

REPORT TO EXECUTIVE

Date of Meeting: 8 February 2022

REPORT TO COUNCIL

Date of Meeting: 22 February 2022

Report of: Director Finance

Title: The Prudential Code for Capital Finance in Local Authorities (Incorporating the Annual Statement of Minimum Revenue Provision)

Is this a Key Decision?

No

Is this an Executive or Council Function?

Council

1. What is the report about?

To set out the proposed 2022/23 prudential indicators for capital finance for adoption by the Council and set the annual statement of Minimum Revenue Provision (MRP).

2. Recommendations:

It is recommended that the Executive recommends to Council to approve the adoption of:

- (1) The Prudential Indicators set out in Appendix A-C; and
- (2) The Annual Statement of Minimum Revenue Provision for the Council

3. Reasons for the recommendation:

With effect from 1 April 2004, the Government abolished the capital finance legislation in Part 4 of the Local Government and Housing Act 1989 and the Local Authorities (Capital Finance) Regulations 1997 (Statutory Instrument 1997/319) and replaced it with a new Prudential system based on self-regulation. This means that Councils are free to borrow for capital investment where the borrowing is affordable.

The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 came into force on 31 March 2008. The Regulations require Full Council to approve an Annual Statement of Minimum Revenue Provision which is the amount set aside from revenue for the repayment of debt principal relating to the General Fund only. The Housing Revenue Account remains exempt from making Minimum Revenue Provision although it can make voluntary set asides if it wishes.

The Prudential Indicators / MRP report will be incorporated within the Budget Book for approval at the full Council meeting as per the statutory requirement.

4. What are the resource implications including non financial resources.

The financial resources required are set out in the body of this report.

5. Section 151 Officer comments:

The Prudential Code, whilst complex, allows members to ensure that capital expenditure and in particular, the impact it has on the revenue budget is both affordable and prudent. The key indicators are set out below and members should ensure that they are comfortable with the limits set and the levels of borrowing allowed.

The MRP policy enables the Council to prudently manage the repayment of debt. The Council's policy of using the annuity method allows it to repay debt in line with the loan repayments required, where borrowing is taken out with the PWLB. This allows repayments to align with the increasing economic benefit that assets are expected to deliver over their useful lives. Members should note that the MTFP relies on the Council taking advantage of the opportunity to use the overpayments made in previous years to help smooth the reductions required in the revenue budget. This is considered prudent by the section 151 Officer.

6. What are the legal aspects?

With effect from 1 April 2004, the Government abolished the capital finance legislation in Part 4 of the Local Government and Housing Act 1989 and the Local Authorities (Capital Finance) Regulations 1997 (Statutory Instrument 1997/319) and replaced it with a new Prudential system based on self-regulation. More detailed information is set out in paragraph 3 above.

7. Monitoring Officer's comments:

The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 came into force on 31 March 2008. The Regulations require Full Council to approve an Annual Statement of Minimum Revenue Provision which is the amount set aside from revenue for the repayment of debt principal relating to the General Fund only. This report details this provision, and therefore raises no issues for the Monitoring Officer.

8. Report details:

The Prudential Code requires authorities to look at capital expenditure and investment plans in the light of overall organisational strategy and resources and ensure that decisions are being made with sufficient regard to the long run financing implications and potential risks to the authority. Effective financial planning, option appraisal, risk management and governance processes are essential in achieving a prudential approach to capital expenditure, investment and debt.

8.1 Key issues to consider

Appendix C summarises the prudential code indicators for the Council and of particular importance are:

- The Capital Financing Requirement - demonstrates the amount that the Council has an underlying need to borrow, regardless of whether that amount has actually been borrowed.

- The Operational Boundary - this sets the amount of borrowing that the Council intends to keep within over the period covered by the indicators.
- The Authorised Limit - the maximum that the Section 151 officer is allowed to borrow to cover the Operational Boundary and day to day cashflow needs. The Council is not allowed to exceed this amount of borrowing without first authorising an increase to the limit.

8.2 Lifting of the HRA Borrowing Cap

Since April 2012 each local authority had a limit on the amount of borrowing it could have for the purposes of the HRA, called the 'debt cap'. For Exeter City Council, the debt cap was £57,882,413.

The HRA debt cap was formally removed on 29 October 2018, as a result local authorities are now able to borrow for housebuilding in accordance with the Prudential Code.

The HRA have borrowed an additional £15.3m for the development of new sites since the debt cap was lifted. Further sites are being identified for the development of new council housing in order to make use of this new flexibility and to contribute to local housing delivery and further investigations by officers for further new sites are ongoing.

8.3 Capital Financing Requirement

Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2022/23 and the following two financial years. This allows some flexibility for limited early borrowing for future years but ensures that borrowing is not undertaken for revenue or speculative purposes.

The Director Finance reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

8.4 ANNUAL STATEMENT OF MINIMUM REVENUE PROVISION

The Regulations require that "a local authority shall determine for the current financial year an amount of minimum revenue provision which it considers to be prudent".

Minimum Revenue Provision (MRP) is an amount set aside from revenue to meet the repayment of debt principal. It is in effect a replacement for depreciation that you would normally expect to see within a Company's Accounts. Under the old Regulations this was 4% of principal outstanding for the General Fund and no requirement to set aside MRP in the Housing Revenue Account. In local government accounting depreciation is charged and then reversed out so it does not affect the level of Council Tax, however MRP is charged to the General Fund and therefore does affect levels of Council Tax.

