**The Scottish Government**

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**CONSULTATION: THE LOCAL AUTHORITY (CAPITAL FINANCE AND ACCOUNTING) (SCOTLAND) REGULATIONS 2016**

**RESPONSE SHEET**

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| **Please enter the name of the organisation responding to this consultation:** | **The Chartered Institute of Public Finance & Accountancy (CIPFA)** |

# If you ask for your response not to be published we will regard it as confidential and we will treat it accordingly. You should be aware that the Scottish Government is subject to the provisions of the Freedom of Information (Scotland) Act 2002 and would therefore have to consider any request made to it under the Act for information relating to responses made to this consultation exercise.

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| **Please indicate if you wish your response to be treated as confidential (i.e. not published):** | **Our response can be made publicly available** |

Unless confidentiality is requested the Scottish Government may also publish responses on the Scottish Government website. Please note that if you wish to provide additional commentary on separate sheets it would be helpful if you set out clearly the questions and/ or parts of the draft regulations to which your comments relate.

This response sheet provides some commentary on the proposed regulations. Please also refer to the consultation draft of the 2016 Regulations and the draft statutory guidance provided as part of the consultation documents.

Where your organisation disagrees with any proposal being made in the 2016 Regulations or the Statutory Guidance we ask that you provide reasons as to why your organisation does not support the proposal. This will help the Scottish Government evaluate whether any changes are required.

**The consultation closes 31 December 2015**

**CONSULTATION QUESTIONS**

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| **THE LOCAL AUTHORITY (CAPITAL FINANCE AND ACCOUNTING) (SCOTLAND) REGULATIONS 2016** |
| **PART 1: General** |
| *Regulation 1: Citation, Commencement and interpretation*We propose the regulations will come into force from 1 April 2016. This means the new regulations will apply from the financial year 2016-17.The new Regulations do not provide a local authority with the power to borrow. Rather, the new Regulations set out the purposes for which a local authority may borrow. This does not represent any change to current legislative arrangements. Section 16 of the Local Government (Scotland) Act 1975 states that “Schedule 3 to this Act shall have effect with respect to the powers of local authorities andjoint boards to borrow and lend money and with respect to certain of their funds”.Regulation 1(3) provides an interpretation of words or phrases used in the regulations. ‘Local authority’ has been defined in the Regulations. This definition reflects the power in The Local Government etc. (Scotland) Act 1994 Act to make regulations applying to certain types of bodies. This does not extend to all bodies classified as local government. The following table sets out each type of local government body, any borrowing powers conferred by legislation and whether the new Regulations will apply to that body.

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| **Local Government Body** | **Power to borrow?** | **Schedule 3/ 2016 Regulations Apply?** |
| 32 Councils  | Yes. s.69 of the Local Government (Scotland) Act 1973 | Yes. |
| Valuation Joint Boards | Yes. s.62 of the Local Government (Scotland) Act 1973 provides Scottish Ministers with the power to create boards by Order. Orders set out the powers of any Board created.The Valuation Joint Boards (Scotland) Orders 1995 create the boards and provide them with the power to hold land and to borrow money.  | Yes. |
| Tay Road Bridge Joint Board | Yes – but is subject to conditions set out in the Tay Road Bridge Order Confirmation Act 1991. This Act permits borrowing for capital expenditure of the Board but only through an advance from the constituent councils. Sets out how the advance is to be repaid. Permits temporary borrowing by the Board. | No.  |
| Integration Joint Boards (IJB) | The Public Bodies (Joint Working) (Scotland) Act 2014 provides Scottish Ministers with the power to create integration joint boards by order. The order creating the board will need to provide any borrowing powers. To date no IJB created has been given powers to borrow. | The Order providing the borrowing power will need to identify that the power is to be exercised in accordance with the 2016 Regulations.  |
| Regional Transport Partnerships | Yes. The Transport (Scotland) Act 2005 provides the power to borrow money for the purpose of the partnerships capital expenditure only. | No. |
| Joint Committees | No. A local authority cannot delegate its borrowing powers to a joint committee (s.56(6) of the 1973 Act). The functions acquired under s.57 cannot therefore include a power to borrow. Being unincorporated (s.62A) it cannot be the recipient of a loan.  | Not relevant. |
| Strategic Planning Authority | No. A joint committee. | Not relevant. |

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|  | Question | Response | Comments / Feedback |
| 1 | Do you agree with the analysis of the specific local government bodies borrowing powers and the application of the 2016 Regulations?If no please provide reasons.  | Yes | **Where a local authority has group arrangements CIPFA interprets the legal definition of ‘local authority’ as referring to the ‘single entity’ (or parent) authority and does not include any subsidiaries.****It should be noted that the Prudential Code for Capital Finance in Local Authorities (the Prudential Code) addresses the group aspects of borrowing by stating “Local authorities with interests in subsidiary or associated companies and joint ventures will also need to have regard to the group accounting requirements of proper accounting practice”.** |
| 2 | Any other comments? | No | **No comment** |
| **PART 2: Borrowing by local authorities** |
