Chorley Council

Report of	Meeting	Date
Chief Finance Officer	Governance Committee	24th Jan 2018

IMPLICATIONS OF REVISED CIPFA PRUDENTIAL CODE AND TREASURY MANAGEMENT CODE AND DCLG GUIDANCE

PURPOSE OF REPORT

1. To update members on
   a. CIPFA's changes to the Treasury Management Code
   b. The proposals from DCLG to change the Prudential Framework of Capital Finance

RECOMMENDATION(S)

2. To note the contents of this report including:
   a. The changes to the Treasury Management Code and the introduction of a new Capital Strategy report.
   b. The proposed changes to the Prudential Framework of Capital Finance that include additional reporting requirements, potential restrictions on investing in assets purely for financial returns and the reduction in the maximum allowable number of years the cost of borrowing can be spread over.

EXECUTIVE SUMMARY OF REPORT

3. The Treasury Management code was last updated in 2011 and since this time councils nationally have begun to invest in assets for the purpose of income generation as well as other strategic objectives. This increasing trend has resulted in potential risks to a Council's revenue budget that may not be picked up in the current Treasury Management Code and reporting requirements.

4. The new treasury management code seeks to address this deficiency and introduces a new **Capital Strategy** report to be approved by Full Council in 2019/20. The report will replace the treasury management and investment strategy report and will include:

   a. a policy statement with the Council's high level policies for borrowing and investments and include policies where the Council has commercial investments held for financial return;
   b. a new treasury management practice that will require the Council to set out the investment management practices for non-treasury investments;
   c. a schedule that will include a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and contingent liabilities and the authority's risk exposure.

5. The consultation recognises the importance of delegating detailed processes to other committees. The Governance Committee will approve the detail and ongoing monitoring of the Capital Strategy, responsibility, at all times, however for the strategy, remains with Full Council.

Local Authorities Investment Code

6. There are many proposed changes to the code some of which follow a similar theme to the changes proposed above. The proposals are for the Council to disclose, presumably in the Capital Strategy report:
   a. the level of risk exposure and rate of return from its financial investments to Councillors;
   b. the dependence on commercial income to deliver statutory services and the amount of borrowing that has been committed to generate that income;
   c. additional disclosure by local authorities who borrow solely to invest in revenue generating investments
   d. the reliance on income from investments in funding core council activities

7. Chorley Council's response to this consultation did not object to additional disclosures provided that they do not compromise commercial confidentiality or jeopardise accruing higher returns from the Council's investments. The Council supports any disclosures that can support good risk management however it does not support disclosing how its 'core functions' are funded.

8. The consultation alludes to a restriction on councils investing in assets purely for generating returns. This would seemingly prohibit investment in assets outside of the Council's boundaries. This restriction of 'borrowing in advance of need' will not affect Chorley Council's current or future planes investments as they all meet other strategic goals such as regeneration and improving housing standards.

Guidance on calculation of Minimum Revenue Provision (MRP)

9. As part of the consultation the proposed changes to the calculation include:
   a. aligning it more closely with the capital financing requirement – Chorley Council supports this change
   b. reducing the maximum useful economic life for assets (other than freehold land) to 40 years – Chorley Council does not support this proposal as financing of some capital assets is spread over 50 years. This is considered to be prudent because it takes account of estimated asset lives provided by professional valuers. To date, the Council's external auditors have agreed financing charges (MRP) for these assets which are being spread over 50 years.

Confidential report Please bold as appropriate	Yes	**No**

Key Decision? Please bold as appropriate	Yes	**No**

REASONS FOR RECOMMENDATION(S)

(If the recommendations are accepted)

10. To provide the Governance Committee with an update on the changes to the Treasury Management Code and the Prudential Framework of Capital Finance.

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

11. Not applicable

CORPORATE PRIORITIES

12. This report relates to the following Strategic Objectives:

Involving residents in improving their local area and equality of access for all		A strong local economy	
Clean, safe and healthy homes and communities		An ambitious council that does more to meet the needs of residents and the local area	✓

TREASURY MANAGEMENT CODE

13. The Treasury Management Code was last updated in 2011 and since then the introduction of the Localism Act has resulted nationally in a significant increase in council's investment and asset portfolios, with subsequent increases in borrowing. As such CIPFA considered it a good time to revise the code and guidance notes. The updated code was published by CI{FA in December 2017.

