cyngor monmouthshire county council sir fynwy

REPORT

SUBJECT:	**2024/25 Capital Strategy, 2024/25 Treasury Management Strategy, Revision to MRP Policy 2024/25**
DIRECTORATE:	**Resources**
MEETING:	**Governance & Audit Committee**
DATE:	**22nd February 2024**
DIVISION/WARDS AFFECTED:	**Countywide**

1. PURPOSE

1.1. Full Council delegates responsibility for the detailed implementation, monitoring and scrutiny of capital investment consequences, including treasury management policy, strategy and practices to the Governance & Audit Committee.

1.2. The purpose of this report is to collect the Committee's views and response to the Council's draft 2024/25 Capital and Treasury Management Strategies, including the Minimum Revenue Provision (MRP) policy.

1.3. The report also highlights a proposed revision to the Council's MRP policy for 2024/25 which the committee are asked to scrutinise.

1.4. As per prudential code requirements, following committee scrutiny the strategies and proposed revision to MRP policy will subsequently be reported to full Council for their own consideration and approval. This is scheduled for Council on the 29th February 2024.

2. RECOMMENDATIONS

2.1. That Governance & Audit Committee scrutinise the proposed change to MRP policy for 2023/24 as shown at ***Appendix 1*** and endorses the proposal for onward circulation and approval by full Council.

2.2. That Governance & Audit Committee considers the draft Capital strategy for 2024/25 as found at ***Appendix 2*** and endorses for onward circulation and approval by full Council.

2.3. That Governance & Audit Committee considers the draft Treasury management strategy for 2024/25 as found at ***Appendix 3*** and endorses for onward circulation and approval by full Council. This includes the:

- 2024/25 Minimum Revenue Provision Policy Statement, and;

- 2024/25 Investment & Borrowing Strategies

2.4. That Governance & Audit Committee note the requirement to review the Council's treasury management activities on behalf of the Council by continuing to receive quarterly treasury management activity updates during 2024/25 as per the requirements of the updated CIPFA Treasury Code of Practice.

3. Proposed revision to the Minimum Revenue Provision Policy for 2023/24

3.1. The Welsh Government updated its statutory guidance regarding MRP in 2018 providing advice on how local authorities may determine prudent charges for MRP. This guidance was issued by Welsh Ministers under section 21(1A) of the Local Government Act 2003 [Revised 2018] and is effective from 1st April 2019. The four options for prudent provision remain as indicated above but with two alternative options under Option 3 as follows:

Option 3(a) – Equal Instalment Method
Option 3(b) – Annuity Method

3.2. For supported borrowing the Council is currently adopting Option 3(a) whereby MRP is based on 2% per annum, equivalent to equal instalments over an assumed 50 year life.

3.3. Neither the guidance nor legislation defines what is prudent. It is therefore a decision for each council to manage this appropriately and to determine prudent repayment based on its own individual circumstance. This will involve taking account of medium/long term financial plans, current budgetary pressures, current and future capital expenditure plans, funding needs and any longer term transformational plans.

3.4. The current MRP policy when combined with the cost of interest on outstanding borrowing places a significant burden on the Council's revenue budget, and these charges are biased towards the early years of the asset rather than being spread more evenly across the whole life of the asset.

3.5. There is also inconsistency in approach between supported and unsupported borrowing which is an additional administrative burden for the financial management of MRP.

3.6. The Council has undertaken a review to determine whether this remains the most appropriate method and whether adoption of 3(b) - the Annuity Method for supported borrowing would result in a more prudent provision than the current Equal Instalment Method.

3.7. In forming an opinion the Council has given regard to the Chartered Institute of Public Finance and Accountancy's (CIPFA) publication *"Practitioners' Guide to Capital Finance in Local Government"* which states the following:

"*it is arguably the case that the annuity method provides a fairer charge than equal instalments as it takes account of the time value of money, whereby paying £100 in 10 years' time is less of a burden than paying £100 now. The schedule of charges produced by the annuity method thus results in a consistent charge over an asset's life, taking into account the real value of the amounts when they fall due. The annuity method would then be a prudent basis for providing for assets that provided steady flow of benefits over their useful life.*"

3.8. It is therefore considered that the equalisation of MRP under an annuity-based calculation will have the effect of ensuring that current and future generations will consume equal benefits from the Council's capital assets.

3.9. The proposals above demonstrate that the policy is consistent, affordable over the longer term and ensures a more equitable spread of debt repayment costs across all generations of taxpayer.

