Report of the Section 151 Officer

Council – 20 December 2018

Minimum Revenue Provision (MRP) Policy Statement 2019/20 and Revision to 2018/19 MRP Policy

Purpose:	To approve the Minimum Revenue Provision Policy Statement for 2019/20 and to revise the 2018/19 Policy and implement in year on the basis that a clear intention to revise the policy has been previously highlighted to both Cabinet and Council.
Policy Framework:	Medium Term Financial Plan
Consultation:	Legal, Finance and Access to Services.
Recommendation(s):	It is recommended that:
1)	Council approves the Minimum Revenue Provision (MRP) Policy Statement as outlined in Section 3.3 of the Report
Report Author:	Jeff Dong
Finance Officer:	Ben Smith
Legal Officers:	Debbie Smith/Tracey Meredith
Access to Services Officer:	Rhian Millar

1 Introduction

1.1 Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery. It is inappropriate to charge the entirety of this expenditure in the year in which it is incurred i.e. the expenditure benefits more than a single year of account. As such, the resulting costs are spread over several years. The manner of spreading these costs is through an annual Minimum Revenue Provision (MRP) which was previously determined under Regulation and now is determined under Guidance. Under the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003, Local Authorities are required to charge to their revenue account, for each financial year, a Minimum Revenue Provision (MRP) to account for the cost of their debt in the preceding financial year. Regulation 21 set out the method Authorities were required to follow in calculating MRP.

1.2 Under the Local Authorities (Capital Finance and Accounting) (Amendment) (Wales) Regulations 2008, the detailed calculation has been replaced with a requirement that local authorities ‘have regard’ to the guidance (attached at Appendix B) and the recommendations within. In principle, an authority is now only required to make a ‘prudent provision’ in respect of its ongoing MRP charge. The broad aim of prudent provision is to ensure that debt is repaid over a period reasonably commensurate with that over which the capital expenditure provides benefits.

1.3 The options for prudent provision (full guidance note is attached at Appendix B) are as follows:

1. Regulatory Method – MRP is equal to the amount determined in accordance with the former 2003 Regulations as if it had not been revoked by the 2008 Regulations.(4% reducing balance)
2. Capital Financing Requirement (CFR) Method – MRP is equal to 4% of the non-housing CFR at the end of the preceding financial year.(4% reducing balance)
3. Asset Life Method – where capital expenditure on an asset is financed wholly or partly by borrowing, MRP is to be made in equal annual instalments over the estimated economic life of the asset. Where capital expenditure is not incurred in the creation of an asset, MRP is to be made in equal annual instalments over a period reasonably reflecting the benefit arising from the expenditure.
4. Depreciation Method – MRP is to be equal to the depreciation of that proportion of the asset on which expenditure has been financed by borrowing.

1.4 The 2008 Regulations recommend that prior to the commencement of each financial year a local authority prepares a statement of its policy on making MRP (Annual MRP Statement) and submits it to full Council. At Council March 2018, the following MRP Policy was approved, subject to review during 2018/19 was reported as:

- Option 1 for pre 2007/08 debt and all new supported borrowing 2007/08 onwards

- Option 3 for all new unsupported borrowing 2007/08 onwards

- HRA MRP remains the regulatory 2%

2. Wales Audit Office Guidance

2.1 The Assistant Auditor General (AAG) for Wales in his letter to all Local Authorities in Wales, dated 7th January 2016, advised that where an amendment to current MRP policy is being considered, a Local Authority should take account of ‘The Well-being of Future Generations (Wales) Act 2015’ (the Act). This is because an amendment from the 4% reducing balance methodology to one based on asset lives will invariably result in a reduced MRP charge in the short-term but an increased MRP charge in the longer term.

2.2 In complying with the Act a Local Authority must ensure that its decisions are sustainable, whereby “the needs of the present are met without compromising the ability of future generations to meet their own needs”, and recognise “the importance of balancing short term needs with the need to safeguard the ability to meet long term needs”.