14. The main theme running through the changes to the code is that non-treasury investments (investments that don't relate to managing cash flow and debt) should now be included in the Council's treasury management strategic reports. These changes include:

    a. the policy statement should include the organisation's high level policies for borrowing and investments and include policies where the organisation has commercial investments held for financial return;
    b. the introduction of a new treasury management practice that will require the Council to set out the investment management practices for non-treasury investments;
    c. the creation of a schedule that will include a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and contingent liabilities and the authority's risk exposure.

15. Suggested schedules to accompany the statement of treasury management practices include:

    a. Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios
    b. Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments
    c. Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision-making in relation to non-treasury investments, and arrangements to ensure that appropriate professional due diligence is carried out to support decision making
    d. Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken
    e. Training and qualifications (TMP10 and schedules), including how the relevant knowledge skills in relation to non-treasury investments will be arranged

16. The changes to the code will result in a new **Capital Strategy** report that will replace the existing Treasury Management and Investment Strategy reports. The Capital Strategy report will be approved annually by Full Council. Approval of the detailed processes related to the report may be delegated to a committee provided that this facilitates a more active discussion of the strategy and performance by those with the most appropriate skills and knowledge. It is proposed that monitoring of the strategy be delegated to the Governance Committee.

PRUDENTIAL FRAMEWORK OF CAPITAL FINANCE

17. On the 9th November 2017 the government released a consultation on changes to:
    a. Local Authorities Investment Code
    b. Minimum Revenue Provision Guidance

    Officers submitted a response to the consultation on 22nd December 2017. The response is found in appendix 1 to this report.

<u>Local Authorities Investment Code</u>

18. The Statutory Guidance on Local Authority investments has not been updated since 2010. As Local Authorities are considering more innovative types of investment activity the Government decided to consult on changes to the code. The Government believes that local authorities need to be better at explaining “why” not just “what” they are doing with their investment activity. That means there is a need to demonstrate more transparency and openness and to make it easier for informed observers to understand how good governance and democratic accountability have been exercised.

19. The revised guidance retains the requirement for an Investment Strategy to be prepared at least annually. However, in recognition that the CIPFA consultation on the Prudential Code introduces a new requirement for local authorities to prepare a **Capital Strategy**, the revised guidance specifically allows the matters required to be disclosed in the Investment Strategy to be disclosed in the Capital Strategy.

20. The revised guidance requires the Council to report to members so that they understand the total exposure of their local authority due to borrowing and investment decisions and that this information is presented in such a way that allows them to compare any change in exposure from year to year. The guidance <u>does not</u> specify what indicators should be used, however it did suggests benchmarking against other authorities.

21. The Council supports the disclosure of risk exposure and rate of return from its financial investments to Councillors. It also supports disclosures to the public so long as it does not jeopardise any commercial confidentiality or if it reduces the potential rate of return by weakening the Council’s bargaining position. The Council agreed that specific indicators and thresholds should not be introduced as the consultation rightly states that the level of risk appetite is specific to each local authority. For the same reason, it does not support the proposal of benchmarking indicators against other authorities.

22. The Government believes that where local authorities invest in non-financial assets, they should apply the principles of prioritising security and liquidity over yield in the same way that they are required to do for financial assets. The revised guidance seeks to apply existing definitions to non-financial assets (investment in income generating assets):

    a. Security: the revised guidance recognises that a local authority will normally have an asset that can be used to recoup capital invested. Therefore, the revised guidance requires local authorities to consider whether the underlying asset is impaired and if it is, to detail the actions planned or in progress to protect the funds invested.
    b. Liquidity: the revised guidance requires local authorities to set out the procedures for ensuring that funds invested in a non-financial asset can be accessed when they are needed

23. In the response Chorley Council didn’t object to the definitions however it was stressed that it is a decision for each individual council to consider what the optimum balance is for yield, security and liquidity. In some circumstances it is probable that yield will be a more important

consideration than liquidity however it will always be the case that all three principles will be considered when making an investment.