3.10. The change also ensures alignment of policy between supported and unsupported borrowing and removes a level of administrative burden and complexity for finance team in the management of MRP.

3.11. It is therefore proposed that Council are asked to approve a change in MRP policy to the following methods:

Type of Expenditure	**Option Applied**	**MRP Calculation**
Supported Borrowing funded Expenditure	Option 3	Calculated on an annuity basis over the expected useful life of an asset. The MRP element increases over time to reflect a consistent charge over life of the assets taking into account the real value of money.
Unsupported Borrowing funded Expenditure	Option 3	Calculated on an annuity basis over the expected useful life of an asset. The MRP element increases over time to reflect a consistent charge over life of the assets taking into account the real value of money.

3.12. **Financial implications**

3.13. The revised MRP calculation will be based on charging the expenditure over the expected useful life of the relevant asset as the principal repayment on an annuity with an annual interest rate equal to the average relevant PWLB rate for the year of expenditure, starting in the year after the asset becomes operational.

3.14. A consequence of this more prudent provision is significant MRP savings over the medium term:

Financial Year	Estimated Current MRP £'000	Revised MRP £'000	Difference £'000
2023/24	1,812	805	-1,007
2024/25	1,861	861	-1,000
2025/26	1,861	891	-970
2026/27	1,861	922	-939
2027/28	1,861	954	-907

3.15. Annual monetary savings continue to 31st March 2047 by applying the Annuity Method together with an increased annual cost thereafter albeit recognising the time value of money. Crucially, the overall amount of provision remains the same, and ensures that full provision is made over time to match the debt needing to be repaid.

4. 2024/25 Capital Strategy

Overview

4.1. The Capital Strategy sets out the longer-term context in which capital investment decisions are made and demonstrates that the Authority takes capital investment decisions that are in line with its Corporate priorities, and gives consideration to both risk, reward and impact. It also demonstrates that these decisions are taken whilst having proper regard to the stewardship of public funds, value for money, prudence, sustainability and affordability.

4.2. The capital plans of the Authority are inherently linked with the treasury management activities it undertakes, and therefore this report is brought alongside the Treasury management strategy report.

4.3. The main considerations arising from the Capital strategy shown in ***Appendix 2*** are summarised in this report below.

4.4. The Capital strategy gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability.

4.5. The Cabinet's Community and Corporate Plan establishes a clear purpose to become a zero-carbon county, supporting wellbeing, health and dignity for everyone at every stage of life and sets the goals for Monmouthshire to be a:

- A Fair place to live where the effects of inequality and poverty have been reduced;
- A Green place to live and work, with reduced carbon emissions, and making a positive contribution to addressing the climate and nature emergency;

- A Thriving and ambitious place, where there are vibrant town centres, where businesses can grow and develop;
- A Safe place to live where people have a home and community where they feel secure;
- A Connected place where people feel part of a community and are valued;
- A Learning place where everybody has the opportunity to reach their potential.

4.6. Achievement of these objectives will be pursued via actions driven by an array of enabling plans and individual service plans. In some instances, these actions will involve a requirement for capital investment.

4.7. A large degree of capital investment is funded from grants, or internal resources such as capital receipts and specific reserves, which do not impact on borrowing levels, but where borrowing is required, it is important that the approved limits are not exceeded.

4.8. This is an important area of overall financial management governance in that debt funded capital expenditure, and the external borrowing that results, locks in the Council into financing costs sometimes for as long as 50 years. These costs are comprised of the external loan interest costs and the provision for financing the debt funded capital expenditure, known as Minimum Revenue Provision (MRP).

4.9. In the current climate of financial constraints and a continued Medium Term Financial Projection (MTFP) revenue budget gap, capital investment needs to remain within affordable limits. Demand for capital resources remains high and therefore inevitably, prioritisation of projects, leveraging in other sources of funding and working with partners remain key to meeting this demand.

4.10. Within the context of significant demands for capital resources and limited availability, there is the need to develop and link our use of the various strategic plans across the organisation which drive the need for capital investment and develop alternative strategies to meet demand so the Councils own capital programme is prioritised within an affordable framework.

