FOR CONSULTATION

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. "2003 Act" means the *Local Government Act 2003*.
3. "2003 Regulations" means the *Local Authorities (Capital Finance and Accounting) (England) Regulations 2003*. All references to specific "regulations" throughout this document refer to the 2003 Regulations unless otherwise stated.
4. "2007 Act" means the *Local Government and Public Involvement in Health Act 2007*.
5. "Accounting Code" means the *Code of practice on local authority accounting in the United Kingdom*, published by CIPFA and established as proper practices in accordance with regulation 31(a) of the 2003 Regulations.
6. "Capital Financing Requirement" has the same meaning as defined in the *Prudential Code*.
7. "Capital loan" means the giving of a loan which is treated as capital expenditure in accordance with regulation 25(1)(b).
8. "Credit Arrangements" has the meaning given in section 7 of the 2003 Act.
9. "Debt" means borrowing (internal and external) and credit arrangements.
10. "Expected credit loss" has the same meaning as defined in the Accounting Code.
11. "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.
12. "Housing Revenue Account" has the meaning given in section 74(1) of the *Local Government Housing Act 1989.*
13. "Lease" means a lease transaction as defined under the Accounting Code.
14. "Local authority" has the meaning given in section 23 of the 2003 Act.
15. "Major Repairs Reserve" has the meaning given in regulation 7(5) of *the Accounts and Audit Regulations 2015.*
16. "Minimum Revenue Provision" has the meaning given in regulation 27(1) of the 2003 Regulations.
17. "Non-housing CFR" has the meaning given in regulation 28(11) of the 2003 Regulations as originally drafted.
18. "Proper practices" has the meaning as given in Section 21(2) of the 2003 Act.
19. "Prudential Code" means the statutory code of practice, published by CIPFA, referred to in regulation 2 of the 2003 Regulations.

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20. “Prudential Framework” is the legislative framework and relevant statutory guidance that sets the powers, duties and practices by which local authorities borrow and invest.

21. “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 capital expenditure that is supported by capital grant.

22. “Useful Life” has the same meaning as defined in the Accounting Code.

APPLICATION

Effective date

23. This guidance applies for accounting periods starting on or after 1 April 2024. Where changes are required to practices as a consequence of the revisions to regulations and guidance that apply from that date, they should be applied prospectively.

Local authorities

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

INTRODUCTION

25. Under the Prudential Framework (the “Framework”), in place since 2004, local authorities have wide freedoms to borrow and invest without seeking the government’s prior approval. This is underpinned by powers set out in the 2003 Act and the associated 2003 Regulations. The objective of the Framework is to support local decision-making to best meet local needs, while ensuring accountability and driving sound investment and borrowing decisions that are prudent, affordable and sustainable. In addition to the legislation, the Framework also includes four statutory codes that set out best practice and the behaviours the government expects local authorities to demonstrate to meet the objectives of the Framework. Under statute, local authorities must have regard to these codes; “have regards to” has a specific meaning that local authorities should comply with the guidance unless, having duly considered the guidance, there is justifiable reason to depart from it. Decisions that do not "have regard to" relevant guidance may be susceptible to challenge.

26. The duty to make Minimum Revenue Provision (“MRP”) is an important component of the Framework. Where local authorities finance capital expenditure with debt, they must set aside an amount of money each year to ensure that debt can be repaid[1]. In practice, the application is more complex, but when it operates effectively it should ensure that local authorities do not take on more debt than they can afford. Therefore, in deciding whether any capital expenditure is affordable, an authority must consider whether it can meet the cost of the associated MRP charged within an affordable budget. The amount of MRP should be determined with respect to an authority’s Capital Finance Requirement (“CFR”).

[1] Throughout this document, ‘financing’ refers to the general provision of money for expenditure whereas ‘funding’ is used to refer to the means by which the expenditure is ultimately paid for through capital or revenue resources.

27. Under **regulation 27**, local authorities are required to charge MRP to their revenue account in each financial year in respect of all capital expenditure financed by debt. 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**, which gives local authorities flexibility in how they calculate MRP, providing the amount is 'prudent'. In calculating a prudent provision, local authorities are required to have regard to this guidance.

28. The 2003 Regulations were further amended with effect from April 2024 to expressly provide that in determining a prudent provision local authorities cannot exclude any amount of CFR from it calculation, unless by an exception set out in statute. Further, that capital receipts cannot be used to directly replace, in whole or part, the prudent charge to revenue. Specific exceptions were introduced for capital loans, alongside appropriate risk mitigations. These measures were taken to strengthen compliance with the duty to make MRP.

29. Local authorities must comply with the duty to make MRP and failure to do so, through under-charging of MRP, creates risk to the authority, the finance system and to local and national taxpayers. Under-provision can result in a local authority being unable to repay a proportion of its debt, passing the liability to future taxpayers, which will need to be met from capital receipts or accelerated MRP payments. Further, if a prudent charge is not made, then this can also encourage the local authority to take on greater levels of debt than might otherwise be affordable. The duty to charge MRP is an important mechanism in the Framework to constrain risk and ensure the affordability of capital expenditure.

ANNUAL MRP STATEMENT

30. Before the start of each financial year a local authority should prepare a statement of its policy on making MRP (the "MRP Statement") 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.

31. This guidance does not provide prescriptive requirements as to the content and format of the MRP Statement. However, to ensure transparency and accountability, as a minimum the MRP Statement should set out:

    i. the policy to making MRP, the major assumptions applied and the methodologies used;

    ii. any changes to policy or methodologies from the prior year and explain the rationale and financial impact;

    iii. how the local authority has considered the requirements set out in statute and this guidance to ensure it is meeting its duty to make prudent provision;

    iv. a description of any departures from this guidance and explain why the approach adopted results in a more prudent charge;

    v. details as to how capital receipts will be used to reduce indebtedness and the impact on the MRP charge;

    vi. an explanation of where MRP is not being made with respect to any amount of CFR and the statutory basis for this; and

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vii. the detail of any planned voluntary overpayment of MRP.

32. Local authorities may vary the methodologies that they use to determine prudent provision during the year provided there is justifiable reason to do so in compliance with statute, this guidance and proper practices. Local authorities should not change their MRP policy or methodologies where the primary objective of any change is to reduce the revenue charge. When a local authority varies the methodology used to determine prudent provision, they should present a revised MRP statement to the next full Council or equivalent explaining the rationale for the change and the financial impact. Where a change in MRP methodology would impact on the value for money assessment of investments, the updated statement should summarise this impact.

