

**Annual MRP Statement**

**Revised MRP Policy for 2016/17 and MRP Policy for 2017/18**

**Background:**

1. For many years local authorities were required by Statute and associated Statutory Instruments to charge to the Revenue Account an annual provision for the repayment of debt associated with expenditure incurred on capital assets. This charge to the Revenue Account was referred to as the Minimum Revenue Provision (MRP). In practice MRP represents the financing of capital expenditure from the Revenue Account that was initially funded by borrowing.
2. In February 2008 the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [Statutory Instrument 2008/414] were approved by Parliament and became effective on 31<sup>st</sup> March 2008. These regulations replaced the formula based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new regulations required a local authority to determine each financial year an amount of MRP which it considers to be 'prudent'. Linked to this new regulation, the Department of Communities and Local Government (CLG) produced Statutory Guidance which local authorities are required to follow, setting out what constitutes a prudent provision.
3. The CLG Guidance recommends that, before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by Full Council. If it is ever proposed to vary the original statement for the current year, a revised statement should be put to the council at that time.
4. The broad aim of the Policy is to ensure that MRP is charged over a period that is reasonably commensurate with the period over which the capital expenditure which gave rise to the debt provides benefits. In the case of borrowing supported by Revenue Support Grant ('Supported Borrowing'), the aim is that MRP is charged over a period reasonably commensurate with the period implicit in the determination of that grant. MRP is not required to be charged to the Housing Revenue Account. Where a local authority's overall underlying need to borrow for capital purposes, known as the Capital Financing Requirement (CFR), is nil or a negative amount there is no requirement to charge MRP.

**MRP Options:**

5. Four options for prudent MRP provision are set out in the CLG Guidance. Details of each are set out below with a summary set out in Table 1 below:

**Option 1 – Regulatory Method:**

6. This method replicates the position that would have existed under the previous regulatory environment. MRP is charged at 4% of the Authority's underlying need to borrow for capital purposes, the Capital Financing Requirement (CFR). The formula includes an item known as "Adjustment A" which was intended to achieve neutrality between the CFR and the former Credit Ceiling, used to calculate MRP prior to the introduction of the Prudential System on 1<sup>st</sup> April 2004. The formula also took into account any reductions relating to the commutation of capital debt made by central government.
7. The latest CLG guidance (effective from 1 April 2012) states that authorities **may** continue to use this method for capital expenditure incurred before 1 April 2008 and supported borrowing, allowing authorities to modify the method if it produces an 'anomalous and disadvantageous result'.

8. This method (which is based on a 4% reducing balance) has been used by the council up until 2015/16 for pre 1 April 2008 and supported borrowing. Under this method however, although the MRP charge reduces each year, the borrowing is never entirely paid off. Consequently, from 2016/17, it is proposed the charge will be based on repaying the debt on a 'straight line' (or equal annual instalment) basis over a 35 year period. This has the advantage of a constant charge which fully repays the debt, which is more prudent. Under the unmodified regulatory method approximately £2.07 million of outstanding debt would still be outstanding after 35 years (see graph 1 below). In addition the effect of this change is that MRP will be lower than it would have been for the first 9 years (with a saving in 2016/17 of around £95,000 in 2016/17), before increasing gradually (see graph 2 below).
9. The annual General Fund MRP charge using this method will be £236,847 starting in 2016/17.

**Option 2 – CFR Method:**

10. This method simplifies the calculation of MRP by basing the charge solely on the authority's CFR but excludes the technical adjustments included in Option 1. The annual MRP charge is set at 4% of the non-housing CFR at the end of the preceding financial year.
11. The General Fund MRP charge for this method is nil for 2016/17 and 2017/18.

**Option 3 – Asset Life Method:**

12. Under this method MRP is determined by the life of the asset for which the borrowing is undertaken. This can be calculated by either of the following methods:
  - (a) Equal Instalments: where the principal repayment made is the same in each year, or
  - (b) Annuity: where the principal repayments increase over the life of the asset.