2.3 In addition the AAG advised that those Local Authorities wishing to amend their current MRP Policy should demonstrate that:

- The lower charge more accurately reflects the lives of assets employed by the authority; or
- The lower charge is reasonably commensurate with the period implicit in the determination of Revenue Support Grant (i.e. a 4% reducing balance basis).

3 Revised MRP Policy

3.1 The Section 151 Officer informed Council in March 2018 of the pending review into the basis of the adopted MRP policy, and that discussions were being held with the Wales Audit Office (WAO) in reviewing the procedural aspects, and in determining whether the proposals were considered prudent.

3.2 The basis of the proposal is for the ‘Asset Life’ method (Option 3) to be applied to all supported borrowing (including capital expenditure incurred before 1st April 2008), which is currently amortised using Option1.

3.3 The proposed amendment to the MRP Policy, effective in financial year 2018/19, is based on the following methodology, discussed with WAO. It is recommended that Council approve:

- For all supported borrowing, including capital expenditure incurred before 1st April 2008, the charge to revenue will be over 40 years by the straight line method, which is commensurate with the average of asset useful economic lives. In essence this replaces the 4% reducing balance method with a 2.5% straight line method. This can be considered a more prudent approach than the current provision because it introduces a more certain period for eliminating the debt liability in full.
- For unsupported borrowing, the charge to revenue will be over 40 years by the straight line method, or over the estimated economic life of the asset if that is less than 40 years. (unchanged)
- Where a regulatory requirement requires a different amortisation period (e.g. Capitalisation Directive for back pay) (unchanged)
- For the Housing Revenue Account, the MRP will remain at 2% of the opening capital Financing requirement (CFR) each year (unchanged) up until April 2021 following which the MRP on new expenditure will need to be on the Asset life or the Depreciation method in line with the new Item 8 determination issued by Welsh Government following the exit of the subsidy system. The preferred method shall be determined in 2021.

3.4 The implications of the proposed amended MRP Policy for the 50 year period which applies to the supported and unsupported borrowing 2018/19 to 2067/68 is outlined in Appendix A and summarised in Table 1 for 2018/19 to 2022/23, with 2022/23 being the final year of the next 3 year Medium Term Financial Plan.

3.5 Table 1 – Implications of Proposed Amended MRP

Financial Year	Estimated Current MRP charge @ 4% reducing balance	Estimated MRP Charge @ Useful Life 40 years (2.5% straight line)	Difference (Saving)
	£'000	£'000	£'000
2018/19	9,917	6,456	3,460
2019/20	9,520	6,456	3,064
2020/21	9,139	6,456	2,683
2021/22	8,774	6,456	2,317
2022/23	8,423	6,456	1,967

The table reflects the MRP on the existing borrowing only. There will be additional savings on the MRP charges (compared to previous policy) in the initial years of new future borrowings, which are themselves likely to be substantial given the scale of ambition of the Council's future capital programme .

3.6 It is evident from Table 1 that significant financial savings averaging £2.7 million per annum are anticipated over the period 2018/19 to 2022/23 arising from the proposed amendment to the MRP Policy.

3.7 In addressing the AAG's requirements in respect of the Act, the following should be noted from Appendix A in respect of the proposed amendment to the MRP Policy:

- A reduced charge to revenue is projected for the period 2018/19 to 2028/29
- An increased charge to revenue is projected for the period 2029/30 to 2056/57
- A reduced charge to revenue per annum is projected from 2057/58, reflecting the full extinguishment of the debt liability under the asset life method by this point in time
- In respect of opening CFR debts as at 31/3/18, by the 4% reducing balance method, a balance of £33.5m still remains after 50 years and even after 100 years, a liability of £4.3m still remains whereas with the 2.5% straight line method the debt is totally extinguished by 2057/58 (i.e. in 40 years)

3.8 In conclusion, the proposed amendment to the MRP Policy determines a more prudent annual charge to revenue whilst acknowledging the Council's responsibility to its current and future citizens in responding to the requirements of the Act. Appendix A clearly demonstrates that by applying the proposed average asset useful economic life of 40 years on a straight line basis to supported borrowing including capital expenditure incurred before 1st April 2008, this historic liability is actually extinguished after 40 years instead of leaving a residual debt balance for citizens 100 years plus into the future. This residual liability will mean that future citizens will be required to finance this historic debt, at the expense of real services making a real difference to citizens' lives.