4.11. **Setting Capital Budgets**

Final 2024/25 Capital Medium Term Financial Plan

Scheme Type	**Indicative Budget 2024/25**	**Indicative Budget 2025/26**	**Indicative Budget 2026/27**	**Indicative Budget 2027/28**
Asset Management Schemes	2,630,049	2,230,049	2,230,049	2,230,049
School Development Schemes	19,456,606	4,151,797	0	0
Infrastructure & Transport Schemes	6,144,740	4,204,740	4,204,740	4,204,740
Regeneration Schemes	150,000	730,200	730,200	730,200
Inclusion Schemes	1,150,000	1,200,000	1,200,000	1,200,000
ICT Schemes	303,000	413,000	413,000	413,000
Vehicles Leasing	1,500,000	1,500,000	1,500,000	1,500,000

Capitalisation Directive	3,357,500	507,500	507,500	507,500
Other Schemes	550,000	570,000	570,000	570,000
Total Expenditure	**35,241,896**	**15,507,287**	**11,355,490**	**11,355,490**

4.12. The capital MTFP and capital strategy seek to work towards a financially sustainable core capital programme, whilst balancing the need to deliver capital investment plans in line with policy commitment and need.

4.13. The current capital MTFP does not cover all the capital budget pressures that have been identified. This shows that there is more demand for capital spending than the Council considers it can reasonably afford. This means that capital schemes will have to be ranked or the capital available has to be divided more widely than is ideal.

4.14. All stakeholders must understand that paying for capital spending by borrowing only pushes the cost to revenue budgets over future years, but at the same time if capital maintenance works are put off then the total lifetime costs of keeping an asset are likely to go up. This effect is often hidden in medium term financial planning as asset lives are much longer than four years.

4.15. The capital programme includes yearly investment for property maintenance, highways maintenance, relevant specific capital grants and the future schools programme. This will help to deal with the most urgent backlog issues, focussing on worst condition first and related risk. However, estate rationalisation programs, closure/disposal of assets, asset transfers and other capital projects to refurbish or replace operational properties will also be used to reduce the backlog funding needed. This will not solve the specific total backlog but is a way of targeting the main issues in a reasonable way.

4.16. **Capital Financing**

4.17. All capital expenditure incurred has to be physically financed. Once the finite available sources of internal financing (capital receipts, reserves/revenue) and external grant financing are extinguished the Authorities only recourse is to debt (borrowing).

Medium term capital financing

Financing source	**Final Budget 2024/25**	**Indicative Budget 2025/26**	**Indicative Budget 2026/27**	**Indicative Budget 2027/28**
Debt	14,489,533	8,221,113	7,782,990	7,782,990
External sources	16,351,863	6,215,674	2,502,000	2,502,000
Capital Receipts	4,147,500	967,500	967,500	967,500
Reserves	253,000	103,000	103,000	103,000
Total Funding	**35,241,896**	**15,507,287**	**11,355,490**	**11,355,490**

4.18. Approval of capital expenditure funded through borrowing locks the Council into committing revenue funding over a very long period (as long as 50 years). Minimum Revenue Provision (MRP) is required to be funded from revenue budgets to cover expected borrowing repayments and the level of MRP is increasing over the medium-term so the Authority needs to ensure its capital plans remain affordable and sustainable.

Proportion of financing costs to net revenue stream

Proportion of financing Costs to net revenue stream	**2023/24 Estimate £m's**	**2024/25 Estimate £m's**	**2025/26 Estimate £m's**	**2026/27 Estimate £m's**	**2027/28 Estimate £m's**
Net Interest payable	6.6	5.9	6.9	7.1	7.1
MRP	6.0	6.2	6.7	7.0	6.7
Total Financing costs	**12.6**	**12.1**	**13.6**	**14.1**	**13.8**
Net Revenue Stream	189.6	198.5	203.2	208.1	213.2
Proportion of net revenue stream %	**6.65%**	**6.09%**	**6.72%**	**6.74%**	**6.48%**

4.19. The table above compares financing costs to the net revenue stream i.e. the amount of income from Council Tax, business rates and general government grants. The overall proportion of financing costs remains fairly stable over the MTFP window which is reflective of the total revenue stream increasing in line with expected inflationary impacts whilst the financing costs increase moderately in line further capital investment made, most notably the completion of the new Abergavenny 3-19 school.

4.20. Total financing costs remain sustainable within the context of the Authorities overall revenue budget in so much that they are fully provided for within the medium term financial plan.

