TREASURY MANAGEMENT STRATEGY 2020/21

ANNEX F – Minimum Revenue Provision (MRP) Strategy 2020/21 - 2022/23

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1. Minimum Revenue Provision (MRP) Strategy

1.1 Local authorities are required to set aside 'prudent' revenue provision for debt repayment (MRP) where they have used borrowing or credit arrangements to finance capital expenditure. Statutory Guidance covering Minimum Revenue Provision (MRP) was revised and updated in February 2018 by the Ministry of Housing Communities and Local Government (MHCLG) and applies to accounting periods on or after 1 April 2019. The guidance sets out various options and boundaries for calculating prudent provision which are set out in paragraph 1.5 below.

1.2 Local authorities can vary the Minimum Revenue Provision methodologies they use during the year and if they do so must present a revised Minimum Revenue Provision statement to the next full Council. Where a change would impact on the value of money assessment of non-financial investments the updated statement should summarise this impact.

1.3 Under the new guidance, where a change takes place the calculation of Minimum Revenue Provision under the new method should be based on the residual Capital Financing Requirement (CFR) at the point the change in method is made (i.e. it should not be applied retrospectively). Changing the method used to calculate Minimum Revenue Provision 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 charge of £nil for the accounting period in which the charge is made, or in a subsequent period, on the grounds that it needs to recover overpayments of Minimum Revenue Provision relating to previous years.

1.4 Whilst 'prudent provision' is not specifically defined, the guidance suggests that debt ought to be repaid over a period that is either commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Revenue Support Grant, it is reasonably commensurate with the period implicit in the determination of the grant.

1.5 There are four options set out in the statutory guidance for determining the Minimum Revenue Provision:

Option 1 - Regulatory Method
Option 2 - The Capital Financing Requirement (CFR) Method
Option 3 - Asset Life Method (the Minimum Revenue Provision is determined by reference to the life of the asset either by equal instalments of principal or the annuity method)
Option 4 - Depreciation Method (Minimum Revenue Provision is equal to the provision required under depreciation accounting).

1.6 Options 1 and 2 may only be used in relation to capital expenditure incurred before 1April 2008, which form part of its supported capital expenditure. For expenditure incurred on or after 1 April 2008, which does not form part of the authority's supported capital expenditure, prudent approaches include options 3 and 4.

1.7 Minimum Revenue Provision (MRP) Policy Statement for 2020/21 is as follows:

(i) In 2016/17 under the previous Statutory Guidance on Minimum Revenue Provision the Council changed its policy on all supported capital expenditure incurred prior to 1st April 2008 and for future supported capital expenditure, the Minimum Revenue Provision is based on the 2% straight line method, before making an adjustment for £24.1m, which is the difference between debt calculated under the prudential code (as at 1 April 2004) and debt calculated under the previous 'statutory' capital controls regime which commenced on 1 April 1990. This method is considered to be better than the previous method because it ensures that all the debt incurred prior to 1 April 2008 is repaid over a finite number of years. The method will continue to be used for 2020/21 and for future years.

(ii) For capital expenditure incurred after 1 April 2008 and financed by unsupported borrowing, a major proportion of the Minimum Revenue Provision will be based on option 3, the Asset Life Method. This method is considered both appropriate and prudent and will continue to be used in 2020/21.

(iii) In exceptional circumstances Minimum Revenue Provision for capital expenditure incurred after 1 April 2008 and which is funded by unsupported borrowing can be calculated using the Annuity Method (a variation allowed under option 3 of the 2018 Regulations). However, this method is only suitable for particular types of capital expenditure projects where the benefits are expected to increase in later years or where the income stream generated by the new project mirrors the Annuity profile. It may be particularly attractive in connection with projects promoting regeneration or administrative efficiencies where revenues will increase over time. This method may only be used if it receives approval by the Treasury Management Panel.

(iv) In the case of finance leases, where a right-of-use asset is on the balance sheet, and on balance sheet PFI contracts, the Minimum Revenue Provision requirement is by a charge equal the element of the rent/charge that goes to write down the balance sheet liability.

(v) Where on or after 1 April 2008 expenditure is incurred which is:

- Financed by borrowing or 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 majority of Minimum Revenue Provision will be calculated in accordance with Option 3, the asset life method. The asset life used is set out in the table for the relevant expenditure type which is included in the Statutory Guidance on Minimum Revenue Provision (4th Edition) issued on 2 February 2018.

(vi) In the case of investment properties below £500,000 where their acquisition has been partially or fully funded by an increase in borrowing or credit arrangements, Minimum Revenue Provision will be charged in accordance with option 3, the Asset Life Method.

(vii) In accordance with the Statutory Guidance no Minimum Revenue Provision will be charged on borrowing or credit arrangements used to finance capital expenditure on housing assets,

to which Section 74(1) of the Local Government Housing Act 1989 applies.

(viii) The Council provides loans to wholly owned subsidiaries on a commercial basis. Under these arrangements, the cash advances are used by the companies to fund capital expenditure which in turn improves the standard of rented housing available in the local area and also improves the standard of local transport. These loans are funded by borrowing which in turn increases the Capital Financing Requirement (CFR). Loan repayments of principal are treated as a capital receipt and are available to be offset against the CFR. As a result there is no need to set aside MRP to repay the increased borrowing. The outstanding loans are reviewed on an annual basis and if necessary a provision for Minimum Revenue Provision will be made.

(ix) Including the business loans made to wholly owned subsidiaries above the Council's Business Loans Fund provides loan finance to businesses to help regenerate the local economy. The loans are made by the Council on a commercial basis and follow a comprehensive due diligence process, ensuring that recipients of the loans provide security against non-repayment and also have in place a valid and robust business plan. As with the loans to subsidiary companies, these third party loans are funded by borrowing which also increases the CFR. Loan repayments of principle are treated as a capital receipt and are available to be offset against the CFR. As a result there is no need to set aside Minimum Revenue Provision to repay the increased borrowing. The outstanding loans are reviewed on an annual basis and if necessary a provision for Minimum Revenue Provision will be made.

(x) In the case of investment properties over £500,000, Minimum Revenue Provision will be applied on an impairment basis. The council has the ability to sell an investment asset or action a number of varied approaches to raise capital – for example, joint venture, equity share, partial sale or additional lease. Through raising capital from the sale of the asset or an alternative route, the Council is able to repay any outstanding debt liabilities related to the purchase. Assets will be valued on an annual basis and Minimum Revenue Provision will be charged on the amount of the fall in the value of the asset, which allows the council to set aside a prudent provision for repayment of outstanding debt. For assets acquired within 12 months, the cost of acquisition will be regarded as the asset's value, unless a material change in the occupation or condition of the building occurs and/or the market undergoes a significant change. In light of major purchases approved in 2019/20, this approach will be used from 2019/20 and will continue to be used in 2020/21.

(xi) The above policy will ensure that the Council satisfies the requirement to set aside a prudent level of Minimum Revenue Provision.

The Minimum Revenue Provision Strategy is currently under external review, any subsequent changes following the evaluation will be brought to a future meeting. The review is a relatively long term action and no amendments are anticipated before the Budget Council meeting on the 9 March 2020.