| *Regulations 2 to 4: Borrowing of money by a local authority*Regulation 2(1)(a) to (d) sets out the purposes for which a local authority may borrow. Regulation 2(1)(a) replaces paragraph 1(1)(a) to (c) of Schedule 3 – capital expenditure of the local authority. Capital expenditure is defined in the 2016 Regulations by reference to proper accounting practices.Regulation 2(b) permits a local authority to borrow for treasury management activities. This Regulation does not confer any new or additional power to borrow other than to provide a slightly wider power reflecting the wider treasury needs of an authority to refinance existing borrowing, use of internal cash reserves, borrowing in advance or after capital expenditure is incurred and for general liquidity purposes. Regulation 2(c) permits a local authority to borrow to lend to other bodies as set out in Part 3 of the 2016 Regulations.Regulation 2(d) permits a local authority to borrow for any purpose which any other enactment specifically allows them to borrow for. This replaces the same provision contained in paragraph 1(1)(f) of Schedule 3. The Scottish Government is not aware that any other enactment currently exists but has replicated the provision to future-proof the Regulations.Regulation 2(2) provides a power for Scottish Ministers to provide their consent for a local authority to borrow for other purposes not listed in Regulation 2(1). This replaces the same power provided at paragraph 2(2) of Schedule 3. Regulation 3 replaces paragraph 9 of Schedule 3 and permits two or more authorities to combine to exercise their powers of borrowing. Schedule 3 sets out the sources and types of borrowing available to a local authority when exercising their powers to borrow. The new Regulations being proposed do not set out any sources or types. In its place Regulation 4 requires a local authority, when exercising its borrowing powers, to have regard to recognised codes of practice and guidance in relation to treasury management. The CIPFA Treasury Management Code is considered recognised guidance.Paragraph 1(3) of Schedule 3 permits a local authority to borrow to provide working capital for the purposes of a public utility undertaking. Statutory conditions apply. This power is not continued in the 2016 Regulations.  |
|  | Question | Response | Comments / Feedback |
| 3 | Do you agree that local authorities no longer have any public utility undertakings and that no provision is made in the 2016 Regulations for their borrowing needs? If you consider there is a need please provide an explanation for that need. | Yes | **The definition of ‘public utility undertakings’ in the existing 1975 legislation is unclear. Additionally the intention, at the time, of including public utility undertakings in the 1975 legislation is unclear. The review group discussed whether this could have related to water and sewerage functions, which are no longer local authority responsibilities, however this has not been confirmed. On this basis excluding reference to public utility undertakings from the new legislation is supported.** |
| 4 | Any other comments? | No Comment | **No comment.** |
| *Regulation 5: Credit arrangements*Local authorities finance capital expenditure through leasing and private finance initiatives (PPP/PFI/NPD). The 2016 Regulations recognise credit arrangements for the purposes of financing capital expenditure of the local authority. Regulation 1 defines a credit arrangement, which is based on proper accounting practices for leases and lease type arrangements.  |
|  | Question | Response | Comments / Feedback |
| 5 | Do you agree that the definition of a credit arrangement as set out in Regulation 1 correctly identifies leases, PFI, PPP, NPD and similar credit arrangements used to finance capital expenditure of the local authority? If no please provide reasons.  | Yes | **CIPFA notes that the definition of ‘credit arrangement’ for legal purposes will therefore differ from that used in England, which is stated in The Local Government Act 2003 Section 7. Notably the Scottish legal definition:**1. **includes the short term liability element of credit arrangements, whereas this is excluded in England**
2. **Specifically requires that there is an asset recognised as part of the same transaction. This does not appear to be the case in England.**
3. **Specifically restricts the definition to leases; arrangements “akin to” (with the substance of) a lease; and service concession arrangements**
 |
| 6 | Any other comments? | Yes | 1. **The difference between the English and Scottish definition of credit arrangements, specifically relating to short term credit arrangement liabilities, will lead to some difference in the practical application of the Prudential Code for Capital Finance in Local Authorities (the Prudential Code), in particular in the determination for the authorised limit for external debt. The materiality of this difference is not yet clear, however in normal situations it is anticipated that the most material elements of such liabilities will be in the longer term (>12 months).**
2. **The specific definition proposed for Scotland appears to be clear and should assist practitioners in complying with the legislation. Potential future changes to lease accounting are proposed by the IASB. The potential also exists for novel financing arrangements to be developed in future. Consideration could therefore be given as to the legal means by which, in the future, other future financing arrangements might be addressed, if they would not be covered by the proposed definition.**
3. **CIPFA generally welcomes the definition and use of the terms ‘debt amounts’ and ‘external debt’ in the proposed legislation as providing clarity. CIPFA notes however that the Prudential Code will need to be applied by Scottish local government in accordance with the Scottish legislation and terminology definitions.**
