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Pool Rate for 2022-23 Onwards

Summary

1. This paper follows on from DSG (2021) paper 9 and investigates the financial impact of reverting from the current methodology of calculating the pool rate back to the old methodology.

Views sought

2. Members are asked to agree their preference of which methodology is used from the 2022-23 settlement onwards.

Previous papers

Distribution Sub-Group (2021) Paper 09 – Pool Rate for 2022-23 onwards

Background

3. The Partnership Council introduced a pool rate of interest for Welsh local authorities for the 2000-01 Settlement.
4. The pool rate is used to determine the debt financing element of the revenue settlement. The debt financing model calculates the estimated average outstanding debt for the settlement year and applies the pool rate to estimate the interest charged on this debt.
5. From 2010-11 onwards, the pool rate used to determine the debt financing element of the revenue settlement has had unsupported borrowing reversed out of total outstanding debt.
6. In May 2015, the DSG agreed that the basket of loans taken out through PWLB totalling £919 million to fund the buyout from the HRA subsidy scheme would be excluded from the pool rate calculations for the 2017-18 Settlement onwards.
7. In recent years, the DSG have felt that the year-on-year increases in the Pool Rate did not reflect the wider financial landscape, and therefore should be reviewed.
8. In response to DSG 2021 Paper 9, in the July meeting, the group suggested reverting back to the old pool rate methodology where unsupported borrowing is not reversed out, subject to assessing the financial implications of doing so.
9. This paper looks at the impact of reverting back to the old methodology.

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Analysis

10. Table 1, below, shows the divergence of the pool rate of interest when reversing and not reversing out the unsupported borrowing. This illustrates that, when leaving the unsupported borrowing in the model, the pool rate gradually reduces; however, when reversing the unsupported borrowing out of the model at the lower interest rate the pool rate gradually increases.

Table 1: Pool rate with and without reversing out unsupported borrowing

Year of pool rate model	10-11	11-12	12-13	13-14	14-15	15-16	16-17	17-18	18-19	19-20	20-21	21-22	22-23
Unadjusted pool rate	5.49	5.49	5.43	5.41	5.35	5.13	5.14	5.02	4.94	4.80	4.51	4.43	4.14
Adjusted Pool rate	5.68	5.76	5.81	5.94	6.06	5.91	6.15	6.29	6.22	7.10	6.69	7.44	7.52

Note: figures are provisional and still subject to changes

11. As the pool rate of interest has continued to increase when general interest rates have remained stable or have decreased, this brings into question the methodology behind the reversal out of the unsupported borrowing.

Financial implications

12. As the 2022-23 pool rates are still provisional, the following exemplifies the 21-22 unadjusted pool rate on the 2021-22 settlement.

Table 2: Exemplification of using the unadjusted pool rate on the 2021-22 settlement

	2021-22	Unadjusted pool rate	Difference	
	AEF		N	%
Isle of Anglesey	104,825	104,680	-145	-0.1%
Gwynedd	194,793	194,455	-338	-0.2%
Conwy	166,906	166,806	-100	-0.1%
Denbighshire	158,632	158,503	-129	-0.1%
Flintshire	206,778	206,862	84	0.0%
Wrexham	188,856	189,158	301	0.2%
Powys	191,897	191,117	-780	-0.4%
Ceredigion	109,658	109,139	-519	-0.5%
Pembrokeshire	179,387	179,252	-135	-0.1%
Carmarthenshire	284,820	284,700	-120	0.0%
Swansea	352,642	352,662	20	0.0%
Neath Port Talbot	236,680	236,670	-10	0.0%
Bridgend	212,192	212,399	207	0.1%
The Vale Of Glamorgan	168,316	168,735	418	0.2%
Rhondda Cynon Taf	404,375	404,226	-150	0.0%
Merthyr Tydfil	101,476	101,450	-26	0.0%
Caerphilly	292,367	292,778	410	0.1%
Blaenau Gwent	120,361	119,927	-433	-0.4%
Torfaen	146,340	146,246	-94	-0.1%
Monmouthshire	101,483	101,484	1	0.0%
Newport	240,796	241,181	385	0.2%
Cardiff	487,913	489,066	1,154	0.2%
Wales	4,651,494	4,651,494		

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13. We see that this has large financial implications across authorities with the monetary changes ranging from a £780k decrease in AEF for Powys to a £1.15m increase for Cardiff. Similarly the percentage change ranges from a 0.5% decrease in Ceredigion’s AEF to a 0.2% increase in the Vale of Glamorgan.
14. As table 1 shows, the provisional pool rate figures for the 2022-23 settlement has widened further between both options, therefore this is likely to further amplify the changes in the distribution for 2022-23.
15. Given the large financial changes, some further options are detailed below.
16. If the DSG wish to incorporate the unadjusted pool rate into the 2022-23 settlement then the group may wish to phase the change over, for example, 4 years to reduce the year-on-year financial impact.
17. Table 3 demonstrates one phasing method if the group wished to revert to using the unadjusted pool rate over a period of time.
18. In this example, because the adjusted and unadjusted pool rates are fixed at a point in time (the 21-22 settlement), the changes each year are a quarter of the final amount. In reality, if DSG were to consider this option, we would suggest the adjusted pool rate remains fixed at its 21-22 value (7.44%) with the unadjusted pool rate updated yearly throughout the phasing.