Proportionality

24. The Government is concerned that some local authorities may become overly dependent on commercial income as a source of revenue for delivering statutory services. Given the nature of assets that local authorities are investing in this could leave them exposed to macro-economic trends. For this reason the Government proposes requiring local authorities to disclose their dependence on commercial income to deliver statutory services and the amount of borrowing that has been committed to generate that income. Specifically

   - detail the extent to which funding expenditure to meet the core functions of the local authority is dependent on achieving the expected net yield
   - detail the local authority's contingency plans should it fail to achieve the expected net yield

25. In response Chorley Council agreed with the overall concept of proportionality and did not object to principle of the additional disclosures outlined in the draft guidance however the requirement to state what level of core functions are funded through expected yield should be removed as it is not clear what the definition is for these core functions. The Council believes the risk to the council's balanced budget of not generating investment yields will also be outlined in the Council's MTFS.

Borrowing in Advance of Need

26. The consultation suggests that borrowing solely to invest rather than to deliver statutory services or strategic objectives is considered to be borrowing in advance of need. The Government believes that it is appropriate for the revised guidance that recognises this and the consultation requires additional disclosure by local authorities who borrow solely to invest in revenue generating investments

27. This definition of borrowing in advance of need has led to many news stories suggesting that the Government wishes to clamp down on the amount of borrowing Councils undertake to generate income. A clarification has been requested as part of the consultation with the following response by the Government:

   We do not want to restrict opportunities for local authorities to use commercial structures to kick start local economic regeneration to deliver services more effectively. However, the prime duty of a local authority is to provide services to local residents, not to take on disproportionate levels of financial risk by undertaking speculative investments, especially where that is funded by additional borrowing.

   For this reason we are proposing that all local authorities disclose the contribution that each investment makes towards the core objectives of the local authority. The proposals also make it clear that borrowing solely to fund yield generating investments is borrowing in advance of need. Local authorities will be able to borrow to fund investments that have multiple objectives, including generating yield.

28. Chorley Council's capital investments, including planned investments included in the MTFS, in yield (surplus) generating assets all have superior objectives such as the regeneration of the town centre, the creation of local jobs and the improvement in the standards of local housing. This restriction on borrowing in advance of need would seem to prohibit investments in assets outside of the Council's boundaries. As such this change is <u>not seen as a risk to the Council</u> however it could restrict future investments if the Council chose to pursue such non-local investment.

GUIDANCE ON CALCULATION OF MINIMUM REVENUE PROVISION (MRP)

29. MRP Definition: “provision for the borrowing which financed the acquisition of the asset should be made over a period bearing some relation to that over which the asset continues to provide a service”.

30. The Government proposes to change the definition of prudent provision to one that requires local authorities to set MRP in a way that covers the gap between the Capital Financing Requirement and the amount of that requirement that is funded by income, grants and receipts. Chorley Council responded with no objection to this proposal.

31. The Government has concerns that some local authorities may be setting artificially long asset lives to reduce the annual charge for MRP and thereby deferring revenue costs into future years. The Government does not believe that this is a prudent approach and for this reason the updated Guidance includes a maximum useful economic life of 50 years for freehold land and 40 years for other assets. The useful economic lives have been selected with commonly used practices in depreciation accounting in mind

32. Chorley Council does not agree with a maximum useful life of 40 years for assets other than freehold land. We have specific examples of assets where the useful life has been identified by our valuer to be longer than suggested in the draft guidance. Our external auditors have already accepted as being prudent longer periods for charging MRP. To reduce the MRP period by 10 years from 2018/19 onwards would not cost the Council any more in total, but re-phasing of MRP would add to budget pressure in the short term. In the longer term the asset would continue in use but no MRP would be chargeable in later years.

NEXT STEPS

33. What is clear from these consultations is that additional disclosures will need to be made regarding the risks of the various investments the Council has made and will make. These disclosures should be created and agreed by Chorley Council and reported through the Capital Strategy report.

