

GUIDANCE ON MINIMUM REVENUE PROVISION

**Issued by Welsh Ministers
under section 21(1A) of the
Local Government Act 2003**

DEFINITIONS

1. in this guidance:

2003 Act means the *Local Government Act 2003*.

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

2003 Regulations means the *Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003* [SI 2003/3239, as amended].

2007 Regulations means the *Local Authorities (Capital Finance and Accounting) (Amendment) (Wales) Regulations 2007* [SI 2007/1051].

2008 Regulations means the *Local Authorities (Capital Finance and Accounting) (Amendment) (Wales) Regulations 2008*.

Local authority has the meaning given in section 23 of the 2003 Act. (This guidance does not apply to Community and Town councils and charter trustees).

MRP means Minimum Revenue Provision.

Prudential Code means the code of practice referred to in regulation 2 of the 2003 Regulations .

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

Non-housing CFR means that part of the capital financing requirement which is not housing CFR.

Credit arrangement has the meaning given in section 7 of the 2003 Act.

Supported Capital Expenditure means the total amount of capital expenditure which a local authority has been notified is to be taken into account in the calculation of the revenue support grant due to the authority in respect of its use of borrowing and credit. It excludes any expenditure which is supported by capital grant.

INTRODUCTION

2. Under regulation 21 of the 2003 Regulations, local authorities are required to charge to their revenue account for each financial year MRP to account for the cost of their debt in that financial year. Prior to its amendment by the 2008 Regulations, regulation 21 set out the method authorities were required to follow in calculating MRP. For the financial year 2007/08 and subsequent financial years, the detailed calculation has been replaced with a requirement that local authorities calculate an amount of minimum revenue provision which they consider to be prudent. This guidance is issued under section 21(1A) of the 2003 Act (as inserted by section 238(2) of the 2007 Act) and addresses this new requirement in regulation 22. In accordance with section 21(1B) of the 2003 Act, local authorities must have regard to this guidance.

ANNUAL MRP STATEMENT

3. It is recommended that before the start of each financial year a local authority prepares a statement of its policy on making MRP in respect of that financial year and submits it to the full council. The statement should indicate which of the options listed in paragraphs 7 to 15 below are to be followed in the financial year.

MEANING OF “PRUDENT PROVISION”

4. Regulation 22 of the 2003 Regulations (as amended by regulation 4 of the 2008 Regulations) requires a local authority to calculate for the current financial year an amount of minimum revenue provision which it considers to be prudent. The Secretary of State recommends that, for the purposes of regulation 22, the prudent amount of provision should be determined in accordance with paragraphs 5 and 6 below.

5. The broad aim of prudent provision is to ensure that debt is repaid over a period reasonably commensurate with that over which the capital expenditure provides benefits.

6. The Secretary of State considers that each of the following options in paragraphs 7 to 15 normally constitutes prudent provision, subject to the conditions in paragraphs 16 to 18.

OPTIONS FOR PRUDENT PROVISION

Option 1: Regulatory Method

7. MRP is equal to the amount determined in accordance with the former regulations 22 of the 2003 Regulations, as if it had not been revoked by the 2008 regulations.

Option 2: CFR Method

8. MRP is equal to 4% of the non-housing CFR at the end of the preceding financial year. If the CFR at that date is nil or negative, no MRP is required.

Option 3: Asset Life Method

9. Where capital expenditure on an asset is financed wholly or partly by borrowing or credit arrangements, MRP is to be made in equal annual instalments over the life of the asset, in accordance with the following formula:

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

where-

A is the amount of the 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.

10. **Commencement of provision.** Subject to paragraph 13 below, MRP should normally commence in the financial year following the one in which the expenditure was incurred.

11. **Asset life.** The estimated life of the asset should be determined in the year that MRP commences and not subsequently be revised.

