Report to	**Cabinet**	**Item**
	03 February 2016	11
Report of	Chief finance officer	
Subject	Change of Minimum Revenue Provision Policy	

Purpose

To seek approval for a change in the council's policy with respect to Minimum Revenue Provision

Recommendation

To approve the change in Minimum Revenue Policy to asset life – annuity basis

Corporate and service priorities

The report helps to meet the corporate priority value for money services

Financial implications

Moving to the recommended policy would save the council £3.5m over the next five years. Savings continue to be made until 2035/36. After this year the costs increase until the capital financing requirement is fully paid down in 2064/65. The net present value over the fifty years under the recommended policy is £11.2m, whereas under the current method it is £13.9m

Ward/s: All Wards

Cabinet member: Councillor Stonard - Resources and income generation

Contact officers

Justine Hartley	01603 212440
Philippa Dransfield	01603 212562

Background documents

None

Report

Introduction

1. Local authorities are required to prepare an annual Minimum Revenue Provision (MRP) Statement which is approved as part of the Treasury Management Strategy Statement (TMSS). This section of the report sets out a proposed change to the policy for 2015-16, which under the council's financial regulations requires Cabinet approval and a report to full Council.

Background

2. The statute and regulations with regard to MRP are covered in The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 and the DCLG document, Capital Finance Guidance on Minimum Revenue Provision (February 2012).

3. Regulations 27 and 28 (as amended in 2008) require that a local authority "shall determine for the current financial year an amount of Minimum Revenue Provision which it considers to be prudent". MRP is a charge to the revenue account in relation to capital expenditure financed from borrowing or credit arrangements.

4. The council's MRP policy was created in 2007 at the start of the new MRP system, therefore it has now been in place for 8 years, and the council now faces a substantially different financial context. Significant challenges remain and the council needs to review the method and application of its policies to ensure these remain appropriate and reasonable. The council is seeking to ensure a stable and deliverable financial transition over the next few years, in the interest of prudent management of the council's finances generally (not just MRP).

5. The council's current MRP policy adopts the 'CFR Method' of 4% of capital financing requirement (CFR) at each year end.

6. There are three other suggested options. In DCLG Guidance issued February 2012; the asset life method for MRP is stated as the preferred option, although any prudent provision is permitted.

Analysis of options considered

7. The four options for MRP policy under Local Authorities (Capital Finance and Accounting) (England) Regulations 2008 are:

    a. The Regulatory method – MRP is equal to the amount determined in accordance with the former regulations 28 & 29 of the 2003 Regulations, as if they had not been revoked by the 2008 Regulations.
    b. The CFR Method' of 4% of capital financing requirement (CFR) at each year end. This is the method the council currently uses.

c. Asset Life Method – under this method the MRP is determined by reference to the life of the asset. This is either done on an equal instalment method or by annuity method (MRP is the principal element for the year of the annuity required to repay over the asset life the capital expenditure financed by borrowing or credit arrangements).
d. Depreciation Method – MRP is equal to the provision required in accordance with depreciation accounting in respect of the asset on which the capital expenditure financed by borrowing or credit arrangements.

8. The Regulatory method is only available for the CFR relating to pre-2008 assets.

9. The CFR Method is a reducing balance formula which has the characteristic that the debt is never entirely repaid, because each year repays 4% of the outstanding balance at that time. It would take over 200 years to repay to near zero under the current method. In addition, an amount of debt equal to Adjustment A ((the difference between the credit ceiling and the Capital Financing Requirement on 1st April 2004) is never repaid at all. In Norwich's case, Adjustment A amounts to £2.2m.

10. The asset life equal instalments method:

   a) saves the council £471,263 in 2015/16 & £429,515 in 2016/17.
   b) the savings reduce but continue until 2029/30, after this there is extra annual cost to the council.
   c) the net present value of the MRP under the equal instalments method over 50 years is £13,770,212; that for MRP under the current method over the same period is £13,862,164, a saving of only £91,952.

