Report To:	Audit and Governance Committee.
Date:	Wednesday, 29 January 2025.
Subject:	Update on changes to Statutory Guidance: “Capital Finance: Guidance on Minimum Revenue Provision” and the IFRS9 Statutory Accounting Override for Pooled Investments
Purpose:	To provide Members with an update on changes to the Statutory Guidance: “Capital Finance: Guidance on Minimum Revenue Provision”, the IFRS9 Statutory Accounting Override for Pooled Investments and the impact of these on the Council.
Key Decision:	No
Portfolio Holder:	Cllr Thomas Kemp, Portfolio Holder for Finance.
Report Of:	Christine Marshall, Deputy Chief Executive - Corporate Development (S151).
Report Author:	Sean Howsam, Interim Treasury Manager (PSPSL).
Ward(s) Affected:	None directly.
Exempt Report:	No

Summary

This report updates Members on recent changes to Statutory Guidance “Capital Finance: Guidance on Statutory Minimum Revenue Provision” which is mainly effective from the 2025/26 financial year.

Statutory Guidance on Minimum Revenue Provision prescribes how Council’s calculate their annual Minimum Revenue Provision (MRP) charge for all unfinanced capital expenditure which makes up its Capital Financing Requirement (CFR).

The Statutory Accounting Override in relation to Pooled Investments ends on 31 March 2025 and this report updates on the current Government stance which is that they are not minded to extend the override.

As this report is a Treasury Management Report it is being brought to Audit and Governance for scrutiny prior to its submission to Council on 5 March 2025.

Recommendations

It is recommended that Members of the Audit and Governance Committee:

1) Note the changes to Statutory Guidance "Capital Finance: Guidance on Statutory Minimum Revenue Provision".
2) Consider the proposed changes to the 2025/26 MRP Policy (paragraph 2.7) which will be recommended to Council as part of the budget setting report (included in the Treasury Management Strategy 2025/26) which will detail how MRP will be calculated on the unfinanced capital equity investments in Property Funds.
3) Note the increased MRP budget pressure on the Council in relation to its total unfinanced capital equity investment in Property Funds starting from the 2025/26 financial year.
4) Note the implications to the Council resulting from the ending of the Statutory Accounting Override for pooled investments from the 2025/26 financial year.

Reasons for Recommendations

The CIPFA Code of Practice for Treasury Management suggests that members should be informed of Treasury Management activity. As there is legislation and statutory guidance change in relation to Treasury Management with financial implications to the Council, this report is being brought to Audit and Governance for scrutiny, prior to its submission to Council. This report therefore ensures this Council is embracing Best Practice in accordance with CIPFA's revised Code of Practice.

Other Options Considered

As this is an update report there are no further options for consideration, but Members of the Audit and Governance Committee will be able to make any observations or comments to Council for its consideration as they see fit.

1. Background

1.1 The Council approves a Capital Programme each year as part of the budget setting report. This capital expenditure can be financed from grant receipts or the use of reserve balances such as capital receipts or other reserves. Expenditure financed in this way does not increase the Council's Capital Financing Requirement (CFR) (also referred to as an underlying need to borrow). Where the capital expenditure is financed, there is no requirement to make a Minimum Revenue Provision (MRP) charge annually over the lifetime of the asset because it has been paid for.

1.2 Where capital expenditure is "unfinanced" this creates an "underlying need to borrow" which subsequently increases the Council's CFR and this requires the Council to charge MRP annually over the lifetime of the asset. Where there is a borrowing requirement, the Council has the option to externally borrow (usually from the Public Works Loan Board (PWLB)) to cover the expenditure or it can internally borrow (utilise its cash balances) if it is a Council which is generally a net lender.

1.3 The Council is required to approve its MRP Policy ahead of each financial year as part of the budget setting report. This policy explains how the Council will calculate the MRP charge on its unfinanced capital expenditure.

2. Report

Statutory Minimum Revenue Provision Changes

2.1 On 10 April 2024, the Secretary of State issued "Capital Finance: Guidance on Minimum Revenue Provision (5th edition) which replaced the previous version of this guidance.

2.2 The new guidance is effective for accounting periods on or after 1 April 2025 except for any new capital loan issued from 7 May 2024. MRP on these new loans must be calculated based on the new guidance.

2.3 The first charge of MRP is made in the first full financial year after the year in which the expenditure is incurred and there is no change to this under the new guidance.

