STATUTORY GUIDANCE ON MINIMUM REVENUE PROVISION

Guidance issued by the Secretary of State under section 21(1A) of the *Local Government Act 2003*

POWER UNDER WHICH THE GUIDANCE IS ISSUED

1. The following Guidance is issued by the Secretary of State under section 21(1A) of the *Local Government Act 2003.* Under that section local authorities are required to "have regard" to this guidance.

DEFINITION OF TERMS

2. The **2003 Act** means the *Local Government Act 2003.*

3. The **2007 Act** means the *Local Government and Public Involvement in Health Act 2007.*

4. The **2003 Regulations** means the L*ocal Authorities (Capital Finance and Accounting) (England) Regulations 2003* [as amended].

5. **Local authority** has the meaning given in section 23 of the 2003 Act.

6. **MRP** means Minimum Revenue Provision.

7. The **Prudential Code** means the statutory code of practice, issued by CIPFA, referred to in Regulation 2 of the 2003 Regulations.

8. **CFR** means the Capital Financing Requirement, as defined in the Prudential Code.

9. **Non-housing CFR** has the meaning given in Regulation 28(11) of the 2003 Regulations, before this was amended. This is the total CFR for a local authority less the Housing Revenue Account CFR, where a local authority has a Housing Revenue Account.

10. **Credit Arrangement** has the meaning given in Section 7 of the 2003 Act.

11. **Supported Capital Expenditure** means the total amount of capital expenditure which a local authority had been notified by one or more Government departments was to be taken into account in the calculation of the revenue grant due to the local authority in respect of it its use of borrowing and credit. It excludes any expenditure that is supported by capital grant.

12. **Housing assets** means any land, dwellings or other property to which Section 74(1) of the Local Government Housing Act 1989 (duty to keep a Housing Revenue Account) applies.

13. **UEL** means the useful economic life of an asset as determined by proper accounting practice.

APPLICATION

Effective date

14. This guidance applies for accounting periods starting on or after 1 April 2018. However, early adoption is encouraged.

Local authorities

15. This guidance applies to all local authorities in England and their relevant bodies. It does not apply to parish councils or charter trustees.

INTRODUCTION

16. Under Regulation 27 of the 2003 Regulations, local authorities are required to charge MRP to their revenue account in each financial year. Before 2008, the 2003 Regulations contained details of the method that local authorities were required to use when calculating MRP. This has been replaced by the current Regulation 28 of the 2003 Regulations, which gives local authorities flexibility in how they calculate MRP, providing the calculation is 'prudent'. In calculating a prudent provision, local authorities are required to have regard to this guidance.

ANNUAL MRP STATEMENT

17. Before the start of each financial year a local authority should prepare a statement of its policy on making MRP in respect of that financial year and submit it to full Council for approval. For local authorities without a full Council the statement should be presented for approval at the closest equivalent level. The statement should describe how it is proposed to discharge the duty to make prudent MRP during that year.

18. Local authorities can vary the methodologies that they use to make prudent provision during the year. If they do so they should present a revised MRP statement to the next full Council or equivalent. Where a change in MRP methodology would impact on the value for money assessment of non-financial investments, the updated statement should summarise this impact.

MEANING OF PRUDENT PROVISION

19. Regulation 28 of the 2003 Regulations requires a local authority to calculate in each financial year an amount of MRP that it considers to be prudent.

20. An underpinning principle of the local authority financial system is that all capital expenditure has to be financed either from capital receipts, capital grant or eventually from revenue income. The broad aim of prudent provision is to require local authorities to put aside revenue over time to cover the gap between the CFR and grant income/capital receipts. In doing so, local authorities can align the period over which they charge MRP to one that is commensurate with the period over which their capital expenditure provides benefits.

21. In the case of historic borrowing originally supported by grant income rolled into Revenue Support Grant the meaning of prudent provision is to put funds aside over a period commensurate with the period implicit in the determination of that original grant.

22. The Secretary of State considers that the methods of making prudent provision include the options set out in paragraphs 30 to 36. However, this does not rule out or otherwise preclude a local authority from using an alternative method should it decide that is more appropriate. Any method used is subject to the conditions in paragraphs 37 to 41 as far as these are relevant.

OVERPAYMENTS OF MRP

23. Local authorities may choose to pay more MRP than they consider prudent in any given year. If they do so they should separately disclose the in-year and cumulative amount of MRP overpaid in the Statement presented to full council

MEANING OF CHARGE TO A REVENUE ACCOUNT

24. A charge to a revenue account cannot be a negative charge.

25. A charge to a revenue account can only be £nil if:
    - A local authority's CFR was nil or negative on the last day of the preceding financial year; or
    - A local authority chooses to offset a previous year's overpayment (as defined in paragraph 23) against the current year's prudent provision. 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.