Ongoing Capital Programme Development

4.21. In light of continuing funding constraints, it is important that the Council understands the key risks and future aspirations for capital investment. These are captured through various plans and strategies across the Council. There will be a range of priorities originating from these plans which will look to deliver on aspirational long term objectives such as the decarbonisation agenda and affordable housing.

4.22. Alongside this, it is important to consider the requirement to maintain the Councils current asset base. As noted previously, this is something that has been severely impacted by constrained funding levels in previous years and has resulted in a maintenance backlog developing, which gives rise to the potential for major asset failures to occur where issues have developed over time. Although the risks associated are captured through ongoing condition surveys and monitoring, it is inevitable that as time progresses that more significant sums of investment will be required to maintain or substantially refurbish ageing assets.

4.23. There will inevitably be other priorities to be considered for inclusion within the capital programme over the medium to longer term, with the next phase of WG’s Sustainable Communities for Learning Programme and further regeneration schemes that will require substantial match funding commitments. The consideration to support such priorities will need to be carefully balanced against other competing demands.

4.24. **Capital Receipts**

4.25. In circumstances where property is deemed surplus to requirements and can be sold, the Disposal Strategy within the Asset management strategy (AMS) provides the process by which this happens and considerations for doing so. To enable a consistent approach to the disposal of surplus land and property, the Disposal policy clarifies the circumstances within which the council will achieve its requirements for best consideration, whilst supporting the Council's objectives as per the Community & Corporate Plan and AMS.

Forecast Capital receipts

	2023/24	2024/25	2025/26	2026/27	2027/28
	£000	£000	£000	£000	£000
Balance as at 1st April	12,446	8,785	7,004	6,700	5,835
Less: capital receipts used for financing	(2,778)	(1,815)	(460)	(460)	(460)
Less: capital receipts used to support capitalisation directive	(3,008)	(3,358)	(508)	(508)	(508)
Capital receipts for Redundancies	(1,000)	0	0	0	0
Capital receipts Received	1,043	0	0	0	0
Capital receipts Forecast	2,092	3,393	663	103	103
Forecast Balance as at 31st March	**8,785**	**7,004**	**6,700**	**5,835**	**4,970**

4.26. The value of Capital receipts forecast after 2024/25 drops off quite considerably which is reflective of the replacement local development plan (RDLP) not proceeding as quickly as envisaged in the original delivery agreement. Whilst candidate sites have now been submitted, this will have an impact on the balance of receipts available to fund future capital investment demands in the near term.

4.27. Traditionally receipts have been earmarked to finance the Authorities future schools investment. Whilst the Council has further future schools aspirations, in recent years it was not proposed to advocate a similar approach to members in respect of tranche B. Schools based assets commonly have a useful life of 50 years+, and as such traditional long term loan funding can be sourced at competitive rates with limited annual revenue volatility. The Council derives greater revenue benefit by using capital receipts in affording replacement of short life assets, given the avoidance of proportionately more significant minimum revenue provision.

5. 2024/25 Treasury Management Strategy

Overview

5.1. The treasury management strategy sets out the Council's longer term borrowing requirement and plans, which is driven mainly by the capital programme requirements and the resulting impact on the revenue budget.

5.2. It includes how it will manage and invest its surplus cash which also have various targets/limits set as part of prudential indicators, treasury management indicators and also includes additional guidance of the Welsh Government Investment Guidance and the Minimum Revenue Provision Policy.

5.3. Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the TM Code) which outlines that capital expenditure plans should be:

Affordable: It is important that the Council's capital investment remains within sustainable limits. The Code requires Councils to consider the resources currently available to them and those estimated to be available in the future, together with the totality of the capital plans and income and expenditure forecasts. As well as capital expenditure plans, Councils should consider the cost of past borrowing, ongoing and future maintenance requirements, planned asset disposals and the MRP policy, which all impact upon affordability.

Prudent: All external borrowing and other long-term liabilities are within prudent levels. The full Council set an authorised limit and operational boundary for external debt, these need to be consistent with the Council's plans for affordable capital expenditure and financing, and with its treasury management policy statement and practices.

Sustainable: taking into account the arrangements for repayment of debt (including through MRP) and consideration of risk and the potential impact on the Council's overall financial sustainability in the medium to longer term.

5.4. The Governance & Audit Committee in its role as the Council's delegated body to review and scrutinise the authority's financial affairs must receive as a minimum a quarterly treasury update report including an annual report after its close on treasury management activities during the year.

