808m, (in respect of an increase of £34.743m to Adjustment A, and earlier year revenue contributions to capital of £13.054m, (adjusted for alternate Minimum Revenue Provision liability)), the Council will determine for any subsequent financial year the extent to which they propose to reduce the amount of Minimum Revenue Provision liability that would have arisen, but for these savings. Additionally, the Council will continue to apply the higher amount of Adjustment A indicated above to have been identified.

S THOMPSON

DIRECTOR OF RESOURCES