

TAUNTON DEANE BOROUGH COUNCIL

EXECUTIVE 25TH JUNE 2003

REPORT OF THE HEAD OF FINANCE

This Matter Is The Responsibility of Executive Cllr Williams (Leader of the Council)

COMMUTATION ADJUSTMENT

1. Purpose of Report

1.1 To brief the Executive on the historic, current and proposed treatment of the commutation adjustment within Taunton Deane's accounts.

2. The Legislative Background

2.1 On 1/10/92, the Secretary of State exercised powers (s157 of the 1989 Act) to make single payments to Councils to commute all entitlement to future years improvement grant subsidy on works carried out before 1992/93. Where Councils had outstanding PWLB debt, the payments instead of being made to the Council were made directly to the PWLB to reduce or extinguish debts.

2.2 This payment (the commuted sum) served to reduce the credit ceiling. The credit ceiling is a notional figure, i.e. it is a memorandum item rather than a "real" figure in the Statement of Accounts. In theory it measures the net indebtedness of the Council arising from past capital projects. It is also used as the basis (after some technical adjustments) for calculating the MRP (Minimum Revenue Position), which is the statutory amount, which the Council has to include within its budget for the repayment of debt.

2.3 The single payment made by the Govt reduced authorities indebtedness, thereby reducing its credit ceiling (notional) and as a consequence its MRP (real), and Debt Interest (real) charges to the revenue account.

2.4 However, this reduction was not enough to compensate Councils for the loss of the annual improvement grant subsidy received previously. The calculation of the MRP was therefore amended to include the "Commutation Adjustment". This was intended to "compensate" authorities, and to return their accounts to the position to that which would have been held if the commutation exercised had not taken place (i.e. over the lifespan of the commutation adjustment the overall effect should be nil).

2.5 The calculation of the commutation adjustment is set out in regulation 138 and Schedule 2 to the 1997 Regulations. The CIPFA guidance notes state "*the commutation adjustment adds considerable complexity to the calculation of the MRP and can result in substantial adjustments to the charge to be made to the Consolidated Revenue Account.*"

3. Taunton Deane's Position

- 3.1 Taunton Deane Borough Council have not been following the full requirements of this section of the 1989 Act in their Statement of Accounts. The situation is further complicated by the policy of "voluntary top-ups" to MRP, which was policy within Taunton Deane until the financial year 2001/02.
- 3.2 With the help of our treasury advisors, Sector, we have gone back through the Councils accounts to April 1992 and calculated the commutation adjustment for each financial year thereafter.
- 3.3 The relevant figures for each year are set out in Appendix 1.
- Column 1 shows the MRP figure that was charged to TDBC's accounts.
 - Column 2 shows the MRP figure that could have been charged to TDBC's accounts if we had followed the statutory provisions in their entirety (i.e. taken the commutation adjustment, and not had a voluntary top-up to the MRP figure).
 - Column 3 is the difference between the two.
- 3.4 In summary, the difference between what we have charged to the accounts, and what we were required to charge to the accounts over the period to the end of 2001/02 is £2,883,222.
- 3.5 During this period, TDBC operated a voluntary top-up to MRP policy, and this cannot be unwound. Reintroducing this to the equation reduces the above figure to £1,823,899 (Table b in Appendix 1). This lower figure is simply the aggregate value of previous years commutation adjustment, which the Authority had not made within the General Fund.
- 3.6 This £1.8m (or any amount up to this limit) can be taken back into this Councils accounts and transferred to the General Fund Reserve. However, there are ongoing costs associated with doing this - in simple terms, this is due to the commutation adjustment reducing the MRP, which in turn leaves the credit ceiling higher than it would have been. This higher credit ceiling means higher future annual MRP charges to the revenue account. The costs equate to roughly 4% of the "positive adjustment", plus an increase in debts costs borne by the General Fund.
- 3.7 In making the decision on how much of the £1.8m this Council "takes back into the accounts", it is important to consider:-
- The need for capital funding.
 - The future costs associated with it;
 - The aspirations of the Council re repayment of debt.
 - The impact of this decision on the new Prudential Regime.
- 3.8 Appendix 2 attempts to show the ongoing annual costs of returning the commutation adjustment to the Councils reserves in increments of £250,000.

- 3.9 The Council could choose not to take any of the £1.8m back to the General Fund Reserve – by leaving the funds in the accounts as they are, but describing them as the early repayment of debt.