MEANING OF PRUDENT PROVISION

33. **Regulation 27** specifies that local authorities must charge an amount to revenue with respect to all capital expenditure financed by debt. **Regulation 28** requires a local authority to calculate in each financial year an amount of MRP that it considers to be prudent.

34. An underpinning principle of the local authority financial system is that all capital expenditure has to be ultimately funded either from capital receipts, capital grants (or other contributions) or eventually from the revenue of an authority. While local authorities may finance capital expenditure using debt, this debt must be affordable. On this basis, the broad aim of prudent provision is to require local authorities to put aside revenue over time to reduce debt used to finance capital expenditure to nil over an appropriate period.

35. The MRP charge must be calculated with respect to all capital expenditure financed by debt (and which has not yet been provided for). The appropriate measure for this is CFR as, when calculated correctly, this a complete measure of all capital expenditure that has not yet been funded by either capital or revenue resources, and will include capital expenditure financed by external borrowing, internal borrowing and credit arrangements. It is therefore important that when local authorities calculate CFR, they do so accurately and consistently in accordance with the Prudential Code.

36. The Prudential Code sets out that the CFR should relate to all capital expenditure and be calculated directly from the local authority's balance sheet by consolidating its:

    - tangible fixed assets (i.e. property, plant and equipment, heritage assets, investment properties and non-current assets held for sale);
    - intangible assets;
    - long-term debtors relating to capital transactions (where applicable);
    - investments that treated as capital expenditure under proper practices or applicable regulations;
    - revaluation reserve;
    - capital adjustment account;
    - donated assets account;
    - other items on the Balance Sheet that relate to capital expenditure, but excluding the underlying liability.

37. As set out in **regulation 27 (1)(a)**, local authorities cannot exclude any proportion of their CFR from the determination of a prudent charge, because MRP must be charged in respect

of *all* capital expenditure financed by debt. Notwithstanding the allowances for the timing of making the MRP charge (paragraphs 62 and 63), and the specific statutory provision for capital loans (paragraphs 69 to 74), a local authority must calculate the annual prudent charge on the *entirety* of its CFR. An authority may not exclude any amount of CFR when calculating the MRP charge, including where the debt is associated with assets, such as investment assets, that the council believes will retain or increase in capital value.

38. To ensure transparency, local authorities should include in the MRP Statement a description of the calculation of the CFR on which MRP is determined and clearly set out where the authority has not included any amount of debt-financed capital spend within the value of CFR used in the MRP determination (where this is permitted under statute).

39. In determining the period of time over which the debt should be reduced to nil, local authorities should align the period over which they charge MRP to one that is commensurate with the period over which their capital expenditure provides benefits.

40. In the case of historical 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.

41. The government considers that the methods of making prudent provision include the options set out in paragraphs 52 to 58. 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 59 to 63 as far as these are relevant.

42. 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 MRP Statement presented to full Council or equivalent.

MEANING OF A CHARGE TO THE REVENUE ACCOUNT

43. MRP is the prudent charge to revenue which must be determined in accordance with statute and in having regard to this guidance. That is, there should not be circumstances where a prudent charge is determined and a different amount charged to revenue. This is particularly relevant in considering the use of capital receipts to repay debt and the interaction with the MRP charge (paragraphs 67 and 68).

44. A charge to a revenue account for MRP in any financial year cannot be a negative charge.

45. A charge to a revenue account for MRP in any financial year can only be nil if:

    i. A local authority's CFR was nil or negative on the last day of the preceding financial year after excluding any CFR on which MRP is not (or may not be) required under **regulation 27(3) or 27(4)**;
    ii. Where after any such exclusions set out in (i) above, the only remaining CFR relates to the Housing Revenue Account and the local authority has determined no further revenue charge is required with respect to this (as set out in paragraph 65);
    iii. A local authority applies a loan repayment which is a capital receipt in accordance with **regulation 28(5)** such that the revenue charge is nil;
    iv. A local authority reduces its CFR to nil during the financial year using resources other than MRP, including the application of capital receipts, such that the CFR is nil at the year end;

v. A local authority chooses to offset a previous year's overpayment (as set out in paragraph 42) 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 MRP Statement presented to full Council.

LOCAL AUTHORITIES IN GOVERNMENT FINANCIAL SUPPORT

46. In very exceptional cases, where the government has made arrangements to intervene in a local authority and has, or is in the process of, put in place financial support arrangements for that authority, it may be appropriate to reflect the nature of any such financial support in the determination of a prudent amount. Where this is the case the local authority must seek agreement from the government on how any assumptions with respect to support are reflected in the determination of MRP.

CHANGING METHODS FOR CALCULATING MRP

47. A local authority may change the method(s) that it uses for calculating part or all of its MRP at any time provided it has sufficient justification for doing so in accordance with its statutory duty, this guidance and considering proper practices.

48. Where a local authority changes the method(s) that it uses to calculate MRP, it should explain in its MRP Statement, why the change will better allow it to make prudent provision. The primary objective of any change cannot be to reduce the MRP charge. Any methodologies that deviate from this guidance must be accompanied with detail of how the local authority met its duty to have regard to this guidance and on what basis it deems it appropriate to depart, and an assessment of risk.

49. 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 (i.e. it should not be applied retrospectively), as would be the case with a change in accounting estimate in accordance with *International Accounting Standard 8* as adopted for local government by the Accounting Code.

50. Changing the method used to calculate MRP can never give rise to an overpayment in respect of previous years, and should not result in a local authority making a reduced charge or a charge of nil for the accounting period in which the change is made, or in any subsequent period, on the grounds that it needs to recover overpayments of MRP relating to previous years.

TRANSFERRING DEBT

51. 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

52. 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.

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Option 1: Regulatory method

53. 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 2004-05. However, it would be reasonable for local authorities to correct any perceived errors in adjustment A, if the correction would be in their favour.

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

Option 2: CFR method

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

Option 3: Asset Life Method

56. 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 useful 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: 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 useful life of the asset expires. The original estimate of the life is determined at the outset and should not be varied thereafter unless to correct an error.

(b) Annuity method

MRP is the principal element for the year of the annuity required to repay over the asset's useful 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.

Option 4: Depreciation method

57. MRP is deemed 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. This should include any amount for impairment charged to the income and expenditure accounts.

