

<b>Report to:</b>	Cabinet Council	<b>Date of Meeting:</b>	10 February 2022 3 March 2022
<b>Subject:</b>	Treasury Management Policy and Strategy 2022/23		
<b>Report of:</b>	Executive Director of Corporate Resources and Customer Services	<b>Wards Affected:</b>	All Wards
<b>Portfolio:</b>	Cabinet Member - Regulatory, Compliance and Corporate Services		
<b>Is this a Key Decision:</b>	Yes	<b>Included in Forward Plan:</b>	Yes
<b>Exempt / Confidential Report:</b>	No		

### Summary:

This report sets out the following proposed policy and strategy documents:

- a) Treasury Management Policy (Appendix A)
- b) Treasury Management Strategy (Appendix B)
- c) Minimum Revenue Provision Policy Statement (Appendix C).

### Recommendation(s):

**Cabinet** is recommended to:

- 1) Recommend to Council that the Treasury Management Policy Document for 2022/23 be agreed;
- 2) Recommend to Council that the Treasury Management Strategy Document for 2022/23 be agreed;
- 3) Recommend to Council that the Minimum Revenue Provision Policy Statement 2022/23 be agreed.

**Council** is recommended to:

- 1) Approve the Treasury Management Policy Document for 2022/23;
- 2) Approve the Treasury Management Strategy Document for 2022/23;
- 3) Approve the Minimum Revenue Provision Policy Statement 2022/23.

### Reasons for the Recommendation(s):

The Council has adopted CIPFA's Code of Practice on Treasury Management in the Public Services. The Code requires that the Council sets a policy and strategy for the effective operation of the Council's Treasury Management function during the financial year. This will ensure that cash flow is adequately planned, surplus monies are invested commensurate with the Council's risk appetite whilst providing

adequate portfolio liquidity, and that the borrowing needs of the Council are properly managed to ensure that the Council can meet its capital spending obligations.

**Alternative Options Considered and Rejected:**

None

**What will it cost and how will it be financed?**

**(A) Revenue Costs**

All financial implications arising from this report are contained within the Councils overall revenue budget

**(B) Capital Costs**

All financial implications arising from this report are contained within the Councils overall capital budget

**Implications of the Proposals:**

**Resource Implications (Financial, IT, Staffing and Assets):**

The policy and strategy will allow for the Council's investment income and the financing costs for the Capital Programme to be managed within the budget for 2022/23.

**Legal Implications:**

None.

**Equality Implications:**

None.

**Climate Emergency Implications:**

The recommendations within this report will

Have a positive impact	N
Have a neutral impact	Y
Have a negative impact	N
The Author has undertaken the Climate Emergency training for report authors	N

The Council will during 2022/23, invest its reserves and balances overnight with either banks or money market funds in order to maintain high security and liquidity of such balances.

It may also have the opportunity to invest in longer term financial instruments or investment funds for which there may be a chance to consider the impact on the Council's Climate Emergency motion. In the event that the Council has more surplus balances available in future that may lead to longer term investing, the Council will take account of the climate emergency when discussing the options available with its Treasury Management Advisors.

## Contribution to the Council's Core Purpose:

Protect the most vulnerable: n/a
Facilitate confident and resilient communities: n/a
Commission, broker and provide core services: n/a
Place – leadership and influencer: Support strategic planning and promote innovative, affordable and sustainable capital investment projects through application of the CIPFA Prudential Code.
Drivers of change and reform: The Treasury Management function ensures that cash flow is adequately planned, and cash is available when needed by the Council for improvements to the borough through its service provision and the Capital Programme.
Facilitate sustainable economic prosperity: Pursuit of optimum performance on investments activities, minimising the cost of borrowing, the effective consideration / management of associated risks which continues to contribute to a balanced budget for the Council.
Greater income for social investment: n/a
Cleaner Greener: n/a

## What consultations have taken place on the proposals and when?

### (A) Internal Consultations

The Executive Director of Corporate Resources and Customer Services (FD6685/22) is the author of the report.

The Chief Legal and Democratic Officer (LD4885/22) has been consulted and any comments have been incorporated into the report.

### (B) External Consultations

The Council's external Treasury Management Advisors, Arlingclose Ltd, have provided advice with regards to the Treasury Management Policy and Strategy.

## Implementation Date for the Decision

Following the Call-In period for this committee.

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**Appendices:**

Appendix A – Treasury Management Policy 2022/23

Appendix B – Treasury Management Strategy 2022/23

Appendix C – Minimum Revenue Provision Policy Statement 2022/23

**Background Papers:**

There are no background papers available for inspection.

## 1. Background

- 1.1. The Council has adopted CIPFA's 2017 Code of Practice on Treasury Management in the Public Services which recommends the production of annual Treasury Management Policy and Strategy documents.
- 1.2. In addition, the Council has adopted and incorporated into both documents:
  - a) The requirements of the 2017 Prudential Code for Capital Finance in Local Authorities; and
  - b) An Investment Strategy produced in line with the Ministry of Housing Communities and Local Government (MHCLG) Statutory Guidance on Local Government Investments 2018. This sets out the manner in which the Council will manage its investments, giving priority to the security and liquidity of those investments.
- 1.3. CIPFA published a revised Code of Practice on Treasury Management and a revised Prudential Code for Capital Finance in Local Authorities in December 2021. The new codes take effect immediately, except that authorities may defer introducing revised reporting requirements until 2023/24. Sefton will therefore adopt the revised reporting requirements in the 2023/24 Treasury Management Policy and Strategy documents to allow time for proper scrutiny and consultation with treasury management advisers to take place.

## 2. Treasury Management Policy and Strategy Documents

- 2.1. The Code requires the Council to produce:
  - a) A Treasury Management Policy Document – which outlines the broad policies, objectives and approach to risk management of its treasury management activities;
  - b) A Treasury Management Strategy Document – This sets out specific treasury activities which will be undertaken in compliance with the Policy in 2022/23; and
  - c) Suitable Treasury Management Practices, setting out the manner in which the organisation will seek to achieve these policies and objectives, prescribing how it will manage and control those activities.

The content of the Policy Statement and the Treasury Management Practices will follow the recommendations contained in sections 6 and 7 of the Treasury Management Code. The Treasury Management Practices will incorporate the changes to the 2017 Code pertaining to the management and reporting of non-treasury management investment activity. Any further amendment to reflect the particular circumstances of the Council will not result in the Council materially deviating from the Code's key principles.