3.9 In responding to the AAG's requirement in paragraph 2.3, an evaluation of the Council's fixed assets concludes that an average useful life of 40 years is prudent and sensible since it reflects current and future useful economic lives of recently created assets. In addition, a maximum useful life of 40 years for infrastructure assets is consistent with other Local Authorities.

3.10 This is particular pertinent to note in relation to arrangements under the City Deal where all three other local authority partners have already changed their MRP policy. Furthermore, a direct consequence of City Deal financing falling over an equal instalment basis over a period of 15 years, but up front spending and borrowing heavily loaded towards earlier years, likely peaking by 2025-26 means that there is an imbalance of funding over the time period. This can be partly offset by reducing the front loading of some capital financing costs by the change to the MRP Policy method. This is a fairer way of smoothing and sharing costs over the medium term.

3.11 Finally, and wholly in line with the Reserves Policy agreed by Council in both 2017 and 2018, any early years underspending on capital financing, including that achieved by the proposed MRP Policy Change, will itself be set aside into the Capital Equalisation Reserve rather than used to directly reduce revenue spending. As explained previously to Council this Equalisation Reserve is itself used to smooth costs and address some aspects of the timing difference between spend over a shorter period than the reimbursement flowing from the 15 year equal funding instalments offered by the City Deal.

4 Financial Implications

4.1 For the 2018/19 financial year and for the period of the Medium Term Financial Plan 2019/20 to 2022/23, revenue savings of circa £2.7 million per annum are projected.

4.2 Annual revenue savings will continue to be realised until the 2028/29 financial year following which an increased charge to revenue is evident until the 2056/57 financial year before annual savings are again realised from the 2057/58 financial year, as a result of the full extinguishment of the debt under the asset life method for the MRP Policy.

4.3 In the prudent planning for the future City Deal, it is recognised the revised MRP policy provides for (as set out in the report) the differences in timing of costs . Taken in conjunction with the timing of future City Deal grant financing flows, and the continued proposed use of the Capital Equalisation Reserve to smooth yet further charges to revenue, this change, justifies and mitigates, appropriately, the changed profile of

MRP repayment, whilst remaining, in the professional opinion of the S151 Officer, prudent.

5. Legal Implications

5.1 The Authority is under a duty to make arrangements for the proper administration of its financial affairs. Failure to do so will be a breach of that duty. The statutory provisions and guidance imposing such a duty on the Authority are as set out in the main body of the Report.

5.2 That includes specific duties under the Wellbeing of Future Generations Act. It is clear that the revised MRP Policy as set out in the report, addresses its obligations under the Act, and provides for:

- an equalisation of the cross generational subsidy inherent in the previous policy
- eliminates payment into perpetuity for the historically incurred debt burden.
- appropriate amortisation period for debt commensurate with the life of the asset acquired

6. Equality Impact Implications

6.1 The Council is subject to the Public Sector Equality Duty (Wales) and must, in the exercise of their functions, have due regard to the need to:

- Eliminate unlawful discrimination, harassment and victimisation and other conduct prohibited by the Act.

- Advance equality of opportunity between people who share a protected characteristic and those who do not.

- Foster good relations between people who share a protected characteristic and those who do not.

Our Equality Impact Assessment process ensures that we have paid due regard to the above. An equality impact assessment screening has been undertaken and it concludes that there are no equality impact implications arising from this report.