34. CIPFA recognises that the Capital Strategy cannot be created in time for the 2018/19 budget setting process. However it is proposed to this committee that an additional note is appended at the end of the Treasury Strategy 2018/19. This will summarise the future non-treasury investments that could be arise as part of the Medium Term Financial Strategy (MTFS).

35. Further guidance is expected from CIPFA regarding the format of the Capital Strategy report. The first draft of the report will be taken to Governance Committee during 2018/19 in time for feedback and amendments for the final report to be taken with the budget setting papers in February 2019.

36. The Governance Committee will approve the detail and ongoing monitoring of the Capital Strategy, responsibility, at all times, however for the strategy, remains with Full Council.

37. The Council does not deem it necessary to adjust its MRP calculations for future investment proposals from 50 years to 40 years. This would have an impact on the forecast borrowing costs of investments such as the extension to Market Walk and the Digital Office Park. However the Council feels that the current 50 year calculation on its long term assets is sufficiently prudent and should not be adjusted.

IMPLICATIONS OF REPORT

38. This report has implications in the following areas and the relevant Directors' comments are included:

Finance	✓	Customer Services	
Human Resources		Equality and Diversity	
Legal		Integrated Impact Assessment required?	
No significant implications in this area		Policy and Communications	

COMMENTS OF THE STATUTORY FINANCE OFFICER

39. The various consultations will require the Council to produce an annual Capital Strategy report. This will be taken to Full Council in February 2019 for approval and taken to Governance Committee before this time to agree the format and content. More guidance surrounding this new report is expected in 2018/19.

40. The Council is not planning to retrospectively adjust the MRP calculations for assets currently in the calculation with lives of more than 40 years, this includes Market Walk. If the changes to the calculation of MRP were to be implemented retrospectively by the Council it would have a £100k negative impact on the revenue budget, predominantly due to the shopping centre.

41. The changes to the MRP calculation remain purely guidance for the Council. There is nothing preventing the Council from continuing to use 50 years however it may result in an adverse audit opinion as part of accounts closure.

COMMENTS OF THE MONITORING OFFICER

42. No Comment

GARY HALL
CHIEF FINANCE OFFICER

Background Papers			
Document	**Date**	**File**	**Place of Inspection**
CIPFA "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes, 2017 Edition"	December 2017	Electronic	Town Hall

Report Author	**Ext**	**Date**	**Doc ID**
James Thomson/Michael Jackson	5025/5490	16/01/18	

Appendix 1 Consultation on the proposed changes to the prudential framework of capital finance – December 2017

The consultation provides changes to and draft guidance of:

- Local Authorities Investment Code
- Minimum Revenue Provision Guidance

Statutory Guidance on Local Authority Investments

Transparency and democratic accountability (paragraphs 12-16)

The revised guidance retains the requirement for an Investment Strategy to be prepared at least annually. However, in recognition that the CIPFA consultation on the Prudential Code introduces a new requirement for local authorities to prepare a Capital Strategy, the revised guidance specifically allows the matters required to be disclosed in the Investment Strategy to be disclosed in the Capital Strategy.

Question 1: Do you agree with the proposed change? If not why not; and what alternative would you propose?

Chorley Council has no objection

Principle of Contribution (paragraph 17)

The core function of a local authority is to deliver statutory services to local residents. Where a local authority chooses to invest in non-core activities, management time and resource will be diverted from that core function. Where a local authority is investing in a yield bearing investment, the contribution may be the net return that can be invested in core activities. However, the Government is aware that investments made by local authorities may have more than one objective and as a result a local authority may have a different risk appetite to that it would have if investing solely for yield. For this reason the Government believes that a new principle requiring local authorities to disclose the contribution that non-core investments make towards core functions is important.

Question 2: Do you agree that it is important for local authorities to disclose the contribution that investment activities make to their core functions? If not why not; and what alternative would you propose?

Question 3: Are there any other measures that would increase the transparency of local authority financial and non-financial investments that you would suggest for inclusion in the Investments Guidance to assist scrutiny by the press, local taxpayers and councillors?

Chorley Council has held property investments for many years, the income from which forms a core part of its budget. It will be impossible to define what is “core” and “non-core” in a meaningful and helpful way.

