Report to the Cabinet
Meeting to be held on Thursday, 12 July 2018

Report of the Chief Executive and Director of Resources

Part I

Electoral Division affected: (All Divisions);

Changes to the County Council's Minimum Revenue Provision Policies

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Executive Summary

The Local Authorities (Capital Finance and Accounting) Regulations 2003 require local authorities to charge to their revenue account in each financial year a minimum amount to finance capital expenditure. This is commonly referred to as Minimum Revenue Provision.

In the context of significant medium term financial pressures the council continues to review the efficiency and effectiveness of all aspects of spend. As part of this review, and with advice from the Local Government Association, the council has reassessed the expenditure that is required under statute relating to a prudent Minimum Revenue Provision.

This report proposes changes to the county council's Minimum Revenue Provision policy statements for the years 2017/18 and 2018/19 including a change to the method used to calculate Minimum Revenue Provision.

Based on the proposed policy, the county council has created an historic over provision of Minimum Revenue Provision of c£134m and as a consequence of this will reduce its future annual provision until the over provision has been recovered or it is deemed appropriate to set additional monies aside. It is estimated that this could result in a reduced charge for 14 years from 2017/18.

The immediate financial effect of these changes is a saving of £13.2m in 2017/18 and £9.4m in 2018/19. The council will continue to review its provisioning policy annually in the years thereafter to identify whether there is a need to make a provision, or whether there are further opportunities to save whilst ensuring statutory obligations are met.

Lancashire County Council

Recommendation

Cabinet recommends to Full Council revised Minimum Revenue Provision policy statements for both 2017/18 and 2018/19, utilising the annuity method to calculate the Minimum Revenue Provision of both supported and self-financed capital expenditure.

Background and Advice

The Local Authorities (Capital Finance and Accounting) Regulations 2003 ("the regulations") require local authorities to charge to their revenue account in each financial year a minimum amount to finance the cost of capital expenditure. This is commonly referred to as Minimum Revenue Provision. The Minimum Revenue Provision and the amount set aside each year must be "prudent".

In establishing the annual Minimum Revenue Provision, there is no specific approach prescribed for determining a prudent charge and local authorities are required to have regard to guidance issued by the Secretary of State. This guidance categorises the council's capital expenditure as either 'supported' or 'self-financed'. The 'supported' element relates to that for which historically central government provided funding through the Revenue Support Grant. Self-financed is where no grant support is received.

The four approaches to calculating the annual provision, set out in the Ministry of Housing, Communities & Local Government guidance, are identified as:

- Regulatory
- Reducing balance
- Asset Life
- Depreciation

Existing policy

The Minimum Revenue Provision charge for self-financed capital expenditure has been calculated based on the life of the assets. This was one of the methodologies outlined in the Ministry of Housing, Communities & Local Government guidance and initially this was applied on a straight line method to most schemes. However, in 2015/16 this was changed to an annuity method which is the cheapest Minimum Revenue Provision option in the early years but once interest costs are taken into account maintains a constant impact on the revenue account over the useful life of the asset being financed.

For supported capital expenditure the Minimum Revenue Provision charge was initially set in legislation at a rate of 4% and it was the amount assumed in the calculations used for distributing the Revenue Support Grant between authorities. With the changes in local government financing it was decided by Full Council in 2015/16 that it would be more appropriate to consider the length of time it is anticipated the assets have an economic benefit. Consistent with the county council's depreciation policy it was deemed appropriate for the Minimum Revenue Provision charge relating to the supported capital expenditure to be distributed over 50 years on a straight line basis under the asset life method.

Proposed changes

Under the regulations, the overriding principle is that the council must make a prudent Minimum Revenue Provision. However, the council is also obligated to make decisions that present good value for money and must approve a balanced budget each year.

In the context of significant medium term financial pressures the council continues to review the efficiency and effectiveness of all aspects of spend. As part of this review the council has reassessed the expenditure that is required under statute relating to Minimum Revenue Provision to identify the level of provision that would satisfy the requirement for a prudent provision to be made.

The council has also requested the Local Government Association to act as "critical friend" and provide assurance that the council has taken all reasonable steps as it continues to develop a long term sustainable strategic solution to its financial challenges. As part of this work, the charge made for Minimum Revenue Provision was identified as an area for further consideration. In particular, whether the flexibilities in relation to Minimum Revenue Provision overprovision were being fully utilised within the prevailing regulation and guidance.

