

Appendix 8

MRP Options

1. SUPPORTED BORROWING

| OPTION 1 Regulatory Method | OPTION 2 Capital Financing Requirement Method |
|---|--|
| Existing method of charge, no change to revenue account | Similar to Option 1, but with a change that omits a Calculation 'Adjustment A' that was caused by LGR in 1996. |

Recommendation - to use Option 2 which reflects the continuation of current arrangements.

2. UNSUPPORTED BORROWING

| OPTION 3 Asset Life Method | OPTION 4 Depreciation Method |
|---|---|
| Two approaches to calculate charge to revenue: - a) Equal Instalment Method (EIM) Divides value of borrowing by estimated life of asset. Currently use 25 years. b) Annuity Method More complex with lower charge in early years, higher charge towards end of asset, when life of asset coming to end. | Similar to Option 3 but considers the revaluation of the asset and revisions to the expected asset life. Can lead to uncertainty in respect of future charges to revenue account. |

Recommendation - to use Option 3 and EIM which reflects the continuation of current arrangements.

One further change, applicable to the introduction of Options 3 and 4, is a delay in the commencement of the MRP charge. Under the existing statutory approach, the charge commences in the financial year following that in which the borrowing was incurred. Under these Options, it commences when the asset, which the borrowing has been used to finance, becomes operational. There will be no ongoing effect to the revenue account as a consequence of this change.

MRP in respect of leases and Private Finance Initiative schemes brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.