

SL(6)295 – The Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2022

Background and Purpose

The Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2022 (“the Regulations”) are made by the Welsh Ministers, in exercise of the powers conferred by sections 21(1), 24, and 123(1) and (2) of the Local Government Act 2003.

The Regulations amend the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 (“the 2003 Regulations”) by inserting regulation 24L, which makes provision about the accounting practices to be followed by a local authority where a component of an infrastructure asset has been replaced. Regulation 24L applies to local authorities that are required to prepare a statement of accounts in accordance with regulation 8 of the Accounts and Audit (Wales) Regulations 2014. A local authority must either assume the carrying amount of the derecognised part is nil or calculate the carrying amount in line with the accounting practices identified under regulation 25 of the 2003 Regulations.

Due to significant historical information deficits, many authorities are unable to provide sufficient evidence of the value of replaced components of infrastructure assets when they are derecognised. This is particularly the case in relation to roads. Some of these issues date back to 1994, when these assets were first brought onto local government balance sheets. Furthermore, the reporting requirements have not been consistent over time.

This issue has contributed to delays in the completion of 2021-22 local authority audits as both local authorities and auditors have sought a resolution. Without resolution, there is a significant risk that many local authority financial statements could be subject to qualified audit opinions in this area, whereby the auditor is unable to give an opinion that the accounts are not misstated. It is anticipated that this may also lead to delays to future audits.

The Welsh Government has indicated that it recognises a long-term solution is needed that addresses the underlying issues but, due to the complexity of the issue, it will take both time and resources to fully address. Therefore, the override is provided by the Regulations on a temporary basis as an isolated measure to mitigate the risks of widespread accounts qualifications and delays to audit completion.

Regulation 24L applies to accounts for financial years in respect of the periods beginning with 1 April 2021 and ending with 31 March 2025. As such, it will apply retrospectively to local authority accounts for the financial year 2021-22 where an audit has not yet been completed.

Procedure



Negative

The Regulations were made by the Welsh Ministers before they were laid before the Senedd. The Senedd can annul the Regulations within 40 days (excluding any days when the Senedd is: (i) dissolved, or (ii) in recess for more than four days) of the date they were laid before the Senedd.

Technical Scrutiny

No points are identified for reporting under Standing Order 21.2 in respect of this instrument.

Merits Scrutiny

The following 4 points are identified for reporting under Standing Order 21.3 in respect of this instrument.

1. Standing Order 21.3(ii) – that it is of political or legal importance or gives rise to issues of public policy likely to be of interest to the Senedd

We note the breach of the 21-day convention (i.e. the convention that 21 days should pass between the date a “made negative” instrument is laid before the Senedd and the date the instrument comes into force), and the explanation for the breach provided by Rebecca Evans AS/MS, Minister for Finance and Local Government, in a letter to the Llywydd dated 30 November 2022.

In particular, we note the following:

“The reason for not adhering to the 21 day convention in this case is that local authorities are expected to make and secure approval of accounts in good time. This issue was identified earlier this year but could not be resolved by the professional accounting bodies and accordingly statutory provision was required. This has delayed the timetable for accounts audit and approval beyond the original expected date of 30 November. Local authorities are currently facing significant budget pressures and some very difficult decisions over services. They will receive their draft settlement on the 14 December 2022 and will need to focus all available officer and council time on budget and service planning. If further delayed the accounts approval process would take up officer and council time at a critical point. A delay also has a knock-on impact on Audit Wales’s timetables, with work being delayed until January/ February 2023 impacting on capacity in Audit Wales to complete all the community council audits and the start of the 2022-23 local authority audits.”

2. Standing Order 21.3(ii) – that it is of political or legal importance or gives rise to issues of public policy likely to be of interest to the Senedd

We note the following reasons set out in paragraph 5.2 of the Explanatory Memorandum why no formal consultation was undertaken on the Regulations:



“Given the technical nature of these changes no public consultation has been undertaken by Welsh Government. However the Welsh Government has consulted with local authority treasurers, Welsh Local Government Association, CIPFA and Audit Wales to draw on their specialist expertise in drafting the technical amendments and to ensure that the instrument meets its intended purposes. Those that the Welsh Government has spoken to have been supportive of both the principle and form of the accounting treatment set out in this instrument.”

