CYNGOR SIR CEREDIGION COUNTY COUNCIL

Report to:	**Governance & Audit Committee**
Date of meeting:	**3 June 2021**
Title:	**Revised Minimum Revenue Provision (MRP) Policy for 2021/22**
Purpose of the report:	**To consult the Governance & Audit Committee on the proposed Revised MRP Policy for 2021/22.**
For:	**For information**
Cabinet Portfolio:	**Cllr. Gareth Lloyd** **Finance, Procurement and Public Protection**

1. INTRODUCTION

Under the Local Authority (Capital Finance and Accounting) (Wales) Amendment regulations 2008, Local authorities are required to set aside 'prudent' revenue provision for debt repayment (MRP) where they have used borrowing or credit arrangements to finance capital expenditure. MRP for the Council's Supported Borrowing is calculated using the Capital Financing Requirement (CFR) as a base. The CFR is a measure of the Council's underlying need to borrow for capital purposes.

During 2015 a review of the MRP Policy was undertaken which resulted in Council revising the 2015/16 MRP Policy. The largest element of the MRP relates to historic and supported debt which the Council agreed to provide for on a 2% straight line basis over the estimated life of the assets which was 50 years.

2. Review of MRP Policy for Historic and Supported Debt

Officers have recently undertaken a further review to ensure that the Policy continues to remain prudent. Issues that have been considered:

i. The Council can determine its own basis for charging MRP. The WG guidance 2018 (https://gov.wales/sites/default/files/publications/2019-06/guidance-on-minimum-revenue-provision.pdf) does however include four options for calculating the charge. One of the options is the Asset Life Method. This option allows the charge to be profiled on an equal installment method / straight line basis or the charge could be profiled using an Annuity Method.

ii. Flintshire, Merthyr and Powys have adopted the Annuity Method along with other Councils in England and Scotland.

iii. CIPFA's Practitioner's Guide to Capital Finance in Local Government' (2019) states: *'The Annuity Method provides a fairer charge than equal instalments as it takes account the time value of money, whereby paying £100 in 10 years' time is* *less of a burden than paying £100 now. The schedule of charges produced by the Annuity Method thus results in a consistent charge over the asset's life, taking into account the real value of the amounts when they fall due. The Annuity Method would then be a prudent basis for providing for assets that provided a steady flow of benefits over their useful life.'* Adopting the Annuity Method is a fairer basis for all generations and therefore this is a prudent approach for the Council to adopt.

iv. The WG Guidance states that if Councils use the Annuity Method it should use an appropriate interest rate. It does not state which interest rate to use. The Historic and Supported Debt has funded the many assets that have been pooled together where Council approved an average life of 50 years some 6 years ago. It is not possible to allocate the loans against individual assets. Therefore maintaining the pooling approach an appropriate Annuity Rate for this debt is to use the average borrowing rate of loans outstanding as of 31 March 2021 - being 4.20%.

v. The table and chart below shows a comparison between the MRP charges for the Straight Line method and the Annuity Method. The Straight Line method is charged over a 50 year period and includes MRP chargeable since 2015/16. The Annuity Method also includes MRP chargeable since 2015/16 but is charged over a 44 year period. Adopting a different number of years for the methods only has a minor impact on the overall calculations. The total charge is the same for both methods. The charge using the Annuity Method increases annually and is lower than the Straight Line Method up until 2045/46 but then in subsequent years it is higher.