58. 37. 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

59. 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.
60. For expenditure incurred on or after 1 April 2008, which does not form part of the local authority's supported capital expenditure, prudent approaches include options 3 and 4. It is not expected that these options are appropriate for supported capital expenditure.
61. Subject to paragraph 62 below, MRP may commence in the financial year following the one in which the expenditure was incurred. This is specified in **regulation 27(3)**.
62. When incurring capital expenditure towards an asset, the local 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. This is specified in **regulation 27(3).**
63. Where a local authority uses options 3 or 4 or where it uses another methodology that has the useful life of assets as a component to the calculation, it should normally not exceed a maximum useful life of 50 years. Local authorities can exceed this maximum in two scenarios:
    - where a local authority has an opinion from an appropriately qualified professional advisor that an asset will deliver service functionality for more than 50 years it can use the life suggested by its professional advisor; and
    - for a lease or PFI asset, where the length of the lease/PFI contract exceeds 50 years. In this case the length of the lease/PFI contract should be used.

LEASES AND PFI

64. In the case of leases where a right-of-use asset is on the balance sheet and on balance sheet PFI contracts, the prudent charge revenue can be regarded being equal to the element of the rent/charge that goes to write down the balance sheet liability. Where a lease (or part of a lease) or PFI contract is brought onto the balance sheet, having previously been accounted for off-balance sheet, 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 balance sheet liability that arises from the restatement.

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HOUSING REVENUE ACCOUNT

65. Since the 2003 Regulations amendments in 2008, there is no statutory provision that excludes borrowing or credit arrangements used to finance capital expenditure on housing assets i.e. the CFR associated with the Housing Revenue Account ("HRA"), from the duty to make MRP. However, as local authorities are required to charge depreciation to the surplus or deficit on the provision of services in the HRA, in accordance with the requirements of the *Item 8 Credit and Item 8 Debit (General) Determination* and which is then transferred to the Major Repairs Reserve (MRR) in accordance with the Accounts and Audit Regulations 2015 (regulation 7(5)(a)), a local authority may determine that no further revenue charge for MRP is required, provided that it has determined that through its duty to charge depreciation and hold an MRR that prudent provision has been made

INVESTMENT PROPERTIES

66. The duty to make MRP extends to investment properties where their acquisition has been partially or fully funded by an increase in borrowing or credit arrangements. As depreciation is not charged on investment properties, Option 4: *the Depreciation method* is not a suitable approach for calculating the MRP to be charged in respect of investment properties. As set out in paragraph 37, a local authority cannot exclude any proportion of its debt from the determination of a prudent MRP charge on the basis that the debt is associated with an investment asset that the authority believes will retain or increase capital value.

APPLICATION OF CAPITAL RECEIPTS

67. A local authority can use capital receipts to repay debt under **regulation 23**, however, **regulation 28(4)** sets out that an authority may not use capital receipts to directly offset the MRP charge. MRP is a charge to revenue under statute, and the charge to revenue cannot be replaced using a capital resource, unless under the exceptions provided for by **regulation 28(5).**

68. A local authority cannot determine a prudent charge (using options in this guidance or otherwise as appropriate) and then not make that charge to the revenue account on the basis that it is 'offset' or reduced by an equivalent amount of a capital receipt. As set out in paragraph 43, MRP is both the prudent charge and the charge made to revenue. This is no way restricts a local authority from applying a capital receipt to reduce its CFR and then calculating the MRP charge on the residual CFR. As MRP is calculated with respect to CFR, all else being equal, a reduction in CFR should translate to a reduction in the MRP charge for later years.

CAPITAL LOANS

69. **Regulation 27(4)** allows authorities to exclude capital loans that are financed by debt from the requirement to make MRP, provided the loan is not a commercial loan. A commercial loan is defined in **regulation 27(5)** as a loan from the authority to another entity for a purpose which, if the authority were to undertake itself, would be primarily for profit; or, where the loan is itself capital expenditure undertaken primarily for profit. Local authorities *must* make MRP with respect to any debt used to finance a commercial capital loan; paragraph 74 provides further detail on the methodology that should be used with respect to loans which are capital expenditure.

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70. From April 2024, for all new and existing capital loans other than commercial capital loans the amended 2003 Regulations provide local authorities a policy choice as to whether to charge MRP with respect to any debt used to finance a capital loan. Where a local authority has a policy to charge MRP on debt used to finance capital loans (whether elected or mandatory), then **regulation 28(5)** allows the authority to reduce the relevant MRP charge by an amount up to the value of any repayment of that loan received by the local authority. This also applies where the authority is the lessor in a lease arrangement which is accounted for as a loan under proper practices, and the lease payment includes a capital receipt. The option to apply this provision can only be used where that loan repayment is a capital receipt that is used to pay down debt, under **regulation 23**. That is, if a local authority received capital receipts which is a loan repayment and uses this to fund further capital spend, rather than reduce its CFR, then the MRP charge with respect to that loan cannot be reduced.

71. A local authority can only reduce the MRP charge by a loan repayment in the financial year that the repayment is received by the authority and applied to reduce debt under **regulation 23**. A local authority cannot reduce the MRP charge from what is has calculated to be a prudent charge on the *expectation* that a loan repayment will be received in a future financial year.

72. **Regulation 28(2)** specifies that for any capital loan financed by debt, where an expected credit loss or an impairment is recognised in any financial year with respect to that loan in accordance with proper practices, a local authority must include in the MRP charge an amount at least equal to the amount recognised. The reference to expected credit loss refers to the loss recognised in accordance with the expected credit loss model as set out in *International Financial Reporting Standard 9: Financial Instruments* as adopted by the Accounting Code.

73. The intent of **Regulation 28(3)** is to allow that the MRP charge made in accordance with **Regulation 28(2)** may be less than the loss recognised under proper practices only if the CFR with respect to the relevant loan is less than the loan value recognised in the balance sheet to which the loss applies. This will be the case where the local authority has made MRP in prior years with respect to the debt used to finance the loan or otherwise applied resources at any time to reduce or limit the CFR. The intent of this is that at any time a local authority will have fully provided for any amount of a capital loan that will not (or is not expected to) be repaid insofar as that capital loan was financed by debt. A local authority should then always be able to repay its own liabilities, even if it incurred a loss on a loan. If a local authority makes an MRP charge with respect to an expected credit loss that is reversed in a future financial year, it may not treat this as a 'negative' MRP charge, but may treat this as an 'overpayment'. This may be treated in the same way as would a voluntary overpayment, and be used to reduce future MRP charges.

