TO:	Policy Council
FROM:	Director of Finance and IT
DATE:	3rd December 2015

TITLE OF BRIEFING PAPER: Medium Term Financial Strategy and Minimum Revenue Provision Policy Review 2015-16

1.0 PURPOSE

1.1 To provide an update on the emerging Medium Term Financial Strategy and outline a proposed change to the Council's MRP (Minimum Revenue Provision) Policy.

2.0 RECOMMENDATIONS

2.1 That the update on the emerging MTFS is noted.

2.2 The Council is recommended to approve the proposed change to the Council's Minimum Revenue Provision (MRP) Policy for 2015-16, so that existing capital expenditure financed from;

a) debt up to 2007/08 and

b) from Government-supported borrowing arising in 2007/08 and thereafter,

is paid over 50 years on a straight-line basis i.e. in equal repayments over the period.

3.0 BACKGROUND

3.1 Council Forum in September 2014 received details of the Medium Term Financial Strategy and the predicted budget position for 2015-2018. Council agreed a range of advance budget savings proposals for early implementation to assist in setting a balanced budget for 2015/16 at Finance Council in March 2015 and in making further savings in the following two years.

3.2 Since then the Chancellor has continued to indicate that there will be further spending cuts in the public services until 2020 as he aims to generate a budget surplus by that date.

3.3 In finalising the budget for 2015/16, and in reviewing forecasts of future central government funding and cost pressures in particular, the MTFS reported to Finance Council in March 2015 indicated (after taking into account the advance savings proposals already reported), residual shortfalls of £12.706m in 2016/17 and a further £13.155m in 2017/18.

MTFS Summary	2015/16	2016/17	2017/18
	£000s	£000s	£000s
Forecast shortfall	**(19,093)**	**(35,352)**	**(39,387)**
Advance savings proposals agreed at Council Forum September 2014	15,988	22,646	26,232
Further proposals to set a balanced budget for 2015/16, including use of reserves	3,105	-	-
Remaining forecast budget gap	**-**	**12,706**	**13,155**

3.4 Following the Emergency Budget announcements made in the summer after the General Election, and consistent with the budget monitoring reports to Executive Board this year, there are a number of areas that are likely to now increase the budget shortfall further. These include:

- further anticipated reductions in central government funding, i.e. above those already forecast in specific grants such as Public Health Grant which has already been subject to a late in-year cut of £1M in 2015/16
- continuing pressures across demand-led services and Adult Social Care in particular and
- continuing Welfare, Education and NHS reforms

3.5 In March 2015 Finance Council approved the MRP Policy for 2015-16.

3.6 Over the past few months the MRP charge to the Income and Expenditure Account has been reviewed as part of the wider review of the key components of the Medium Term Financial Strategy. The findings of the review are that a change to the policy would provide a simplification of the calculation, a smoothing of the cost by using a straight-line rather than a reducing-balance basis whilst maintaining a prudent payment profile which is in fact of shorter duration.

4.0 RATIONALE AND KEY ISSUES

4.1 Minimum Revenue Provision (MRP) Policy for 2015-16

4.1.1 The Council's current MRP Policy states that;

(a) for existing capital expenditure financed from debt <u>up to 2007/08</u> (i.e. prior to the changes made to local government borrowing in moving from Supported Borrowing to the Prudential Borrowing regime) ***and*** *for all new <u>Government-supported</u> borrowing arising in 2007/08 and thereafter, we will use the* ***Regulatory Method*** *to determine MRP and,*

*(b) for capital expenditure financed from debt arising in 2007/08 and thereafter that is <u>self-financed</u> (i.e. not supported by the Government), we will use the **Asset Life Method** to determine MRP.*

This means in practice that;

(a) 4% of the total outstanding balance of

1. the pre 2007/08 debt and
2. the Government-supported debt taken since then,

is charged to the Income and Expenditure account each year. The 4% reducing-balance basis is reflective of the historical basis on which local authorities were expected to finance debt as this was factored into the Revenue Support Grant received from Government for borrowing approvals.