- 2.2. The proposed Policy and Strategy Documents are attached at **Appendix A and B** respectively.

- 2.3. In view of the complex nature of Treasury Management, update reports will be presented to the Audit and Governance Committee at each cycle and a mid-year report will also be presented to Cabinet and Council. An annual outturn report will also be presented to Audit and Governance Committee and both Cabinet and Council.

### **3. Financial Procedure Rules – Banking Arrangements**

- 3.1. The Treasury Management Policy Document at **Appendix A** delegates certain responsibilities to the Executive Director for Corporate Resources and Customer Services, including all executive decisions on borrowing, investment or financing, in line with the Constitution of the Council.

### **4. Minimum Revenue Provision (MRP) Policy Statement**

- 4.1. Local Authorities have a statutory requirement to set aside each year part of their revenues as a provision for the repayment of debt, called the Minimum Revenue Provision (MRP). The provision is in respect of capital expenditure incurred in previous years and financed by borrowing.
- 4.2. Regulations 27 and 28 in the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 [SI 3146, as amended] require local authorities to make a prudent amount of minimum revenue provision (MRP).
- 4.3. The statutory requirement to make an MRP charge does not apply to the Housing Revenue Account (HRA).
- 4.4. The MRP regulations were revised by the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414]. These regulations were complimented by the publication of guidance on determining the “prudent” level of MRP, to which authorities are required to have regard. The 2008 regulations and associated guidance allowed local authorities more flexibility in calculating their MRP annual charge.
- 4.5. Authorities are required to prepare an annual statement of their MRP policy for submission to their full Council before the start of each financial year. The aim is to give elected Members the opportunity to scrutinise the proposed application of the MRP guidance.
- 4.6. Revised guidance was published in February 2012 and again in February 2018. Changes made in the 2018 Guidance have been set out in the MRP policy statement.
- 4.7. In November 2021, the Department for Levelling Up, Housing and Communities (DLUHC) published a consultation seeking views on proposed changes to the (Capital Finance and Accounting) (England) Regulations 2003 to better enforce the duty of local authorities to make prudent Minimum Revenue Provision each year. The proposed changes seek to (1) stop local authorities using capital receipts in lieu of a prudential charge to revenue, and (2) to ensure that they make an MRP charge in respect of borrowing

associated with investment assets or capital loans. These changes are not intended to have any impact on the Housing Revenue Account, or on treasury management activities that do not score as capital spend. The proposed changes will come into effect from 1 April 2023, and therefore do not require any amendments to the MRP policy for 2022/23.

- 4.8. The proposed MRP Policy Statement is set out in **Appendix C**.

**Appendix A**

Corporate Resources and Customer Services

**Treasury Management Policy**

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2022/23



## **1. Treasury Management Policy**

### 1.1. The Council defines Treasury Management as:

The management of the Authority's borrowing, investments and cash flows; its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.

### 1.2. The Council's Statement of Treasury Management Policy is:

- a) Effective Treasury Management is acknowledged as providing support towards the achievement of the Council's business and service objectives. It is therefore committed to the principles of achieving best value in Treasury Management, and to employing suitable performance measurement techniques, within the context of effective risk management.
- b) The successful identification, monitoring and control of risk are regarded as the prime criteria by which the effectiveness of the Council's Treasury Management activities will be measured. Accordingly, the analysis and reporting of Treasury Management activities will focus on their risk implications for the organisation.

### 1.3. A dedicated team of three officers carries out the day-to-day treasury management activities. Two of the officers are qualified accountants, and one is a qualified accounting technician. The Service Manager – Treasury & Capital has obtained the CIPFA/Association of Corporate Treasurers sponsored qualification Certificate in International Treasury Management – Public Finance, which is aimed at giving a solid grounding in treasury management and which is tailored to the public sector.

### 1.4. Members should receive training in the Treasury Management function in order to assist in the understanding of this complex area. This will be addressed via the provision of regular reporting to Cabinet and the Audit and Governance Committee. Also, specific training and information on Treasury Management is available to all councillors on an annual basis. This is provided from the Authority's external advisors.

## **2. Policy on the use of external service providers**

### 2.1. Following the completion of a successful tender exercise in September 2020, the Council has engaged Arlingclose Ltd. as its treasury consultants from 1<sup>st</sup> October 2020 to 30<sup>th</sup> September 2023, with a further option of a one-year extension.

### 2.2. The Council recognises that responsibility for treasury management decisions rests with the Council at all times. However, access to external treasury consultants provides access to specialist skills, knowledge, and advice. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly documented and subjected to regular review.

### **3. Treasury Management Strategy**

- 3.1. The Annual Strategy Document sets out in detail how the Treasury Management Activities are to be undertaken in a particular financial year to comply with the Council's Policy. The strategy for 2022/23 is attached at **Appendix B**.

### **4. Delegated Powers**

- 4.1. The Executive Director for Corporate Resources and Customer Services, under the Council's Constitution, is given the following authority:
- a) All money in the hands of the Council shall be aggregated for the purposes of Treasury Management and shall be under the control of the Executive Director for Corporate Resources and Customer Services, the Officer designated for the purposes of Section 151 of the Local Government Act, 1972;
  - b) All executive decisions on borrowing, investment or financing shall be delegated to the Executive Director for Corporate Resources and Customer Services (or in their absence the Deputy Section 151 Officer) who shall be required to act in accordance with the Council's Treasury Policy, Treasury Management Practices and CIPFA's Standard of Professional Practice on Treasury Management.

### **5. Reporting Requirements/Responsibilities**

5.1. Cabinet and Council will:

- a) Approve, prior to each financial year, the Treasury Management Policy and Strategy Documents;
- b) Monitor these documents and approve any in-year amendments necessary to facilitate continued effective Treasury Management activity; and
- c) Receive a mid-year report on Treasury Management activity during the financial year and an annual outturn report following each financial year.

5.2. Audit and Governance Committee will:

- a) Monitor performance on at least a quarterly basis to ensure continued scrutiny of Treasury Management activity;
- b) Receive an annual outturn report on Treasury Management activity following each financial year; and
- c) Will be responsible for ensuring effective scrutiny of treasury management policies.