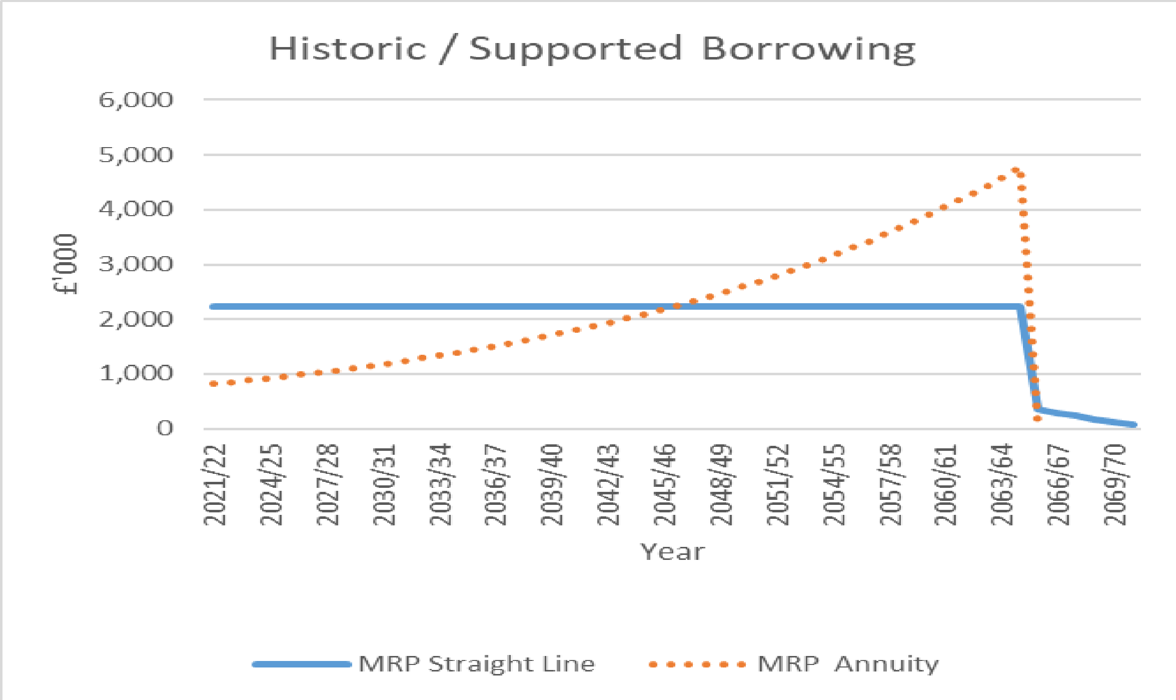
vi. Net Present Value (NPV) Calculation. The cash differences between each year, as referenced in the bullet point above, have been subject to a NPV calculation which takes into account the time value of money – this is also shown in table and chart below. The calculation illustrates that a change to the Annuity Method is nearly £10m cheaper (taking into account the time value of money) which supports that this approach will not negatively impact on future generations. The NPV calculation is based on a rate of 3.5% which is recommended by HM Treasury and can be considered to be an assumed rate for inflation.

vii. The Council currently adopts the Straight Line basis for calculating MRP for the PFI scheme. If changes are made to how MRP is calculated for the Historic and Supported Debt it would be appropriate to adopt the same method for this group of assets. MRP for the PFI scheme is charged against the General Fund but the charge is subsequently reversed so any change will have no cash impact on the Council. The entries are required to ensure the Council's Statement of Accounts remain compliant.

viii. The table below illustrates the MRP charge on the Straight Line Method and on the Annuity Method both in cash terms and discounted for the effect of time. The range of the MRP charge, when discounted for the effect of time, is narrower using the Annuity Method being £813k to £506k (column e) compared to £2,221k to £1,087k using the Straight Line method (column d) which supports the proposal as being fairer for all generations. The graph below illustrates the Straight Line Method and on the Annuity Method on a cash basis.

Historic / Supported Borrowing

	In cash terms			Discounted for the effect of time		
	a	b	c=b-a	d	e	f=e-d
Year	MRP Straight Line	MRP Annuity	Difference	MRP Straight Line	MRP Annuity	Difference
	£'000	£'000	£'000	£'000	£'000	£'000
2021/22	2,221	813	1,408	2,221	813	-1,408
2022/23	2,221	847	1,374	2,146	819	-1,328
2023/24	2,221	883	1,339	2,074	824	-1,250
2024/25	2,221	920	1,301	2,004	830	-1,174
2025/26	2,221	959	1,263	1,936	835	-1,100
2026/27	2,221	999	1,223	1,870	841	-1,029
2027/28	2,221	1,041	1,181	1,807	847	-960
2028/29	2,221	1,085	1,137	1,746	852	-894
2029/30	2,221	1,130	1,091	1,687	858	-829
2030/31	2,221	1,178	1,044	1,630	864	-766
2031/32	2,221	1,227	994	1,575	870	-705
2032/33	2,221	1,279	943	1,522	876	-646
2033/34	2,221	1,332	889	1,470	882	-588
2034/35	2,221	1,388	833	1,420	888	-533
2035/36	2,221	1,446	775	1,372	894	-479
2036/37	2,221	1,507	714	1,326	900	-426
2037/38	2,221	1,571	651	1,281	906	-375
2038/39	2,221	1,636	585	1,238	912	-326
2039/40	2,221	1,705	516	1,196	918	-278
2040/41	2,221	1,777	445	1,155	924	-231
2041/42	2,221	1,851	370	1,116	930	-186
2042/43	2,221	1,929	292	1,079	937	-142
2043/44	2,221	2,010	211	1,042	943	-99
2044/45	2,221	2,095	127	1,007	949	-57
2045/46	2,221	2,183	39	973	956	-17
2046/47	2,221	2,274	-53	940	962	22
2047/48	2,221	2,370	-148	908	969	61
2048/49	2,221	2,469	-248	877	975	98
2049/50	2,221	2,573	-352	848	982	134
2050/51	2,221	2,681	-460	819	989	170
2051/52	2,221	2,794	-572	791	995	204
2052/53	2,221	2,911	-690	765	1,002	237
2053/54	2,221	3,033	-812	739	1,009	270
2054/55	2,221	3,161	-939	714	1,016	302
2055/56	2,221	3,294	-1,072	690	1,023	333
2056/57	2,221	3,432	-1,210	666	1,029	363
2057/58	2,221	3,576	-1,355	644	1,036	393
2058/59	2,221	3,726	-1,505	622	1,043	421
2059/60	2,221	3,883	-1,661	601	1,051	449
2060/61	2,221	4,046	-1,824	581	1,058	477
2061/62	2,221	4,216	-1,994	561	1,065	504
2062/63	2,221	4,393	-2,171	542	1,072	530
2063/64	2,221	4,577	-2,356	524	1,079	555
2064/65	2,221	4,770	-2,548	506	1,087	580
2065/66	350		350	77		-77
2066/67	291		291	62		-62
2067/68	233		233	48		-48
2068/69	175		175	35		-35
2069/70	117		117	23		-23
2070/71	60		60	11		-11
Total	98,970	98,970	0	51,487	41,509	-9,978