74. Where a local authority makes a capital loan to a third party that is capital expenditure financed by debt, MRP should be made in accordance with Option 3 using the useful life of the assets purchased by the third party as the maximum value of "C" (paragraph 76). That is, the calculation is no different than if the local authority had directly incurred capital expenditure on the assets. Therefore, the time period over which an authority makes MRP may differ from either the term of the loan to the third party or the term of any loan or loans the local authority has undertaken to on-lend.

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CAPITALISED EXPENDITURE

75. Where on or after 1 April 2008 a local 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)** of the 2003 Act or **Regulation 25(1)** of the 2003 Regulations, The authority should calculate MRP in accordance with Option 3.

76. For the purpose of the formula in paragraph 56 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 useful life 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 useful life of the assets for in relation to which the third party expenditure is incurred
Regulation 25(1)(c) Repayment of any grant or other financial assistance given to the local authority for capital expenditure	"C" equals 25 years or the period of the repayment if longer
Regulation 25(1)(d) Acquisition of share capital	"C" equals 20 years
Regulation 25(1)(e) Expenditure on works to assets not owned by the local authority	"C" equals the useful life of the assets
Regulation 25(1)(ea) Expenditure on assets for use by others	"C" equals the useful life of the assets
Regulation 25(1)(f) Payment of levy on large scale voluntary transfers (LSVT) of dwellings	"C" equals 25 years

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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—

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

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),

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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

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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).

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ANNEX B – INFORMAL COMMENTARY ON THE STATUTORY GUIDANCE ON MINIMUM REVENUE PROVISION

Introduction

1. **The main section** of this document contains Statutory Guidance on Minimum Revenue Provision ("the Guidance") issued by the Secretary of State. **Annex A** provides the former **regulations 28 and 29** of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. These have now been amended and have no force in statute. However, the calculations in these Regulations are still used for recommended option 1, the CFR method, so these former regulations have been included as an Annex to this Guidance. **Annex B** provides an informal commentary ("the commentary") the Guidance.

2. Local authorities are normally required each year to set aside some of their revenues as provision for debt. More precisely, the provision is in respect of capital expenditure financed by borrowing or credit arrangements but, both in commentary notes and in the Guidance, it has generally proved more convenient to use the term "debt" as shorthand for that technically more accurate form of expression. Throughout the Guidance, CFR is taken to be the most appropriate measure of overall capital indebtedness provided. Local authorities should therefore determine a prudent MRP charge with respect to the CFR in accordance with statutory provisions and the Guidance.

Application date

3. The Guidance and the commentary apply from 1 April 2024. All previous editions of the MRP Guidance and any commentary published with that Guidance are superseded.

MRP calculation – amendments

4. Amendment **regulation 4(1)** of SI 2008/414 revised the former **regulation 28**. In the new **regulation 28**, the detailed rules are replaced with a simple duty for a local authority each year to make an amount of MRP which it considers to be "prudent". The regulation does not itself define "prudent provision". However, the Guidance makes recommendations to local authorities on the interpretation of that term. The operative date of the change is 31 March 2008, which means that it applies to the financial year 2007/08 and to subsequent years.

5. The 2003 Regulations were further amended in 2024 to expressly provide that in determining a prudent provision local authorities cannot exclude any amount of CFR, unless by an exception set out in statute. Further, that capital receipts cannot be used to directly replace, in whole or part, the prudent charge that is made to revenue. These amendments were as a result of the government's concerns that some local authorities were employing practices that resulted in under-payment of MRP, including not making MRP with respect to debt that was associated with the financing of investment assets, and using capital receipts as a direct replacement for a charge to revenue. To mitigate the risk that these changes could have unintended consequences, specifically where authorities have made capital loans to companies for the purposes of service delivery or housing provision, the amendments also made provision for certain capital loans such that MRP need not be made provided that the loans would be repaid in full.

6. The amendments made, effective from April 2024, introduced more prescription into statute, but were not a substantive policy change. The government was clear at the time that these changes were a "strengthening" of the duty to make MRP. Those local authorities that were

already making prudent provision would be unaffected. The provision with respect to exempting certain capital loans from the duty to make MRP reflected practices identified at that time and gave local authorities statutory provision to continue those practices, with specified risk mitigations to ensure the objective of the MRP duty is still met.

Power to issue guidance

7. The issuing of statutory MRP guidance was made possible by section 238(2) of the Local Government and Public Involvement in Health Act 2007, which amends section 21 of the Local Government Act 2003. Section 21 already allowed regulations to be made on accounting practices and is the power under which the existing MRP regulations were made. The amendment inserts a new section 21(1A) into the 2003 Act, enabling the Secretary of State also to issue guidance on accounting practices and thus on MRP.

8. Local authorities are obliged by new section 21(1B) to "have regard" to such guidance – which is exactly the same duty as applies to other pieces of statutory guidance including, for example, the CIPFA Prudential Code, the CIPFA Treasury Management Code and the DLUHC Guidance on Local Government Investments.

9. The Guidance itself is the front section of this document. This document is Annex B of the Guidance, and provides commentary explaining the policy intention in more detail and including other information to help practitioners.

10. Specific requirements of the Guidance are considered in more detail below. All paragraph references are with respect to the Guidance.

Annual MRP Statement [paragraphs 30-32]

11. Local authorities are asked to prepare an annual statement of their policy on making MRP for submission to their full Council (for authorities without a full Council, approval of the statement should be at the closest equivalent level). This mirrors the existing requirements to report to the council on the prudential borrowing limit and investment policy. The Guidance does not prescribe the contents or the format of the MRP Statement, but does set out minimum expectations of what it should contain in order to allow users of the Statement (including Members and those charged with governance) to understand how the local authority is complying with the duty to make prudent provision.

12. The aim is to give elected Members the opportunity to scrutinise the proposed use of the additional freedoms conferred under the new arrangements. If it is ever proposed to vary the terms of the original statement during the year, a revised statement should be put to the council at that time. To underpin this recommendation, SI 2008/516 amended the Local Authorities (Functions and Responsibilities) (England) Regulations 2000 to specify that of formulating a plan or strategy for the control of the local authority's minimum revenue provision is not the sole responsibility of an authority's executive.

13. Local authorities should not change their MRP policies or method for calculating MRP unless doing so result in a more prudent charge. Changing the approach to MRP can never be justified where the primary objective is to reduce revenue costs.