For the financial year commencing 1st April 2018, new regulations introduce restrictions to Minimum Revenue Provision such that a "*change in method can never give rise to an overpayment in respect of previous years, and should not result in a local authority making a reduced charge or a charge of £nil for the accounting period in which the change is made, or in any subsequent period, on the grounds that it needs to recover overpayments of Minimum Revenue Provision relating to previous years*."

The calculation methodologies set out in the Ministry of Housing, Communities & Local Government guidance have been explored and it has been identified that if the council adopted the annuity method for both supported and self-financed capital expenditure from 2007/08 an overpayment of Minimum Revenue Provision would accrue. Based on the proposed policy change to be applied in 2017/18 the estimated amount overprovided up to 2016/17 is c£129m on the supported capital expenditure and c£5m relating to self-financed capital expenditure, totalling c£134m overall.

It is not permissible to have a negative Minimum Revenue Provision, as such, the total c£134m cannot simply be reduced from the 2017/18 Minimum Revenue Provision value, and would need to be reduced from future Minimum Revenue Provision budgets. It is estimated that this could result in a reduced charge for 14 years from 2017/18, until the overpayment has been recovered.

Proposed policy costs

For illustrative purposes, a comparison of the Minimum Revenue Provision charge before and after the proposed change is shown in the following table for the next 6 years. The main change is in supported capital expenditure due to the application retrospectively of the annuity method policy, commencing 2007/08.

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	£m	£m	£m	£m	£m	£m
Self-financed						
Current basis	4.352	3.890	4.015	4.144	4.277	4.414
Proposed	0	3.402	4.241	4.376	4.515	4.659
Difference	-4.352	-0.488	0.226	0.232	0.238	0.245
Supported						
Current basis	8.887	8.887	8.887	8.887	8.887	8.887
Proposed	0	0	0	0	0	0
Difference	-8.887	-8.887	-8.887	-8.887	-8.887	-8.887
Total Difference	-13.239	-9.375	-8.661	-8.655	-8.649	-8.642

Consultations

Given the changes to the 2017/18 policy are being proposed after the end of the financial year to which they relate, leading counsel opinion was sought on three counts:

1. Whether it would be lawful for the county council to vary its Minimum Revenue Provision policy statement at this point in time, i.e. after the end of the financial year but before the accounts for 2017/18 have been finalised;
2. Whether the proposed changes to the county council's Minimum Revenue Provision policy statement for 2017/18 would be in accordance with the applicable statutory guidance and satisfy the obligation under the regulations;
3. Whether the fact that the Minimum Revenue Provision policy statement for 2018/19 has been approved by Full Council previously, would constrain the council's ability to amend its Minimum Revenue Provision policy statement for the year 2017/18.

Counsel has confirmed that in his view the council would be acting lawfully in making its proposed variations.

Implications:

This item has the following implications, as indicated:

Financial Implications

The financial effect of the recommendations in this report is a saving of £13.2m in 2017/18 and £9.4m in 2018/19. The amount saved in 2017/18 will form a contribution to reserves in 2017/18. The saved amount in 2018/19 will form an underspend on the capital financing budget in that year. There will continue to be a Minimum Revenue Provision charge for schemes that have always been on an annuity basis and for the impact of new capital expenditure incurred.

Reductions in Minimum Revenue Provision increase the overall net cost of borrowing for the council. However, the overpayment of Minimum Revenue Provision deprives the council of revenue funds which it would otherwise have been able to use to carry out its other responsibilities. The Minimum Revenue Provision policy therefore needs to balance these two competing requirements and the council will continue to review its provisioning policy annually to identify whether there is a need to make a provision, or whether there are further opportunities to save whilst ensuring statutory obligations are met.

Risk management

Based on the statutory guidance, failure to agree a change in policy before the closure of the 2017/18 accounts will prohibit the ability to make the proposed changes in future. Under the regulations, the overriding principle is that the council must make a prudent Minimum Revenue Provision. However, the council is also obligated to make decisions that present good value for money and must approve a balanced budget on an annual basis.

List of Background Papers

Paper	Date	Contact/Tel
DCLG Guidance on Minimum Revenue Provision	February 2012	Khadija Saeed/(01772) 536195
Statutory Guidance on Minimum Revenue Provision	Updated February 2018	
Lancashire County Council Minimum Revenue Provision Statement 2015/16	February 2015	
Lancashire County Council Minimum Revenue Provision Statement 2016/17	February 2016	
Lancashire County Council Minimum Revenue Provision Statement 2017/18	February 2017	
Lancashire County Council Minimum Revenue Provision Statement 2018/19	February 2018	

Reason for inclusion in Part II, if appropriate

N/A