The Secretary of State for Communities and Local Government has issued guidance under section 21(1A) of the Local Government Act 2003. This states that "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 the grant."

The guidance notes detail five options which the Secretary of State considers prudent. These are described in section 8.6 below:

- (a) Regulatory Method;
- (b) Capital Financing Requirement Method;
- (c) Asset Life (Equal Instalment) Method;
- (d) Asset Life (Annuity) Method; and
- (e) Depreciation Method

8.5 Key issue to consider

Section 8.7 sets out the proposed policy for MRP, which matches the amount set aside against the useful life of the assets. The only exception to this is the writing off of historic debt which is being undertaken over 50 years.

8.6 MRP OPTIONS

Regulatory Method

MRP is equal to the amount determined in accordance with the former regulations 28 and 29 of the 2003 Regulations as if they had not been revoked. In effect this is 4% of the debt principal outstanding.

Capital Financing Requirement Method

MRP is equal to 4% of the non-housing Capital Financing Requirement, which is a Prudential Indicator.

Asset Life (Equal Instalment) Method

Where capital expenditure on an asset is financed wholly or partly by borrowing then MRP is determined by reference to the life of the asset and an equal amount charged in each year.

Asset Life (Annuity) Method

MRP is the principal element for the year of the annuity required to repay over the asset life the amount of capital expenditure financed by borrowing.

Depreciation Method

MRP is equal to the provision required in accordance with depreciation accounting in respect of the asset, including any amount of impairment chargeable to the Income and Expenditure Account. As standard depreciation rules are used where an asset is part financed by loan, e.g. 50% loan, 50% Capital Receipt, then the full 100% depreciation charge on the asset is required to be charged as MRP. MRP is required to be charged

annually until the cumulative amount of the provision is equal to the original expenditure financed by borrowing. Should the asset be disposed of then the charge needs to continue as if the asset had not been disposed of unless the debt is repaid.

8.7 MINIMUM REVENUE PROVISION POLICY 2022/23

The Council's MRP policy is to match borrowing against specific capital investment and adopt either the Asset Life (Equal Instalment) or the Asset Life (Annuity) method for MRP. In this way the funding for the asset will be paid off over the useful life of that asset. This will ensure that loans are repaid over the asset life thus freeing financial resources for investment in other schemes or in asset renewal. They are also simple to operate and gives certainty in each year as to the level of charge for principal.

The other advantage is that it makes business cases and scheme appraisals easier to compile. As a general rule the Council will seek to borrow over the same period of the asset life up to a maximum of 50 years in line with the Regulations. The total capital financing requirement at the end of 2021/22 is likely to be approximately £244.972 million. The MRP for 2022/23 will be calculated based on the capital financing requirement at the end of 2021/22 using the varying periods of repayment. The MRP charge for 2022/23 will be approximately £1.783 million. For the avoidance of doubt, it is proposed to use both options from 2016/17 onwards, depending on the asset being financed. However, unless there is a good reason, for not doing so, all borrowing will adopt the Asset Life (Annuity) method.

8.8 MRP Overpayments

A change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory minimum revenue provision (MRP), voluntary revenue provision or overpayments, can, if needed, be reclaimed in future years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. Up until the 31 March 2022 the total VRP overpayments will be £3.836 million.

8.9 Capital Financing Requirement

Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2022/23 and the following two financial years. This allows some flexibility for limited early borrowing for future years but ensures that borrowing is not undertaken for revenue or speculative purposes.

The Director Finance reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

9. How does the decision contribute to the Council's Corporate Plan?

The Capital Programme contributes to all of the key purposes, as set out in the Corporate Plan.

10. What risks are there and how can they be reduced?

Areas of budgetary risk are highlighted to committee as part of the quarterly budget monitoring updates.

11. Equality Act 2010 (The Act)

- 11.1 Under the Act's Public Sector Equalities Duty, decision makers are required to consider the need to:
- eliminate discrimination, harassment, victimisation and any other prohibited conduct;
 - advance equality by encouraging participation, removing disadvantage, taking account of disabilities and meeting people's needs; and
 - foster good relations between people by tackling prejudice and promoting understanding.
- 11.2 In order to comply with the general duty authorities must assess the impact on equality of decisions, policies and practices. These duties do not prevent the authority from reducing services where necessary, but they offer a way of developing proposals that consider the impacts on all members of the community.
- 11.3 In making decisions the authority must take into account the potential impact of that decision in relation to age, disability, race/ethnicity (includes Gypsies and Travellers), sex and gender, gender identity, religion and belief, sexual orientation, pregnant women and new and breastfeeding mothers, marriage and civil partnership status in coming to a decision.
- 11.4 In recommending this proposal no potential impact has been identified on people with protected characteristics as determined by the Act because the report is for information only

12. Carbon Footprint (Environmental) Implications:

- 12.1 No direct carbon/environmental impacts arising from the recommendations.

13. Are there any other options?

No

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Local Government (Access to Information) Act 1972 (as amended)

Background papers used in compiling this report:-

None

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