Appendix E – Minimum Revenue Provision (MRP) Policy Statement 2023/24 and 2024/25

Introduction

1. Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 ('the 2003 Regulations') requires local authorities to 'charge to a revenue account a minimum revenue provision (MRP) for that year'. The minimum revenue provision is an annual amount set aside from the General Fund to meet the cost of capital expenditure that has not been financed from available resources, namely: grants, developer contributions (e.g. s.106 and community infrastructure levy) revenue contributions, earmarked reserves or capital receipts.

2. MRP is sometimes referred to as the mechanism for setting aside monies to repay external borrowing. In fact, the requirement for MRP set aside applies even if the capital expenditure is being financed from the Council's own cash resources and no new external borrowing or other credit arrangement has been entered into.

3. Regulation 28 of the 2003 Regulations requires full Council to approve a Minimum Revenue Provision (MRP) Statement setting out the policy for making MRP and the amount of MRP to be calculated which the Council considers to be prudent. This statement is designed to meet that requirement.

4. In setting a prudent level of MRP local authorities must "have regard" to guidance issued from time to time by the Secretary of State for Housing, Communities and Local Government. The latest version of this guidance (version four) was issued by Ministry of Housing, Communities and Local Government (MHCLG) in February 2018.

5. The Department for Levelling Up, Housing and Communities (DLUHC) published a consultation on changes to the Capital Finance Regulations and the Statutory MRP Guidance in December 2023. A summary of the proposed changes is set out at paragraph 11 below. The changes being consulted upon will take effect from 1 April 2024. Consequently the MRP Policy Statement for 2024/25 must have regard to the proposed changes as well as the extant legislation and MRP Guidance.

6. In setting a level which the Council considers to be prudent, the Guidance states that the broad aim is to ensure that debt is repaid over a period reasonably commensurate with that over which the capital expenditure provides benefits to the Council.

7. The Guidance sets out four "possible" options for calculating MRP, as set out below,

Option	Calculation method	Applies to

1: Regulatory method	Formulae set out in 2003 Regulations (later revoked)	Expenditure incurred before 1 April 2008
2: CFR method	4% of Capital Financing Requirement	Expenditure incurred before 1 April 2008
3: Asset life method	Amortises MRP over the expected life of the asset	Expenditure incurred after 1 April 2008
4: Depreciation method	Charge MRP on the same basis as depreciation	Expenditure incurred after 1 April 2008

8. Two main variants of Option 3 are set out in the Guidance (i) the equal instalment method and (ii) the annuity method. The annuity method weights the MRP charge towards the later part of the asset's expected useful life and is increasingly becoming the most common MRP option for local authorities.

9. The Guidance also includes specific recommendations for setting MRP in respect of finance lease, investment properties and revenue expenditure which is statutorily defined as capital expenditure under the 2003 Regulations (also referred to as revenue expenditure funded from capital under statute or REFCUS). Examples of REFCUS include capitalised redundancy costs, loans or grants to third parties for capital purposes, and the purchase of shares in limited companies.

10. Other approaches are not ruled out however they must meet the statutory duty to make prudent MRP provision each financial year.

DLUHC consultation

11. DLUHC published a consultation on changes to the Capital Finance Regulations and Statutory Guidance in respect of MRP in December 2023. This follows two earlier consultations in November 2021 and February 2022. The aim of the changes proposed is to strengthen the requirement for local authorities to make a prudent MRP provision, in response to two issues which have led to underpayment of MRP at a number of authorities including Woking:

    (a) excluding a proportion of debt from the MRP determination in two areas:

        (i) firstly, debt associated with investment properties or investments defined as capital expenditure, on the basis that such assets retain their capital value and that the asset can be sold at any time in the future to repay the associated debt. The Government have stated that this is not prudent. The proposals will amend the 2003 Capital Finance Regulations to make clear that MRP is required on such expenditure;

        (ii) secondly, debt associated with making loan advances to third parties for a capital purpose. The argument put forward by authorities exempting such debt from MRP calculations is that the repayments of principal would be used to repay debt. The proposed changes will require local authorities to continue to set aside MRP on "commercial loans" (defined as a loan undertaken for profit), but allows local authorities an exemption from charging MRP for non-commercial loans, but will require local authorities to set aside as MRP an amount for any expected credit loss calculated under IFRS9. In other words for non-commercial loans as soon as there is evidence that the debtor might be unable to repay all or some of the loan, the authority would be required to set aside the full amount of the estimated loss.

(b) using capital receipts in place of charging MRP to revenue. Authorities following this approach would use capital receipts to pay for the amount of MRP due for the individual financial year. This practice effectively treated capital receipts as a revenue source, which is not permissible under Regulation 23 of the Capital Finance Regulations. The proposed changes to the Capital Finance Regulations make clear that capital receipts can only be used to reduce the overall level of the CFR, which in turn forms the basis for calculating the MRP charge, based on the residual CFR after the application of capital receipts.