(b) for the self-financed debt incurred in 2007/08 and beyond, the MRP is charged evenly over the lives of the assets acquired under Prudential Borrowing.

*(The guidance provided by DCLG on these approaches/options is detailed at **Appendix A** for information).*

4.1.2 The Council has not had any Government-supported debt allocations since 2010-11, as the Government has chosen to cease supporting capital programmes in this way. Subsequent reductions in local government funding have also seen significant reductions in central government support through Revenue Support Grant. This has severed the link between the Regulatory Method of calculating MRP (above) and the associated funding provided through the local government funding settlement. It is therefore reasonable to take a more evenly balanced and prudent approach to standing the cost of both the pre 2007/08 and Government-supported debt as opposed to the approach in the existing MRP policy which front-loads the cost into earlier years and results in the MRP being charged indefinitely, though ultimately in very small amounts.

4.1.3 It is proposed to amend the MRP policy, with immediate effect from 2015-16, ***for all existing capital expenditure financed from debt up to 2007/08 and all new Government-supported borrowing arising in 2007/08 and thereafter***, to spread the cost evenly over 50 years (i.e. at 2% per annum). This shortens the timeframe for ultimate repayment and, as a consequence of re-profiling the payments themselves, results in significant reductions in cost in earlier years i.e. reductions of £1.73 million in 2015/16, £1.59 million in 2016/17 and £1.46 million 2017/18. Costs would start to increase slightly from 2032/33, and more materially a few years later, with the highest increase compared to the current MRP Policy being around £0.75 million from the 2050's.

Though there would be higher costs in later years, the overall profile remains prudent and shorter in duration.

4.1.4 This proposal, though not directly aligned to any of the four specific options outlined in the DCLG Guidance issued when MRP was introduced (see Appendix A), is clearly in line with the overriding principle that all councils should make prudent provision to redeem debt liability over a period which is reasonably commensurate with that over which the capital expenditure is estimated to provide benefits. A number of other local authorities have made equivalent changes to their MRP Policy both last year and this year.

We have also referred the matter to our treasury advisers, Arlingclose, who are comfortable with our proposals, and have informed our auditors of the report and our recommendations to Policy Council.

4.2 Medium Term Financial Strategy

4.2.1 As we await the Autumn Statement on 25 November (date of publication of this report) and thereafter the local government finance settlement (date and likely period of settlement as yet unknown), we have been continually revising our MTFS forecasts. This will require a further comprehensive review of the allocation of resources across the Council. This includes detailed reviews of all expenditure and income budgets, contractual commitments, property holdings and staffing structures. This will be set in the context of the Council's statutory responsibilities, risks and corporate priorities.

4.2.2 This will include:

- A bottom up approach to reviewing budgets for both statutory services and those which are the Council's priorities.
- A comprehensive review of the Adult Social Care budget, Better Care Fund arrangements with the NHS, the impact of closer integration with the health sector and the ongoing work of the department in association with of the Councils' appointed efficiency partner
- Working towards a net nil cost/neutral position for commercial and/or income generating services
- The implementation of channel shift and digital automation encouraging people to self-serve on-line whilst providing support for those who cannot access the internet
- A review of the Council's long term loans portfolio and an assessment of the requirement for investment in the infrastructure of the borough over the long term.
- Review of inflation assumptions in the MTFS
- Review of the Council's MRP (Minimum Revenue Provision) policy
- Review of Council Tax discounts
- Consideration of increased Council Tax
- Impact of the growth agenda linked to the plan for prosperity and delivery of the local plan

4.2.3 A further update of the MTFS will be provided to Council Forum in January or Finance Council in March 2016 pending receipt of the funding settlement, anticipated in December.

5.0 POLICY IMPLICATIONS

5.1 The report includes proposed changes to the Council's Minimum Revenue Provision Policy i.e. from the current policy outlined in 4.1.1 to the proposed changes in 4.1.3.