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| *Regulation 6: The authorised limit for external debt*This is a **new** requirement. A local authority is to determine, before the start of each financial year, how much external debt it can afford during that financial year and each of the subsequent two financial years.  The statutory requirement reflects the CIPFA Prudential Code requirement for an authority to set an authorised limit for external debt. However, the statutory calculation of the authorised limit for external debt required by the 2016 Regulations differs to that set out in the Prudential Code. The Prudential Code identifies the authorised limit for external debt as being the sum of the authorised limit for borrowing and the authorised limit for other long-term liabilities. Other long-term liabilities relate to the liabilities outstanding under credit arrangements as defined by statute for England Wales and Northern Ireland. The statutory definition only relates to those liabilities classified as liabilities that are for periods in excess of 12 months. The proposed Scottish requirement is that both the short and long term liability is form part of the authorised limit and external debt definition.An authority is required to set a single authorised limit for external debt and to separately identify the amount of borrowing and the amount of credit arrangements. These are defined as the authority’s ‘debt amounts’ (Regulation 6(2)). Debt amounts is defined in Regulation 1.A local authority may vary its authorised limit/s (separate authorised limits are required to be set for three financial years) at any time if it considers it prudent to do so (Regulation 6(3)(a)). A local authority may also exceed either of its debt amounts (borrowing or credit arrangements) provided its authorised limit is not exceeded. (Regulation 6(3)(b). This reflects the Prudential Code (Paragraphs 17 and 18).Regulation 6(6)(a) requires the section 95 to report any debt amounts which have been exceeded. Regulation 6(6)(b) and 6(7) reflects the requirement in the Prudential Code (Paragraph 27 first bullet) that where a chief finance officer (section 95 officer in Scotland) forms the view that a limit is likely to be breached they are required to report to the authority, and the authority is to consider whether to vary its authorised limit or borrowing limits. The determination of the authorised limit and any variation of that limit is a function of the authority itself and may not be delegated (Regulation 6(4)). The statutory requirement takes precedence over the Prudential Code, which requires the setting or revising of prudential indicators to follow the same route as setting or revising the budget of the local authority.Recognising that the Regulations will not come into force until 1 April 2016, the 2016 Regulations, at Regulation 23, include a transitional provision. This requires the authorised limit for external debt for 2016-17 to be determined no later than 1 June 2016. The Scottish Government will be discussing with CIPFA changes that may be required to the Prudential Code to recognise the 2016 Regulations. |
|  | Question | Response | Comments / Feedback |
| 7 | Do you agree that the legislative calculation of the authorised limit for external debt will correctly identify all local authority external debt? | Yes | **As noted above (response to 5) the differing legal definitions of ‘credit arrangement’ between Scotland and England will mean some difference in practical application of the Prudential Code. CIPFA considers that the inclusion of short term liabilities in respect of leases, arrangements with the substance of a lease, and service concession arrangements is in accordance with the principles of the Prudential Code.** |
| 8 | Do you foresee any difficulties in calculating actual external debt at 31 March from the balance sheet using the statutory definition of external debt? If yes, please provide details. | No | **In relation to ‘actual external debt’ the Prudential Code includes the statement that the currently defined elements “will be obtained directly from the local authority’s balance sheet”.****CIPFA considers that the professional processes and practices which are required to show a ‘true and fair view’ of the financial position in the balance sheet should provide sufficient detail to allow the proposed statutory definition of actual external debt to be calculated. It should be noted however that detailed short term liabilities for credit arrangement may not be specifically disclosed in the annual accounts if they are not regarded as material.** |
| 9 | As a transition arrangement a local authority has until 1 June 2016 to determine its first set of authorised limits for external debt. Does this date provide sufficient time for a local authority to make the first statutory determination of its authorised limit? If no, please suggest a date providing reasons for this alternate date. | Yes | **CIPFA welcomes the provision of this transition arrangement to support practical implementation of the legislation. Local authorities will be best placed to indicate whether extension to 1 June 2016 is a sufficient period for transition.**  |
| 10 | The Scottish Government will be discussing with CIPFA changes that may be required to the Prudential Code. Are there any aspects of the Prudential Code you consider the Scottish Government should raise as part of that dialogue? If yes please provide details of what you would wish the Scottish Government to raise with CIPFA. | No Comment | **Not applicable.** |
| 11 | Any other comments? | Yes | **CIPFA specifically welcomes the acknowledgement of the responsibilities of the Chief Financial Officer (CFO, section 95 officer) and the formal support that the legislation provides in the discharge of those responsibilities.** |
| *Regulations 7 to 10 - Security for money borrowed*Regulations 7 to 10 set out the arrangements for the security of money borrowed. As with Schedule 3 (paragraphs 8(1) and 8(2)) the security is provided against all the income streams of a local authority and not otherwise. The 2016 Regulations are drafted slightly differently and specifically prohibit a local authority from using its property as security for money borrowed (implied in Schedule 3 drafting).Trust fund and common good revenues do not form part of the revenues of the authority in terms of providing security for money borrowed (Regulation 7(2)(b) and (c)). Paragraph 8(3) and 8(4) of Schedule 3 makes similar provision. Similarly, local government pension funds do not form part of the revenues of the authority in terms of providing security for money borrowed (Regulation 7(2)(a)). This is a new provision.  |
|  | Question | Response | Comments / Feedback |