4. The Choices

- 4.1 In addition to the £1.8m (which deals with the position up to the end of 2001/02) the Council has budgeted for the repayment of debt within the General Fund budget in both 2002/3 and 2003/4 under the existing (incorrect) method of calculation, a follows:-

	£
2002/3	116,500
2003/4	153,660
Total	<u>270,160</u>

These amounts will no longer be a cost to the General Fund, with the 2002/3 element being reported as part of the 2002/3 outturn report (thereby showing a larger underspend than that expected at Qtr 3). The 2003/4 element will be reported to Members at the first quarterly budget monitoring exercise.

- 4.2 The area of choice surrounds this Councils treatment of the £1.8m. It is clear that whilst there is a need for monies to support capital spending, this must be balanced with the ongoing revenue costs that this adjustment will incur.
- 4.3 The accounts presented to you next month must reflect your decision re the backdated commutation adjustment. This issue cannot be delayed for future financial years. It would be prudent therefore, to take the maximum commutation allowance now, and to take some time to consider how this should be best used to meet the Councils priorities. The funds if not required, will be returned to the reserve in 2003/04 and noted as early repayment of debt. This will be considered during the budget setting exercise later this year.
- 4.3 The impending introduction of the Prudential Regime will change all the current regulations re MRP, and the allocation of interest charges between the various Council Funds (ie HRA and General Fund). As stated in the report to the Executive in May 2003, some of the detail of the new system has not been published yet - therefore the future financial impact of this decision is based on the existing capital finance regulations.
- 4.4 District Audit have reviewed and audited our calculations and have accepted the position as shown in this report.

5. Impact on Corporate Priorities

- 5.1 The capital finance regulations underpin all aspects of local authority capital spending. The transfer of the commutation adjustment funds to earmarked capital reserves will offer this Council flexibility in delivering their corporate priorities.

6. Recommendation

6.1 The Executive is requested to note the current position on the commutation adjustment and to recommend Council to:

- a) Approve the transferring of the backdated commutation adjustment amounting to £1,823,899 to the General Fund Reserve and the immediate earmarking of these funds for capital purposes (RCCO in 2002/03);
- b) Approve the transfer of the 2002/03 commutation adjustment amounting to £116,500 to the General Fund Reserve and the immediate earmarking of this for capital purposes (RCCO in 2002/03);
- c) Approve the transfer of the 2003/04 commutation adjustment amounting to £153,660 to the General Fund Reserve and the immediate earmarking of this for capital purposes (RCCO in 2003/04).

Shirlene Adam
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Table A - Minimum Revenue Position 1992 – 2002

Year	Actual MRP Charged £	Statutory MRP £	Difference £
1992/3	951,339	852,329	99,010
1993/4	846,621	598,668	247,953
1994/5	844,175	624,896	219,279
1995/6	856,910	618,112	238,798
1996/7	875,968	599,743	276,225
1997/8	912,712	569,001	343,711
1998/9	859,022	524,540	524,540
1999/0	863,851	506,087	506,087
2000/1	992,888	454,269	454,269
2001/2	666,860	439,479	227,381
		Total	2,883,222

Table B - Minimum Revenue Position 1992 – 2002

Year	Actual MRP Charged £	Statutory MRP + Voluntary Top Ups £	Difference £
1992/3	951,339	899,773	51,566
1993/4	846,621	740,397	106,224
1994/5	844,175	619,297	124,878
1995/6	856,910	711,959	144,951
1996/7	875,968	705,940	170,028
1997/8	912,712	709,717	202,995
1998/9	859,022	631,303	227,719
1999/0	863,851	616,444	247,407
2000/1	992,888	716,277	276,612
2001/2	666,860	395,341	271,519
		Total	1,823,899

Impact of Adjustment to Credit Ceiling

Adjustment Value £	Annual MRP 'Cost' £	GF Interest Cost in 2003/4 £	Total Revenue Cost £
250,000	10,000	5,500	15,500
500,000	20,000	10,920	30,920
750,000	30,000	16,240	46,240
1,000,000	40,000	21,450	61,450
1,250,000	50,000	26,590	76,590
1,500,000	60,000	27,540	87,540
1,750,000	70,000	31,830	101,830
1,823,899	72,956	33,080	106,036