CHANGING METHODS FOR CALCULATING MRP

26. A local authority may change the method(s) that it uses for calculating part or all of its MRP at any time.

27. 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.

28. 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. Changing the method used to calculate MRP can never give rise to an overpayment, and should not result in a LA making a charge of £nil for the accounting period in which the change is made.

TRANSFERRING DEBT

29. Where debt is transferred between authorities, the authorities concerned should agree on the arrangements for the continued making of MRP and adjust their unfunded CFRs accordingly. Normally the authority releasing the debt should cease to make MRP in respect of it and the authority taking it over should begin to make MRP in the same way that it would do for any other increase in CFR.

OPTIONS FOR MAKING PRUDENT PROVISION

30. This Guidance presents four ready-made options for calculating prudent provision. Local authorities can use a mix of these options for debt taken out at different times should they consider it appropriate to do so.

<u>Option 1: Regulatory method</u>

31. MRP is equal to the amount determined in accordance with the former Regulations 28 and 29 of the 2003 Regulations as if they had not been revoked by the 2008 amendment to those regulations. For the purposes of that calculation, the adjustment A should normally continue to have the value attributed to it by the local authority in the financial year 2005-05. However, it would be reasonable for local authorities to correct any perceived errors in adjustment A, if the correction would be in their favour.

32. The former Regulations 28 and 29 of the 2003 Regulations are included at **Annex A**.

<u>Option 2: CFR method</u>

33. MRP is equal to 4% of the non-housing CFR at the end of the preceding financial year.

<u>Option 3: Asset Life Method</u>

34. Where capital expenditure on an asset is financed wholly or partly by borrowing or credit arrangements, MRP is to be determined by reference to the life of the

asset. There are two main methods by which this can be achieved, as described below.

(a) Equal instalment method

MRP is the amount given by the following formula:

$$\frac{A - B}{C}$$

Where:

A is the amount of capital expenditure in respect of the asset financed by borrowing or credit arrangements.

B is the total provision made before the current financial year in respect of that expenditure.

C is the inclusive number of financial years from the current year to that in which the estimated life of the asset expires.

(b) Annuity method

MRP is the principal element for the year of the annuity required to repay over the asset life the amount of capital expenditure financed by borrowing or credit arrangements. The authority should use an appropriate interest rate to calculate the amount. Adjustments to the calculation to take account of repayment by other methods during repayment period (e.g. by the application of capital receipts) should be made as necessary.

<u>Option 4: Depreciation method</u>

35. MRP is deemed to be equal to the provision required in accordance with deprecation accounting in respect of the asset on which expenditure has been financed by borrowing or credit arrangements. This should include any amount for impairment charged to the income and expenditure accounts.

36. For this purpose standard depreciation accounting procedures should be followed, except in the following respects:
    - MRP should continue to be made annually until the cumulative amount of provision made is equal to the expenditure originally financed by borrowing or credit arrangements. Thereafter the authority will cease to make MRP.
    - On disposal of the asset, the charge should continue in accordance with the depreciation schedule as if the disposal had not taken place. This does not affect the ability to apply capital receipts or other funding sources at any time to repay all or part of the outstanding debt.

- Where the percentage of the expenditure on the asset financed by borrowing or credit arrangements is less than 100%, MRP should be equal to the same percentage of the provision required under depreciation accounting.

CONDITIONS FOR USING THE OPTIONS

37. **Use of options.** Options 1 and 2 may only be used in relation to capital expenditure incurred before 1 April 2008, which form part of its supported capital expenditure.

38. For expenditure incurred on or after 1 April 2008, which does not form part of the authority's supported capital expenditure, prudent approaches include options 3 and 4.

39. **Commencement of provision.** Subject to paragraph 31 below, MRP should normally commence in the financial year following the one in which the expenditure was incurred.

40. **MRP Commencement.** When borrowing to provide an asset, the authority may treat the asset life as commencing in the year in which the asset first becomes operational. Therefore, it may postpone beginning to make MRP until the financial year following the one in which the asset becomes operational. 'Operational' here means when an asset transfers from Assets under Construction to an Assets in Use category under normal accounting rules.

41. Useful economic life of assets. Where a local authority uses options 3 or 4 or where it uses another methodology that has the useful economic life of assets as a component to the calculation the following maximum useful economic lives should be used irrespective of any other considerations:
- Freehold land 50 years
- Any other asset class 40 years

FINANCE LEASES AND PFI

42. In the case of finance leases and on balance sheet PFI contracts, the MRP requirement would be regarded as met by a charge equal to the element of the rent/charge that goes to write down the Statement of Financial Position liability. Where a lease (or part of a lease) or PFI contract is brought onto the Statement of Financial Position, having previously been accounted for off- Statement of Financial Position, the MRP requirement would be regarded as having been met by the inclusion in the charge for the year in which the restatement occurs, of an

amount equal to the write-down for that year plus retrospective writing down of the Statement of Financial Position liability that arises from the restatement.