| 12 | Do you agree that local government pension funds should be excluded from being revenues of the local authority for the purposes of providing security for money borrowed by the local authority? If no, please provide reasons. | Yes | **CIPFA agrees. The funds held by Local Government Pension Scheme administering authorities as pension scheme assets are required by regulation (Regulation 4 of The Local Government Pension Scheme (Management and****Investment of Funds) (Scotland) Regulations 2010) to be held solely for the purposes set out in those regulations. They cannot be used, for example, to meet any other local authority liabilities. Therefore to allow LGPS assets to be offered as security for local authority borrowing, when they could not be used to repay local authority borrowing, would misstate the authorities financial capacity to service that borrowing.**  |
| 13 | Any other comments? | No | **No comment** |
| *Regulations 11: Borrowing otherwise than in sterling*If a local authority wishes to borrow other than in sterling they require the consent of Scottish Ministers. This is a changed provision from that placed on local authorities under paragraph 4 of Schedule 3, which also requires Scottish Ministers consent to borrow outwith the UK. |
|  | Question | Response | Comments / Feedback |
| 14 | Any comments? | No Comment | **No comment** |
| *Regulation 12: Protection for lenders*This provides the same protection for lenders as set out in paragraph 26 of Schedule 3. |
|  | Question | Response | Comments / Feedback |
| 15 | Any comments? | No Comment | **No comment** |
| *Regulation 13 and 14: External Funds*For the purpose of the 2016 Regulations, money borrowed by a local authority for a pension fund, a trust fund or the common good are not to be treated as borrowing of the local authority. The temporary use by a local authority of money forming part of these funds, otherwise than for the purposes of the fund, is to be treated as borrowing by the authority for the purposes of the 2016 Regulations. |
|  | Question | Response | Comments / Feedback |
| 16 | Any comments? | Yes | **CIPFA concurs that the temporary use of such funds is a form of borrowing, particularly since these funds are held for specific purposes, usually with legal restrictions on their use and a requirement to act in the best interests of the fund etc rather than the authority. A consequence of this is that such funds may receive payment of interest based on the amount and duration of borrowing by the authority.** |
| **PART 3: Borrowing in respect of lending by local authorities** |
| *Regulation 15 and 16: Borrowing to lend and advance money*Regulation 2(1)(c) provides that a local authority may borrow money to lend to other bodies as set out in Part 3. Regulation 15 sets out those statutory bodies that a local authority may lend to. A local authority may only lend where that statutory body has a statutory power to borrow. A local authority is therefore under an obligation to check, before borrowing to on-lend, that the statutory body has a statutory borrowing power. The 2016 Regulations do not confer borrowing powers, they set out the purposes for which a local authority may borrow. For further information read the commentary on Part 1 / Regulation 1 above.Schedule 3 had similar provisions as to the bodies that a local authority could lend to. Regulation 15 replicates the bodies from Schedule 3 and adds the new integration joint boards. At this time no integration joint board has been given any powers to borrow. As such a local authority is unable to lend to these bodies.Regulation 16 contains a **new** power. Whilst a local authority may borrow for its common good funds Schedule 3 provisions did not provide for a local authority to borrow and advance those funds to a common good fund. Regulation 16 provides that power, but only in respect of expenditure by such a fund which would be capital expenditure of the local authority if incurred directly by the authority. |
|  | Question | Response | Comments / Feedback |
| 17 | Do you agree that integration joint boards should be included in the list of bodies that a local authority may lend to (subject to that body having a statutory borrowing power)? If no, please provide a reason for your response. | Yes | **CIPFA agrees that if, in future, IJBs are permitted to borrow that local authorities should be able to provide a borrowing facility.** |
| 18 | Do you agree that a local authority should be able to borrow to on-lend to its common good fund/s? If no, please provide a reason for your response. | Yes | **CIPFA considers that will this allow authorities an appropriate means to support capital expenditure on common good assets, while still requiring that ultimately the common good funds the capital expenditure. As with all loans the authority would need to assess the risk of impairment of any loan made (i.e. debtor balance). Generally, on a ‘true and fair view’ and ‘faithful representation’ basis, it is assumed, subject to rebuttal, that for the authority ‘single entity’ balance sheet such loans would be presented as if made to a separate legal entity.** |
| 19 | Any other comments? | No Comment |  |
| **PART 4: Loans Funds** |
| *Regulation 17: Duty to maintain a loans fund.*The requirement for a local authority to maintain a loans fund under paragraph 12 of Schedule 3 continues to be a requirement in the 2016 Regulations.The loans fund is to be administered in accordance with the 2016 Regulations, proper accounting practices and prudent financial management.The 2016 Regulations do not set out in detail how a loans fund is to be administered. This is set out in statutory guidance. A draft of the proposed statutory guidance ‘Loans Fund Accounting’ forms part of the consultation. Further detail on the statutory guidance can be found later in this response sheet.In terms of comparing the 2016 Regulations and statutory guidance with Schedule 3 there are the following key differences:* External borrowing is no longer carried to the Loans Fund
* The loans fund is no longer responsible for repaying external borrowing or paying interest or other costs associated with that borrowing
* The loans fund is to record the amount of expenditure or lending a local authority has determined should be met from borrowing in any financial year. Advances from a loans fund records that expenditure. The repayment of that advance, recognised in the statutory Annual Accounts as the statutory repayment of debt, ensures the original expenditure is charged to the General Fund. The balance on the loans fund at any time represents the amount of expenditure a local authority has a liability to meet from future revenue budgets.