6.0 FINANCIAL IMPLICATIONS

6.1 The financial implications arising from the proposed change in MRP Policy will be reflected in the Medium Term Financial Strategy and in Revenue Budget projections for 2016-17 and will be incorporated into Corporate Budget Monitoring Reports.

6.2 The table below provides the current Medium Term Financial forecast, excluding the savings which would arise from the proposed change in MRP policy.

Medium Term Financial Strategy - March 2015 (Assumes 40% reduction in Revenue Support Grant over 4 years)	**2015/16**	**2016/17**	**2017/18**	**2018/19**	**2019/20**
	£ 000's	£ 000's	£ 000's	£ 000's	£ 000's
Resources					
Government Resources	70,067	62,759	59,794	56,525	55,189
Council Tax (base position)	41,873	41,953	41,953	41,953	41,953
Parish precepts	153	153	153	153	153
Local Share of Business Rates	22,773	23,228	23,693	24,167	24,650
Deficit (-ve) or surplus on collection fund	325	0	0	0	0
Total resources	135,191	128,093	125,593	122,798	121,945
Net expenditure					
Portfolio cash limits - 2015/16 baseline *(*Note 1)*	111,283	115,410	115,516	115,516	115,516
Contingencies (committed)	3,365	3,725	2,751	2,751	2,751
Contingencies for inflation	116	4,795	7,324	9,912	12,560
Adult Social Care pressures	4,000	4,000	4,000	4,000	4,000
Interest and borrowing	23,230	24,930	25,701	25,701	25,701
Parish Precepts / Grants	180	180	180	180	180
Earmarked reserves	-2,983	-181	-25	0	0
Total Net expenditure	139,191	152,859	155,447	158,060	160,708
Shortfall *(**Note 2)*	**4,000**	**24,766**	**29,854**	**35,262**	**38,763**

*** Note 1:** *The Advance savings programme (agreed September 2014) will be subject to further review and as such the portfolio cash limits are stated using the 2015/16 baseline i.e. excluding those elements of the savings programme yet to be delivered*

*****Note 2:*** *the 15/16 budget may have to be balanced by a combination of reduced spending in other areas, application of the revised MRP policy (if approved) and use of appropriate earmarked and unallocated reserves*

6.3 The advance savings options agreed at Council Forum in September 2014 need to be reviewed in order to confirm their deliverability. These will assist in closing the budget shortfall noted above, but even taking these into consideration the forecast gap that the Council faces would still be over £28.5m per year by 2019/20 if no further action is taken beyond delivering those advance savings.

7.0 LEGAL IMPLICATIONS

7.1 Under the Local Government Act 2003, local authorities determine locally their levels of capital investment and associated borrowing. The Prudential Code has been developed to support local authorities in taking these decisions, and the Council is required by Regulation to have regard to the Code when carrying out its duties under Part 1 of the Local Government Act 2003.

8.0 RESOURCE IMPLICATIONS

8.1 None.

9.0 EQUALITY IMPLICATIONS

9.1 None.

10.0 CONSULTATIONS

9.1 None.

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Date: 17th November 2015

Background papers: Treasury Management Strategy and MRP Policy Report for 2015-16 approved at Council 2nd March 2015.

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: -

1. 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.
2. 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.

Option 1: Regulatory Method

Under the previous MRP regulations, MRP was set at a uniform rate of 4% of an adjusted Capital Financing Requirement (CFR) on a reducing balance method (which in effect meant that MRP charges would stretch into infinity). This historic approach may be used for all capital expenditure incurred in years before the start of this new approach. It may also be used for new capital expenditure up to the amount which is deemed to be supported through the Supported Capital Expenditure annual allocation.

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 the debt arising from most new capital expenditure, including where desired, that which may alternatively continue to be treated under options 1 or 2.

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:

a. equal instalment method – equal annual instalments
b. annuity method – annual payments gradually increase during the life of the asset

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.