The annuity method has the advantage of linking MRP to the benefits arising from capital expenditure, where these benefits are expected to increase over the life of the asset.

13. MRP commences in the financial year following that in which the expenditure is incurred or, in the year following that in which the relevant asset becomes operational. This enables an MRP "holiday" to be taken in relation to assets which take more than one year to be completed before they become operational.
14. The estimated life of the asset will be determined in the year that MRP commences and will not be subsequently revised. However, additional repayments can be made in any year which will reduce the level of payments in subsequent years.
15. If no life can be reasonably attributed to an asset, such as freehold land, the life is taken to be a maximum of 50 years. In the case of freehold land on which a building or other structure is constructed, the life of the land will be treated as equal to that of the structure, where this would exceed 50 years.
16. In instances where central government permits revenue expenditure to be capitalised, the Statutory Guidance sets out the number of years over which the charge to revenue must be made. The maximum useful life for expenditure capitalised by virtue of a direction under s16(2)(b) is 20 years.
17. MRP in respect Finance Leases brought onto the Balance Sheet falls under Option 3.
18. The General Fund MRP charge using this method is estimated at £1.119 million 2016/17 and £0.867 million for 2017/18 (subject to approval of the proposal regarding the repayment of debt relating to capital loans made in paragraph 24 below).

**Option 4 - Depreciation Method:**

19. The depreciation method is similar to that under Option 3 but MRP is equal to the depreciation provision required in accordance with proper accounting practices to be charged to the Income and Expenditure account.
20. The General Fund MRP charge for this method is nil for 2016/17 and 2017/18.

**Conditions of Use:**

21. The CLG Guidance puts the following conditions on the use of the four options:

Options 1 and 2 can be used on all capital expenditure incurred before 1<sup>st</sup> April 2008 and on Supported Capital Expenditure on or after that date.

Options 3 and 4 are considered prudent options for Unsupported Capital Expenditure on or after 1<sup>st</sup> April 2008. These options can also be used for Supported Capital Expenditure whenever incurred.

**MRP Policy for 2016/17 and 2017/18:**

22. It is proposed that the council adopts
  - the modified Option 1 – repayment over 35 years on a straight line basis - for borrowing incurred before 1 April 2008, which is Supported Borrowing
  - Option 3 for borrowing after 1 April 2008 and Unsupported Borrowing. For Option 3, the annuity method for calculating MRP will be used when applicable as it has the advantage of linking MRP to the benefits arising from capital expenditure, where these benefits are expected to increase over the life of the asset.