12. In addition, paragraph 46 of the draft MRP Guidance states that for local authorities where the Government has made arrangements to intervene and has, or is in the process of, put in place financial support arrangement for the authority, that it may be appropriate to reflect the nature of any such financial support when determining a prudent level of MRP for the forthcoming financial year. The draft Guidance goes onto state that the authority must seek agreement from the Government on how any such assumptions with respect to support are reflected in the determination of MRP. The draft Guidance goes onto explain that paragraph 46 is not a new policy but clarifies an issue that previous editions of the Guidance was silent on. As such, the Government expects this to apply to prior periods (or MRP from prior periods).

Local Government Reorganisation

13. Prior to vesting day for the new Somerset Council, all five abolished authorities had different MRP policies and practices. When the MRP policy was set for the new Council as part of the budget setting process for 2023/24, the MRP Policy Statement set out that past charges would not be re-visited but that a consistent approach would be developed for the new Council.

14. The quality of the records available to date inherited have not been sufficient to enable this as explained below:

- Only one authority appeared to have any MRP stream in respect of pre 2007/08 and supported capital expenditure incurred 2008-2011. This seems unlikely given that the amortisation period would have been a minimum of 25 years from 1 April 2008 when the current system of MRP came into force;

- For unsupported capital expenditure incurred since 1 April 2008, only two authorities appeared to have capital finance records which showed expenditure on an asset by asset basis necessary to support the asset life method which all five authorities reported they were following;

- Asset lives used for the MRP calculations at three authorities appeared to default to 50 years. The asset life method is required to charge MRP over a period commensurate with the period over which their capital expenditure provides benefits. Therefore it is extremely unlikely that the asset lives would all be 50 years. Potentially this means that the authorities would be setting MRP for a period longer than that which provided benefits, which would be imprudent.

- There were no detailed asset life records for the former county council and it has been necessary to apportion the county's CFR pro rata to the net book value of the assets held by the county, in order to estimate a split of the CFR by asset type and then apply asset lives more appropriate to the relevant asset class.

15. In view of this the MRP Policy Statement for 2023/24 is to be amended and the 2024/25 to provide a continuation of the MRP policies for the legacy expenditure from the abolished authorities and a standard policy for unfinanced capital expenditure incurred by the new Council since 1 April 2023.

16. This approach is recommended subject to work being undertaken to establish more accurate records from the abolished authorities over the next 12 months and revisit the MRP policy during 2024/25 where necessary in order to move to a consistent MRP policy across the whole Council and one which fully complies with the Statutory MRP Guidance – both the current 2018 edition and the 2024 edition currently out to consultation.

Minimum Revenue Provision (MRP) policy statement

17. Having regard to current Guidance on MRP issued by MHCLG and the "options" outlined in that Guidance, the Council is recommended to approve the following MRP Statement to take effect from 1 April 2024, on the basis that this represents "a prudent provision" in line with Regulation 28.

MRP stream	Policy	Explanation
Legacy MRP		
Mendip DC: 1. Operational expenditure	MRP will be calculated on a straight-line basis over the	This complies with Option 3(i) of the MRP Guidance.

2. Investment property	expected asset lives established by the former authority. MRP will be calculated on an annuity basis over the expected asset lives established by the former authority of 20 years	This complies with Option 3(i) of the MRP Guidance.
Sedgemoor DC: 1. Pre-2008 capital expenditure and supported capital expenditure 2. Unsupported capital expenditure incurred since 1 April 2008 3. Commercial investment 4. Loans to third parties	MRP will be charged on a 4% reducing balance in respect of the previous year's CFR MRP will be charged on annuity basis over the expected asset lives established by the former authority MRP will be charged on a straight-line basis over the remaining 47 year asset lives established by the former authority. MRP will be charged on a straight-line over the remaining period of the loans	This complies with Option 2 This complies with Option 3(ii), but will need detailed asset records to be established to confirm use of the method. This complies with Option 3(i) but will need detailed asset records to be established to confirm use of the method. This complies with Option 3(i) but will need detailed asset records to be established to confirm use of the method.
South Somerset DC Unsupported capital expenditure incurred since 1 April 2008	MRP will be charged on a straight-line basis over the remaining period of the standard 50 year asset lives	This complies with Option 3(i) but will need detailed asset records to be established to confirm use of the method and to reflect the actual asset lives of the assets financed.