11. The asset life annuity method :

   a) In 2015/16 produces a saving of £801,336, in 2016/17 a saving of £751,967.
   b) The savings reduce but continue until 2035/36, after this there is extra annual cost to the council.
   c) The net present value of the MRP under the annuity method over fifty years is £11,161,731; that for MRP under the current method over the same period is £13,862,164, a saving of £2,700,433. It should be noted that the balance of the CFR after 50 years is zero under the annuity method but £3,389,071 under the current CFR method.

12. Under the depreciation method alignment with the depreciation must include any amount for impairment chargeable to the Comprehensive Income and Expenditure Statement. This method would produce similar results to the asset life equal instalments method but with added uncertainty around impairments, therefore this method was not considered.

13. The detailed annual savings and graphs for the asset life method of calculating MRP are contained in the Appendices to this report. Appendix 1 is a graphical representation of the effect of each asset life method on MRP each year into the

future, MRP will be lower in the early and higher in the later years. For both asset life methods there is a drop in 2048 due to one asset coming to the end of its life. Appendix 2 is a table of the actual values of MRP under the two asset life methods and the saving of each of these over the current CFR 4% method.

14. The Capital Financing Requirement (CFR) is a measure of capital expenditure financed by borrowing. It is written off by MRP charges. After 50 years, the Council's CFR and debt would be lower under either asset life method than under current arrangements because asset life methods repay the whole General Fund Loans CFR over 50 years rather than leaving a balance perpetually outstanding. Appendix 3 is a graphical representation of the CFR at the end of each financial year. Appendix 4 is a table of the actual values of CFR at the end of each financial year.

15. Appendix 5 is a graphical representation of the net present value of the MRP charges over a fifty year period.

16. Appendix 6 is the proposed new MRP policy

17. This analysis is based on the Council's current borrowing; any new prudential borrowing in the future would increase the CFR accordingly and result in additional MRP.

18. The methodology and calculations have been shared with the council's external auditors and, subject to checking the figures to the council's accounting records, they have agreed the calculations and consequent savings.

Recommendation

19. It is recommended that Cabinet approve the change of MRP policy to the asset life – annuity basis. This will deliver the following savings:

    a) In 2015/16 produces a saving of £801,336, in 2016/17 a saving of £751,967.
    b) The savings reduce but continue until 2035/36, after this there is extra annual cost to the council.
    c) The net present value of the MRP under the annuity method over fifty years is £11,161,731; that for MRP under the current method over the same period is £13,862,164, a saving of £2,700,433.

Integrated impact assessment

NORWICH City Council

The IIA should assess **the impact of the recommendation** being made by the report
Detailed guidance to help with completing the assessment can be found here. Delete this row after completion