 |
|  | Question | Response | Comments / Feedback |
| 20 | Do you agree that there is no longer a statutory need for external borrowing, or its repayment, to be a function of the statutory loans fund? If no, please provide a reason for your response | Yes | **The new legal specification of the Loans Fund seems to be clearly stated. CIPFA notes that the full removal of the requirement for a Loans Fund in England did not appear to cause insurmountable challenges in terms of accounting or Treasury Management practices. The change in the legally specified role of the Loans Fund may result in some practical management changes. For example some changes to the processes for the allocation of interest charges and debt management expenses may arise. Authorities may identify whether significant system and working practices changes will be required.** |
| 21 | Any other comments? | Yes | **CIPFA considers it likely that authorities and other stakeholders will request revised guidance since existing references, such as LASAAC Guidance Note No. 2, will no longer be relevant. In particular there may be a focus on the determination of interest and debt management expenses related to the Housing Revenue Account (HRA).** |
| *Regulation 18: Loan fund advances*Each financial year a local authority is required to make a loans fund advance for any expenditure incurred, or lending made, by the local authority, which the local authority has determined should be met from borrowing, as permitted by Regulation 2. A loans fund advance may not be made for treasury management activities (Regulation 18(2)(a)). A loans fund advance may not be made for credit arrangements (Regulation 18(2)(b)). The accounting treatment, including the repayment of this type of borrowing, is set out in Local Government Finance Circular 4/2010. Fuller details can be found in the proposed statutory guidance. |
| 22 | Any comments? | No Comment | **No comment** |
| *Regulation 19: Duty to make a statutory repayment of loans fund advances.*The detailed arrangements for repayment (equal instalment / annuity) as set out in Schedule 3 are replaced in the 2016 Regulations with a duty to make a statutory repayment of loans fund advances. Regulation 17(2) requires a loans fund to be administered in accordance with the 2016 Regulations, proper accounting practices and prudent financial management. Regulation 19(1) requires a local authority to determine the period over which the advance is to be repaid and the amount of repayment to be made in each financial year in that period. Regulation 19(2) allows a local authority to subsequently vary either the period of the amount of the repayment, or both, if it considers it prudent to do so.The 2016 Regulations do not define prudent financial management. What is considered to be prudent as it relates to repayment of loans fund advances is set out in the proposed statutory guidance.  |
| 23 | Any comments? | Yes | **CIPFA supports the application of proper accounting practice.****Prudent Financial Management****The term ‘prudent financial management’ in** **Regulation 17(2) is not defined in the regulations nor is it specifically defined in the statutory guidance. Consequently it may be open to some interpretation.****For the purposes of these regulations CIPFA therefore suggests that the term is not used in regulation 17(2) but that reference to ‘prudent administration’ would be more appropriate. This would provide a more specific and context dependent term which would be less open to wider usage and non-specific application outside the context of the regulations and loans fund administration.****This would also be more closely in alignment with the terminology of the Local Government (Scotland) Act 1973, specifically section 95 which refers to “the proper administration of [each authority’s] financial affairs”.** **The responsibility for prudent administration should primarily rest with the governance arrangements of each authority, as recognised in regulations 19(1) & 19(2), including securing the services of a section 95 officer.****Statutory Adjustment** **The current statutory adjustment (reversal of depreciation and charging of loans fund advances to the General Fund) relies upon the Local Government (Scotland) act 1795 Schedule 3 section 15(1) which includes “all sums advanced to a borrowing account of a local authority or to a relevant authority shall be repaid within the fixed period”. The proposed wording of 19(1) “the period over which the advance is to be repaid to the loans fund, and****…. the amount of repayment to be made to the loans fund” would presumably be the basis for continuing statutory adjustment.** **CIPFA suggests that the phrasing could be more definitive or specific to emphasise that loans fund advances are charged to the General Fund. This would provide a clear basis for the reversal of depreciation from the General Fund. CIPFA accepts that it can be argued that the proposed statutory guidance sufficiently covers this point.** **Timing of Loans Fund Advance****Regulation 19 (1) includes “at the time of making a loans fund advance”. This may, for any specific relevant expenditure, potentially occur after the end of the financial year that the permitted expenditure was incurred in. It is assumed that this does not pose any specific difficulties for compliance purposes.** |
| **PART 5 Consequential amendments, revocations and transitional provision** |
| Regulations 20 and 21 have been included to tidy up the 1975 legislation where there are references to Schedule 3 provisions to be repealed.Regulation 22 revokes SI’s currently in force to regulate local authority borrowing by way of local authority stocks, bonds or mortgages. These are being revoked as the 2016 Regulations no longer detail the types of borrowing a local authority may undertake.  |
|  | Question | Response | Comments / Feedback |
| 24 | Do you agree that the Regulations currently in force to regulate local authority stocks and bonds should be revoked? If no, please provide an explanation for your answer. | Yes | **Given the removal of limitations on the form of borrowing, CIPFA considers that authority reliance on and adherence to best professional practices regarding borrowing and Treasury Management, for example the Prudential Code and the Treasury Management Code (Treasury Management in the Public Sector),** **is appropriate, .** |