5.3. The Executive Director for Corporate Resources and Customer Services will:

- a) Draft and submit to Cabinet and Council prior to each financial year, the Treasury Management Policy and Strategy Documents;
- b) Implement and monitor these documents resubmitting any necessary in-year revisions/amendments (at least on a quarterly basis) to Cabinet and Council for approval;
- c) Draft and submit a mid-year report during the financial year and an annual outturn report on Treasury Management activity to Cabinet and Council following each financial year-end;
- d) Draft and submit an annual outturn report (and quarterly performance reports) on Treasury Management activity to the Audit & Governance Committee following each financial year-end;
- e) Maintain suitable Treasury Management Practices (TMP), setting out the manner in which the Council will seek to achieve its objectives. The TMP's will also prescribe how the treasury activities will be managed and controlled;
- f) Be responsible for the execution and administration of treasury management decisions; and
- g) Act in accordance with the Council's Policy Statement and Treasury Management Practices, and also in accordance with CIPFA's Standard of Professional Practice on Treasury Management.

## **6. Borrowing and investments**

- 6.1. The Council's borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken, and the type of borrowing should allow the Council transparency and control over its debt.
- 6.2. The Council's primary objective in relation to investments remains the security and liquidity of capital. The yield earned on investments remains important but is a secondary consideration.

Corporate Resources and Customer Services

## **Treasury Management Strategy**

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2022/23

## **1. Introduction**

- 1.1. The Treasury Management Strategy Document sets out in detail how the Treasury Management Activities are to be undertaken in a particular financial year to comply with the Council's Treasury Management Policy.
- 1.2. The Strategy has been produced to incorporate the requirements of the CIPFA Code of Practice on Treasury Management 2017 and the Prudential Code for Capital Finance 2017.

## **2. Treasury Management Strategy 2022/23**

- 2.1. The Strategy for 2022/23 covers:
  - a) Treasury Limits in force which will limit the borrowing activity of the Council (2.2);
  - b) Prudential Indicators 2022/23 to 2024/25 (2.3);
  - c) Credit Risk (2.4);
  - d) Markets in Financial Instruments Directive (MIFID II) (2.5);
  - e) Interest Rates (2.6);
  - f) Exchange Rates (2.7);
  - g) Capital Borrowing (2.8 & 2.9);
  - h) Debt Rescheduling opportunities (2.10);
  - i) Municipal Bond Agency (2.11);
  - j) Borrowing in advance of need (2.122);
  - k) The Use of Financial Instruments for the Management of Risks (2.133);
  - l) Investment Strategy (2.144);
  - m) Non-Treasury Investments (2.15);
  - n) Ethical Investing (2.14.146);
  - o) The Climate Emergency (2.17);
  - p) Member and Officer Training (2.18).

### **2.2. Treasury Limits for 2022/23**

The Treasury Limits set by Council in respect of its borrowing activities are:

Affordable Borrowing Limit	Maximum	£220m
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It is a statutory duty under S.3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the 'Affordable Borrowing Limit'. The Affordable Borrowing Limit takes into account the Council's current debt, an assessment of external borrowing to fund the Capital Programme in 2022/23, the need to fund capital expenditure previously met from internal funding, and cash flow requirements.

Short-term Borrowing Limit	Maximum	£30m
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The Short-Term Borrowing limit takes into account an assessment of any potential short-term financing the Council may need (e.g. bank overdraft, short-term funding in anticipation of grant receipts). Short-Term Borrowing is defined as being for less than 12 months.

### 2.3. Prudential Indicators

The following prudential indicators are considered relevant by CIPFA for setting an integrated Treasury Management Strategy:

#### 2.3.1. Debt Maturity Indicators

These indicators are designed to be a control over an authority having large concentrations of debt needing to be replaced at times of high interest rates. The control is based on the production of a debt maturity profile, which measures the amount of borrowing that will mature in each period as a percentage of total projected borrowing. Any borrowing decision and related maturity dates will be taken by the Council mindful of maturity profile limits set out below to ensure large concentrations of debt do not fall due for repayment in any one future financial year. The profile reflects borrowing advice provided by Arlingclose, the Council's Treasury Management Advisors.

<b>Maturity Structure of Borrowing During 2022/23</b>	<b>Upper Limit %</b>	<b>Lower Limit %</b>
Under 12 months	35%	0%
12 months and within 24 months	40%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and within 15 years	75%	0%
15 years and above	90%	25%

The table above shows, for each maturity period, the minimum and maximum amount of debt that the Council can hold as a percentage of its total external debt. For example, when deciding to take out a loan that is due to mature within the next 24 months, the Council must ensure that this does not take the total amount of debt due to be repaid to more than 40% of all Council debt.

#### 2.3.2. Principal sums invested for periods longer than 365 days

An upper limit is set on the value of principal sums invested for periods over 365 days for that year. This limit is set to contain the Authority's exposure to the possibility of loss that might arise as a result of having to seek early repayment of principal sums invested.

The limits set for 2022/23 and the next two years are shown below:

Principal Sums Invested for Longer Than 365 Days			
	2022/23	2023/24	2024/25
Upper Limit	£15m	£10m	£10m

#### 2.4. Credit risk

All investments involve a degree of risk. In order to mitigate these risks, the Council will consider the credit ratings supplied by the three main credit rating agencies - Fitch, Moody's and Standard & Poor's as part of the process to determine the list of counterparties where the level of risk is acceptable. As part of this process advice from Arlingclose will also be considered in terms of asset class, maximum duration, and level of investment.

Sole reliance will not be placed on the use of this external service and the Council will also consider alternative assessments of credit strength, and information on corporate developments and of market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution;
- Sovereign support mechanisms;
- Credit default swaps (where quoted);
- Share prices (where available);
- Economic fundamentals, such as a country's net debt as a percentage of its GDP;
- Corporate developments, news, articles, markets sentiment and momentum;
- Background research in the financial press
- Discussion with our treasury consultants
- Internal discussion with the Executive Director for Corporate Resources and Customer Services.

The Council will only invest with institutions of high credit quality that meet the following criteria:

- i. are UK based; and/or
- ii. are non-UK and domiciled in a country which has a minimum sovereign Long-Term rating of AA-
- iii. have a minimum long-term rating of A- (or equivalent).

A further explanation of credit ratings can be found at **Appendix B3**.

The Council maintains a full record of each investment decision taken, each of which is authorised by an appropriate level of signatory.