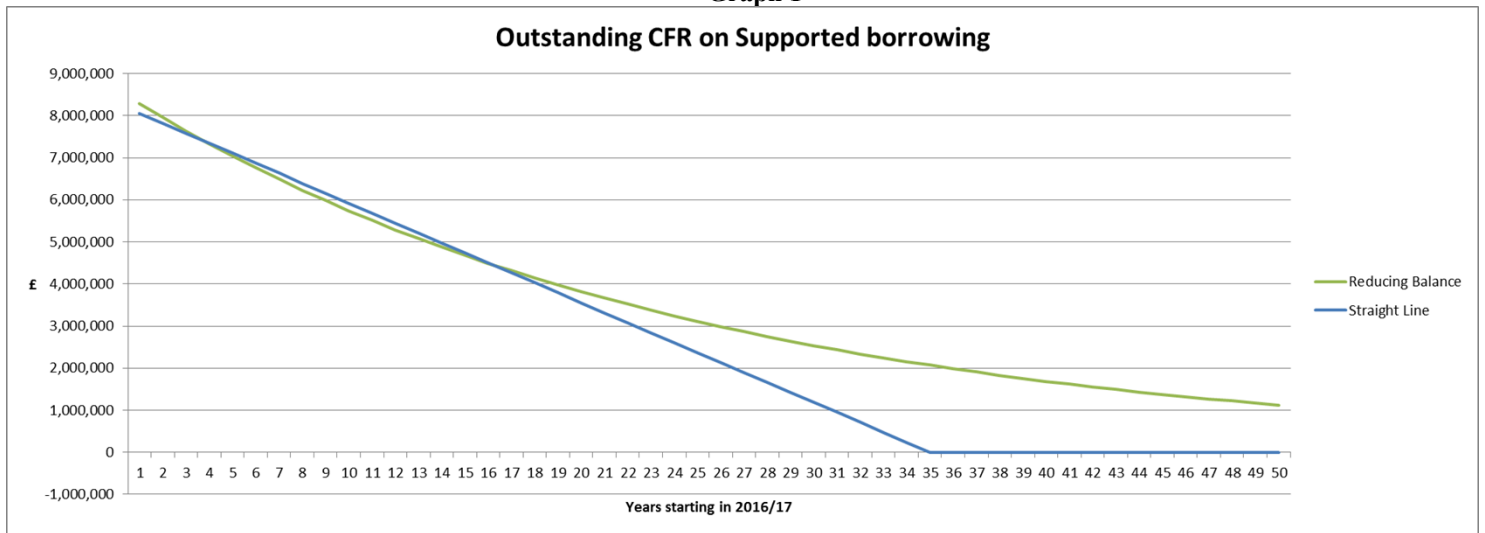
**Repayment of debt relating to capital loans made:**

23. In recent years the council has made a number of capital loans to Gloucestershire Airport, The Everyman Theatre and Cheltenham Borough Homes (CBH) funded from prudential borrowing. Currently the council is setting aside MRP to repay this debt over the life of the loans (equivalent to the estimated life of the capital assets) using option 3's annuity method, as permitted by the CLG guidance. The annual repayments from the borrowers (which match the MRP) must be treated as capital receipts, so are used to fund the capital programme in lieu of revenue funding. In this way the impact of these loans on the revenue account is neutral, since the additional MRP is matched by an equivalent reduction in the revenue funding for the capital programme.
24. This policy, although currently neutral on the revenue account, is however constraining the council's ability to make further capital loans should it wish, since this would increase the MRP further, whilst generating more capital receipts than required to fund the capital programme. The capital finance regulations allow the council to use capital receipts to 'repay the principal of any amount borrowed', therefore it is proposed, from 2017/18, to replace MRP provision for repaying the debt on capital loans with set aside of the equivalent amount from usable capital receipts, equal to the annual repayments of principal by the borrowers. This would reduce the capital receipts available to fund the capital programme, but would also reduce MRP by an equivalent amount. The borrowers are contracted to fully repay the loans over their lives in annual instalments, so all of the debt will be repaid. The amount of debt to be repaid by this method in 2017/18 is approximately £236,000.

**Table 1**  
**MRP under the CLG Guidance**

MRP Options	1 Regulatory Method	2 CFR Method	3 Asset Life Method	4 Depreciation Method
Classifications of Capital Expenditure impacting on the CFR	Capital expenditure incurred before 1 April 2008		Unsupported Capital expenditure incurred after 1 April 2008	
	Supported Capital expenditure incurred after 1 April 2008		Expenditure capitalised by virtue of a Direction under s16(2)(b) of the Local Government Act 2003	
MRP Basis	Former regulations 28 and 29	4% of Non-Housing CFR	Equal Annual Instalments of Principal	Depreciation
Aspects of MRP charges	CFR excludes element attributable to Unsupported Capital Expenditure		EIP commences when asset operational	Depreciation MRP commences when asset operational
			Freehold land 50 years.	Depreciation MRP ceases when CFR component is £Nil
			Freehold land with structure >50 years	Depreciation MRP not adjusted for capital receipt
			Capitalisation periods	Depreciation MRP based on proportion of asset financed from "borrowing".
			PFI/Operating Leases brought on Balance Sheet under IFRS	

**Graph 1**



**Graph 2**

