

Explanatory Memorandum to The Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2026

This Explanatory Memorandum has been prepared by the Local Government Funding Policy and Sustainability Division and is laid before Senedd Cymru in conjunction with the above subordinate legislation and in accordance with Standing Order 27.1.

Cabinet Secretary'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 2026. I am satisfied the benefits justify the likely costs.

Jayne Bryant MS
Cabinet Secretary for Housing and Local Government
3 March 2026

PART 1

1. Description

- 1.1. The Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 (“the 2003 Regulations”) provide the regulatory regime for the accounting practices to be followed by local authorities in Wales. They set out detailed provisions about the regime for capital finance and accounting controls, including the rules on the use of capital receipts and what is to be treated as capital expenditure. They also modify accounting practices to prevent adverse impacts on local authority revenue resources.
- 1.2. The Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2026 (“the Regulations”) amend the 2003 Regulations by extending the application of the statutory overrides to local authority accounting practices set out in regulations 24K and 24L for a further four financial years up to 31 March 2029. The statutory overrides mitigate the impact of fair value movements on pooled investment funds and alter the accounting practices to be followed by a local authority where a component of an infrastructure asset has been replaced. The extension to the statutory override on pooled investment funds is limited to investments made before 1 April 2025.

2. Matters of special interest to the Legislation, Justice and Constitution Committee

- 2.1 None.

3. Legislative background

- 3.1 Section 21(1), when read with section 24, of the Local Government Act 2003 (“the 2003 Act”) provides that the Welsh Ministers may make provision about the accounting practices to be followed by local authorities. Section 123(1) and (2) of the 2003 Act enables the Welsh Ministers to make different provision for different cases and for different descriptions of local authorities, and to make incidental provision.
- 3.2 Regulation 25(1)(a) of the 2003 Regulations specifies that the accounting practices contained in the “Code of Practice on Local Authority Accounting in the United Kingdom” (“the Code”) are to be regarded as proper practices. The Code is issued by the Chartered Institute of Public Finance and Accountancy (“CIPFA”) who may amend and reissue the code from time to time.
- 3.3 Section 21(3) of the 2003 Act provides that, where there is a conflict between accounting practices required to be followed by legislation, and accounting practices contained in codes of practice, the legislative provisions are to be regarded as the proper practices.

3.4 The Regulations are made under the Senedd annulment procedure by virtue of section 123(6) of the 2003 Act, read with paragraphs 30 and 34 of Schedule 11 to the Government of Wales Act 2006.

4. Purpose and intended effect of the legislation

4.1 The purpose of these Regulations is to extend the application of the statutory overrides in regulations 24K (fair value gains and losses of pooled investment funds) and 25L (infrastructure assets) of the 2003 Regulations. The Regulations extend the overrides for a further four financial years to 31 March 2029.

Pooled investment funds statutory override

4.2 Regulation 24K of the 2003 Regulations sets out a statutory override regarding the accounting treatment by local authorities of fair value gains and losses on pooled investment funds.

4.3 In January 2018, International Financial Reporting Standard 9 (“IFRS 9”) came into force in the United Kingdom and was incorporated by CIPFA into the Code with effect from 1 April 2018. Welsh local authorities expressed concerns that the reporting changes brought in by IFRS 9 would mean that the fair value movements of investments that they held in pooled investment funds would need to be reflected in their budgets.

4.4 There is a statutory requirement on local authorities to set a balanced budget each year, and the need to reflect movements in the value of investments held in pooled investment funds in their revenue accounts could adversely affect local authority budget setting and the determination of council tax. The Welsh Government accepted that the increased budgetary volatility could detrimentally impact service delivery or place undue burdens on council taxpayers. Responding to those concerns raised at the time IFRS 9 came into force, the Welsh Government introduced regulation 24K of the 2003 Regulations which created a statutory override to mitigate against the risks identified by the local authorities. The statutory override was time limited to apply to accounts prepared by local authorities for the financial years between 1 April 2019 and 31 March 2023 to provide time for local authorities to prepare for full compliance with IFRS 9. It was subsequently extended for a further two financial years up to 31 March 2025.