Background papers: None

Appendices:
Appendix A – MRP Projections
Appendix B – MRP Guidance
Appendix C – Equality Impact Assessment

Appendix A

Existing Supported Borrowing CFR					
year ended	CFR	MRP @ 4% reducing balance	CFR	MRP at 40 year useful asset life (2.5% straight line)	Difference
	£'000	£'000	£'000	£'000	£'000
31/03/2018	258,245	10,330	258,245	6,456	3,874
31/03/2019	247,915	9,917	251,789	6,456	3,460
31/03/2020	237,999	9,520	245,333	6,456	3,064
31/03/2021	228,479	9,139	238,877	6,456	2,683
31/03/2022	219,340	8,774	232,421	6,456	2,317
31/03/2023	210,566	8,423	225,964	6,456	1,967
31/03/2024	202,143	8,086	219,508	6,456	1,630
31/03/2025	194,058	7,762	213,052	6,456	1,306
31/03/2026	186,295	7,452	206,596	6,456	996
31/03/2027	178,843	7,154	200,140	6,456	698
31/03/2028	171,690	6,868	193,684	6,456	411
31/03/2029	164,822	6,593	187,228	6,456	137
31/03/2030	158,229	6,329	180,772	6,456	-127
31/03/2031	151,900	6,076	174,315	6,456	-380
31/03/2032	145,824	5,833	167,859	6,456	-623
31/03/2033	139,991	5,600	161,403	6,456	-856
31/03/2034	134,391	5,376	154,947	6,456	-1,080
31/03/2035	129,016	5,161	148,491	6,456	-1,295
31/03/2036	123,855	4,954	142,035	6,456	-1,502
31/03/2037	118,901	4,756	135,579	6,456	-1,700
31/03/2038	114,145	4,566	129,123	6,456	-1,890
31/03/2039	109,579	4,383	122,666	6,456	-2,073
31/03/2040	105,196	4,208	116,210	6,456	-2,248
31/03/2041	100,988	4,040	109,754	6,456	-2,417
31/03/2042	96,949	3,878	103,298	6,456	-2,578
31/03/2043	93,071	3,723	96,842	6,456	-2,733
31/03/2044	89,348	3,574	90,386	6,456	-2,882
31/03/2045	85,774	3,431	83,930	6,456	-3,025
31/03/2046	82,343	3,294	77,474	6,456	-3,162
31/03/2047	79,049	3,162	71,017	6,456	-3,294
31/03/2048	75,887	3,035	64,561	6,456	-3,421
31/03/2049	72,852	2,914	58,105	6,456	-3,542
31/03/2050	69,938	2,798	51,649	6,456	-3,659
31/03/2051	67,140	2,686	45,193	6,456	-3,771
31/03/2052	64,455	2,578	38,737	6,456	-3,878
31/03/2053	61,876	2,475	32,281	6,456	-3,981
31/03/2054	59,401	2,376	25,825	6,456	-4,080

31/03/2055	57,025	2,281	19,368	6,456	-4,175
31/03/2056	54,744	2,190	12,912	6,456	-4,266
31/03/2057	52,555	2,102	6,456	6,456	-4,354
31/03/2058	50,452	2,018	0	0	2,018
31/03/2059	48,434	1,937	0	0	1,937
31/03/2060	46,497	1,860	0	0	1,860
31/03/2061	44,637	1,785	0	0	1,785
31/03/2062	42,852	1,714	0	0	1,714
31/03/2063	41,137	1,645	0	0	1,645
31/03/2064	39,492	1,580	0	0	1,580
31/03/2065	37,912	1,516	0	0	1,516
31/03/2066	36,396	1,456	0	0	1,456
31/03/2067	34,940	1,398	0	0	1,398
31/03/2068	33,542	1,342	0	0	1,342

Appendix B

Minimum Revenue Provision

1. Government Guidance

The Welsh Assembly Government issued new guidance in March 2008 which requires that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start of the financial year to which the provision will relate.