2.4 Where applicable, MRP in respect of assets acquired under Finance Leases or Private Finance Initiative (not applicable) will continue to be charged at an amount equal to the principal element of the annual repayment under the new guidance.

2.5 Unfinanced Capital Loans

Where a Council has unfinanced capital loans, under the new guidance it has been made clear that where a loan repayment is used to reduce the MRP charge it can only be used to reduce the MRP charge relating to the loan for which the payment is received.

From April 2025 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.

The treatment of Expected Credit Losses (ECL) and impairment on capital loans has been clarified as follows:

> The use of capital receipts (which are loan repayments) to be used in lieu of MRP charges with respect to ECL's or impairments has been clarified that this is not permitted.

There is now a requirement to include in the MRP charge an amount equal to any ECL or impairment (subject to permitted reductions) but this only applies to capital loans made by a local authority from the 7 May 2024 and not to any loan made prior to that date. The Council issued £385k of unfinanced capital loans to Invest East Lindsey prior to 7 May 2024.

Where new unfinanced capital loans have been issued on or after 7 May 2024, there is now a requirement to make an MRP charge with respect to the ECL or impairments which must be charged in full in the same year that the loss is recognised. There is no option to spread that charge over future years.

As of 31 December 2024 the Council had no unfinanced capital loans issued on or after 7 May 2024.

2.6 Unfinanced Equity Investments (e.g. Property Fund Investments)

Under the new guidance the Council must make MRP and cannot defer making MRP on the basis that the debt is associated with an investment asset that the authority believes will retain or increase capital value which is the approach taken by this Council currently.

The Council currently makes an annual MRP charge of £1 and makes an additional voluntary revenue provision (VRP) charge equal to the change in the net asset value of the funds each year. At 31 March 24 the Council had made cumulative MRP of £3 and cumulative VRP of £2,631,565.19.

From 2025/26 the Council must make an annual MRP charge based on the lifetime of the asset and guidance states for equity this must be charged over a maximum useful life of 20 years. Where it can be proved that the underlying asset has a greater useful life than 20 years then the greater life can be used. This would have to be backed up by suitably qualified professional opinion.

As the underlying assets of the Property Fund investments are property, it will be recommended that the Council uses an expected life of 50 years when calculating MRP rather than 20 years and seek an appropriate professional opinion that confirms the acceptability of this approach.

The Council has the option to use the Straight Line Method or the Annuity Method for calculating its annual MRP charge but will need to clearly define its chosen method in its 2025/26 Minimum Revenue Provision Policy to be approved by Council in March 2025 as part of the Treasury Management Strategy Statement included as part of the budget setting report.

Where the annuity method is used guidance states that an Authority should use "an appropriate interest rate" within their annuity calculations. Typically, other Local Authorities use an annuity rate which is based on either of the following:

- Weighted average rate of the authority's external borrowing
- PWLB annuity rate at the date of the change in MRP Policy
- Average PWLB annuity rate for the financial year

Council will be recommended to use the annuity method for equity investments based on the PWLB annuity rate at the date of the change in MRP Policy. Based on a 50 year term this rate is currently 5.94%.

Officers have been in discussions with KPMG with a view to obtaining confirmation from them that they are in agreement with this approach being taken by the Council.

As of 31 December 2024, the Council has £19,199,053.15 of unfinanced Property Fund investments (excluding M&G) which will be subject to an annual MRP charge from 2025/26 and will need to be included in the budget. **Appendix 1** provides details of the annual MRP charge over 50 years using the asset life "annuity" method and a rate of 5.94%.

The M&G Property Fund is currently being liquidated and the sale proceeds are being used to finance an equivalent MRP charge to reduce this unfinanced capital expenditure. Expectations are that there will be a small surplus over and above the purchase cost.

It can be seen from **Appendix 1** that over the next five financial years the annual MRP charge and budget pressure based on the unfinanced equity position on 31 December 2025 will be:

Financial Year	New MRP Charge	Previous MRP Charge	Budget Pressure
2025/26	67,456.77	1.00	67,455.77
2026/27	71,463.70	1.00	71,462.70
2027/28	75,708.65	1.00	75,707.65
2028/29	80,205.74	1.00	80,204.74
2029/30	84,969.96	1.00	84,968.96

As VRP has been made in the past, the Council will be able to finance this higher MRP charge each year by reversing an equivalent amount from its cumulative VRP of £2,631,565.19 (as at 31 December 2024) until such time as the full amount of VRP has been reversed.