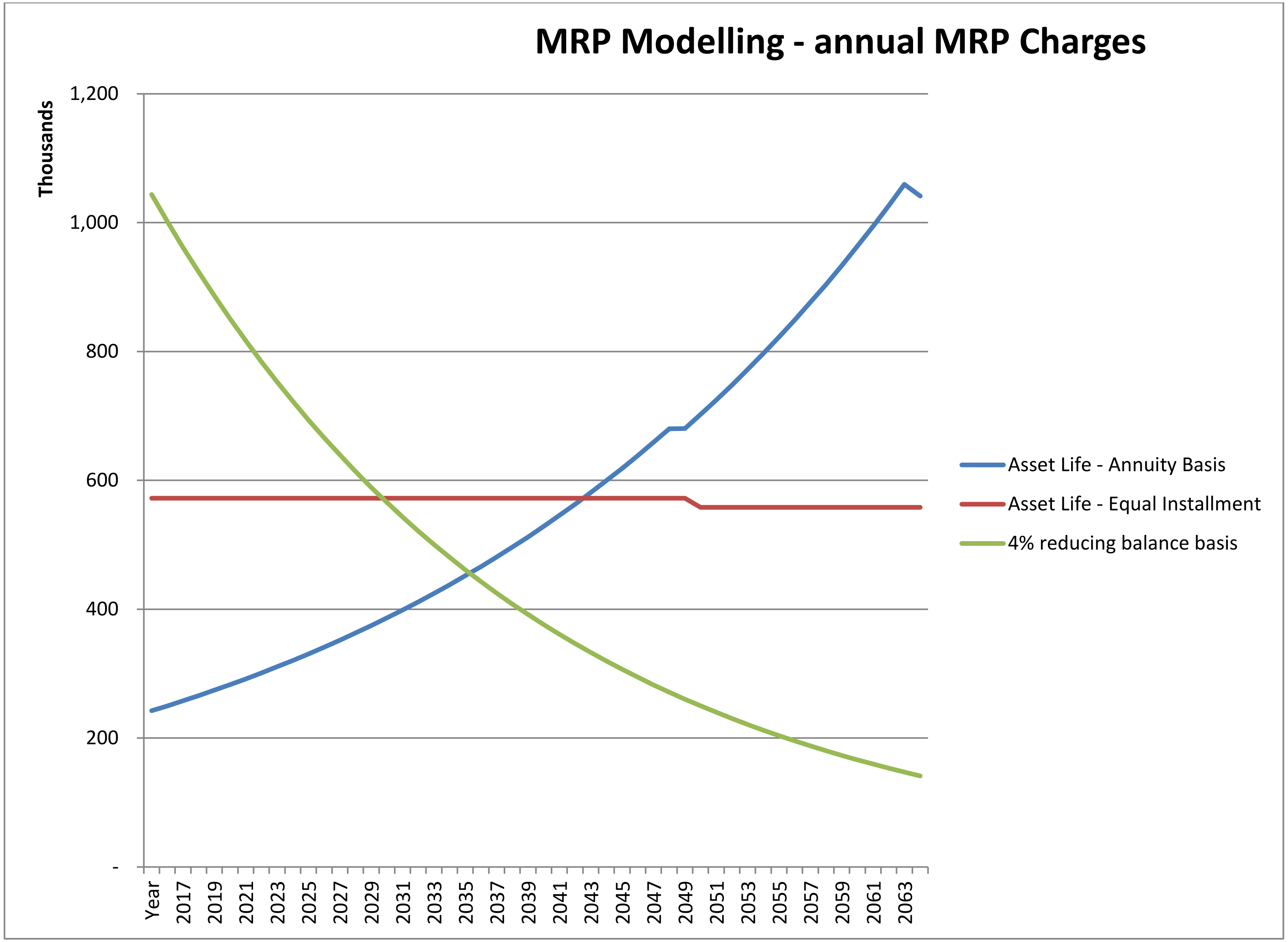
Report author to complete	
Committee:	Cabinet
Committee date:	03 February 2016
Head of service:	Justine Hartley
Report subject:	Change of minimum revenue provision policy
Date assessed:	20 January 2016
Description:	To consider options for the minimum revenue provision policy

	Impact			
Economic (please add an 'x' as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Finance (value for money)	☐	X	☐	Saves the council £3.5m over the next five years (including 2015/16)
Other departments and services e.g. office facilities, customer contact	☐	☐	☐	
ICT services	☐	☐	☐	
Economic development	☐	☐	☐	
Financial inclusion	☐	☐	☐	
Social (please add an 'x' as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Safeguarding children and adults	☐	☐	☐	
S17 crime and disorder act 1998	☐	☐	☐	
Human Rights Act 1998	☐	☐	☐	
Health and well being	☐	☐	☐	
Equality and diversity (please add an 'x' as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Relations between groups (cohesion)	☐	☐	☐	

	Impact			
Eliminating discrimination & harassment	☐	☐	☐	
Advancing equality of opportunity	☐	☐	☐	
Environmental (please add an ‘x’ as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Transportation	☐	☐	☐	
Natural and built environment	☐	☐	☐	
Waste minimisation & resource use	☐	☐	☐	
Pollution	☐	☐	☐	
Sustainable procurement	☐	☐	☐	
Energy and climate change	☐	☐	☐	
(Please add an ‘x’ as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Risk management	☐	☐	☐	

