

Explanatory Memorandum to the Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2016

This Explanatory Memorandum has been prepared by the Local Government Finance Policy Division in the Education and Public Services Group and is laid before the National Assembly for Wales in conjunction with the above subordinate legislation and in accordance with Standing Order 24.1.

Minister's Declaration

In my view, this Explanatory Memorandum gives a fair and reasonable view of the expected impact of the Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2016.

Leighton Andrews
Minister for Public Services
3 February 2016

1. Description

- 1.1 This Statutory Instrument (“the 2016 Regulations”) amends existing Regulations, the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 (“the 2003 Regulations”), so that local authorities can mitigate the impact of having to recognise significant revenue cost as a result of the Housing Revenue Account Subsidy (HRAS) buy out in 2015-16.
- 1.2 The circumstances of the way authorities were required to enter into loan agreements for the purposes of funding their settlement payment to exit the Housing Revenue Subsidy system have led to the need to amend the framework which supports local government capital finance and accounting in Wales. The amendments to the 2003 Regulations are designed to help authorities avoid significant potential revenue implications.

2. Matters of special interest to the Constitutional and Legislative Affairs Committee

- 2.1 None.

3. Legislative Background

- 3.1 Section 21 of the Local Government Act 2003 provides the Welsh Ministers with powers to make provision in regulations about the accounting practices to be followed by a Local Authority, in particular with respect to the charging of expenditure to a revenue account.
- 3.2 The 2016 Regulations are subject to annulment in pursuance of a resolution of the Assembly (the negative resolution procedure).

4. Purpose and intended effect of the legislation

- 4.1 The 2003 Regulations contain detailed provisions for the operation of capital finance and accounting controls applicable to local government bodies in Wales. They also modify accounting practice in various ways to prevent adverse impacts on authorities’ revenue resources.
- 4.2 Accounting treatment of loans from the Public Works Loan Board drawn down on 2 April 2015 (Regulation 25A)

Local Housing Authorities in Wales were required to enter into a loan agreement or agreements from the Public Works Loan Board (PWLB) for the purpose of funding their settlement payment to exit the Housing Revenue Account Subsidy (HRAS) system. The circumstances of the arrangement meant loans were significantly different from the market rate.

Under proper accounting practices local authorities are required to measure assets and financial liabilities at fair value. Fair Value is defined as the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arms length transaction. As a result local authorities are required to recognise the difference between the value of the loan at market rates and the value based on the agreed rate. The sum by which the amount lent exceeds fair value must be recognised in a local authority's revenue account. This is an accounting requirement which was not designed for this type of unique situation.

The 2003 Regulations are being amended to remove the requirement for local authorities to recognise in a revenue account the difference between the fair value and the agreed value of loans acquired by the Welsh local authorities to fund their settlement to exit the HRAS system. The loans to which the 2016 Regulations apply were drawn down on 2 April 2015 for the purpose of exiting the HRAS system and do not apply to any other liabilities of a local authority.

Therefore, where the interest rates applicable to the loans drawn on 2 April 2015 are a rate of interest which is other than the prevailing market rate (which is defined as the PWLB Standard rate) of interest on that date, the local housing authority must not recognise any difference between the loan principal borrowed and the fair value of the loan(s) measured against the prevailing market rate, in a revenue account retained by the local housing authority.

Interest payable on the PWLB loan(s) must continue to be recognised in a local housing authority revenue account as soon as the local housing authority becomes liable for that interest payable.

The purpose of the 2016 Regulations therefore is to mitigate the impact of fair value accounting treatment for the loans taken out by a housing authority to exit the HRAS system on 2 April 2015.

5. Implementation.

- 5.1 The 2016 Regulations will come into force on 31 March 2016.

6. Consultation

- 6.1 The amendments were part of an informal invitation to comment when proposed policy and draft Regulations were put to appropriate stakeholders. This included Local Authorities, Wales Audit Office (WAO), Welsh Local Government Association (WLGA) and the Chartered Institute of Public Finance and Accountancy (CIPFA).
- 6.2 No responses were received. Engagement with stakeholders prior to consultation suggested that the proposed amendment was widely

supported. Therefore, no additional amendments to the Regulations have been included as a result of the consultation.

7. Regulatory Impact Assessment (RIA)

- 7.1 A regulatory impact assessment was considered and has not been produced for this instrument as the amendments to the Regulations do not create an additional regulatory burden. No impact on business, charities or the voluntary sector is foreseen.

8. Post Implementation Review

- 8.1 The current regulatory framework has been in place since April 2004. Since that time the effectiveness of the system in place has been kept under regular review by the Welsh Government and in regular formal and informal situations with interested stakeholders' examples being Local Authorities, WLGA and Wales Audit Office.