## 2.5. MIFID II

2.5.1. From 3rd January 2018, the Financial Conduct Authority was obligated to treat all Local Authorities as “retail clients” under European Union legislation (MiFID II). The client status of the Local Authority relates to its knowledge and experience with regards to the use of regulated investment products and the decision-making processes it has in place for making such investments. The directive is focused on products such as Certificates of Deposit, Gilts, Corporate Bonds and investment funds, including Money Market Funds.

2.5.2. The Council will opt up to “professional status” with its providers of financial services including advisers, banks, brokers and fund managers. Given the size and range of the Authority’s treasury management activities, this represents the most appropriate status and will allow access to the above products as an investment option as they are not available to retail clients.

## 2.6. Interest Rates

2.6.1. Arlingclose provide regular forecasts of interest rates to assist decisions in respect of:

- a) Capital Borrowings (2.8);
- b) Debt Rescheduling opportunities (2.1010);
- c) Temporary borrowing for cash flow; and
- d) Investments strategy (2.144).

2.6.2. **Appendix B2** gives details of Arlingclose’s central view regarding interest rate forecasts.

2.6.3. Interest rate exposure is principally managed by monitoring interest rate risk. An internal view of the likely path of interest rates is formulated and this is considered along with the cash flow for the Council and any future requirements for potential borrowing such as to fund the Capital Programme. This then forms the basis of when to borrow, whether to borrow short or long term, and whether at fixed or variable rates. The maturity date for any loan is then set after a review of the Council’s debt maturity profile to ensure a smooth maturity profile. Any plans for borrowing are discussed with our treasury consultants at regular strategy meetings to ensure the most advantageous position.

2.6.4. The current borrowing portfolio position is monitored via the borrowing charges incurred by the Council, which are monitored on a monthly basis.

2.6.5. The advice from Arlingclose takes into account financial activity both in the UK and world economies and the impact of major national and international events. It is essential that borrowing and investment decisions are taken mindful of independent forecasts as to interest rate movements. The Council will continue to take account of the advice of treasury management advisors.



## 2.7. Exchange Rate Risk Management

2.7.1. The Council has a minimal exposure to exchange rate risk as it has no powers to enter into loans or investments in foreign currency for treasury management purposes.

2.7.2. The Council will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income and expenditure levels.

## 2.8. Capital Borrowing Strategy

2.8.1. The Authority's current debt portfolio is presented below:

<b>Debt Portfolio</b>	<b>31/12/2021</b>
Average Interest Rate	3.74%
<u>Debt Outstanding – Fixed Rate</u>	£m
PWLB	169.849
Other Long-Term Liabilities	8.138
Total Debt	<b>177.987</b>

2.8.2. Other long-term liabilities shown above represent transferred debt from the Merseyside Residuary Body (£1.969m) and finance lease liabilities (£6.169m).

2.8.3. The Council will raise its required finance, following advice from treasury management advisors, from the following sources:

- HM Treasury's PWLB lending facility
- An institution approved for investments (see 2.14 below)
- Banks or building societies authorised to operate in the UK
- UK public sector bodies
- UK public and private sector pension funds (with the exception of Merseyside Pension Fund)
- Capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues.

2.8.4. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- Leasing
- Hire purchase
- Private Finance Initiative
- Sale and leaseback.

2.8.5. The Council's forecast borrowing requirement for 2022/23 is as follows:

<b>Borrowing Requirement</b>	<b>Estimate £m</b>
New Borrowing	6.244
Replacement Borrowing	<u>20.000</u>
<b>Total Borrowing</b>	<b>26.244</b>

- 2.8.6. The new borrowing represents the unsupported borrowing as required by the Capital Programme in 2022/23 and replacement borrowing for existing loans that will mature in year. As further explained in 2.8.9. (below), the Council is internally borrowed and may also take additional borrowing if required, in order to reverse this position.
- 2.8.7. The Arlingclose forecast for interest rates is set out at **Appendix B1**. This would suggest that the following strategy is followed:
- i. The cheapest borrowing will be internal borrowing, which involves reducing cash balances and foregoing interest earned at the current historically low rates. Consideration will always be given to long term borrowing rates and the possibility of rates rising, which could mean borrowing at future higher rates which could erode the advantages of internal borrowing
  - ii. Temporary borrowing from money markets or other local authorities.
- 2.8.8. The authority borrows from the PWLB in order to fund part of the Capital Programme, the maximum that the Council can borrow being the Capital Financing Requirement (CFR) which measures the amount of capital spending that has not yet been financed by capital receipts, capital grants or contributions from revenue income. It measures the underlying need to borrow for a capital purpose.
- 2.8.9. PWLB borrowing as at 31<sup>st</sup> December 2021, plus other long-term liabilities, is £178m, as against an estimated CFR of £234m for 2021/22. This means that the Council is in a position to borrow a further £56m which would take the current borrowing level to the level of the CFR. This strategy is described as being internally borrowed which has the advantage of reducing exposure to interest rate and credit risk. To be internally borrowed is a conscious decision to use cash balances to fund capital expenditure, rather than borrow from the PWLB. This position can be reversed at any time by borrowing from the PWLB, or any other appropriate organisation.
- 2.8.10. As the Bank of England and the UK Government continue to react to the ongoing Coronavirus pandemic, 2022/23 is expected to experience a continuation of a relatively low base rate. Hence, internal borrowing is a sensible option where interest rates on deposits are much lower than the current PWLB borrowing rates, but this will be reviewed should interest rates change significantly.
- 2.8.11. However, as noted in 2.8.7. (above), savings have to be weighed against the potential for incurring long term extra costs by delaying unavoidable new borrowing until later years when PWLB rates are forecast to be higher. This issue will be left under review and discussions with treasury management

advisors will be ongoing to ascertain the optimum time for undertaking future borrowing.

- 2.8.12. Against this background, caution will be adopted in undertaking borrowing in 2022/23. The Executive Director for Corporate Resources and Customer Services will monitor the interest rate market and following advice from Arlingclose, adopt a pragmatic approach to changing circumstances during the year.

## 2.9. Public Works Loans Board Rates

- 2.9.1. The PWLB offers its local authority borrowing facility at a fixed rate above the Government's cost of borrowing and this has historically been the most efficient manner of borrowing for councils. The PWLB will not however, lend to any authority that plans to buy investment assets primarily for yield anywhere in their capital plans. The Council intends to avoid this activity in order to retain its access to PWLB loans.