| 25 | Do you agree that the Regulations currently in force to regulate local authority mortgages should be revoked? If no, please provide an explanation for your answer. | Yes | **CIPFA considers that authority reliance on and adherence to best professional practices regarding borrowing and Treasury Management,** **for example the Prudential Code and the Treasury Management Code (Treasury Management in the Public Sector), is appropriate.** |
| 26 | Do you consider that statutory regulation is required for local authority borrowing through the issue of stock or bonds?If yes, please indicate what you consider should be regulated.  | No |  |
| 27 | Any other comments? | No Comment |  |
| **OTHER QUESTIONS – Items not in the 2016 Regulations** |
| **Schedule 3 provisions**A number of Schedule 3 provisions have **not** been included in the 2016 Regulations. These include:Paragraph 1(3) of Schedule 3 which allows a local authority to borrow for working capital for a public utility undertaking carried on by the authority. Statutory conditions apply. An opportunity to comment on this omission is provided at question 5 above.Paragraph 5 of Schedule 3 provides Scottish Ministers with the power to make regulations to regulate borrowing where the borrowing is raised through the issue of stocks, bonds or mortgages. The existing regulations issued under paragraph 5 are to be revoked (see above). Paragraph 5 will not be revoked and will continue to provide Scottish Ministers with the power to regulate if considered desirable or necessary in the future. An opportunity to comment on the revocation of existing SIs is provided at questions 27 to 29.Paragraph 13 of Schedule 3 is a transitional provision.Subject to non-compliance with the legislation being the subject of a report by the Controller of Audit, Paragraph 18 of Schedule 3 provides Scottish Ministers with the power to petition the Court of Session to grant them the power to require the authority to make such payment or comply with the legislation.Paragraph 20 provides additional protection to lenders where the local authority defaults on a borrowing arrangement.Paragraph 21 makes provision for Scottish Ministers to make regulations about the operation of loans funds. Similar powers are already contained in the Local Government etc. Act 1994, the Act being used to make the 2016 Regulations. |
|  | Question | Response | Comments / Feedback |
| 28 | Do you ~~agree~~ consider any of the provisions omitted should be provided for in the Regulations?If yes, please identify the provision/s and provide an explanation as to why the provision should be made. | No | **No additional comment.** |
| 29 | Any other comments? | No Comment | **No comment** |
| **New purposes for borrowing**The review group proposed that the purposes for which a local authority could borrow should be **extended.** This included a **new** provision to enable a local authority to borrow to either make grants to third parties where these grants fund capital expenditure, or for the authority to incur expenditure directly on third party tangible assets.The review group also proposed a further **new** provision – for a local authority to be able to borrow to lend to any of its subsidiary bodies where the loan is to be used to finance capital expenditure of the subsidiary. The test as to whether it is capital expenditure would be the same test a local authority applies to its own expenditure. The definition of subsidiary body would take the same definition as the Code of Practice on Local Authority Accounting in the UK.Scottish Ministers have asked for further information to demonstrate the need for, and benefits from, including these new statutory purposes for borrowing. Local authorities have the opportunity to provide information for Scottish Ministers to consider. |
| 30 | Do you agree that local authorities should be able to borrow to support the capital investment plans of third parties through a grant payment? | Yes | **The ultimate objective from the use of taxpayer resources is the achievement of outcomes.****The traditional historic ‘direct service delivery’ model for public services is now one of many different methods of securing service delivery. Modern public bodies are now more likely to use a diverse range of service delivery mechanisms, including arm’s length external organisations, charitable bodies and collaborative arrangements with other public sector organisations.****The proposed new borrowing legislation therefore needs to be suitable for the modern era.** **Such increased flexibility however should be used within an acceptable framework that supports the proper stewardship of taxpayer resources. For example the application of the Prudential Code to local authority borrowing, the use of suitable terms & conditions in making grants and the principles of ‘following the public pound’ would all be relevant in ensuring proper stewardship.** |
| 31 | Do you agree that local authorities should be able to borrow to support the capital investment plans of third parties through direct expenditure on third party assets? | Yes | **The ultimate objective from the use of taxpayer resources is the achievement of outcomes. The flexibility to use different means to achieve outcomes should be generally welcome. Such flexibility however should be used within an acceptable framework that supports the proper stewardship of taxpayer resources. For example the application of the Prudential Code to local authority borrowing, the use of suitable terms & conditions surrounding the use of the third party assets and the principles of ‘following the public pound’ would all be relevant in ensuring proper stewardship.** |