The Council are legally obliged by section 21 (1b) to "have regard" to the guidance, which is intended to enable a more flexible approach to assessing the amount of annual provision than was required under the previous statutory requirements. The guidance offers four main options under which MRP could be made, with an overriding recommendation that the Council should make prudent provision to redeem its debt liability over a period which is reasonably commensurate with that over which the capital expenditure is estimated to provide benefits. The requirement to 'have regard' to the guidance therefore means that: -

Although four main options are recommended in the guidance, there is no intention to be prescriptive by making these the only methods of charge under which a local authority may consider its MRP to be prudent.

It is the responsibility of each authority to decide upon the most appropriate method of making a prudent provision, after having had regard to the guidance.

Where the CFR was nil or negative on the last day of the preceding financial year, the authority does not need to make an MRP provision. MRP in the current financial year would therefore by zero,

Option 1: Regulatory Method

Under the previous MRP regulations, General Fund MRP was set at a uniform rate of 4% of the adjusted CFR (i.e. adjusted for "Adjustment A") on a reducing balance method (which in effect meant that MRP charges would stretch into infinity). This option is available for the General Fund share of capital financing requirement which relates to capital expenditure incurred prior to 1 April 2008. It may also be used for new capital expenditure up to the amount which is deemed to be supported by the Welsh Assembly Government annual supported borrowing allocation. The use of the commutation adjustment to mitigate the MRP charge is also allowed to continue under this option.

Option 2: Capital Financing Requirement Method

This is a variation on option 1 which is based upon a charge of 4% of the aggregate CFR without any adjustment for Adjustment A, or certain other factors which were brought into account under the previous statutory MRP calculation. The CFR is the measure of an authority's outstanding debt liability as depicted by their balance sheet.

Option 3: Asset Life Method.
This method may be applied to most new capital expenditure, including where desired that which may alternatively continue to be treated under options 1 or 2.

The guidance suggests that any new borrowing which receives no Government support and is therefore self-financed would fall under option 3

Under this option, it is intended that MRP should be spread over the estimated useful life of either an asset created, or other purpose of the expenditure. There are two useful advantages of this option: -

- Longer life assets e.g. freehold land can be charged over a longer period than would arise under options 1 and 2.
- No MRP charges need to be made until the financial year after that in which an item of capital expenditure is fully incurred and, in the case of a new asset, comes into service use (this is often referred to as being an 'MRP holiday'). This is not available under options 1 and 2.

There are two methods of calculating charges under option 3:

Equal instalment method – equal annual instalments which are calculated using a simple formula set out in paragraph 9 of the MRP guidance,

under this approach, the MRP is provided by the following formula

A – B divided by C

A is the amount of capital expenditure in respect of the asset financed by borrowing or credit arrangements

B is the total provision made before the current financial year in respect of that expenditure

C is the inclusive number of financial years from the current year to that in which the estimated life of the asset expires

Annuity method – annual payments gradually increase during the life of the asset with an appropriate interest rate used to calculate the annual amount

Under both options, the authority may make additional voluntary revenue provision and this may require an appropriate reduction in later years' MRP

In addition adjustments to the calculation to take account of repayment by other methods (e.g. application of capital receipts) should be made as necessary.

Option 4: Depreciation Method
Under this option, MRP charges are to be linked to the useful life of each type of asset using the standard accounting rules for depreciation (but with some exceptions) i.e. this is a more complex approach than option 3.

The same conditions apply regarding the date of completion of the new expenditure as apply under option 3.

2. Date of implementation
The previous statutory MRP requirements cease to have effect after the 2006/07 financial year. However, the same basis of 4% charge in respect of the GF share of CFR may continue to be used without limit until the 2009/10 financial year, relative to expenditure incurred up to 31/3/2008.

The guidance suggests that Options 3 and 4 should be applied to any capital expenditure which results in an increase in the CFR and does not relate to the authority's Supported Capital Expenditure.

The guidance also provides the authority with discretion to apply Options 3 or 4 to all capital expenditure whether or not supported and whenever it is incurred.

Appendix C

Equality Impact Assessment

Please ensure that you refer to the '[Screening Form Guidance]' while completing this form. If you would like further guidance please contact your support officer in the Access to Services team (see guidance for details).