14. It is for each council to consider with its officers the preferred format of the statement Is it, however, important not only to provide Members the opportunity to review the local authorities MRP policy, but to provide complete and accurate information such that the policy

is clear and transparent, and is sufficient to demonstrate that the local authority is complying with its statutory duty

Meaning of prudent provision [paragraphs 33 – 42]

15. The main part of the Guidance is concerned with recommendations on the interpretation of the term "prudent provision" as used in the amended **regulation 28**. The Guidance includes specific examples of options for making "prudent provision".

16. It explains that provision for the debt which financed the acquisition of an asset should be made over a period bearing some relation to that over which the asset continues to provide a benefit to service delivery (including housing provision and regeneration). This recognises that authorities may structure loans in accordance with cash need and other considerations, and that borrowing is fungible and may not be attributable to individual assets. For this reason, MRP is made with respect to CFR as the measure of indebtedness, and the period it is made over should align with the benefits accrued from the capital expenditure with respect to which the debt was incurred.

17. The government is clear that local authorities should not borrow to invest where the primary objective is to make a financial return. Therefore, all capital spend should be contributing to service delivery or priorities such as housing and regeneration, and MRP can be made over the period the benefits are delivered. The government recognises, however, that some local authorities have historically increased their debt to acquire assets that are primarily for financial return and the Guidance makes clear that MRP must be made on debt used to finance such assets. The amendments to the 2003 Regulations in 2024 were, in part, to address the practice of local authorities not making MRP on debt associated with investment assets on the premise that they retained their capital value and could be sold to repay debt. It has been made clear through amendments to the 2003 Regulations and the Guidance that this is not prudent practice.

18. There are limited circumstances in which a local authority may exclude CFR from the determination of MRP by virtue of the type of capital expenditure, and these are clearly set out in statute and relate specifically to capital expenditure that is a capital loan. These exemptions were introduced in 2024 following consultation, where the sector highlighted that it was the practice of a number of local authorities to not make MRP on capital loans to council owned companies, and that doing so could negatively impact the delivery of housing provision. In response, the 2003 Regulations allow capital loans that are not commercial loans to be exempted from the duty to make MRP. This exemption is accompanied by a duty to make MRP equal to any actual or expected credit loss. The overall objective is that MRP may not be made with respect to capital loans for services and local priorities, so long as the loan will be repaid. This is intended to make local authorities consider very carefully the risk of making capital loans, as there is the potential for significant impact to the revenue budget which could necessitate the need to approach the government for financial support should risks materialise.

The charge to a revenue account [paragraphs 43-45]

19. The Guidance makes clear that MRP is the both charge that it determined to be prudent and the charge that is made to revenue. That is, a local authority cannot determine a prudent charge to revenue in accordance with statute and the Guidance, and then make a *lower*

charge to revenue. For example, a local authority cannot replace part or all of the charge to revenue with a *capital receipt* used to reduce debt. This is discussed in further detail later.

20. The charge to a revenue account for MRP cannot ever be negative. It can only be nil in specific circumstances as set out in the Guidance. These are:

    i. Where a local authority does not have a positive CFR balance at the start of the year. As MRP is calculated with respect to CFR, it follows where CFR is nil, the charge may be nil. This may be because the local authority does not hold any capital debt (all capital expenditure has been fully funded from revenue or capital resources). This may also be where the local authority has a positive CFR balance, but it relates entirely to capital debt used to finance capital spend which may be exempted from MRP under the 2003 Regulations. This will include where the debt-financed assets are not yet in use or where the capital spend relates to a capital loan which the local authority has chosen to not make MRP on. It may also be where the CFR relates entirely to the HRA.

    ii. Where a local authority begins the year with a positive CFR balance, but applies a capital receipt to the balance such that the balance is brought to nil in-year (as above, it may be the case that MRP is also nil after permitted exclusions). As set out in the Guidance, a local authority can never use a capital receipt to directly replace the revenue charge, except where there is specific statutory provision to do so, but this in no way prevents a local authority reducing the CFR on which MRP is determined. Should the CFR be effectively reduced to nil, then it follows the MRP charge will be nil.

    iii. Where the only MRP charge in a financial year would be with respect to debt related to a capital loan, and the authority chooses to apply **regulation 28(5)** that specifically allows a capital receipt that is a loan repayment to be offset against the MRP charge. The provision is intended to allow authorities to not make a charge to revenue with respect to debt-financed capital loans where the loan is being repaid. For absence of doubt, a local authority would need to have a policy of charging MRP on its capital loans in order to offset the charge with the capital receipt/loan repayment. If an authority has a policy of not charging MRP on capital loans (that are not commercial loans), then there is no charge to offset.

    iv. If a local authority has elected to make an overpayment of MRP in a prior year, it may reduce the MRP charge by any such overpayment, which may result in a nil MRP charge. It may also be the case that a local authority has made an overpayment of MRP in a prior year where that payment relates to an expected credit loss that has subsequently been reversed (as set out in paragraph 73 of the Guidance). The local authority must have been clear and transparent in its MRP Statement that it overpaid MRP.

<u>Local authorities in financial support [paragraph 46]</u>

21. Where local authorities are unable to manage financial pressures and as a consequence are financially unsustainable or at risk of being so, local authorities should approach the government for support. The circumstances and causes of financial failure may vary significantly, and the extent to which support is needed will also vary. For some local authorities, one-off cost pressures require limited support whereas in other cases the financial failure may be more pervasive and long-term, with support needed over an extended period. In some cases, the government may determine there is need to intervene and may provide financial support with the objective of supporting the authority back to a sustainable position. In such exceptional cases, the authority should consider in agreement

with the government how the external support may affect the determination of a prudent charge.

22. The Guidance is designed to support effective local decision making in a way that is prudent, affordable and sustainable. It is predicated on local authorities adhering to their statutory duties to set and maintain a balanced budget and meet their best value duties. Where there has been financial failure and government intervention is required, these are exceptional circumstances and it may be appropriate and necessary to take these into account in determining the MRP charge. The statutory duty to make prudent provision remains, however, external support may influence how this is determined including the amount and timing of MRP charges.

23. Where a local authority in financial support intends to deviate from this Guidance, it must only do so in agreement with the government as the assumptions will be contingent on government actions.

Change in methods for calculating MRP [paragraphs 47 – 50]

24. Local authorities cannot reduce their MRP charge or take a "payment holiday" by changing the methodology that they use to calculate MRP to give rise to a historical overpayment.