The Revised Guidance on Local Government Investments suggests it does not want to prescriptive. Chorley Council supports this approach and does not believe it is possible to benchmark meaningfully against similar investments by other authorities due to the often complex nature of each investment.

Use of indicators to assess total risk exposure (paragraphs 18-20)
The Government believes that it is important that Councillors or the equivalent, understand the total exposure of their local authority due to borrowing and investment decisions and that this information is presented in such a way that allows them to compare any change in exposure from year to year.

For this reason the Government proposes introducing a new requirement to include quantitative indicators that will allow assessment of exposure. The Government recognises that different local authorities will have different financial positions and risk appetite. For this reason the Government does not propose to specify particular indicators or thresholds.

Question 4: Do you agree with the introduction of a requirement to enable Councillors to assess total exposure from borrowing and investment decisions? If not why not; and what alternative would you propose?
Question 5: Do you agree with the decision not to specify indicators or thresholds? If not why not; and what alternative would you propose?
The Council supports the disclosure of risk exposure and rate of return from its financial investments to Councillors. It also supports disclosures to the public so long as it does not jeopardise any commercial confidentiality or if it reduces the potential rate of return by weakening the Council's bargaining position.

Chorley Council agrees that specific indicators and thresholds should not be introduced as the consultation rightly states that the level of risk appetite is specific to each local authority.

Extension of principle of Security, Liquidity and Yield to non-financial investments (paragraphs 21-36)
The Government believes that where local authorities invest in non-financial assets, they should apply the principles of prioritising security and liquidity over yield in the same way that they are required to do for financial assets.
The Government recognises that the risks to security and liquidity for non-financial assets are different to those for financial assets. For this reason the Government proposes the following definitions for non-financial assets:

- **Security**: the revised guidance recognises that a local authority will normally have an asset that can be used to recoup capital invested. Therefore, the revised guidance requires local authorities to consider whether the underlying asset is impaired and if it is, to detail the actions planned or in progress to protect the funds invested.
- **Liquidity**: the revised guidance requires local authorities to set out the procedures for ensuring that funds invested in a non-financial asset can be accessed when they are needed.

Question 6: Do you agree with the extension of the principles of security and liquidity to non-financial assets? If not why not; and what alternative would you propose?
Question 7: Do you agree with the definitions of liquidity and security for non-financial assets? If not why not; and what alternative would you propose?
Chorley Council does not object to the definitions of liquidity or security however it must be noted that when considering an investment in non-financial assets the balance between yield, security and liquidity will be very different than for financial assets. Para 22 of the draft guidance states:

The generation of yield is distinct from these prudential objectives. However, this does not mean that local authorities are recommended to ignore potential revenues. Once proper levels of security and liquidity are determined, it will then be reasonable to consider what yield can be obtained consistent with these priorities.

Chorley council believes it is a decision for each individual council to consider what the optimum balance is for yield, security and liquidity. In some circumstances it is probable that yield will be a more important consideration than liquidity however it will always be the case that all 3 principles will be considered when making an investment.

Therefore Chorley Council does not agree with the extension of these principles to non-financial assets.

Introduction of a concept of proportionality (paragraphs 37-39)
The Government is concerned that some local authorities may become overly dependent on commercial income as a source of revenue for delivering statutory services. Given the nature of assets that local authorities are investing in this could leave them exposed to macro-economic trends. For example a decline in retail rental yield may leave a local authority that is highly dependent on retail rental income to deliver core services with a structural funding deficit.

For this reason the Government proposes requiring local authorities to disclose their dependence on commercial income to deliver statutory services and the amount of borrowing that has been committed to generate that income. Specifically

- detail the extent to which funding expenditure to meet the core functions of the local authority is dependent on achieving the expected net yield
- detail the local authority's contingency plans should it fail to achieve the expected net yield

Question 8: Do you agree with the introduction of a concept of proportionality? If not why not; and what alternative would you propose?
Chorley Council agrees with the overall concept of proportionality

Chorley council does not object to principle of the additional disclosures outlined in the draft guidance however the requirement to state what level of core functions are funded through expected yield should be removed. The Council believes the risk to the council's balanced budget of not generating investment yields will also be outlined in the Council's MTFS.