Recommendations from impact assessment
Positive
Negative
Neutral
Issues

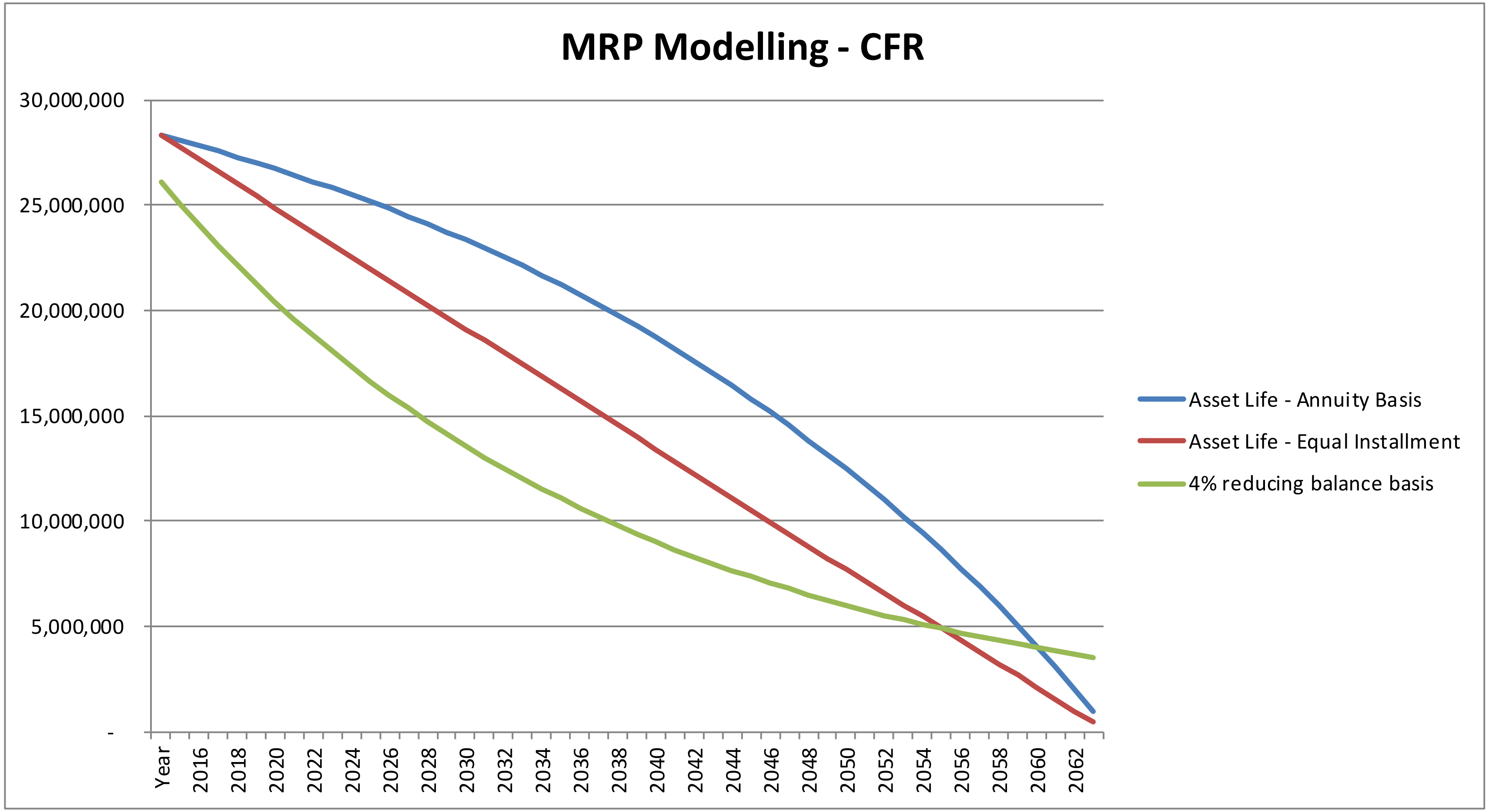
APPENDIX 1


MRP Modelling - annual MRP Charges
Thousands
1,200
1,000
800
600
400
200
-
Year
2017
2019
2021
2023
2025
2027
2029
2031
2033
2035
2037
2039
2041
2043
2045
2047
2049
2051
2053
2055
2057
2059
2061
2063
Asset Life - Annuity Basis
Asset Life - Equal Installment
4% reducing balance basis