This MRP money which will be set aside cannot be recovered to the Councils revenue account at a future point as the rules stand currently, irrespective of the fact that when the assets are sold it is anticipated that full recovery of capital will be received.

Statutory Accounting Override for Pooled Investments

2.7 The original Statutory Accounting Override has been in place since 2018. The original override was a temporary measure due to end 31 March 2023, later extended by two years following consultation with the sector. The override is currently due to end March 2025.

2.8 MHCLG recently issued the consultation on the provisional local government finance settlement 2025/26 and question 10 of this consultation was in relation to the IFRS Statutory Accounting Override. The government is minded to not extend the override beyond March 2025.

2.9 The Council's investments of £3,999,951.46 in the Federated Hermes Property Fund are classified as Pooled Investments and therefore revenue expenditure.

2.10 At the end of each financial year these investments are recorded in the Council's accounts at fair value. As a result of the override, any increases or decreases in the value of these investments are taken to the balance sheet and held in the Pooled Investment Funds Adjustment Account. On 31 March 2024 there was a negative balance of £235k in this reserve because of the reduction in the fair value of the Federated Hermes Property Fund investments. At the 31 December 2024 the reduction in value compared with book cost had reduced to £173k.

2.11 As part of the 2025/26 budget setting process, the Council will include a provision of £200k resulting from the expiry of the Statutory Accounting Override. It will be proposed that a corresponding transfer be made from the Investments Volatility Reserve.

2.12 From 1 April 2025 any change in the fair value of the Federated Hermes Fund will be charged to the Councils revenue account.

2.13 The Council will be reviewing its capital and revenue investments in property funds following these recent changes in accounting regulations and this will be subject to a separate report.

3. Conclusion

3.1 This report provides an update to Members on recent changes to Statutory Guidance “Capital Finance: Guidance on Statutory Minimum Revenue Provision” which is mainly effective from the 2025/26 financial year and the financial implications to the Council.

3.2 The revised MRP Guidance is expected to create a budget pressure in 2025/26 of £67,455.77 as the Council will be required to make a higher annual MRP charge for its unfinanced capital equity investments in Property Funds. This additional budget pressure will be offset by running down the VRP balances made in previous years.

3.3 The expiry of the Statutory Accounting Override for Pooled Investments will require an approximate £200k charge to be included in the Council’s 2025/26 budget which will be offset by a proposed corresponding transfer from the Investments Volatility Reserve.

Implications

South and East Lincolnshire Councils Partnership

None

Corporate Priorities

None

Staffing

None

Workforce Capacity Implications

None

Constitutional and Legal Implications

The Council is required to adhere to regulations and statutory guidance. The regulations are mainly effective from the 2025/26 so the Council will be required to include any financial implications of the legislation in its 2025/26 budget setting process.

Data Protection

None

Financial

The financial implications are covered in detail in **Appendix 1** and in section 2 above.

Risk Management

The Council will consider the financial implications of this report when setting its budget for 2025/26.

It will also consider the increased annual revenue costs charged to the ELDC budget which are attributable to its overall investment in Property Funds and consider these costs when reviewing its investments in Property Funds.

Stakeholder / Consultation / Timescales

The Portfolio Holder for Finance is briefed on treasury matters on a regular basis.

Link Group, who are external treasury advisors to the Council, have been consulted in the production of this report.

Reputation

None.

Contracts

None

Crime and Disorder

None

Equality and Diversity / Human Rights / Safeguarding

None

Health and Wellbeing

None

Climate Change and Environmental Implications

None

Acronyms
CFR – Capital Financing Requirement
CIPFA - Chartered Institute of Public Finance and Accountancy
ECL – Expected Credit Loss
MRP – Minimum Revenue Provision
PWLB - Public Works Loan Board

Appendices

Appendices are listed below and attached to the back of the report:

Appendix 1 - Property Funds Equity, MRP Based on Annuity Rate 5.94% Over 50 Years

Background Papers

Background papers used in the production of this report are listed below: -

Document title.	Where the document can be viewed.
Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management.	CIPFA Website
Statutory Instrument 2004 no. 478 The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2024	The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2024
Guidance on MRP (5th edition)	Capital finance: guidance on minimum revenue provision (5th edition) - GOV.UK
ELDC Treasury Management Strategy Statement for 2024/25	(Public Pack)Agenda Document for Council, 28/02/2024 14:00

Chronological History of this Report

Name of Body	Date
Governance and Audit	29 January 2025 (this report)

Report Approval

Report author: Sean Howsam – Interim Treasury Manager (PSPSL) Sean.Howsam@pspsl.co.uk

Signed off by: Christine Marshall – Deputy Chief Executive (Corporate Development) & S151 christine.marshall@sholland.gov.uk

Approved for publication: Cllr Thomas Kemp, Portfolio Holder for Finance.