5.5. Overall responsibility for treasury management remains with the full Council. In effect, that body delegates the execution and administration of treasury management decisions to the Section 151 officer or deputy who will act in accordance with the Treasury management strategy, treasury management practices and CIPFA's Standard of Professional Practice on treasury management.

5.6. The detailed Treasury strategy for 2024/25 is included at ***Appendix 3***. Key points of interest are summarised below.

Annual Minimum Revenue Provision (MRP) Policy Statement

5.7. The annual Minimum Revenue Provision is the mechanism used for spreading the capital expenditure financed by borrowing over the years to which benefit is provided. Regulations state that the authority must calculate for the current financial year an amount of minimum revenue provision which it considers to be prudent. In addition, there is the requirement for an Annual Minimum Revenue Provision Policy Statement to be drafted and submitted to full Council. This is shown in section 8 of the strategy. The policy also makes consideration of the Welsh Government MRP guidance.

5.8. The policy proposed for 2024/25 is consistent with the changes proposed within this report to revise the policy for 2023/24:

Type of Expenditure	Option Applied	MRP Calculation

Supported Borrowing funded Expenditure	Option 3	Calculated on an annuity basis over the expected useful life of an asset, whereby the MRP element increases over time to reflect a consistent charge over life of the assets taking into account the real value of money
Unsupported Borrowing funded Expenditure	Option 3	Calculated on an annuity basis over the expected useful life of an asset, whereby the MRP element increases over time to reflect a consistent charge over life of the assets taking into account the real value of money
Leases and PFI	N/A	MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability

Borrowing Strategy

5.9. Given the significant cuts to public expenditure over recent years and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

5.10. By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal / short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years.

5.11. The Council has previously raised the majority of its long-term borrowing from the PWLB and expects to continue to do so during 2024/25. PWLB loans are no longer available to local Councils planning to buy investment assets primarily for yield and the Council intends to avoid this activity in order to retain its access to PWLB loans.

5.12. Short term borrowing has traditionally been sourced from the inter-Local authority market and this is expected to continue during 2024/25 as it provides a low administration cost option for borrowing at competitive rates of interest.

Investment Strategy

5.13. Both the CIPFA Code and the WG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income

5.14. The Authority continues to hold a minimum of £10m of investments to meet the requirements of a professional client under the Mifid II regulations (Markets in financial instruments directive) and therefore consideration will continue to be given to investing balances with a more medium to long term outlook, albeit within the confines and framework of the internal borrowing approach outlined above.

5.15. The existing portfolio of strategic pooled funds currently provides a degree of risk diversification into different sectors, however the Council will closely monitor the returns on these investments in light of a heightened interest rate environment.

5.16. The approved counterparty list and limits are shown in the Treasury strategy. The investment limits proposed complement the Authorities objective of striking an appropriate balance between risk and return, whilst minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

5.17. It is important to note that the counterparty rating limits and investment maturities act as limits and not targets and are further informed by market information alongside bespoke periodic advice from our treasury advisers as to sustainability and financial robustness of specific counterparties.

Environmental, social and governance (ESG) policy

5.18. Environmental social and governance (ESG) considerations are increasingly a factor in global investors' decision making, but the framework for evaluating investment opportunities is still developing and therefore the Council's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level.

5.19. When investing in banks and funds, the Council will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.

5.20. An updated list of signatories to the three charters is provided by the Authority's treasury advisors each quarter and will continue to be monitored. Any counterparties not signed up to all three charters will be removed from the Authorities investment portfolio.

5.21. The Council will continue through 2024/25 to engage with its advisors Arlingclose to evaluate its existing investments and assess whether a more sophisticated ESG policy can be applied. Governance and Audit Committee will be kept informed of progress through the regular reporting of treasury performance into committee.

Prudential Indicators

5.22. The prudential and treasury indicators as recommended under the Prudential Code are outlined within the Treasury strategy and set out the limits and indictors that the treasury function will operate under for 2024/25.

6. CONSULTEES:

Deputy Chief Executive (Section 151 officer)

Cabinet Member for Resources

Arlingclose – Treasury Management Advisors to Monmouthshire CC

Audit Wales

7. APPENDICIES:

Appendix 1 – Proposed revision to the MRP policy for 2023/24

Appendix 2 – 2024/25 Capital strategy

Appendix 3 **-** 2024/25 Treasury Management Strategy including the Minimum Revenue Provision policy statement and Investment & Borrowing Strategies

8. AUTHORS:

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