25. MRP should be treated consistently with any accounting estimate under proper practices. In accordance with IAS 8, as adopted by the Accounting Code, changes to accounting estimates are to be prospective, and any changes to the calculation of MRP should therefore be applied over the remaining life of the asset to which the remaining CFR relates

26. Adopting this approach will require local authorities to spread the benefit of charging a lower annual MRP to council tax payers over time, rather than taking all of the benefits up front at the expense of longer term financial sustainability.

Options for prudent provision [paragraphs 52 – 58]

27. Four ready-made options are included in the Guidance (and there are two alternatives under Option 3). The options are those likely to be most relevant for the majority of local authorities but other approaches are not meant to be ruled out, provided that they are fully consistent with the statutory duty to make prudent revenue provision. Any method used by local authorities must comply with statutory provisions.

28. Local authorities must always have regard to the Guidance, but having done so, may in some cases consider that a more individually designed MRP approach is justified. That could involve taking account of detailed local circumstances, including specific project timetables and revenue-earning profiles.

29. Local authorities should, however, never pursue alternative methods where the primary aim is to reduce the charge to revenue; the objective of the Prudential Framework to ensure that all borrowing and investment is prudent, affordable and sustainable must be the primary consideration.

30. Local authorities may wish to consult their legal advisers and external auditors about their approach to MRP if it involves a significant departure from the Guidance or relates to any large, complex or novel schemes.

Option 1: Regulatory Method [paragraphs 53 - 54]

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31. For debt which is supported by the government through revenue support grant (RSG), authorities may continue to use the formulae in the current regulations, since the RSG is calculated on that basis. Although the original regulation 28 was revoked by regulation 4(1) of the 2008 Regulations, authorities will be able to calculate MRP as if it were still in force. The earlier regulations relevant to MRP are included in this Guidance at Annex A.

32. Normally, under this option, the former regulations should be followed exactly as if they had not been revoked. That includes taking advantage, if desired, of the commutation adjustment in the former regulation 29.

33. When introducing the new MRP regime in 2004, as part of the Prudential Framework, the government's policy aim was that the move from the former MRP scheme should not itself increase any authority's MRP liability. Safeguards to achieve that result were built in from the outset (or added later as anomalies came to light).

34. The main device for achieving the neutrality between old and new MRP systems was "Adjustment A" in the original regulation 28. This was an amount to be calculated at the start of the new system in 2004 and not subsequently varied. For the purposes of Option 1, Adjustment A should therefore continue to be given the value attributed to it in the financial year 2004-05, even if that value reflected erroneous calculations under the former capital finance system which reduce MRP liability under the present system. If, however, Adjustment A reflects an error which increases the current MRP liability, the local authority would be justified in recalculating it and hence reducing MRP to its proper level.

35. Similarly, if a local authority considers that, in its particular circumstances, strict compliance with any other aspect of the former regulations would produce an anomalous and disadvantageous result, it may consider modifying the rules to achieve the intended neutrality. Again, such a step should be discussed in advance with external auditors.

<u>Option 2: CFR Method [paragraph 55]</u>

36. This is a technically much simpler alternative to Option 1 which may be used in relation to supported debt. While still based on the concept of the Capital Financing Requirement, which is easily derived from the balance sheet, it avoids the complexities of the formulae in the old regulation 28 (though for most local authorities it will probably result in a higher level of provision than Option 1). It does however still rely on definitions in the original regulation 28(11), which are as follows:

    "Non-housing CFR" means that part of the capital financing requirement which is not housing CFR. "Housing CFR" means that part, if any, of the capital financing requirement which is in respect of borrowing or credit arrangements used to finance capital expenditure on housing assets. "Housing assets" means any land, houses or other property to which subsection (1) of section 74 of the Local Government and Housing Act 1989 (duty to keep Housing Revenue Account) for the time being applies.

<u>Option 3: Asset Life Method [paragraph 56]</u>

37. For new borrowing under the Prudential Framework for which no government support is being given and is therefore self-financed, there are two options included in the Guidance.

38. Option 3 is to make provision over the estimated life of the asset for which the borrowing is undertaken. This is a possibly simpler alternative to the use of depreciation accounting

(Option 4), though it has some similarities to that approach. Within option 3, two methods are identified.

39. The first of these, the equal instalment method, allows the use of the simple formula in paragraph 56(a) of the Guidance. This will normally generate a series of equal annual amounts over the estimated life of the asset. The original amount of expenditure (“A” in the formula) remains constant. The cumulative total of the MRP made to date (“B” in the formula) will increase each year.

40. The outstanding period of the estimated life of the asset (“C” in the formula) reduces by 1 each year. For example, if the life of the asset is originally estimated at 25 years, then in the initial year when MRP is made, C will be equal to 25. In the second year, C will be equal to 24, and so on. The original estimate of the life is determined at the outset and should not be varied thereafter, even if in reality the condition of the asset has changed significantly (paragraph 56).

41. The formula allows a local authority to make voluntary extra provision in any year. This will be reflected by an increase in amount B and will automatically ensure that in future years the amount of provision determined by the formula is reduced.

42. The alternative is the annuity method (paragraph 56(b)), which has the advantage of linking MRP to the flow of benefits from an asset where the benefits are expected to increase in later years. It may be particularly attractive in connection with projects promoting regeneration or administrative efficiencies or schemes where revenues will increase over time.

43. Freehold land cannot properly have a life attributed to it, so for the purposes of Option 3 it should be treated as equal to a maximum of 50 years (paragraph 63). But if there is a structure on the land which the authority considers to have a life longer than 50 years, that same life estimate may be used for the land.

44. Provision for debt under Option 3 will normally commence in the financial year following the one in which the expenditure is incurred (paragraph 61). But paragraph 62 of the Guidance highlights an important exception to this rule. In the case of the provision of a new asset, MRP would not have to be charged until the asset came into service and would begin in the financial year following the one in which the asset became operational. This “MRP holiday” would be perhaps 2 or 3 years in the case of major projects, or possibly longer for some complex infrastructure schemes, and could make them more affordable. There would be a similar effect in the case of Option 4 under normal depreciation rules.

45. Since 2024 the 2003 Regulations specifically provide that MRP is not required to be made until the financial year after the capital expenditure or until the asset is in use if later. The legislation specifies that MRP must be made when the asset is ‘available for use’ and this has the same meaning as used in the Accounting Code. This is expected to be when the asset ceases to be classified as ‘assets under construction’ because it is in use. This provision was added to ensure that local authorities could continue practices that were permitted under the 2018 Guidance following amendments to the 2003 Regulations from April 2024.