- 2.9.2. PWLB borrowing rates will be used when assessing the cost, viability, and affordability of capital schemes when those schemes are being financed from borrowing. The authority will also consider a wider evaluation of funding options from other sources as identified in paragraph 2.8.3 (above).

- 2.9.3. The authority may also consider arranging forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

## 2.10. Debt Rescheduling Opportunities

- 2.10.1. The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

- 2.10.2. The lower interest rate environment and changes in the rules regarding the premature repayment of PWLB loans has adversely affected the scope to undertake meaningful debt restructuring in recent years. The situation will be monitored however, and the Council as in previous years will consider the option of debt restructuring all or part of the debt portfolio during 2022/23, should the financial circumstances allow, for example, by using capital receipts from asset disposals to repay debt.

## 2.11. Use of the UK Municipal Bond Agency

- 2.11.1. The UK Municipal Bonds Agency (MBA) was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities.

2.11.2. The MBA will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be subject to specialist external advice and a separate report will be brought to Cabinet and full Council.

## 2.12. Borrowing in advance of need

2.12.1. The Council will not borrow more than, or in advance of, its needs purely to profit from the investment income made on the extra sums borrowed. Any decision to borrow in advance of need will be considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

2.12.2. In determining whether to borrow in advance of need the Council will: -

- Ensure that there is a direct link between the Capital Programme and maturity profile of the existing debt portfolio which supports the need to borrow in advance of need;
- Ensure that the revenue implications of such borrowing have been considered in respect of future plans and budgets; and
- Consider the merits of other forms of funding.

2.12.3. The total amount borrowed will not exceed the authorised borrowing limit of £220m. The maximum period between borrowing and expenditure is expected to be two years, although the Authority is not required to link loans with particular items of expenditure.

## 2.13. The Use of Financial Instruments for the Management of Risks

2.13.1. Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. Lender Option Borrower Option (LOBO) loans – typically a very long-term loan (40-70 years) and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment). The CIPFA Code requires councils to clearly detail their policy on the use of derivatives in the annual strategy.

2.13.2. The Council's policy on such items is that it will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

2.13.3. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

2.13.4. The Council will only use derivatives after seeking expertise, a legal opinion and ensuring officers and members have the appropriate training for their use. At the present time, no such arrangements are in place.

#### 2.14. Investment Strategy

2.14.1. The Council manages the investment of its surplus funds internally and operates in accordance with the Statutory Guidance on Local Government Investments issued by MHCLG, the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 and the CIPFA Treasury Management in Public Services Guidance Notes 2018 for Local Authorities. Surplus funds are invested on a daily basis ensuring security, followed by portfolio liquidity.

2.14.2. The Council's investment priorities are, in order of priority:

1. The security of capital
2. The liquidity of capital
3. Yield that can be generated.

2.14.3. The Council will aim to achieve the optimum return on its investments commensurate with proper levels of security of principal sums invested and portfolio liquidity, whilst ensuring that robust due diligence procedures cover all external investments.

2.14.4. The Council's investment portfolio as at 31<sup>st</sup> December 2021 is set out below:

<b>Investments Portfolio</b>	<b>£m</b>
Bank Deposits	12.64
Money Market Funds	73.00
CCLA Property Fund	<u>5.00</u>
<b>Total</b>	<b>90.64</b>

2.14.5. The Authority may invest its surplus funds with any of the counterparty types in the table below, subject to the maximum limits shown:

<b>Sector</b>	<b>Time limit</b>	<b>Counterparty limit</b>	<b>Sector limit</b>
The UK Government	50 years	Unlimited	Unlimited
Local authorities & other government entities	25 years	£15m	Unlimited
Secured investments	25 years	£15m	Unlimited
Banks (unsecured)	12 months	£10m	Unlimited

Building societies (unsecured)	12 months	£10m	£15m
Registered providers (unsecured)	5 years	£10m	£15m
Money market funds	n/a	£15m	Unlimited
Strategic pooled funds e.g. Property Funds	n/a	£10m	£15m
Other investments	5 years	£5m	£10m

2.14.6. The risk of exposure to an individual counterparty as a proportion of the Council's total investment portfolio will also be considered so that access to cash is maintained in the event of operational difficulties at any one provider. Operational limits expressed as a percentage of total investments held, may therefore be used for investments in addition to the above maximum limits and will be applied to counterparties that are lent to in the short term or for daily liquidity. The following table outlines the operational limits that will be applied:

Sector	Counterparty limit
Local authorities & other government entities	10%
Banks (unsecured)	5%
Building societies (unsecured)	5%
Money market funds	10%

2.14.7. Advice from our Treasury Management Advisors will also be considered in determining whether shorter maximum investment periods or operational limits for the amount invested is more appropriate during the year.

2.14.8. The Council banks with National Westminster Bank, which is part of the Royal Bank of Scotland Group. It is currently a part government-owned institution. At the present time, it meets the minimum credit criteria of A- (or equivalent) long term. There may be occasions however, when the bank's rating may temporarily fall below these minimum criteria to a BBB rating. The Bank will continue to be used for short term liquidity requirements (overnight and weekend investments) to ensure business continuity when no other options are available.

2.14.9. The current list of countries approved for investment is shown below; this takes account of the most up-to-date credit ratings available in respect of the countries named. It should be noted that a maximum limit of £10m will be applied when investing in any one country outside of the UK. The investment counterparties within each country will also be subject to the limits identified above and will be monitored to ensure they continue to meet the requirements for high credit quality. In the event of a change in credit rating or outlook, the Council, with advice from treasury management advisors, will evaluate its significance and determine whether to include (subject to Council approval) or remove a country from the approval list:

Rating	Country
<b>AAA</b>	<ul style="list-style-type: none"> <li>• Australia</li> <li>• Denmark</li> <li>• Germany</li> <li>• Netherlands</li> <li>• Norway</li> <li>• Singapore</li> <li>• Sweden</li> <li>• Switzerland</li> <li>• USA</li> </ul>
<b>AA+</b>	<ul style="list-style-type: none"> <li>• Austria</li> <li>• Canada</li> <li>• Finland</li> </ul>
<b>AA</b>	<ul style="list-style-type: none"> <li>• France</li> </ul>
<b>AA-</b>	<ul style="list-style-type: none"> <li>• United Kingdom</li> </ul>

2.14.10. The Bank of England Base Rate has remained low at 0.25%. Arlingclose's projection is for this to rise to 0.50% by March 2022 and remain unchanged thereafter (**Appendix B1**). The COVID-19 pandemic however, has increased the risk that the Bank of England may set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. Since investments cannot pay negative income, negative rates will be applied by reducing the value of investments. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

2.14.11. In order to pursue the strategy of maximising returns from surplus funds at an acceptable level of security and portfolio liquidity, the following Brokers will be utilised for investments of over one month:

- ii) BGC Brokers LP;
- iii) Tradition UK Limited;
- iv) Tullet Prebon Limited.