MRP stream	Policy	Explanation
South West and Taunton DC Unsupported capital expenditure incurred since 1 April 2008 Unsupported capital expenditure on investment property	MRP will be charged on a straight-line basis over the remaining 10 year asset life MRP will be charged on an annuity basis over the residual asset life of the asset(s) acquired	This complies with Option 3(i) but will need detailed asset records to be established to confirm use of the method and to reflect the actual asset lives of the assets financed. This complies with Option 3(ii) but will need detailed records to be established to confirm use of the method and to reflect the actual assets financed.
Somerset CC Unsupported capital expenditure incurred since 1 April 2008	MRP will be charged on a straight-line over the standard asset lives of the CFR at 31/3/2023 apportioned to heritage, infrastructure, intangible and plant and equipment assets. MRP on land and buildings will be charged on an annuity basis over a standard asset life of the CFR at 31/3/2023 apportioned to this asset category	This complies with Option 3(i) but will need detailed records to be established to confirm use of the method and to reflect the actual assets financed. This complies with Option 3(ii) but will need detailed records to be established to confirm use of the method and to reflect the actual assets financed
All pre-2007/08 capital expenditure	MRP will be calculated on the reducing balance method set out in Option 1	This complies with Option 1 but will need the records checking for each abolished authority to establish whether such expenditure was outstanding at 31/3/2023.
Ongoing MRP since 1 April 2023		
All operational capital expenditure incurred since 2007/08	MRP will be calculated on a straight-line using the expected useful asset lives of the assets (Option 3 – asset	This complies with the Option 3(ii) of the MRP Guidance and the requirement for a maximum asset life of 50 years.

	life), subject to a maximum useful asset life of 50 years.	
All capital expenditure on commercial assets incurred since 2007/08	MRP will be calculated on an annuity basis using the expected useful asset lives of the assets (Option 3 – asset life), subject to a maximum useful asset life of 20 years and discounted using the PWLB new loan annuity rate applicable on 1 April in the year when MRP commences.	The use of the annuity method complies with Option 3(ii) of the MRP Guidance.

MRP stream	Policy	Explanation
Expenditure capitalised by virtue of a capitalisation direction under section 16(2)(b) of the Local Government Act 2003	MRP on any expenditure capitalised by way of a Direction will be charged over 20 years using the asset-life method using an annuity approach.	The 20 year life is the period specified in para 47 of the MRP Guidance. The use of the annuity method complies with Option 3(ii) of the MRP Guidance.
Loans to third parties	MRP will be charged on a straight-line basis over the expected useful life for which the loan is to be used, subject to a maximum useful asset life of 50 years	The straight-line approach complies with Option 3(i) of the MRP Guidance and the useful life is that set out in para 47 of the MRP Guidance.
Expenditure on the acquisition of share capital	MRP will be charged on a straight-line over 20 years	The straight-line approach complies with Option 3 of the MRP Guidance and the 20 year life is that set out in para 47 of the MRP Guidance.
MRP for service concession contracts	The amount of the MRP charge will be equal to the amount by which the balance sheet liability is written by the unitary charge (i.e. the principal element of the unitary charge)	This complies with para 43 of the MRP Guidance
Asset lives	Asset lives used for MRP calculations will be determined by the Council's RICS-registered valuers, and will be consistent with the depreciation policies set out in the Council's annual Statement of Accounts, and will be kept under regular review. If no life can reasonably be attributed to an asset, such as	This complies with para 42 of the MRP Guidance.

	freehold land, the estimated useful life will be taken to be a maximum of 50 years	
Discount rate for use when applying the annuity method for calculating MRP under Option 3	MRP will be discounted using the PWLB new loan annuity rate applicable on 30 September in the year before MRP commences	The MRP Guidance does not suggest what discount rate(s) to use. By specifying the PWLB new loan annuity rate at 30 September in the year before MRP aligns the discount rate to the middle of the year in which the expenditure is incurred and provides a clearly evidenced trail to the discount rate to be used and reflects the type of borrowing undertaken by the Council.

MRP stream	Policy	Explanation
MRP commencement	MRP should normally begin in the financial year following the one in which the expenditure was incurred. However, in accordance with the statutory Guidance, commencement of MRP may be deferred until the financial year following the one in which the asset becomes operational	This approach complies with para 41 of the MRP Guidance
Use of capital receipts to reduce indebtedness	Capital receipts may be applied to reduce the CFR. This means that subsequent year's MRP charges will reduce by the amount of receipts applied. The MRP reduction will be on a straight line basis over 20 years, [unless the capital receipt relates to identifiable MRP charges, in which case the section 151 officer may determine the annual MRP reduction consistent with those MRP charges.]	This approach complies with para 68 of the draft MRP Guidance

18. On the basis of the above MRP Policy, the MRP for the forthcoming financial year (2024/25) would be £27.5m (equivalent to 2.5% of the closing CFR at 31 March 2024) comprising:

MRP element	£m
Legacy MRP	24.0
PFI	1.3
Unsupported capital expenditure for 2023/24	2.2
TOTAL MRP	**27.5**

19. In amending the MRP Policy for 2023/24 to the above and setting the 2024/25 MRP policy based on the MRP Policy above, this will comply with the Council's duty to set a prudent level of MRP. This MRP Policy is recommended on the basis that work will be

done within the next 12 months to improve the quality of records from the abolished authorities to properly support the use of the asset-life approach underpinning the legacy MRP to:

- ensure improved compliance with the MRP Guidance; and
- transition the new Council to a consistent MRP Policy for all unfinanced capital expenditure.

20. The MRP Policy will be kept under review and updated if necessary in the light of the changes to the Capital Finance Regulations and Statutory MRP Guidance currently being consulted upon by DLUHC.