| 32 | **New purpose** – proposal for a local authority to be able to borrow to lend to any of its subsidiary bodies where the loan is to be used to finance capital expenditure of the subsidiary. This has been left as free format to allow respondents to comment on the proposal. Where a respondent supports the proposal Scottish Ministers are looking for the respondent to demonstrate the need for this to be a statutory provision and the benefits this will provide. A separate response to this item may be submitted. If there is a separate submission please indicate here that this has been made.**CIPFA considers that** **for the purposes of accountability and responsibility for the use of public funds subsidiaries of Scottish local government organisations should normally be regarded, whatever their constitution, as being part of the public sector. As such they should be managed and governed by governance arrangements suitable for the public sector. This should include clear expectations regarding stewardship of public funds, the achievement of best value and the responsibilities of the authority and the section 95 officer.**  |
| **STATUTORY GUIDANCE – LOANS FUND ACCOUNTING (PART 2)** |
| *Loans Fund Advances paragraphs 11 to 23*Regulation 2 of the 2016 Regulations sets out the purposes for which a local authority may borrow. For some of the purposes, such as capital expenditure of the local authority, a local authority is able to use resources other than borrowing to finance that expenditure. For other purposes, such as grants or loans to third parties, where a local authority wishes to treat the expenditure or loan as capital for statutory or Prudential Code purposes, the only source of financing available is borrowing. Regulation 18 requires a local authority to determine each year the amount of expenditure incurred, as permitted by the 2016 Regulations, or by a borrowing consent, to be financed by borrowing. The statutory guidance sets out whether a local authority is required to make any statutory adjustment to the statutory Annual Accounts for expenditure the local authority has determined should be met from borrowing. No guidance is provided for Regulation 2(1)(b) – treasury management activities, as Regulation 18(2)(a) prohibits these transactions from being the subject of a loans fund advance.Guidance is provided for the following:Regulation 2(1)(a) – capital expenditure of the local authority Regulation 2(1)(c) – lending to other bodiesRegulation 2(2) – where a borrowing consent is for capital investment - a capital grants to third parties or expenditure on third party tangible assets, or for non-capital investment. |
| 33 | Do you agree that no statutory adjustment is to be made to the statutory Annual Accounts expenditure incurred for the purpose of Regulation ~~2(1)(a)~~2(1)(b)? | Yes | **CIPFA considers that statutory adjustment is not appropriate for borrowing undertaken for treasury management activities (per regulation 2 (1) (b))** |
| 34 | Do you agree that a statutory adjustment is to be made to the statutory Annual Accounts expenditure incurred for the purpose of Regulation 2(2) where this is expenditure? | Yes | **CIPFA considers that statutory adjustment is appropriate for borrowing undertaken for the purposes in regulation 2(2).** |
| 35 | Do you agree that no statutory adjustment is to be made to the statutory Annual Accounts expenditure incurred for the purpose of Regulation 2(1)(c) and Part 3 or for or Regulation 2(2) for lending of the authority? | Yes | **CIPFA notes that the absence of statutory mitigation for these purposes could mean that an authority is exposed to the immediate impact of any impairment (eg due to non-repayment) of such on-lending. CIPFA considers that this reinforces and emphasises the responsibility of each individual authority for the proper stewardship of taxpayer resources.****The Statutory Guidance Part 1 para 36 (page 6) could possibly be split into two paragraphs:**1. **To address the terms and conditions of the loan made to a relevant body etc (at the discretion of the authority).**
2. **To address the loans fund repayment period for an advance related to any such loan**
 |
| 36 | No guidance has been provided for Regulation 2(1)(d) as the Scottish Government is not aware of any other purpose other legislation has authorised a local authority to borrow. Do you agree that no other legislation provides for other purposes? | Yes | **CIPFA is not aware of any other legislation that would be relevant for regulation 2(1) (d)** |
| *Duty to make a statutory repayment of loans fund advances - paragraphs 24 to 48*Regulation 17(2) requires the loans fund to be managed in accordance with prudent financial management. The 2016 Regulations do not define prudent. Regulation 18(1) requires a local authority to determine, for each loan fund advance, the period over which the advance is to be repaid, and the amount of repayment in each financial year in that period.In making the determination as to repayment of an advance the repayment must be a prudent repayment. The statutory guidance sets out the meaning of prudent repayment (paragraphs 26 and 27).The 2016 Regulations only apply to new loan fund advances made after 1 April 2016. Repayment of loan fund advances made before 1 April 2016 continue to be made in accordance with the repayments identified to be made each financial year applying Schedule 3 of the 1975 Act.The statutory guidance sets out 4 options that are considered to represent prudent repayment (paragraphs 28 to 44). The first option, the statutory method, is a transition option only. It allows a local authority to determine, for a transition period of 5 years, that loans fund advances made from 1 April 2016 will be repaid as if the Schedule 3 had not been repealed. This recognises that a local authority will already have agreed capital investment and associated borrowing plans in the medium term, and taken into account the revenue impact of those plans in future revenue budgets. From 2021 only options 2 to 4 are considered to represent prudent repayment. The other 3 options set out in the statutory guidance are (i) Depreciation Method, (ii) Asset life method, and (iii) Funding/ Income method.Regulation 19(2) allows a local authority to subsequently vary the period and the amount of repayment, or both, if it considers it prudent to do so. The statutory guidance sets out when a local authority may consider it prudent to make a change (paragraphs 45 to 48).The statutory guidance also includes guidance on accounting for loan fund repayments in terms of debiting the General Fund (HRA) and crediting the Capital Adjustment Account. This is a statutory adjustment to the statutory Annual Accounts (paragraph 49).  |