APPENDIX 1

ELDC Property Funds MRP Based On Annuity Rate 5.94% (Excluding M&G)

Property Fund Unfinanced Capital Expenditure	19,199,053.15
Adjustment A (£000)	0.000
Annuity rate	5.94%
Period (years)	50

	Year	Opening CFR Balance	MRP charge @ Annuity	Closing CFR Balance
		£'000	£'000	£'000
1	2025/26	19,199,053.15	67,456.77	19,131,596.38
2	2026/27	19,131,596.38	71,463.70	19,060,132.68
3	2027/28	19,060,132.68	75,708.65	18,984,424.03
4	2028/29	18,984,424.03	80,205.74	18,904,218.29
5	2029/30	18,904,218.29	84,969.96	18,819,248.32
6	2030/31	18,819,248.32	90,017.18	18,729,231.15
7	2031/32	18,729,231.15	95,364.20	18,633,866.95
8	2032/33	18,633,866.95	101,028.83	18,532,838.12
9	2033/34	18,532,838.12	107,029.94	18,425,808.17
10	2034/35	18,425,808.17	113,387.52	18,312,420.65
11	2035/36	18,312,420.65	120,122.74	18,192,297.91
12	2036/37	18,192,297.91	127,258.03	18,065,039.88
13	2037/38	18,065,039.88	134,817.16	17,930,222.72
14	2038/39	17,930,222.72	142,825.30	17,787,397.42
15	2039/40	17,787,397.42	151,309.12	17,636,088.29
16	2040/41	17,636,088.29	160,296.88	17,475,791.41
17	2041/42	17,475,791.41	169,818.52	17,305,972.89
18	2042/43	17,305,972.89	179,905.74	17,126,067.15
19	2043/44	17,126,067.15	190,592.14	16,935,475.01
20	2044/45	16,935,475.01	201,913.31	16,733,561.70
21	2045/46	16,733,561.70	213,906.96	16,519,654.74
22	2046/47	16,519,654.74	226,613.04	16,293,041.70
23	2047/48	16,293,041.70	240,073.85	16,052,967.85
24	2048/49	16,052,967.85	254,334.24	15,798,633.61
25	2049/50	15,798,633.61	269,441.69	15,529,191.92
26	2050/51	15,529,191.92	285,446.53	15,243,745.39
27	2051/52	15,243,745.39	302,402.05	14,941,343.34
28	2052/53	14,941,343.34	320,364.73	14,620,978.61
29	2053/54	14,620,978.61	339,394.40	14,281,584.21
30	2054/55	14,281,584.21	359,554.43	13,922,029.78
31	2055/56	13,922,029.78	380,911.96	13,541,117.82
32	2056/57	13,541,117.82	403,538.13	13,137,579.69
33	2057/58	13,137,579.69	427,508.29	12,710,071.40
34	2058/59	12,710,071.40	452,902.29	12,257,169.11
35	2059/60	12,257,169.11	479,804.68	11,777,364.43
36	2060/61	11,777,364.43	508,305.08	11,269,059.35
37	2061/62	11,269,059.35	538,498.40	10,730,560.94
38	2062/63	10,730,560.94	570,485.21	10,160,075.73
39	2063/64	10,160,075.73	604,372.03	9,555,703.70
40	2064/65	9,555,703.70	640,271.73	8,915,431.98
41	2065/66	8,915,431.98	678,303.87	8,237,128.11
42	2066/67	8,237,128.11	718,595.12	7,518,532.99
43	2067/68	7,518,532.99	761,279.67	6,757,253.32
44	2068/69	6,757,253.32	806,499.68	5,950,753.64
45	2069/70	5,950,753.64	854,405.76	5,096,347.87
46	2070/71	5,096,347.87	905,157.46	4,191,190.41
47	2071/72	4,191,190.41	958,923.82	3,232,266.59
48	2072/73	3,232,266.59	1,015,883.89	2,216,382.70
49	2073/74	2,216,382.70	1,076,227.40	1,140,155.30
50	2074/75	1,140,155.30	1,140,155.30	-