Table 3: Exemplification of phasing the pool rate to the old methodology in 25% increments.

	2021-22 AEF	Y1	Y2	Y3	Y4	n				%			
						Y1-actual	Y2-Y1	Y3-Y2	Y4-Y3	Y1-actual	Y2-Y1	Y3-Y2	Y4-Y3
Isle of Anglesey	104,825	104,789	104,753	104,716	104,680	-36	-36	-36	-36	0.0%	0.0%	0.0%	0.0%
Gwynedd	194,793	194,709	194,624	194,539	194,455	-84	-85	-85	-85	0.0%	0.0%	0.0%	0.0%
Conwy	166,906	166,881	166,856	166,831	166,806	-25	-25	-25	-25	0.0%	0.0%	0.0%	0.0%
Denbighshire	158,632	158,600	158,567	158,535	158,503	-32	-32	-32	-32	0.0%	0.0%	0.0%	0.0%
Flintshire	206,778	206,799	206,820	206,841	206,862	21	21	21	21	0.0%	0.0%	0.0%	0.0%
Wrexham	188,856	188,931	189,007	189,082	189,158	75	75	75	75	0.0%	0.0%	0.0%	0.0%
Powys	191,897	191,703	191,508	191,312	191,117	-194	-195	-195	-195	-0.1%	-0.1%	-0.1%	-0.1%
Ceredigion	109,658	109,529	109,399	109,269	109,139	-129	-130	-130	-130	-0.1%	-0.1%	-0.1%	-0.1%
Pembrokeshire	179,387	179,353	179,319	179,285	179,252	-34	-34	-34	-34	0.0%	0.0%	0.0%	0.0%
Carmarthenshire	284,820	284,791	284,760	284,730	284,700	-30	-30	-30	-30	0.0%	0.0%	0.0%	0.0%
Swansea	352,642	352,647	352,652	352,657	352,662	5	5	5	5	0.0%	0.0%	0.0%	0.0%
Neath Port Talbot	236,680	236,677	236,675	236,672	236,670	-3	-3	-3	-3	0.0%	0.0%	0.0%	0.0%
Bridgend	212,192	212,243	212,295	212,347	212,399	52	52	52	52	0.0%	0.0%	0.0%	0.0%
The Vale Of Glamorgan	168,316	168,420	168,525	168,630	168,735	104	105	105	105	0.1%	0.1%	0.1%	0.1%
Rhondda Cynon Taf	404,375	404,338	404,300	404,263	404,226	-37	-37	-37	-37	0.0%	0.0%	0.0%	0.0%
Merthyr Tydfil	101,476	101,470	101,463	101,457	101,450	-6	-6	-6	-6	0.0%	0.0%	0.0%	0.0%
Caerphilly	292,367	292,470	292,572	292,675	292,778	102	103	103	103	0.0%	0.0%	0.0%	0.0%
Blaenau Gwent	120,361	120,253	120,145	120,036	119,927	-108	-109	-109	-109	-0.1%	-0.1%	-0.1%	-0.1%
Torfaen	146,340	146,317	146,293	146,270	146,246	-23	-23	-23	-23	0.0%	0.0%	0.0%	0.0%
Monmouthshire	101,483	101,483	101,483	101,483	101,484	0	0	0	0	0.0%	0.0%	0.0%	0.0%
Newport	240,796	240,892	240,989	241,085	241,181	96	96	96	96	0.0%	0.0%	0.0%	0.0%
Cardiff	487,913	488,200	488,489	488,778	489,066	287	289	289	289	0.1%	0.1%	0.1%	0.1%
Wales	4,651,494	4,651,494	4,651,494	4,651,494	4,651,494								

19. Whilst this paper focuses on the pool rate aspect of the debt financing model, members may wish to revisit other areas of the model, to ensure it is still relevant.
20. One area which may be worth consideration is the fixed historic profile, which is based on data from March 2004. This data has been used with supported borrowing removed annually to distribute the funding. The group are asked to

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consider whether there is an appetite to update this profile to reflect current debt within authorities. This could be reviewed over a set time period in the future.

21. The debt financing model assumes MRP at 4% reducing balance. In reality not all authorities are repaying the 4% each year, therefore again DSG are asked to consider the appetite to investigate potential changes to this element of the formula.

Conclusion

22. Members' views are sought on reverting the pool rate back to the unadjusted method, whether phasing of the data is required and whether they would like to investigate the potential for further changes to the debt financing model. Further analysis can be circulated via correspondence or at the November DSG meeting if time constraints allow, or this work can be added to the work programme for 2022.

**Local Government Finance Policy and Sustainability
Welsh Government**