3. Review of MRP Policy for Unsupported Debt

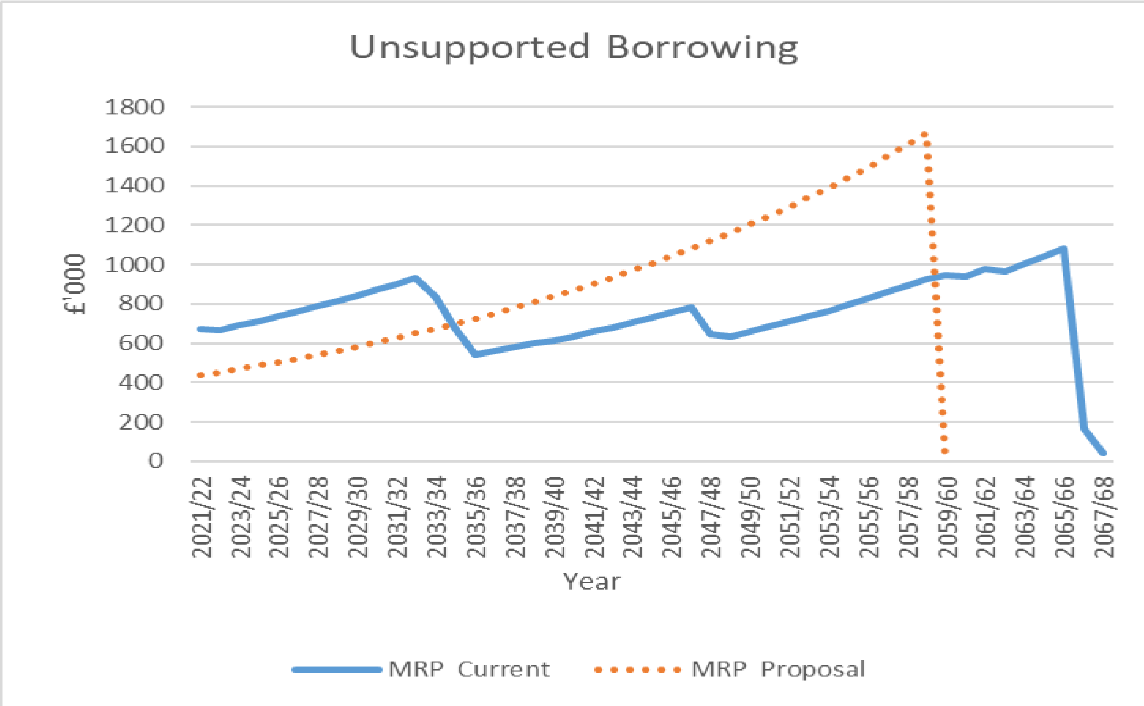
The Councils current Policy already states that the Asset Life Annuity Method is adopted for calculating MRP on unsupported borrowing. The MRP calculation is made on an individual asset basis.