APENDIX 2

Minimum Revenue Provision Charges					Saving	
Year	Asset Life - Annuity Basis	Asset Life - Equal Installment	4% reducing balance basis		Asset Life - Annuity Basis	Asset Life - Equal Installment
2016	242,372	572,445	1,043,708		(801,336)	(471,263)
2017	249,993	572,445	1,001,960		(751,967)	(429,515)
2018	257,859	572,445	961,881		(704,022)	(389,437)
2019	265,979	572,445	923,406		(657,427)	(350,961)
2020	274,359	572,445	886,470		(612,110)	(314,025)
2021	283,010	572,445	851,011		(568,001)	(278,566)
2022	291,939	572,445	816,971		(525,031)	(244,526)
2023	301,156	572,445	784,292		(483,135)	(211,847)
2024	310,671	572,445	752,920		(442,250)	(180,475)
2025	320,492	572,445	722,803		(402,312)	(150,359)
2026	330,630	572,445	693,891		(363,261)	(121,447)
2027	341,095	572,445	666,135		(325,041)	(93,691)
2028	351,898	572,445	639,490		(287,592)	(67,045)
2029	363,051	572,445	613,910		(250,860)	(41,466)
2030	374,563	572,445	589,354		(214,791)	(16,909)
2031	386,448	572,445	565,780		(179,331)	6,665
2032	398,718	572,445	543,149		(144,431)	29,296
2033	411,384	572,445	521,423		(110,038)	51,022
2034	424,461	572,445	500,566		(76,105)	71,879
2035	437,961	572,445	480,543		(42,582)	91,901
2036	451,899	572,445	461,321		(9,423)	111,123
2037	466,288	572,445	442,869		23,419	129,576
2038	481,143	572,445	425,154		55,990	147,291
2039	496,481	572,445	408,148		88,333	164,297
2040	512,316	572,445	391,822		120,494	180,623
2041	528,665	572,445	376,149		152,516	196,296
2042	545,545	572,445	361,103		184,442	211,342
2043	562,973	572,445	346,659		216,314	225,786
2044	580,967	572,445	332,793		248,175	239,652
2045	599,547	572,445	319,481		280,066	252,964
2046	618,730	572,445	306,702		312,028	265,743
2047	638,537	572,445	294,434		344,103	278,011
2048	658,988	572,445	282,656		376,332	289,788
2049	680,105	572,445	271,350		408,755	301,095
2050	680,418	572,445	260,496		419,922	311,949
2051	702,215	558,015	250,076		452,139	307,939
2052	724,721	558,015	240,073		484,648	317,942
2053	747,960	558,015	230,470		517,490	327,545
2054	771,956	558,015	221,251		550,704	336,763
2055	796,733	558,015	212,401		584,332	345,613
2056	822,318	558,015	203,905		618,413	354,110
2057	848,737	558,015	195,749		652,988	362,266
2058	876,017	558,015	187,919		688,098	370,096
2059	904,188	558,015	180,402		723,785	377,612
2060	933,277	558,015	173,186		760,091	384,829
2061	963,316	558,015	166,259		797,057	391,756
2062	994,335	558,015	159,608		834,727	398,406
2063	1,026,367	558,015	153,224		873,143	404,791
2064	1,059,446	558,015	147,095		912,351	410,920
2065	1,041,405	558,015	141,211		900,193	416,803