There are 3 brokers within this list, however as with previous years, this is to provide maximum protection to the Council. It is unlikely that these institutions will all be utilised during the financial year.

2.14.12. It is not proposed to make any investments in 2022/23 that do not comply with the above strategy, however, should the situation change, the Executive Director for Corporate Resources and Customer Services will report to Cabinet requesting appropriate approval to amend the strategy before any such investments are made.

2.14.13. If any of the Council's investments appear at risk of loss due to default (i.e. this is a credit related loss, and not one resulting from a fall in price due to movements in interest rates) the Council will make an assessment of whether a revenue provision of an appropriate amount is required.

2.14.14. Performance monitoring will be reported to the Audit and Governance Committee on a quarterly basis, with mid-year reports and outturn reports also presented to Cabinet and Council.

2.15. Non-Treasury Investments: Loans

2.15.1. The Council will invest its money to support local public services and stimulate local economic growth by providing loans to its subsidiaries. These types of investments are classified as non-treasury investments, further detail of which can be found in the Capital Strategy included in the agenda for this meeting.

2.15.2. Cabinet as the shareholder has agreed the provision of a peak debt facility to Sandway Homes Limited that is due to reach £8.3m before reducing to £3.7m by the end of 2022/23. As this sum is drawn down as per the agreed loan agreement, the Council will if required provide for this sum via the Public Works Loan Board. These sums are included in the prudential indicators for 2022/23 included on this agenda.

2.15.3. A similar arrangement exists for the wholly owned hospitality company, Sefton Hospitality Operations Limited for whom a lower debt facility of £0.5m has been provided.

2.16. Ethical Investment Principles

2.16.1. Where the Council deposits surplus balances overnight or for a short-term, investments will be made with financial institutions in a responsible manner (aligned to the overarching core principles/Councils core values) where possible and in accordance with advice from its Treasury Management Advisor. In the event that the Council has surplus balances that it can invest for the longer term (e.g. terms over 1 year) it will exclude direct investment in financial products that do not contribute positively to society and the environment. This will include the principle that investment in specific financial products whose performance is driven by off-shore trading, financial malpractice, debt swops, short selling, the arms trade and tobacco industry will be avoided. The same rigorous criteria will be used to assess whether investment in certain countries will be contrary to Sefton's core values.

2.16.2. It is recommended that the Executive Director for Corporate Resources and Customer Services, assess whether investment in certain countries will be contrary to Sefton's core values, give consideration to the exclusion of those countries on the EU list of non-cooperative tax jurisdictions (the black list and grey list), which aims to tackle external risks of tax abuse and unfair tax competition, within the Council's Treasury Management Strategy.

2.17. The Climate Emergency

2.17.1. At Full Council in July 2019 a climate emergency was declared by the Council. One of the aspects within this motion was that the Council should review the impact that some of its strategies including its Treasury Management Strategy could have on the successful delivery of the motion.



2.17.2. In recent years, the Council has seen its level of reserves and balances (excluding emergency Covid funding) reduce and as a result where in previous years, it would have invested these surplus resources in longer term financial instruments or investment funds that may have had an impact on the Council's motion, it now deposits these lower value residual funds overnight with either banks or money market funds.

2.17.3. As a result of this, at this stage it is not considered that the Council's investment activity needs to be taken into account when considering its response to the climate emergency. In the event that the council has more surplus balances available during the year that may lead to longer term investing, the council will take full account of the climate emergency when discussing the options available with the Treasury Management Advisors.

2.18. Member and Officer training

2.18.1. CIPFA's Code of Practice requires the Executive Director for Corporate Resources and Customer Services to ensure that all Members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities.

2.18.2. In order to address this, the Service Manager – Treasury & Capital has obtained the CIPFA/Association of Corporate Treasurers sponsored qualification Certificate in International Treasury Management – Public Finance, which is aimed at giving a solid grounding in treasury management and which is tailored to the public sector. Training will be provided for Members of the Audit & Governance Committee and it is intended for such training to occur at least annually.

**INTEREST RATE FORECAST****Arlingclose Interest Rate Forecast as at December 2021**

The Council has appointed Arlingclose as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives their central view:

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
<b>Official Bank Rate</b>													
Upside risk	0.00	0.00	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk	0.00	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
<b>3-month money market rate</b>													
Upside risk	0.05	0.05	0.25	0.35	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.25	0.55	0.55	0.60	0.60	0.60	0.60	0.65	0.65	0.65	0.65	0.65	0.65
Downside risk	0.00	-0.25	-0.25	-0.30	-0.30	-0.30	-0.30	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35
<b>5yr gilt yield</b>													
Upside risk	0.00	0.35	0.45	0.55	0.55	0.55	0.55	0.55	0.55	0.50	0.50	0.45	0.45
Arlingclose Central Case	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.65	0.70	0.75	0.75
Downside risk	-0.10	-0.20	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.30	-0.35	-0.40	-0.40
<b>10yr gilt yield</b>													
Upside risk	0.10	0.25	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55
Arlingclose Central Case	0.80	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.90	0.90	0.95	0.95
Downside risk	-0.10	-0.25	-0.30	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.40	-0.40	-0.40	-0.40
<b>20yr gilt yield</b>													
Upside risk	0.30	0.40	0.45	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	1.00	1.05	1.10	1.10	1.10	1.10	1.15	1.15	1.15	1.20	1.20	1.20	1.20
Downside risk	-0.15	-0.30	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45
<b>50yr gilt yield</b>													
Upside risk	0.25	0.30	0.40	0.45	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.70	0.75	0.80	0.85	0.90	0.95	1.00	1.05	1.05	1.10	1.10	1.15	1.15
Downside risk	-0.15	-0.30	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45