An alternative method has been considered which uses an average asset life for all unsupported borrowing in a year, as opposed to having multiple charges based on an individual assets basis. If this approach is adopted in future years there is also an opportunity to rebase the MRP Policy in place for unsupported borrowing since 2008, which have an average asset life calculated as being 38 years. Taking into account the level of unsupported borrowing in each year the weighted average interest rate is 3.68% which is based on the PWLB annuity rate for each loan as of the 31st of March of the relevant year. 3.68% is thus deemed to be a prudent appropriate Annuity rate to be used in the revised MRP calculation. The table below compares the current MRP charge to the average asset life approach. The total MRP, on a cash basis, payable over the period is the same using either method. The MRP is lower using the average asset life approach until 2033/34. This approach also results in the MRP charge being discharged 9 years earlier. This together with the NPV calculation illustrates that the average asset life approach will not negatively impact on future generations.

The table below illustrates the MRP charge on the Current Method and the Proposed Method in cash terms and discounted for the effect of time. The range of the MRP, when discounted for the effect of time, is narrower using the Proposed Method being £466k to £437k (e) compared to £670k to £238k (2065/66) using the Current method (d) which supports the proposal as being fairer for all generations. The graph below illustrates the Current Method and on the Proposed Method on a cash basis.

Unsupported Borrowing

	In cash terms			Discounted for the effect of time		
	a	b	c=b-a	d	e	f=e-d
Year	MRP Current	MRP Proposal	Difference	MRP Current	MRP Proposal	Difference
	£'000	£'000	£'000	£'000	£'000	£'000
2021/22	670	437	-233	670	437	-233
2022/23	666	453	-213	644	438	-206
2023/24	689	470	-219	643	439	-204
2024/25	712	487	-225	642	439	-203
2025/26	736	505	-231	642	440	-202
2026/27	761	524	-238	641	441	-200
2027/28	787	543	-244	640	442	-199
2028/29	814	563	-251	640	442	-197
2029/30	842	584	-258	639	443	-196
2030/31	871	605	-266	639	444	-195
2031/32	900	627	-273	638	445	-194
2032/33	931	650	-281	638	446	-192
2033/34	832	674	-158	551	446	-105
2034/35	677	699	23	433	447	14
2035/36	541	725	184	334	448	114
2036/37	560	752	192	334	449	114
2037/38	580	779	199	335	449	115
2038/39	601	808	207	335	450	115
2039/40	611	838	226	329	451	122
2040/41	634	869	235	330	452	122
2041/42	656	901	244	330	453	123
2042/43	680	934	254	330	453	123
2043/44	705	968	263	331	454	124
2044/45	730	1,004	273	331	455	124
2045/46	757	1,041	284	331	456	124
2046/47	784	1,079	295	332	457	125
2047/48	647	1,119	471	265	457	193
2048/49	633	1,160	527	250	458	208
2049/50	657	1,202	545	251	459	208
2050/51	683	1,247	564	252	460	208
2051/52	709	1,293	583	253	461	208
2052/53	737	1,340	603	254	461	208
2053/54	766	1,389	624	255	462	207
2054/55	796	1,441	645	256	463	207
2055/56	827	1,494	667	257	464	207
2056/57	859	1,549	689	258	465	207
2057/58	893	1,606	713	259	465	207
2058/59	928	1,665	737	260	466	206
2059/60	944		-944	255		-255
2060/61	941		-941	246		-246
2061/62	976		-976	246		-246
2062/63	965		-965	236		-236
2063/64	1,003		-1,003	236		-236
2064/65	1,042		-1,042	237		-237
2065/66	1,083		-1,083	238		-238
2066/67	162		-162	35		-35
2067/68	40		-40	8		-8
Total	35,020	35,020	0	17,487	17,156	-331



4. External Consultation

The Council's professional Treasury Advisors are supportive of the recommendations in this report. Audit Wales are content with the recommendations.

5. Conclusion

The following changes are reflected in the proposed Revised MRP Policy Statement for 2021/22 which is attached as Appendix A, and will be considered by Council on 17 June 2021.

i. **Historic and Supported Debt** – adopt Option 3 (Asset life method) of the 2018 WG guidance and applying the Annuity Method with an interest rate of 4.20% (the average borrowing rate of loans outstanding as of 01/04/21) over a 44 year period commencing 01/04/2021.

ii. **New Supported Borrowing** – adopt Option 3 (Asset life method) of the 2018 WG guidance and apply the Annuity Method.

iii. **PFI credit arrangements** - adopt Option 3 (Asset life method) of the 2018 WG guidance and apply the Annuity Method.

iv. **Historic Unsupported Prudential Borrowing** – adopt Option 3 (Asset life method) of the 2018 WG guidance and apply the Annuity Method with an interest rate of 3.68% (the weighted average interest rate of the borrowing concerned) over a 38 year period commencing 01/04/2021.

v. **New Unsupported Prudential Borrowing –** adopt average estimated useful life of assets using Option 3 (Asset life method) of the 2018 WG guidance and apply the Annuity Method.