4.5 The override does not impact the investment itself but the accounting treatment of it on 31 March, the end of the financial year. A pooled investment may span the year end. If there is a gain or a loss on a pooled investment at the year end point, it has to be accounted for under IFRS 9 as at that date even if the investment does not crystallise then. If the position is a loss, it would mean the authority may be reporting a deficit for that year and local authorities would need to take steps to mitigate against such a risk.

- 4.6 The Regulations extend the override until 31 March 2029 for investments falling within its remit which are made before 1 April 2025. Such investments made on or after 1 April 2025 will need to be accounted for in compliance with the IFRS 9 as adopted by the Code from accounts relating to the financial year beginning with 1 April 2025 onward. The intention is that all pooled investment funds will eventually be accounted for in compliance with the Code, but where authorities hold such investments based on historic decisions there is additional time for them to take actions necessary to mitigate any risks to their financial positions.
- 4.7 The Ministry of Housing and Local Government has extended the application of the equivalent statutory override provision which has effect in relation to local authorities in England by way of Regulations made on 1 April 2025. That override is limited to apply to investments made before 1 April 2024.
- 4.8 Without the override, Welsh local authorities could potentially have to make financial provision for fair losses on pooled investments instead of being able to use that provision to fund services, putting them and service recipients at a disadvantage compared to their respective counterparts in England. Welsh Ministers consider it expedient that the accounting framework for local authorities in Wales should largely match that for local authorities in England, unless there are strong reasons to the contrary. In this case, there are no policy or accounting reasons to support a divergence of practice on the continuation of the override, save for its limitation to investments made prior to 1 April 2025.

Infrastructure assets statutory override

- 4.9 Regulation 24L sets out a statutory override in relation to the accounting recognition value of replaced infrastructure assets.
- 4.10 When drawing up its accounts, local authorities should normally, in relation to their assets, assess if there is any undepreciated cost remaining in the balance sheet for any replaced components of assets which need to be derecognised when the replacement takes place. The replacement is then added to the asset register and the balance sheet. However, in the case of infrastructure assets, not all local authorities hold adequate financial data on the historic cost, accumulated depreciation and subsequent expenditure on highways assets in a way which can be reliably used to inform the annual accounts to give an accurate reflection of the current infrastructure asset base. In practice, replacements to infrastructure assets are unlikely to be completed within the depreciable life of the original asset so are usually zero net book value. As the original cost and total depreciation cannot be identified from records and removed on replacement, there is a risk that the gross value and accumulated depreciation are incorrect (overstated), while there is a far lower risk that the net book value recorded in the accounts is incorrect. If auditors are unable to verify the correct gross value and

accumulated depreciation then there is a risk that the accounts are qualified on this point.

- 4.11 The statutory override in regulation 24L was inserted into the 2003 Regulations in 2022 and applied to local authority accounts prepared in accordance with regulation 8 of the Accounts and Audit (Wales) Regulations 2014 for four financial years beginning with 1 April 2021 up to and including accounts prepared for the financial year ending with 31 March 2025. The same time limited provision was made by the UK Government in respect of local authorities in England.
- 4.12 The Regulations extend the application of the override in regulation 24L for accounts prepared for a further four financial years beginning with 1 April 2025 and up to and including accounts prepared for the financial year ending with 31 March 2029. The reason the extension is necessary is because there has, as yet, been no change to the CIPFA Code to manage the issues arising with the accounting treatment of replacement components of infrastructure assets and the impact on timely audits.
- 4.13 The UK Government has made Regulations to extend the override for local authorities in England until 31 March 2029 while CIPFA LASAAC complete more work on finding an approach to resolve the issue. Welsh Ministers consider it expedient that the accounting framework for local authorities in Wales should largely match that for local authorities in England, unless there are strong reasons to the contrary. If the override is not extended in Wales then there would be an impact on audit completion and therefore in this case, there are no policy or accounting reasons to support a divergence of practice.

5. Consultation

- 5.1 There is no statutory requirement to consult and as the Regulations make limited technical amendments affecting only a limited number of professional stakeholders, a public consultation did not take place.
- 5.2 Welsh Government officials have engaged closely with the local government sector in Wales, with Audit Wales and CIPFA Wales regarding the extension of the statutory overrides and the limitation on the override for pooled investment funds. That engagement has confirmed the local government sector in Wales supports the extension of the statutory overrides for a further four financial years to 31 March 2029, including the limitation on the pooled investments override, which will have the effect of maintaining parity of accounting practices with their counterparts in England.