Option 4: Depreciation Method [paragraphs 57 to 58]

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46. Alternatively, for new borrowing under the Prudential system for which no government support is being given, Option 4 may be used. This means making MRP in accordance with the standard rules for depreciation accounting.

47. Authorities will normally need to follow the standard procedures for calculating depreciation provision. But this Guidance identifies some necessary exceptions:

    a) MRP continues until the total provision made is equal to the original amount of the debt and may then cease.

    b) The capital receipt from the disposal of the asset may not be used for revenue spending. Capital receipts may be used only as specified in **regulation 23** of the 2003 Regulations.

    c) If only part of the expenditure on the asset was financed by debt, the depreciation provision is proportionately reduced.

Use of Options [paragraphs 59 – 63]

48. The intention is that Options 1 and 2 should be used for government-supported borrowing. Options 3 and 4 are meant to be used for all self-financed borrowing.

Commencement of MRP [paragraphs 61-62]

49. Regulation 27(3) provides that where capital expenditure is financed by debt, MRP can commence in the financial year following the expenditure or that MRP may not be provided for with respect to assets financed by debt until they are 'assets in use'. These provisions were added to the 2003 Regulations to apply from April 2024, but to the extent that this only provides a statutory basis for a practice that was permitted under the previous Guidance, this is not a change in policy.

50. The premise is to allow the matching of the benefits of the capital expenditure to the period over which MRP is charged. Long term projects, for example infrastructure or regeneration, may be transferred from "assets under construction" to "available for use" over a number of years. Available for use has the same meaning as used in the Accounting Code i.e. when the asset is in the location and condition necessary for it to be capable of operating in the manner intended by management. Local authorities should consider commencing to provide MRP on debt, apportioned by when each stage of the project transfers is available for use.

Estimated useful life of assets [paragraph 63]

51. Local authorities should not make capital investments that can only be justified as being value for money by providing for MRP over a much longer period that any debt instruments taken out to finance acquisition. Under current Public Works Loan Board (PWLB) terms, local authorities can typically refinance their debt. However, it is impossible to guarantee that PWLB terms of trade for new loans will remain unchanged over the lifetime of existing loans. If PWLB terms of trade changed for new loans, local authorities that had otherwise expected to be able to freely refinance existing debt may instead be required to choose between significantly increasing their annual charge to 'top-up' their MRP or develop other plans to manage increased liquidity risk on repayment of debt.

52. Whilst the normal maximum asset life has been set at 50 years, the Guidance recognises that there may be circumstances where this maximum can be prudently exceeded. By service

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functionality, the Guidance means assets that are directly used to deliver the functions of the authority. It does not include investment assets. Where local authorities are applying asset lives longer than 50 years, they should discuss this with their auditors and, where necessary, DLUHC.

Leases and PFI [paragraph 64]

53. Adoption of International Finance Reporting Standard 16 introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is low value. Implementation of this standard is expected to bring more lease contracts and the related assets and liabilities onto the balance sheet.

54. When these lease contracts along with the related assets and liabilities come onto the balance sheet, a local authority will increase its long term liabilities. This will increase the quantum of debt that MRP needs to cover. Generally accepted accounting practice requires these changes to be accounted for retrospectively, with the result that an element of the rental or service charge payable in previous years (and previously charged to revenue accounts) will be taken to the balance sheet to reduce the liability. On its own, this change in the accounting arrangements would result in a one-off increase to the capital financing requirement and an equal increase in revenue account balances.

55. This is not seen as a prudent course of action and the Guidance aims to ensure local authorities are in the same position as if the change had not occurred. It does this by recommending the inclusion in the annual MRP charge of an amount equal to the amount that has been taken to the balance sheet to reduce the liability, including the retrospective element in the first year. This approach will produce an MRP charge comparable to that under Option 3, in that it will run over the life of the lease or PFI scheme and will have a profile similar to what the annuity method gives. DLUHC recognises the complexity of the accounting in this area and acknowledges that the recommendations in paragraph 64 of the Guidance and in this commentary may not be entirely appropriate in all cases. It will be open to local authorities to consider a different approach to the calculation, subject to compliance with the overriding statutory requirement to make a prudent level of MRP.

Housing assets [paragraph 65]

56. Under regulation 28 of the 2003 Regulations prior to its amendment by the 2008 Regulations, the duty to make MRP did not extend to cover borrowing or credit arrangements used to finance capital expenditure on housing assets (HRA CFR). Since 2008, there has been no statutory basis on which CFR associated with the HRA is excluded from the duty to make a prudent charge to revenue. Guidance cannot override the statutory provision. Therefore, since 2008, local authorities have a duty to determine a prudent MRP charge with respect to HRA CFR. Not making a revenue charge for HRA CFR can only be consistent with statute if such a charge is determined to be nil. The amendments to the 2003 Regulations in 2024 have not changed this.

57. Although HRA CFR is not exempt from the determination of a prudent charge, the government expects that a prudent charge can be nil. The rationale for this is that local authorities with HRAs are required to charge depreciation to the surplus or deficit on the provision of services in the HRA, in accordance with the requirements of the *Item 8 Credit and Item 8 Debit (General) Determination* and which is then transferred to the Major Repairs

Reserve (MRR) in accordance with the Accounts and Audit Regulations 2015 (regulation 7(5)(a)). This serves a similar function as MRP in that the cost of capital is passed to the revenue account over time. Further, unlike MRP, the MRR is not incorporated into the calculation of CFR. Due to this statutory requirement that is specific to the HRA, it is reasonable that a local authority may determine that no further charge to revenue is required with respect to the HRA CFR.

58. This does not remove the requirement for an authority to consider the debt associated with its HRA and ensure sufficient provision is made over the life of the assets to repay debt, and make additional charges with respect to MRP if deemed necessary.

Investment properties [paragraph 66]

59. Where a local authority classifies an asset as an investment property, it is declaring that it is holding that asset primarily for financial return i.e. for rental income or capital appreciation. Therefore, it should fully provide for debt taken on to acquire that asset over the lifetime of that debt. In addition, as investment properties are not subject to depreciation, Option 4 – the depreciation method, is not appropriate for calculating prudent provision and cannot be used.

60. The Guidance recognises that some local authorities may have made different assumptions when they acquired investment properties. For this reason the maximum life that should be used for calculating MRP on such assets has been set at 50 years, which is the maximum loan period for PWLB debt.