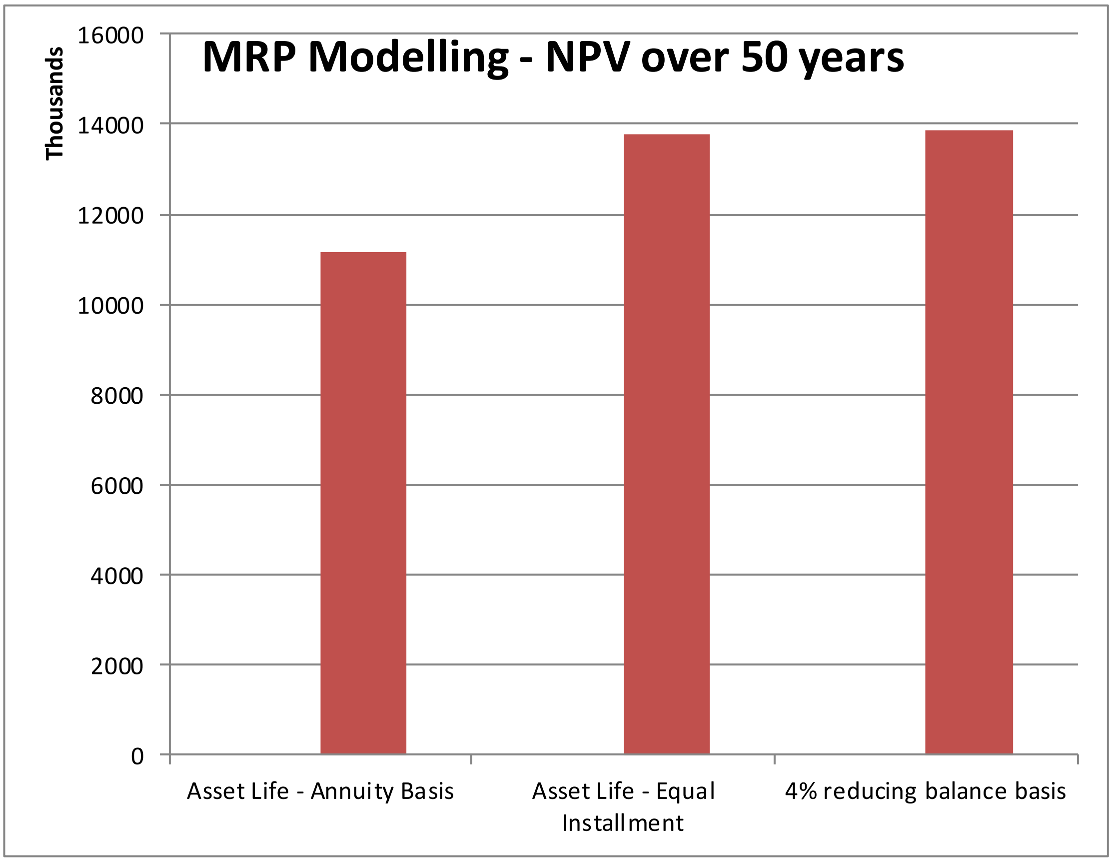
APPENDIX 3



MRP Modelling - CFR
30,000,000
25,000,000
20,000,000
15,000,000
10,000,000
5,000,000
-
Year
2016
2018
2020
2022
2024
2026
2028
2030
2032
2034
2036
2038
2040
2042
2044
2046
2048
2050
2052
2054
2056
2058
2060
2062
Asset Life - Annuity Basis
Asset Life - Equal Installment
4% reducing balance basis

APPENDIX 4

Balance of CFR Outstanding at year end			
Year	Asset Life - Annuity Basis	Asset Life - Equal Installment	4% reducing balance basis
	28,293,938	28,293,938	26,092,699
2016	28,051,567	27,721,494	25,048,991
2017	27,801,574	27,149,049	24,047,032
2018	27,543,714	26,576,605	23,085,150
2019	27,277,736	26,004,160	22,161,744
2020	27,003,376	25,431,715	21,275,275
2021	26,720,366	24,859,271	20,424,264
2022	26,428,427	24,286,826	19,607,293
2023	26,127,271	23,714,382	18,823,001
2024	25,816,600	23,141,937	18,070,081
2025	25,496,109	22,569,493	17,347,278
2026	25,165,479	21,997,048	16,653,387
2027	24,824,384	21,424,603	15,987,251
2028	24,472,486	20,852,159	15,347,761
2029	24,109,435	20,279,714	14,733,851
2030	23,734,872	19,707,270	14,144,497
2031	23,348,423	19,134,825	13,578,717
2032	22,949,706	18,562,381	13,035,568
2033	22,538,321	17,989,936	12,514,146
2034	22,113,860	17,417,491	12,013,580
2035	21,675,899	16,845,047	11,533,037
2036	21,224,000	16,272,602	11,071,715
2037	20,757,712	15,700,158	10,628,847
2038	20,276,569	15,127,713	10,203,693
2039	19,780,088	14,555,269	9,795,545
2040	19,267,772	13,982,824	9,403,723
2041	18,739,107	13,410,379	9,027,574
2042	18,193,562	12,837,935	8,666,471
2043	17,630,589	12,265,490	8,319,812
2044	17,049,621	11,693,046	7,987,020
2045	16,450,075	11,120,601	7,667,539
2046	15,831,345	10,548,157	7,360,838
2047	15,192,808	9,975,712	7,066,404
2048	14,533,820	9,403,267	6,783,748
2049	13,853,714	8,830,823	6,512,398
2050	13,173,296	8,258,378	6,251,902
2051	12,471,081	7,700,364	6,001,826
2052	11,746,360	7,142,349	5,761,753
2053	10,998,400	6,584,334	5,531,283
2054	10,226,445	6,026,319	5,310,032
2055	9,429,712	5,468,305	5,097,630
2056	8,607,394	4,910,290	4,893,725
2057	7,758,657	4,352,275	4,697,976
2058	6,882,639	3,794,260	4,510,057
2059	5,978,452	3,236,246	4,329,655
2060	5,045,175	2,678,231	4,156,469
2061	4,081,859	2,120,216	3,990,210
2062	3,087,524	1,562,201	3,830,601
2063	2,061,157	1,004,187	3,677,377
2064	1,001,711	446,172	3,530,282
2065	-	-	3,389,071