Section 1
What service area and directorate are you from?
Service Area: Financial Services & Service Centre
Directorate:Resources

Q1(a) WHAT ARE YOU SCREENING FOR RELEVANCE?

Service/ Function	Policy/ Procedure	Project	Strategy	Plan	Proposal
☐	☐	☐	✓	☐	☐

(b) Please name and describe below

MINIMUM REVENUE PROVISION (MRP) POLICY- this policy sets out the appropriate amortisation periods for different forms of debt incurred by the Authority

Q2(a) WHAT DOES Q1a RELATE TO?

Direct front line service delivery	Indirect front line service delivery	Indirect back room service delivery
☐ **(H)**	☐ **(M)**	✓**(L)**

(b) DO YOUR CUSTOMERS/CLIENTS ACCESS THIS SERVICE…?

Because they need to	Because they want to	Because it is automatically provided to everyone in Swansea	On an internal basis i.e. Staff
☐ **(H)**	☐ **(M)**	☐ **(M)**	✓ **(L)**

Q3 WHAT IS THE POTENTIAL IMPACT ON THE FOLLOWING…

	High Impact **(H)**	Medium Impact **(M)**	Low Impact **(L)**	Don't know **(H)**
Age	☐	☐	✓	☐
Disability	☐	☐	✓	☐
Gender reassignment	☐	☐	✓	☐
Marriage & civil partnership	☐	☐	✓	☐

Pregnancy and maternity	☐	☐	✓	☐
Race	☐	☐	✓	☐
Religion or (non-)belief	☐	☐	✓	☐
Sex	☐	☐	✓	☐
Sexual Orientation	☐	☐	✓	☐
Welsh Language	☐	☐	✓	☐
Poverty/social exclusion	☐	☐	✓	☐
Carers	☐	☐	✓	☐
Community cohesion	☐	☐	✓	☐

Q4 Have you / will you undertake any public consultation and engagement relating to the initiative?

☐ **Yes** ✓ **No** **(If no, you need to consider whether you should be undertaking consultation and engagement – please see the guidance)**

If yes, please provide details below

Q5(a) HOW VISIBLE IS THIS SERVICE/FUNCTION/POLICY/PROCEDURE/ PROJECT/ STRATEGY TO THE GENERAL PUBLIC?

High visibility to general public	Medium visibility to general public	Low visibility to general public
☐ **(H)**	☐ **(M)**	✓ **(L)**

(b) WHAT IS THE POTENTIAL RISK TO THE COUNCIL'S REPUTATION? ***(Consider the following impacts – legal, financial, political, media, public perception etc…)***

High risk to reputation	Medium risk to reputation	Low risk to reputation
☐ **(H)**	✓ **(M)**	✓☐ **(L)**

Q6 Will this initiative have an impact (however minor) on any other Council service?

Yes ✓ **No** **If yes, please provide details below**

Q7 HOW DID YOU SCORE? ***Please tick the relevant box below***
– NOTE: Q3 counts as a single H, M or L (and one H / M outscores any nº of Ls)

MOSTLY H and/or M ⟶ HIGH PRIORITY ⟶ ☐ EIA to be completed

Please go to Section 2

MOSTLY L ⟶ LOW PRIORITY / ⟶ ✓Do not complete EIA

NOT RELEVANT **Please go to Q8 followed by Section 2**

Q8 If after completing the EIA screening process you determine that this service/function/policy/project is not relevant for an EIA you must provide adequate explanation below.

This is an accounting policy which affects the methodology adopted to amortise debt in the Authority's financial statements and has no direct impact on the groups identified in Q3

Section 2

Please send this completed form to the Access to Services Team for agreement before obtaining email approval from your Head of Service.

Screening form completed by:
Name: Jeff Dong
Location: 1.4.1c
Telephone Number: 6934
Date: 7/11/18

Approval by Head of Service:
Name: B Smith
Position: Section 151 Officer
Date: 7/11/18/

Please return the completed form to accesstoservices@swansea.gov.uk