Chorley council does object to the following disclosure as any borrowing for investment purposes should be more than self-financing and so not impact on other borrowing capacity.

- Where a local authority has funded investment activity through prudential borrowing, the Strategy should detail the opportunity costs of using that borrowing capacity for investment rather than service delivery activity.

Borrowing in advance of need
Borrowing solely to invest rather than to deliver statutory services or strategic objectives has always been considered to be borrowing in advance of need. The Government believes that it is appropriate for the revised Guidance that recognises this and requires

additional disclosure by local authorities who borrow solely to invest in revenue generating investments.

Question 9: Do you agree that local authorities who borrow solely to invest should disclose additional information? If not why not; and what alternative would you propose?

The draft guidance states "Borrowing solely to invest in a yield bearing opportunity is borrowing in advance of need."

Under the current (2010) guidance it is clear that "borrowing in advance of need" relates solely to financial investments and financial instruments whereas investments such as commercial property rightly count as capital expenditure as they involve the acquisition of a physical asset and as such are eligible for funding from borrowing.

If the new guidance were to extend borrowing in advance of need to non-financial investments this would have a disastrous effect on the services Chorley Council could provide to its residents. It is a necessity for the council to continue to invest in yield bearing non-financial assets so as to balance the budget in future years and to therefore protect the services Chorley Council's residents. This is solely as a result of the continued large scale funding reductions from central government experienced over the past 7 years, including the recent changes to New Homes Bonus allocations.

The guidance states that if the council should invest in a yield bearing opportunity the Strategy should explain the policies in investing the money borrowed, including management of the risks. Chorley council supports full disclosure of information where this does not impair commercial confidentiality.

Capacity, skills and culture

The Investments Guidance has always required disclosure of the steps Treasury Management professionals have taken to ensure that they have sufficient knowledge and expertise to be able to take sensible decisions. The Government believes that it is sensible to extend this requirement to statutory officers, Councillors and other key individuals in the decision making process.

Question 10: Do you agree with the extension of the disclosure requirement on steps taken to secure sufficient expertise to include all key individuals in the decision making process? If not why not; and what alternative would you propose?

This seems to be an unnecessary burden. This disclosure arguably goes beyond the requirements of the Financial Conduct Authority in specifying requirements for local authorities to elect to act up to professional investor status under MiFID II, where decisions are delegated to officers, and so it is hard to see the justification for this. The disclosure requirement should be aligned with local decision making and specified locally.

Minimum Revenue Provision Guidance

Definition of 'Prudent Provision' in the MRP Guidance (paragraphs 19-22) Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 requires local authorities to make "prudent provision". The current MRP Guidance explains that "provision for the borrowing which financed the acquisition of the asset should be made over a period bearing some relation to that over which the asset continues to provide a service". The thinking behind this principle is that MRP is the cost that LAs recognise in their accounts instead of depreciation and therefore prudent provision should align to depreciation as far as is relevant.

Given that the purpose of MRP is to make prudent provision for debt the Government believes that this definition is slightly misleading. For this reason the Government proposes to change the definition of prudent provision to one that requires local authorities to set MRP in a way that covers the gap between the Capital Financing Requirement and the amount of that requirement that is funded by income, grants and receipts.

In doing so, local authorities will be able to better align the period over which they charge MRP to one that is commensurate with the period over which their capital expenditure provides a benefit.

Question 11: Do you agree with the change to the definition of the basis of MRP? If not why not; and what alternative would you propose?

We agree that the definition should be based on the borrowing requirement in the capital finance requirement.

Meaning of a charge to the revenue account (paragraphs 24 & 25)

Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 requires local authorities to make a charge to a revenue account. There have been some reports of local authorities who have determined that they have previously overpaid and as a result have made a credit to the account for MRP.

The Government does not believe that crediting the revenue account is either prudent or within the spirit of the approach set out in the Regulations. For this reason, the Government has included a clear statement in the updated Regulations that a charge to the account should not be a negative charge.