MRP Modelling - NPV over 50 years
Thousands
16000
14000
12000
10000
8000
6000
4000
2000
0
Asset Life - Annuity Basis
Asset Life - Equal Installment
4% reducing balance basis

Minimum Revenue Provision Policy

Introduction

1. The Government's Capital Finance and Accounting Regulations require local authorities to make 'prudent annual provision' in relation to capital expenditure financed from borrowing or credit arrangements. This is known as Minimum Revenue Provision or MRP. The Government has also issued statutory Guidance on MRP, to which the Council is required to have regard.

2. This policy applies to the financial years 2015/16 and going forward. Any interpretation of the Statutory Guidance or this policy will be determined by the Chief Finance Officer.

Principles of debt repayment provision

3. The term 'prudent annual provision' is not defined by the Regulations. However, the statutory Guidance says:
   "the broad aim of 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 Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant".

   The Guidance does not prescribe the annual repayment profile to achieve this aim, but suggests four methods for making MRP which it considers prudent, and notes that other methods are not ruled out. The City Council regards the broad aim of MRP as set out above as the primary indicator of prudent provision, whilst recognising the flexibilities which exist in determining an appropriate annual repayment profile.

4. The City Council considers that 'prudent' in this context does not mean the quickest possible repayment period, but has regard to the prudent financial planning of the authority overall, the flow of benefits from the capital expenditure, and other relevant factors.

5. As expected by the Statutory Guidance, the City Council will not review the individual asset lives used for MRP as a result of any changes in the expected life of the asset or its actual write off. Some assets will last longer than their initially estimated life, and others will not; the important thing is the reasonableness of the estimate.

6. **General Fund MRP policy: prudential borrowing** The general repayment policy for prudential borrowing is to repay borrowing within the expected life of the asset being financed, up to a maximum of 50 years. This is in accordance with the "Asset Life" method in the Guidance. The repayment profile will follow an annuity repayment method, which is one of the options set out in the Guidance. This means that MRP will be calculated on an annuity basis (like many domestic mortgages) over the estimated life of the asset.

   This is subject to the following details:
   a. An average asset life for each project will normally be used. There will not be separate MRP schedules for the components of a building (e.g. plant, roof etc). Asset life will be determined by the Chief Finance Officer. A standard schedule of asset lives will generally be used, but where borrowing on a project exceeds £10m, advice from appropriate advisers may also be taken into account.
   b. MRP will commence in the year following the year in which capital expenditure financed from borrowing is incurred, except for single assets where over £1m financed from borrowing is planned, where MRP will be deferred until the year after the asset becomes operational.

c. Other methods to provide for debt repayment may occasionally be used in individual cases where this is consistent with the statutory duty to be prudent, as justified by the circumstances of the case, at the discretion of the Chief Finance Officer.