We note also, as set out in paragraph 5.1 of the Explanatory Memorandum, that the Chartered Institute of Public Finance and Accountancy issued its own urgent consultation on 12 May 2022 concerning the temporary changes to the Code of Practice on Local Authority Accounting in the United Kingdom with a view to resolving these infrastructure assets reporting issues, [Urgent Infrastructure Assets Task and Finish Group | CIPFA](#), which closed on 14 June 2022.

3. Standing Order 21.3(ii) – that it is of political or legal importance or gives rise to issues of public policy likely to be of interest to the Senedd

We note the following reasons set in paragraph 6.1 of the Explanatory Memorandum why no Regulatory Impact Assessment was undertaken in relation to these regulations:

“As this instrument makes a technical amendment to the proper practices for local authority accounting for a time limited period only, which maintains the historical treatment of infrastructure assets, and the amendments do not alter the impact to the readers of the accounts in any significant way an RIA is not required.”

Whilst the urgency of the Regulations is noted, it is unclear based on them and the accompanying Explanatory Memorandum, whether the revised treatment of the assets in question under new regulation 24L will, in fact, alter the resulting accounts. It would be helpful if the Welsh Government could clarify whether such treatment of these assets will result in potentially inflated accounts due to the presumed nil valuation for depreciation purposes where new regulation 24L(3)(a) is relied upon? And, if this is the case, whether a Regulatory Impact Assessment is required under the relevant Code of Practice as the changes introduced by the Regulations go beyond the mere technical?

4. Standing Order 21.3(ii) – that it is of political or legal importance or gives rise to issues of public policy likely to be of interest to the Senedd

We note that Standing Order 15.4 has been relied upon to justify the laying of an English only Explanatory Memorandum. Whilst it may be the case that the urgency of the issue justifies this, we note the unusual circumstances of the Regulations and the useful detail set out in the clearly drafted English Explanatory Memorandum, which is of considerable help in explaining the need for the Regulations and the complexity of the issue they seek to address. Bearing in mind the Regulations will be in force until 31 March 2025, a Welsh version Explanatory Memorandum would be of similar help to any Welsh speakers who are equally interested in the background, purpose and effect of the Regulations.



Welsh Government response

Technical Scrutiny point : No points identified

Merit Scrutiny points 1-2 : No Government response required

Merit Scrutiny point 3

The Regulations continue the status quo for the way these assets have been treated by local authorities since infrastructure assets were first recognised in conventional local authority balance sheets. The CIPFA accounting Code aligned reporting on assets more closely with other UK generally accepted accounting principles (GAAP), moving from older capital accounting systems based on financing requirements. This was on 1 April 1996 in Wales.

Accounting for subsequent expenditure on infrastructure assets, and specifically whether local authorities should be assessing if there is any undepreciated cost remaining in the balance sheet for the replaced components that needs to be derecognised, has recently been subject to heightened audit focus, primarily in England. This led to the review by CIPFA, regulations made for Wales and England, statutory guidance issued in Scotland and an update to the Code by CIPFA.

It is unlikely that the net book value will be inflated as a result of the regulations due to the programme of repairs and replacements in LAs only occurring where an infrastructure asset is worn out. It is the net book value that is used in the balance sheet as part of the total asset value of an authority.

There may have been some over inflation of historical cost and accumulated depreciation previously within the notes to the accounts, where authorities are unable to separately identify the components of infrastructure assets to remove them from the asset register. This is why CIPFA have amended the Code to take out the requirement to include these elements in the accounts so that it does not lead to a distorted view of assets levels for a reader of the accounts. For these reasons a Regulatory Impact Assessment is not considered necessary.

CIPFA have set up a working group to look at the way infrastructure assets are accounted for from 1 April 2025. This has Welsh Government representation.

Merit Scrutiny point 4:

In the circumstances, including in particular the urgency with which the Regulations needed to be made it was not reasonably practicable for a Welsh language Explanatory Memorandum to be laid alongside the Regulations.

Committee Consideration

The Committee considered the instrument and Welsh Government response at its meeting on 12 December 2022 and reports to the Senedd in line with the reporting points above.