Application of capital receipts [paragraph 67-68]

61. From April 2024, regulation 28(4) specifically prohibits local authorities using capital receipts to directly reduce the MRP charge (the exception is if a loan repayment is used in accordance with regulation 28(5)). The amendment was made in response to government identifying that some local authorities were using capital receipts in such as a way as to reduce the MRP charge to a low or even negligible amount through directly offsetting with a capital receipt. For example, if a prudent charge were calculated with respect to a CFR of £100m were £4m, using the methodology set out by the authority in its MRP Strategy, then if in the same year £3m of capital receipts were applied to reduce the CFR an authority might only charge £1m to revenue. This is not correct as the outcome is as if the capital receipts had replaced the charge to revenue. As set out, MRP is both the charge determined to be prudent and the charge to revenue.

62. This is no way prevents a local authority applying capital receipts to reduce the CFR in accordance with regulation 23(b) or (d), which permit the use of capital receipts to repay the principle of any amount borrowed or the liability of a credit arrangement. But in such cases, taking the example above, the capital receipt would be applied to reduce the CFR to £96m on which a prudent determination would be made. This has the important objective of ensuring that local authorities need to consider the full implications of capital debt each year, and avoids the potential to delay the consequences to revenue by using capital receipts thereby pushing the risks into the future.

Capital loans [paragraphs 69 to 74]

63. From April 2024, specific statutory provisions apply to capital expenditure which is a capital loan provided by a local authority to a third party (regulation 27(4)). The basis for this is that

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when the government strengthened the MRP duty through amendments to the 2003 Regulations in 2024, local authorities highlighted risks to the delivery of local investment through companies, particularly with respect to housing delivery. Many authorities expressed the view through consultation that being required to make MRP on such loans would make the projects financially inviable. In response, the government made provision that local authorities may choose to not make MRP on debt used to finance capital loans.

64. To safeguard the exemption for capital loans, the government also put in place measures designed to reduce associated risk. Firstly, the exemption does not apply to 'commercial loans'. That is, loans that are for capital expenditure which if incurred directly by the local authority would be primarily for financial return. A loan may also be a commercial loan if it was made primarily for financial return, for example, to make a profit on the interest charged. Where a local authority has incurred debt in providing a commercial capital loan, it must make MRP.

65. Where MRP is made with respect to a capital loan (by choice or required) a local authority may reduce the MRP charge by an amount up to the value of a repayment against the relevant loan only provided the capital receipt is set side to reduce debt. This may only be done in the financial year that the capital receipt is received and used to reduce the CFR. The objective is to allow authorities to avoid a revenue charge to the extent that the loan is being repaid. This also applies where a local authority is a lessor in a lease arrangement which, under proper practices, is accounted for as the local authority having provided a loan which is financed by debt. In these circumstances, where an annual repayment is received the amount that is treated as capital and reduces the loan value may be taken to offset the MRP charge under regulation 28(5).

66. To further mitigate risk with respect to capital loans, regulation 28(2) provides that a local authority must include within its MRP charge an amount at least equal to any expected or actual credit loss as recognised in its accounts under proper practices. International Financial Reporting Standard 9: Financial Instruments (IFRS 9) was adopted by the Accounting Code in 2018. It requires that entities must recognise an *expected credit loss* (ECL) based on an estimation of credit losses at each reporting date, even if no loss event has occurred. Actual credit losses occur when there is no realistic expectation of recovering cashflows, and represents a derecognition event for part or all of the financial asset. The relevance of IFRS 9 to the Guidance is insofar as it applies to financial instruments which are loans.

67. Irrespective of a local authority's policy of charging MRP on capital loans, it must include within its MRP charge the amount of loss recognised under IFRS 9. The charge made through MRP may only be less than the loss recognised where the CFR with respect to the loan to which the loss relates is less than the outstanding loan amount. This would be because the local authority had either reduced the CFR through MRP or through the use of capital receipts to fund the loan (applied when the loan was made or subsequently to reduce the outstanding debt). As a simplified example, an authority provides a maturity capital loan of £10m, but £2m of this is funded by capital receipts and MRP is made at £0.5m per year on the remaining £8m financed by debt (a straight-line charge over 16 years). By year 5, the CFR with respect to the loan is £6m, but the carrying amount on the balance sheet remains £10m as none of it has been repaid. If a loss (an impairment or under the ECL model) is then recognised of £5m, the authority is not required to take this in full as an MRP charge as £4m is already provided for. The authority should take £1m as the MRP charge. The authority

has now set aside £5m ensuring that the amount that is the (potentially) non-recoverable element of the loan has been provided for.

68. As local authorities are required to follow IFRS 9 for the purposes of statutory financial reporting, the requirement to match MRP to the loss allowance or write-off is intended to provide a consistent and understood methodology for reflecting the risk of non-recovery of loans and ensure that prudent provision is made. The intended overall objective is that a local authority will be able to repay its own liability because the loan has been repaid in full, or it has sufficiently provided for any loss it has incurred.

69. Where a local authority recognises an expected credit loss and this is reversed in a future financial year in accordance with IFRS 9, the local authority cannot reverse the historic MRP charge that had been made as a result of the expected credit loss. However, a local authority may treat an MRP charge that was made with respect to a recognised expected credit loss that has been subsequently reverse as a historic overpayments and adjust future MRP charges in accordance with the Guidance.

Capitalised Expenditure [paragraphs 75-76]

70. Revenue costs may be treated as capital expenditure by virtue of either a capitalisation direction (section 16(2)(b) of the 2003 Act) or regulation 25(1) of the 2003 Regulations. Where these costs are financed by debt, this will increase the local authorities CFR and require MRP to be made.

71. The Guidance recommends that MRP in such cases is determined under Option 3. However, since the expenditure does not relate (directly at least) to an asset for which a life can be estimated, guidance is given on how to determine the value of the variable “C” in the formula in paragraph 76 of the Guidance.

72. The table in paragraph 76 of the Guidance gives the value of “C” for each of the categories listed in regulation 25(1). The basic principle is that, where the capitalised expenditure can be indirectly linked to an asset, the estimated life of that asset should be used.

73. In other cases, 25 years is proposed as a reasonable default. But for the acquisition of share capital (regulation 25(1)(d)), the slightly shorter period of 20 years is specified, because the aim of that regulation is to discourage the use of those particular forms of investment.

74. Similarly, 20 years is specified in the case of expenditure capitalised by direction, since the government again does not wish to encourage reliance upon that practice.

75. It should be noted that the value of “C” given in each case applies only in the initial year of making MRP. Subsequently, the value will decrease by 1 in each successive year.

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