Recommendation(s):	**Governance and Audit Committee is requested to confirm if it is supportive of the proposed Revised MRP Policy for 2021/22.**	

Wellbeing of Future Generations:	**Has an Integrated Impact Assessment been completed? If, not, please state why Summary.**	Yes
	Long term:	The Policy ensures a prudent approach to financing the repayment of debts is adopted which covers the short and long term.
	Integration:	Indirectly by ensuring an appropriate budget is ring fenced for the cost of repaying debt
	Collaboration:	N/A
	Involvement:	N/A
	Prevention:	The Policy ensures a prudent approach to financing the repayment of debts is adopted which covers the short and long term.

Reasons for decision:	To revise the Minimum Revenue Policy for 2021/22
Overview and Scrutiny:	Report presented to Governance and Audit Committee
Policy Framework:	2021/22 Treasury Management Strategy
Strategic Objectives:	Ceredigion County Council is an organisation that is fit-for-purpose to deliver improving services to meet the needs of our citizens
Financial Implications:	A prudent charge for Debt Repayment for all generations is approved
Statutory Powers:	Local Government Act 2003
Background Papers:	Welsh Government Guidance on MRP – Revised 2018
Appendices:	Appendix A: 2021/22 Revised MRP Policy Statement

Corporate Lead Officer:	Stephen Johnson (Finance & Procurement)
Reporting Officer:	Justin Davies (Corporate Manager – Core Finance) Duncan Hall (Corporate Manager – Service Finance)
Date:	11/05/2021

Appendix A

Revised 2021/22 MRP Policy Statement

1. General Principles
   a) The Council's proposed Minimum Revenue Provision (MRP) Policy for 2021/22 follows the principles of the guidance issued by the Welsh Government under section 21(1A) of the Local Government Act 2003, through using one of the options outlined in the guidance, combined with introducing a further option that is underpinned by the principle of prudent provision.
   b) Estimated life periods will be determined in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom unless WG require or determine otherwise. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.
   c) As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

2. Methods for calculating MRP
   a) The major proportion of the MRP for 2021/22 will relate to the more historic debt liability that existed pre 2008 or post 2008 where it relates to Supported Borrowing funded by WG. The MRP liability on the Council's Capital Financing Requirement that relates to pre 2008 debt and post 2008 Supported Borrowing funded by WG through RSG will be provided for using Option 3 (Asset life method) of the 2018 WG guidance and applying the Annuity Method with an interest rate of 4.20% (the average borrowing rate of loans outstanding as of 01/04/21) over a 44 year period commencing 01/04/2021.
   b) As further new Supported Borrowing is utilised in the Capital Programme, the MRP liability on each new tranche of Support Borrowing will also be provided for using Option 3 (Asset life method) of the 2018 WG guidance and applying the Annuity Method.
   c) A significant proportion of the MRP for 2021/22 will relate to the Historic Unsupported Prudential Borrowing since 2008 which is reflected within the Capital Financing Requirement. The MRP liability on the Council's Capital Financing Requirement that relates to post 2008 Unsupported Borrowing will be provided for using Option 3 (Asset life method) of the 2018 WG guidance and applying the Annuity Method with an interest rate of 3.68% (the weighted average interest rate of the borrowing concerned) over a 39 year period commencing 01/04/2021.
   d) As further Unsupported Prudential Borrowing is utilised in the Capital Programme, the MRP liability reflected within the Capital Financing Requirement will be charged over a period commensurate with the average estimated useful life of assets using Option 3 (Asset life method) of the 2018 WG guidance and applying the Annuity Method.
   e) Where there is Temporary Borrowing in lieu of future Capital receipts (e.g. WG repayable finance loans or temporary Unsupported Prudential Borrowing) the principal of not charging MRP will continue, e.g. whilst awaiting the realisation of capital receipts from the sale of surplus assets.
   f) Where an asset is under construction, the Council reserves the right to not make an MRP charge until the financial year after that in which the capital expenditure is incurred and in the case of a new asset comes into service use.
   g) MRP on PFI credit arrangements will be charged over a period commensurate with the estimated useful life applicable to the asset and using the Annuity Method.

h) Where MRP relates to a pre-determined profile linked to a credit arrangement (e.g. Finance Lease) then the MRP calculation will be in accordance with the relevant bespoke repayment profile.

i) The Council has the option of making additional Voluntary MRP contributions in addition to the above MRP calculations at any point in time. E.g. The Council may treat any Voluntary MRP as ‘up-front’ provision (having a similar impact to the early repayment of debt) and thus recalculate future MRP charges accordingly.