PWLB Standard Rate (Maturity Loans) = Gilt yield + 1.00%

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%

PWLB Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

**Arlingclose Economic and Interest Rate Forecast (Commentary)**

**Underlying assumptions:**

- The global recovery from the pandemic has entered a more challenging phase. The resurgence in demand has led to the expected rise in inflationary pressure, but disrupted factors of supply are amplifying the effects, increasing the likelihood of lower growth rates ahead. The advent of the Omicron variant of coronavirus is affecting activity and is also a reminder of the potential downside risks.
- Despite relatively buoyant activity survey data, official GDP data indicates that growth was weakening into Q4 2021. Other data, however, suggested continued momentum, particularly for November. Retail sales volumes rose 1.4%, PMIs increased, and the labour market continued to strengthen. The end of furlough did not appear to have had a significant impact on unemployment. Wage growth is elevated.
- The CPI inflation rate rose to 5.1% for November and will rise higher in the near term. While the transitory factors affecting inflation are expected to unwind over time, policymakers' concern is persistent medium term price pressure.
- These factors prompted the MPC to raise Bank Rate to 0.25% at the December meeting. Short term interest rate expectations remain elevated.
- The outlook, however, appears weaker. Household spending faces pressures from a combination of higher prices and tax rises. In the immediate term, the Omicron variant has already affected growth – Q4 and Q1 activity could be weak at best.
- Longer-term government bond yields remain relatively low despite the more hawkish signals from the BoE and the Federal Reserve. Investors are concerned that significant policy tightening in the near term will slow growth and prompt the need for looser policy later. Geo-political and coronavirus risks are also driving safe haven buying. The result is a much flatter yield curve, as short-term yields rise even as long-term yields fall.
- The rise in Bank Rate despite the Omicron variant signals that the MPC will act to bring inflation down whatever the environment. It has also made clear its intentions to tighten policy further. While the economic outlook will be challenging, the signals from policymakers suggest their preference is to tighten policy unless data indicates a more severe slowdown.

**Forecast:**

- The MPC will want to build on the strong message it delivered this month by tightening policy despite Omicron uncertainty.
- Arlingclose therefore expects Bank Rate to rise to 0.50% in Q1 2022, but then remain there. Risks to the forecast are initially weighted to the upside, but becoming more balanced over time. The Arlingclose central forecast remains below the market forward curve.
- Gilt yields will remain broadly flat from current levels. Yields have fallen sharply at the longer end of the yield curve, but expectations of a rise in Bank Rate have maintained short term gilt yields at higher levels.
- Easing expectations for Bank Rate over time could prompt the yield curve to steepen, as investors build in higher inflation expectations.
- The risks around the gilt yield forecasts vary. The risk for short and medium term yields is initially on the upside but shifts lower later. The risk for long-term yields is weighted to the upside.

**CREDIT RATING EXPLANATION**

The following is an explanation of the ratings applied by Fitch.

**Short term rating**

This places greater emphasis on the liquidity necessary to meet financial commitments.

- F1** highest credit quality (+ denotes exceptionally strong)
- F2** good credit quality
- F3** fair credit quality.

**Long term rating**

- AAA** highest credit quality – lowest expectation of credit risk and exceptionally strong capacity to pay financial commitments
- AA** very high credit quality – very low credit risk and very strong capacity to pay financial commitments
- A** high credit quality – low credit risk and considered to have strong capacity to pay financial commitments, but may be vulnerable.

**Viability rating**

This assesses how a bank would be viewed if it were entirely independent and could not rely on external support.

- aaa** highest fundamental credit quality
- aa** very high fundamental credit quality
- a** high fundamental credit quality
- bbb** good fundamental credit quality
- bb** speculative fundamental credit quality
- b** highly speculative fundamental credit quality
- ccc** substantial fundamental risk
- cc** very high levels of fundamental credit risk
- c** exceptionally high levels of fundamental credit risk
- f** failed.

**Support rating**

Judgement of a potential supporter's (either sovereign state of parent) propensity to support the bank and its ability to support it.

- 1** extremely high probability of external support
- 2** extremely high probability of external support
- 3** moderate probability
- 4** limited probability
- 5** cannot rely on support.

Corporate Resources and Customer Services

## **Minimum Revenue Provision Policy Statement**

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2022/23

## **1. Background**

- 1.1. Local Authorities have a statutory requirement to set aside each year part of their revenues as a provision for the repayment of debt, called the Minimum Revenue Provision (MRP). The provision is in respect of capital expenditure incurred in previous years and financed by borrowing.
- 1.2. Previously the Council was required to follow a prescriptive MRP calculation as set out in former regulations 27, 28 and 29 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 [SI 2003/3146, as amended]. This system was revised by the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414].
- 1.3. As part of those regulations the Government issued guidance recommending local authorities to prepare an annual statement of its strategic policy on the MRP, to be approved by the full council. The guidance requires each authority to determine its own MRP within the given framework and that the amount of MRP charged is a prudent amount.
- 1.4. The broad aim of a prudent amount is to ensure that the debt is repaid over a period that is either reasonably commensurate with the period over which the capital expenditure provides benefit, or, in the case of borrowing supported by formula grant, reasonably commensurate with the period implicit in the determination of that grant.

## **2. Strategic Options**

- 2.1. The Council is free to determine its own method for calculating a prudent provision, but the guidance includes four options for calculating MRP. The Council can choose from or use a combination of the available options. The options are as follows:

### **Option 1 – Regulatory Method**

- 2.2. This provides for local authorities to continue to calculate MRP in line with the minimum existing statutory charge of 4% of outstanding debt related to supported borrowing only, less an adjustment that ensures consistency with previous capital regulatory regimes no longer in force. This option is available for all capital expenditure incurred prior to 1 April 2008.

### **Option 2 – Capital Financing Requirement Method**

- 2.3. This is very like the regulatory method, but it does not take account of the adjustment that ensures authorities do not pay more MRP than under the previous capital regulatory regimes. For most authorities, this method may not be appropriate as it would result in a higher level of provision than option 1.

### **Option 3 – Asset Life Method**

- 2.4. This method is appropriate for calculating MRP in relation to debt incurred as unsupported borrowing (also known as prudential borrowing) and must be used for revenue expenditure capitalised by direction or regulation (such as that for equal pay). Under this option there are two methods available:
- i. **Equal instalment method.** This generates a series of equal annual amounts over the life of each asset that is financed by borrowing, with the life determined upon acquisition. This means that the charge to revenue closely matches the period of economic benefit of the asset.
  - ii. **Annuity method.** This method links the MRP to the flow of benefits from an asset where the benefit is expected to increase in later years.
- 2.5. Under this option authorities should consider the type of assets that they finance through prudential borrowing, as the type of asset may have a significant impact on the level of MRP and the method used to calculate the MRP.

