Meeting: Resources Board

Date: 22 September 2022

Future of the IFRS 9 statutory override: Mitigating the impact of fair value movements of pooled investment funds

Purpose of report

For decision / clearance of response

Summary

This report outlines a proposed response to a consultation from DLUHC on the future of the statutory override to International Financial Reporting Standard 9 (IFRS 9) for members to agree. The report proposes the response should call for the override to be made permanent or (as a minimum) be extended.

Recommendation/s

That the Resources Board approve the draft response to the consultation appended to this report, subject to any amendments agreed at the meeting.

That officers make any amendments to the draft responses and arrange submission to DLUHC.

Contact details

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Future of the IFRS 9 statutory override: Mitigating the impact of fair value movements of pooled investment funds

Background

1. IFRS 9 (International Financial Reporting Standard 9) Financial Instruments was introduced in local authority accounting from the 2018/19 financial year and was applied to the balance sheet of local authority accounts. IFRS 9 specifies how financial instruments are classified and measured in accounts (that is accounts of all types of entities, not just local authorities). The statutory override under consideration in this consultation only applies to pooled investment funds, not to other financial instruments
2. The IFRS 9 statutory override was introduced in 2018 following concerns raised by the sector that without it councils would be subject to unnecessary financial volatility that would have unwanted impacts. In January 2018 the then Chair of the LGA's Resources Board wrote to then Local Government Minister calling for an override; the call was backed across the sector, including by CIPFA and Treasurers' Societies. The Government then undertook a formal consultation on proposals to introduce the override for a period of three years.
3. The issue was considered by the LGA's Resources Board in September 2018. The Board approved the response to that consultation, and argued for an override to be introduced and made permanent, or failing that to run for a period of at least five years.
4. This was agreed by the Government who introduced a five-year override from April 2018 to March 2023. The current consultation offers three options – either end the override, extend it, or make it permanent.

Proposed response

5. A proposed response to the consultation is attached as an appendix to this report. This follows the approach taken in 2018 and calls for the override to be made permanent or extended again; members may wish to comment on this.
6. There would appear to be a strong view that that the Government was right to introduce an override in 2018. Recent evidence from a survey by Room 151 magazine of 77 local authorities showed that over the last three balance sheet dates the majority of those surveyed held investments that were affected by the override and all that did experienced a change in value that would have impacted in the revenue account if the override was not in place. About a third of them experienced such volatility that the value of their investments went up and down significantly at the different balance sheet dates in that short period. Having the override in place meant that these councils did not have to make unnecessary cuts in service in response to these differences in valuations between balance sheet dates.

7. More recent reports in the same magazine report the Presidents of at least two of the council Treasurer societies, speaking on behalf of their societies, support continuation of the override.
8. A contrary view may be held by the Accountancy Institutes, one of which has been reported as saying that councils should “prepare for a ‘post-override’ world” and take stock of their investment risk management framework accordingly.
9. Members may wish to consider the following points.
    - Having the override in place does not mean that local authorities do not have monitor or measure changes in value at balance sheet date, just that such changes, particularly temporary changes, do not affect the revenue account directly in the short term.
    - The investments affected by the override (pooled funds) are long-term investments and if the override is not in place, holders of such investments will have to make revenue adjustments for what are paper changes in value at balance sheet dates. The balance sheet is a snapshot at a single date; the paper valuations could be different a few days before and few days after or before the balance sheet date.
    - The point that a change in value actually has a real impact is the point at which any real gain or loss is realised. Having to make real revenue provisions for temporary paper losses or take real revenue cash for temporary paper gains, measured at a single date each year, creates unnecessary real revenue risks that could have a significant negative impact on a local authority’s ability to provide local services.
    - Even with the override in place, local authorities still have report on changes to the paper value of the relevant investments and should take this account of possible gains and losses in their risk management framework.
    - The paper valuation at balance sheet date is only a snapshot of the value at a specific date (31 March). Proper management of investments requires much more frequent monitoring of fair value of investments than a year end figure at a single date. Risk management based on the recording a single paper figure each year will be entirely inadequate and councils will not be doing this.
10. The above points are all included in the draft response appended to this report.

Implications for Wales

11. The statutory override affects local authorities in England only. The Welsh Government implemented a separate override for Welsh local authorities in 2018 that also runs out in March 2023. The Welsh Government has not yet come forward with proposals on taking this forward.

Financial Implications

12. The work covered in this paper is included in the LGA’s core budget.

Equalities implications

13. It is difficult to assess whether the statutory override for IFRS 9 has any specific impacts for individuals with protected characteristics. The override itself does not have any identified negative impacts, but if the override were to cease this would be likely to have a negative impact on councils' ability to fund service and so could have a negative impact on individuals with protected characteristics.

Next steps

14. That officers make any amendments to the draft responses and arrange submission to DLUHC.