12. **Freehold land.** If no life can reasonably be attributed to an asset, such as freehold land, the life should be taken to be a maximum of 50 years. However, in the case of freehold land on which a building or other structure is constructed, the life of the land may be treated as equal to that of the structure, where this would exceed 50 years.

13. **Construction period.** When borrowing to construct an asset, the authority may treat the asset life as commencing in the year in which the asset first becomes operational. It may accordingly postpone beginning to make MRP until that year. “Operational” here has its standard accounting definition. Investment properties should be regarded as becoming operational when they begin to generate revenues.

Note: As an alternative an authority could calculate and charge MRP on an annuity basis under this option.

Option 4: Depreciation Method

14. MRP is to be equal to the provision required in accordance with depreciation accounting in respect of the asset on which expenditure has been financed by borrowing or credit arrangements.

15. For this purpose standard depreciation accounting procedures should be followed, except in the following respects.

(a) MRP should continue to be made annually until the cumulative amount of such provision is equal to the expenditure originally financed by borrowing or credit arrangements. Thereafter the authority may cease to make MRP.

(b) On disposal of the asset, the amount of the capital receipt should not be taken to the revenue account and the authority must comply with the normal requirements of the 2003 Act on the use of capital receipts.

(c) 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

16. Options 1 and 2 should only be used in relation to:

- (a) capital expenditure incurred before 1 April 2008; and
- (b) capital expenditure incurred on or after that date which the authority is satisfied forms part of its Supported Capital Expenditure.

17. Options 3 and 4 should be used in relation to all capital expenditure incurred on or after 1 April 2008 which is to be financed by borrowing or credit arrangements and which does not form part of the authority's Supported Capital Expenditure.

18. Option 3 should be used for all capitalised expenditure (see paragraph 22).

CFR ADJUSTMENT

19. Where the authority has used Options 3 or 4, the CFR for the purposes of Options 1 and 2 should be treated as not being increased by the amount of the expenditure on the asset. In addition, the CFR should not be treated as being decreased by the amount of the MRP made under Options 3 and 4. However, for the purposes of determining the affordability of borrowing in accordance with the Prudential Code, the CFR should continue to be calculated as specified in that document.

FINANCE LEASES AND PFI

20. 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 balance sheet liability. Thus, Option 3 will apply in a modified form.

TRANSFERRED DEBT

21. Where debt is transferred between authorities, the authority relinquishing the debt should cease to make MRP in respect of it and the authority taking it over should begin to make MRP as if it were undertaking new borrowing.

CAPITALISED EXPENDITURE

22. Where on or after 1 April 2008 an authority incurs expenditure which is:

- (a) financed by borrowing or credit arrangements; and
- (b) treated as capital expenditure by virtue of either a direction under section 16(2)(b) of the 2003 Act or regulation 20(1) of the 2003 Regulations

the authority should make MRP in accordance with Option 3.

23. For the purpose of the formula in paragraph 9 above, in the initial year of making MRP the variable “C” should be given the following maximum values:

<u>Expenditure type</u>	<u>Maximum value of “C” in initial year</u>
Expenditure capitalised by virtue of a direction under s16(2)(b)	“C” equals 20 years
Regulation 20(1)(a) Expenditure on computer programs	“C” equals the value it would have for computer hardware
Regulation 20(1)(b) Loans and grants towards capital expenditure by third parties	“C” equals the estimated life of the assets in relation to which the third party expenditure is incurred
Regulation 20(1)(c) Any payments to the National Assembly for Wales as result of “pooling of receipts from the disposal of housing land”.	“C” equals 25 years
Regulation 20(1)(d) Acquisition of share or loan capital	“C” equals 20 years
Regulation 20(1)(e) Repayment of grants and loans for capital expenditure	“C” equals 25 years
Regulation 20(1)(f) Expenditure on works to assets not owned by the authority	“C” equals the estimated life of the assets
Regulation 20(1)(g) Payment of levy on Large Scale Voluntary Transfers (LSVTs) of dwellings	“C” equals 25 years