HOUSING ASSETS

43. The duty to make MRP does not extend to cover borrowing or credit arrangements used to finance capital expenditure on housing assets (as defined in paragraph 12 above).

CAPITALISED EXPENDITURE

44. Where on or after 1 April 2008 an authority incurs expenditure which is:
    - Financed by borrowing and credit arrangements; and
    - Treated as capital expenditure by virtue of either a direction under section 16(2)(b) f the 2003 Act or Regulation 25(1) of the 2003 Regulations,

    The authority should calculate MRP in accordance with Option 3.

45. For the purpose of the formula in paragraph 33 above, in the initial year of making MRP the variable "C" should be given the maximum values as set out in the following table:

Expenditure type	**Maximum value of "C" in initial year**
Expenditure capitalised by virtue of a **direction under s.16(2)(b)**	"C" equals 20 years
Regulation 25(1)(a) Expenditure on computer programmes	"C" equals the shorter of the UEL of the hardware or the length of the software license.
Regulation 25(1)(b) Loans and grants towards capital expenditure by third parties.	"C" equals the UEL of the assets for in relation to which the third party expenditure is incurred.
Regulation 25(1)(c) Repayment of grants and loans for capital expenditure	"C" equals 25 years or the period of the loan if longer.
Regulation 25(1)(d) Acquisition of share or loan capital	"C" equals 20 years.
Regulation 25(1)(e) Expenditure on works to assets not owned by the authority	"C" equals the UEL of the assets.
Regulation 25(1)(ea) Expenditure on assets for use by others.	"C" equals the UEL of the assets.
Regulation 25(1)(f) Payment of levy on large scale voluntary transfers (LSTV) of dwellings	"C" equals 25 years.

ANNEX A – REGULATIONS 28 AND 29 OF THE 2003 REGULATIONS BEFORE THESE WERE AMENDED

Calculation of minimum revenue provision

28.—(1) Subject to paragraphs (2) and (3) and regulation 29, the minimum revenue provision for the current financial year shall be calculated by the local authority in accordance with the following formula—

$$\frac{4[CFR \quad (A - HC)]}{100}$$

where—

- CFR is the capital financing requirement at the end of the preceding financial year;
- A is an adjustment (which may be a positive, nil or negative amount) to be calculated in accordance with the following formula—

$$[CFRM - (HA + NHA)] + \frac{(HA - HB)}{2}$$

where—

    - CFRM is the capital financing requirement on 31st March 2004;
    - HA is the housing amount on 31st March 2004;
    - HB is the opening HRA capital financing requirement for the financial year beginning on 1st April 2004, except that if that opening HRA capital financing requirement is a negative amount, HB is nil; and
- NHA is the non-housing amount on 31st March 2004; and
- HC is the opening HRA capital financing requirement for the current financial year, except that if that opening HRA capital financing requirement is a negative amount, HC is nil.

(2) An additional amount of minimum revenue provision for the current financial year ("the additional amount") shall be calculated by the local authority where—

(a)a credit approval, within the meaning of regulation 136 of the Local Authorities (Capital Finance) Regulations 1997 (use of certain credit approvals)(1), was issued to the local authority before 1st April 2004; and

(b)the amortisation period specified in the credit approval expires during or after the current financial year,

and the additional amount shall be the total amount determined by the local authority under regulation 136(2) of those Regulations for the current financial year, as if those Regulations were still in force for the purposes of this regulation.

(3) Where, in relation to the current financial year, the total of—

(a)the amount calculated in accordance with the formula for the minimum revenue provision in paragraph (1); and (b)the additional amount, if any, calculated under paragraph (2),

is a negative amount, the minimum revenue provision for the current financial year shall be treated as nil.

(4) For the purposes of this regulation—

"arms length management organisation" means a body set up by a local authority as a housing management company to exercise management functions as agent of the local authority under an arrangement approved by the Secretary of State under section 27 of the Housing Act 1985 (management agreements)(**2**);

"capital financing requirement" has the same meaning as in the "Prudential Code for Capital Finance in Local Authorities" published by CIPFA, as amended or reissued from time to time(**3**);

"certified value" means the market value certified by the district valuer or by a suitably qualified valuer employed by the local authority;

"current financial year" means any financial year for which the local authority is determining the amount of its minimum revenue provision;

"district valuer", in relation to any land in the district of a local authority, means an officer of the Commissioners of Inland Revenue appointed by them for the purpose of exercising, in relation to that district, the functions of the district valuer under the Housing Act 1985;

"housing amount" and "non-housing amount" have the same meaning as those terms had on 31st March 2004 in Part XII of the Local Authorities (Capital Finance) Regulations 1997 (minimum revenue provision);