Question 12: Do you agree that the Guidance should clarify that a charge to an account cannot be a credit? If not why not; and what alternative would you propose?

There may be circumstances in which an MRP charge should be a credit, if a correction is required to deal with overprovision in previous years. Though Chorley Council does not anticipate having to make such a correction, we suggest that there should be flexibility to do so and to seek agreement of the external auditors.

Impact of changing methods of calculating MRP (paragraphs 26 & 27)

The Government continues to believe in the importance of allowing local authorities to have the flexibility to change the methods that it uses to calculate MRP from time to time.

However, the Government has concerns that some local authorities have been changing methodologies, not because the change would better allow them to make prudent provision, but instead to reduce their annual charge and in some cases to allow them to defer payments into future years. The Government does not believe that either of these rationales for changing methodologies are prudent.

For this reason, the Government has decided to clarify the approach to be adopted when changing the methodologies used to calculate MRP. Under the updated code, local authorities will be allowed to offset overpayments of MRP against charges in future years. However, the revised guidance makes it clear that an overpayment cannot be calculated retrospectively.

For example, if a local authority calculated MRP of £15m in 2013-14 and decided to charge £20m of MRP, it would have a £5m overpayment that could be offset against charges in future years. However, if the local authority changed its methodology in 2016-17 and based on the revised calculation determined that it should have charged £12m in 2013-14, it would still have a £5m overpayment that could be offset.

Question 13: Do you agree that changing MRP methodology does not generate an overpayment of MRP? If not why not; and what alternative would you propose?
This should be a matter for each council and their external auditor. There may be cases where preparation of the current year's statement of accounts leads to errors in calculation of MRP in earlier years being identified. If the errors were material the previous year's figures would be restated. If not material, the correction would be made in the current year. Every council should have the flexibility for a credit back to the local authority if that is appropriate.

Introduction of a maximum economic life of assets (paragraph 41)
Two of the four recommended options for calculating MRP in the Guidance use asset life as the denominator. The Government has concerns that some local authorities may be setting artificially long asset lives to reduce the annual charge for MRP and thereby deferring revenue costs into future years.

The Government does not believe that this is a prudent approach and for this reason the updated Guidance includes a maximum useful economic life of 50 years for freehold land and 40 years for other assets. The useful economic lives have been selected with commonly used practices in depreciation accounting in mind.

Question 14: Do you agree that the guidance should set maximum useful economic lives for MRP calculations based on asset life? If not why not; and what alternative would you propose?
Chorley Council supports this in principle, provided that the years specified in the guidance are seen as a guide rather than an absolute maximum. There should be flexibility to take account of local circumstances applying to specific assets, which may have maximum useful lives longer than those suggested in the guidance.

Question 15: Do you agree with the maximum useful economic lives selected? If not why not; and what alternative would you propose?
Chorley Council does not agree with a maximum useful life of 40 years for assets other than freehold land. We have specific examples of assets where the useful life has been identified by our valuer to be longer than suggested in the draft guidance. Our external auditors have already accepted as being prudent longer periods for charging MRP. To reduce the MRP period by 10 years from 2018/19 onwards would not cost the Council any more in total, but rephasing of MRP would add to budget pressure in the short term. In the longer term the asset would continue in use but no MRP would be chargeable in later years.

Implementation timetable

The Government would like both updated codes to come into force for the 2018-19 financial year.

Question 16: Do you agree that the codes should be implemented in full for 2018-19? If not, are there any specific proposals where implementation should be deferred, and what would be the implications of not doing so?

Chorley Council does not agree that the Local Authorities Investment Code and MRP Guidance should be implemented in full for 2018/19. Some of the proposed changes would have an effect on revenue budget provision in 2018/19. Preparation of that budget began several months ago, and will be at an advanced stage of completion at the point the proposals are finalised. To make budget changes at a late stage could be disruptive.

We would wish to brief members of the Council about the changes, offering training where appropriate. If the update code and guidance are adopted for 2018/19, there will be insufficient time to advise members about the changes before a number of reports reflecting the changes are presented to them.

Chorley Council suggests that implementation of any changes should be deferred to financial year 2019/20.