### **Finance Leases and PFI**

- 2.6. The guidance indicates that for finance leases and on balance sheet PFI contracts, the MRP requirement is met by making a charge equal to the element of the finance lease rental that goes to write down the balance sheet liability under proper accounting practices. This is in effect a modified version of the annuity method of Option 3.

### **Option 4 – Depreciation Method**

- 2.7. This method is appropriate for calculating MRP in relation to debt incurred as unsupported (prudential) borrowing. Under this method, MRP is equal to the amount of depreciation charged on assets funded from unsupported borrowing. This method may cause volatility in the annual charge for MRP because assets are revalued on a periodic basis, giving rise to significant changes in the amount of depreciation charged. Given this potential adverse impact on future budgets this option is not considered viable.

### **Use of Capital Receipts**

- 2.8. In addition to the four options listed above, the Local Authorities (Capital Finance and Accounting) Regulations 2003 [SI 2003/3146] allow local authorities to use capital receipts to meet “any liability in respect of credit arrangements, other than any liability which, in accordance with proper practices, must be charged to a revenue account”.
- 2.9. For both finance leases and PFI contracts, proper accounting practices require that the element of the annual rental relating to the repayment of the liability is used to write down that liability on the balance sheet and is not charged to revenue. It therefore follows that local authorities are permitted to apply capital receipts to fund the principal element of the annual rental of a finance lease or on balance sheet PFI contract.

### **3. MRP Statutory Guidance (February 2018)**

3.1. In February 2018, the Government issued revised statutory guidance on the minimum revenue provision.

3.2. The key changes to the guidance included:

- The definition of 'Prudent Provision' used in the guidance was updated so that the broad aim of prudent provision is to require local authorities to put aside revenue over time to cover their Capital Financing Requirement (CFR).
- Where a local authority changes the method(s) that it uses to calculate MRP, it should explain in its Statement, why the change will better allow it to make prudent provision.
- The calculation of MRP under the new method(s) should be based on the residual CFR at the point the change in method is made (i.e. it should not be applied retrospectively). Changing the method used to calculate MRP 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 MRP relating to previous years.
- A charge to a revenue account for MRP cannot be a negative charge.
- If a local authority chooses to offset a previous year's overpayment, they should disclose this fact and any remaining cumulative overpayment of MRP in the Statement presented to full council.
- Where a local authority uses MRP options 3 or 4 or where it uses another methodology that has the useful life of assets as a component to the calculation, it should normally not exceed a maximum useful life of 50 years. Local authorities can exceed this maximum in two scenarios:
  - i. where a local authority has an opinion from an appropriately qualified professional advisor that an asset will deliver service functionality for more than 50 years it can use the life suggested by its professional advisor; and
  - ii. for a lease or PFI asset, where the length of the lease/PFI contract exceeds 50 years. In this case the length of the lease/PFI contract should be used.



#### 4. MRP Policy for 2022/23

4.1. The recommended MRP policy is summarised below:

<u>Category</u>	<u>Basis of MRP Calculation</u>
Supported borrowing	Annuity Basis - Calculated over 50 years (commencing from 1 April 2015)
Unsupported (prudential) borrowing	Annuity Basis - Calculated using (Option 3) the estimated life method

<u>PFI and Leasing Arrangements</u>	<u>Basis of MRP Calculation</u>
On balance sheet PFI contracts	MRP charge to be equal to the principal element of the annual rental
On balance sheet leasing arrangements (finance leases)	MRP charge to be equal to the principal element of the annual rental

4.2. Standard asset lives to be applied to calculate the MRP charge for unsupported (prudential) borrowing:

Intangibles (Software)	3 Years
Vehicles, Plant & Equipment	5 to 10 Years
Revenue Expenditure Funded for Capital Under Statute – Capitalised Redundancy Costs	20 Years
Revenue Expenditure Funded for Capital Under Statute - Other	25 Years
Community Assets (Parks, Gardens etc.)	25 Years
Land	50 Years
Buildings – Scheme Value under £250,000	25 Years
Buildings – New Build (Value over £249,999)	Building Life per Asset Register *
Buildings – Acquisitions (Value over £249,999)	
Buildings – Refurbishment / Remodelling (Value over £249,999)	30 Years
Buildings – New Strand Shopping Centre	25 Years
Infrastructure - Capitalised Highways Maintenance	10 Years
Infrastructure - Other	40 Years

\* The building life used in the MRP calculation will be subject to a maximum of 50 years.

4.3. The Executive Director for Corporate Resources and Customer Services will retain discretion to use alternative lives for assets (capital schemes) that have characteristics that mean using the standard life would not be considered appropriate. It is anticipated that this will only apply in very limited circumstances.

4.4. Assets acquired with the intention of onward sale which will not be used in the delivery of services will not generally attract MRP as in these events the capital receipts generated by the loan and sale will be set aside to repay debt.

4.5. Loans made to third parties to enable them to incur capital expenditure are repaid by the borrower and so MRP provision does not need to be made by the Council from Council Tax.

4.6. Commencement of MRP Charges

Provision for debt under Option 3 (Asset Life Method) will normally commence in the financial year following the one in which the expenditure is incurred. However, the MRP guidance highlights an important exception to this rule. In the case of the provision of a new asset, MRP would not have to be charged until the asset came into service and would begin in the financial year following the one in which the asset became operational. This delay would be perhaps 2 or 3 years in the case of major projects, or possibly longer for some complex infrastructure schemes.

4.7. Use of Capital Receipts to Reduce MRP Charges

Any proposal to use capital receipts to reduce future MRP charges will be presented for approval in-line with the Council's Financial Procedure Rules prior to the application of the capital receipts.

4.8. Housing Revenue Account

The Housing Revenue Account (HRA) is not subject to a statutory requirement to make a minimum revenue provision. As a result, the MRP policy set out above only applies to borrowing to fund non HRA assets. However, the Council may make an annual voluntary provision for debt repayment in the HRA. The level of provision (if any) will be determined annually as part of the closure of the HRA.