"Housing Revenue Account", also referred to as "HRA", has the same meaning as in section 74 of the Local Government and Housing Act 1989 (duty to keep Housing Revenue Account)(**4**);

"major repairs reserve" has the same meaning as in regulation 7(5) of the Accounts and Audit Regulations 2003 (statement of accounts)(**5**);

"opening HRA capital financing requirement" means—

(a) for the financial year beginning on 1st April 2004, the amount calculated in accordance with paragraph (5);

(b) for the financial year beginning on 1st April 2005 and any subsequent financial year, the amount calculated In accordance with paragraph (6); and

"preceding financial year" means the financial year immediately preceding the current financial year.

(5) The amount referred to in sub-paragraph (a) of the definition of "opening HRA capital financing requirement" in paragraph (4) is the amount calculated in accordance with the following formula—

$$OHCC + IA - ID$$

where—

OHCC is the opening HRA credit ceiling for the financial year beginning on 1st April 2003, which has the same meaning as the "opening HRA credit ceiling" in paragraph 7.1 of the Item 8 Credit and Item 8 Debit (General) Determination 2003-2004 ("the Determination")(**6**);

IA means the total of—

(a)

the items to be aggregated as specified in paragraph 7.2 of the Determination but substituting "2003-2004" for "2002-2003" in each place where it occurs in that paragraph; and

(b)

the amounts of all supplementary credit approvals issued in respect of financial years beginning before 1st April 2004 under section 54 of the Local Government and Housing Act 1989 (supplementary credit approvals)(7) for the purposes of expenditure in relation to arms length management organisations; and

ID means the items to be deducted as specified in paragraph 7.3 of the Determination but substituting “2003-2004” for “2002-2003” in each place where it occurs in that paragraph.

(6) The amount referred to in sub-paragraph (b) of the definition of “opening HRA capital financing requirement” in paragraph (4) is the amount calculated in accordance with the following formula—

$$OCFR + TIA - TID$$

where—

- OCFR means the opening HRA capital financing requirement for the preceding financial year;
- TIA means the total items to be aggregated, being the total of the following—

(a) the capital expenditure of the local authority financed by borrowing or credit arrangements which was incurred during the preceding financial year on any interest in housing land; and

(b) the certified value of any interest in housing land which commenced or recommenced to be accounted for in the Housing Revenue Account in the preceding financial year for a reason other than acquisition by the local authority;

- TID means the total items to be deducted, being the total of the following—

(a) such part of any capital receipt from the disposal of an interest in housing land which was used during the preceding financial year to repay the principal of any amount borrowed by the local authority or to meet any liability in respect of credit arrangements;

(b) 75 per cent. of the certified value of any interest in a dwelling, and 50 per cent. of the certified value of any interest in other housing land, that ceased to be accounted for in the Housing Revenue Account in the preceding financial year other than by virtue of disposal by the local authority;

(c) the amount of the provision for the repayment of the principal of any amount borrowed by the local authority or the meeting of any liability in respect of credit arrangements which the local authority determined during the preceding financial year to make from the Housing Revenue Account; and

(d) the amount of the provision for the repayment of the principal of any amount borrowed by the local authority or the meeting of any liability in respect of credit arrangements which the local authority determined during the preceding financial year to make from the major repairs reserve.

Commutation adjustment

29.—(1) Subject to paragraph (2), where a commuted payment was made to or for the benefit of a local authority in the financial year beginning on 1st April 1992, the local authority may reduce the amount of its minimum revenue provision for the current financial year, calculated in accordance with regulation 28, by an amount calculated in accordance with the following formula—

$$G \quad (I - M)$$

where—

- G is the total amount of contributions, grants and subsidies which would have been payable to the local authority by the Secretary of State for the current financial year but for commutation;

- I is the total of—

(a) the amount by which interest, payable by the local authority in the current financial year on loans, is reduced; and

(b) the amount by which interest, payable to the local authority in the current financial year on deposits and investments, is increased, by virtue of commutation; and

- M is the amount of minimum revenue provision for the current financial year which would have been calculated by the local authority in accordance with regulation 28 but for commutation, less the amount of minimum revenue provision for the current financial year actually calculated in accordance with regulation 28.

(2) Where the amount calculated in accordance with the formula in paragraph (1) is a negative amount, that amount shall be treated as nil.

(3) For the purposes of paragraph (1)—

"commutation" means the making of a commuted payment to, or for the benefit of, a local authority in the financial year beginning on 1st April 1992;

"commuted payment" has the same meaning as that term had on 31st March 2004 in section 157 of the Local Government and Housing Act 1989 (commutation of, and interest on, periodic payments of grants etc.)(8); and

"current financial year" has the same meaning as in regulation 28(4).