PART 2: REGULATORY IMPACT ASSESSMENT

Options

This Regulatory Impact Assessment (RIA) presents three options.

Costs and benefits

Option 1 – Do nothing

Option 1 would not require any legislative change. Local authorities would be required to comply with the accounting requirements set out in the CIPFA Code relating to the fair value of pooled investments and infrastructure assets in IFRS 9 in full.

The advantage is that accounts would fully comply with IFRS and the CIPFA Code with no adjustments required to areas of the accounts to explain the treatment of the areas in the accounts covered by the overrides.

The disadvantages are that local authorities would have to manage any volatility from the impact of fair value movements on pooled investment funds on local authority budget setting and council tax setting.

The issues relating to asset valuation that gave rise to the statutory override on infrastructure asset valuations are still in place as CIPFA has not yet produced a revised code with a solution or guidance. If these Regulations are not made, authorities would have significant issues with audit of accounts where asset valuations are proving extremely difficult due to past systems for recording assets, replacement components and costs. This would cause reputational damage to local authorities over a technical accounting adjustment and distract staff time from setting 2026-27 budgets and progressing transformation plans for long term sustainability of services.

This could add costs for local authorities, both in staff time in getting suitable records prepared for audits, preparing accounts, answering audit queries and in additional audit costs.

If consistent overrides with England are not put in place in Wales, Welsh authorities could be disadvantaged compared to their English counterparts, in managing any losses reported on pooled investments or qualification of accounts relating to infrastructure assets.

Option 2 – Make regulations to extend the overrides indefinitely

Option 2 would be to extend the existing statutory overrides in regulations 24K (fair value of pooled investments) and 24L (infrastructure assets) indefinitely. The benefits associated with this option include greater flexibility for local

authorities in their investments strategies to maximise the gain from investments, rather than drive possibly suboptimal decisions based on an accounting reporting standard. The benefit of continuing the asset valuation override indefinitely would reduce the preparation and audit time for local authorities in what is a difficult and time-consuming area with the large asset portfolios that authorities have.

Disadvantages of putting indefinite overrides in place are an ongoing divergence from standard accounting practices required in the CIPFA code and a divergence from accounting treatment between English and Welsh authorities.

There are no additional costs for authorities of this option as it continues the status quo of the overrides.

Option 3 – Make regulations to extend the overrides for a period of four years until 31 March 2029

Option 3 would extend the existing statutory override in regulation 24K (fair value of pooled investments) for a further four years, in relation to investments made prior to 1 April 2025. This would give any authority time, with the knowledge that the override will be ending on 31 March 2029, to either withdraw from pooled investments, change the timing of investments so that they don't straddle the year end or prepare for reserves to cover any volatility. It would also ensure equal accounting treatment across England and Wales.

The extension of the statutory override in regulation 24L (infrastructure assets) gives authorities time to continue and finalise work that they have started on asset records and valuations. It also gives CIPFA time to complete its work on possible solutions within the Code or guidance on asset valuations, including through indexation.

There are no additional costs for authorities of this option as any change to investment strategies can be made in the normal course of business. There may be small reductions in the level of investment income for some authorities if they have previously invested in successful pooled investments, but this is balanced by the reduction in risk of possible adverse results compared to other investments. Authorities already have plans of work underway for asset valuations and are working closely with Audit Wales to expedite these where needed.

Option selection

The benefits of Option 3 are considered to outweigh the benefits of Option 2 and Option 1. Option 3 is, therefore, the Welsh Government's preferred option.

Duties

Well-being of Future Generations (Wales) Act 2015. There is no impact on future generations from the extension of these overrides as they are time limited and related to technical accounting changes.

UNCRC. No particular impact on the rights of children has been identified.

Welsh language. No effect on the opportunities to use the Welsh language or the equal treatment of the language has been identified.

Equalities. No specific impacts, positive or negative, on persons who share a protected characteristic (as determined by the Equality Act 2010) have been identified.

Voluntary sector. No specific impacts on the voluntary sector have been identified.

Justice. The changes proposed will have no impact on the justice system.

Competition assessment

No competition impacts have been identified.

Post-implementation review

Local authorities are subject to annual audits by Audit Wales who assess compliance with the CIPFA Code of Practice and relevant financial regulations.