| 37 | Do you agree with the meaning of prudent repayment as set out in the statutory guidance? If no, please provide reasons. | Yes | **CIPFA concurs with the overall approach to the description of prudent repayments in the statutory guidance. However, we suggest that it might be best expressed as the repayments of the loan should be reasonably commensurate with the period and pattern (amount of the repayment) over which the relevant expenditure provides benefits to the authority. This then provides a description under which the options can be assessed and would allow for the income approach.****The *Code of Practice on Local Authority Accounting in the United Kingdom* (the Accounting Code) 2015/16 (4.1.2.6) defines depreciation as “… the systematic allocation of the depreciable amount of an asset over its useful life.” The Code (4.1.2.44) also states that the depreciation method used should reflect “the pattern in which the asset’s future economic benefits or service potential are expected to be consumed”. On this basis we consider the description of prudent repayment reflects the general principles adopted by the accounting requirements.** |
| 38 | Do you agree that Option 2, the depreciation method represents prudent repayment? If no, please provide reasons. | Yes | **We consider that a prudent basis for repayment of the loan should be reasonably commensurate with the period and pattern over which the capital expenditure provides benefits to the authority. As the definition of depreciation represents the consumption of the economic benefits and service potential inherent in the asset then CIPFA concurs that generally this represents a prudent provision.****We understand that the ‘depreciation’ approach is not commonly used in England when determining Minimum Revenue Provision. As the proposals currently stand it is possible that Option 2 (depreciation) may not be commonly used in Scotland.****Historical Cost****CIPFA suggests that the statutory guidance could clarify that the prudent repayment should be the historical cost element of depreciation and the historical cost element of impairment charges that would impact on the General Fund. As all other options are based on financing historical cost it would make sense to clarify that option 2 should be based on the historical cost element of depreciation. (see the Accounting Code of practice 2015/16 para 4.1.3.2 re the historical cost element of depreciation)****If this is not clarified authorities might be substantially dissuaded from using option 2 to avoid the risks of potentially significant debits (this is likely to be even more substantial following the move to measuring the Highways Network Asset at current value).** **Additionally, where an asset is revalued and the value increases over time, use of current value (total) depreciation would accelerate the meeting of loans fund advances that are based on historical cost, such that they will be paid off in advance of the end of an asset’s life.****Impairment and Derecognition****There appears to be a potential contradiction between Part 2 paragraph 33 (which requires any amount of impairment to be reflected in the annual loans fund repayment) and part 2 paragraph 35 (where a 100% impairment would effectively represent a derecognition but the loans advance repayment would not be affected).** **This difference raises the question as to why a partial impairment is considered to require a change to the planned loans fund advances, when a derecognition (for any reason) does not warrant this.****We accept that the proposed treatment of unchanged advance repayments on derecognition could be a pragmatic response to ameliorate the impact on the General Fund.****Component Derecognition****There may also be a potential question concerning the derecognition of components on replacement. The Highways Network Asset proposals for 2016/17 allow an assumption that a component is fully consumed when it is replaced. (See ED 2 para 4.11.2.14 which includes “Authorities shall assume that the asset has reached the end of its useful life and/or has been fully utilised”). It may be that separate guidance would be required in relation to the Highways Network Asset.****If a component is replaced it may not be clear whether this should be treated as an impairment or as a derecognition under the statutory guidance.****Additionally where one loans fund advance is made covering a single asset split into several components, the application of the statutory guidance may not be clear where a component is derecognised. In accounting terms from the asset’s perspective this is a derecognition. Would this be a derecognition for the purposes of the statutory guidance?** |
| 39 | Do you agree that Option 3, the Asset life method, represents prudent repayment? If no, please provide reasons. | Yes | **CIPFA considers that linking the advance repayments period to the asset life is a prudent approach.****There is however some concern that part 2 paragraphs 39 & 48 (no change to advance repayments period if the asset life increases or decreases) may create pressure and an undesirable incentive to take an optimistic view of asset life from the outset. Clearly a professional and prudent approach should guard against such assumptions, which would also be subject to audit scrutiny.**  |
| 40 | Do you agree that Option 4, the funding, income method, represents prudent repayment? If no, please provide reasons. | Yes | **CIPFA considers that linking the advance repayments period to a specifically related funding stream is prudent, subject to the prudent estimation of the funding stream being relied upon. Requiring advances to be split to reflect pro-rata funding is also supported.****The phrasing of part 2 paragraph 44 appears to allow more flexibility and latitude for judgement,** **with less prescription, to cope with changing circumstances and assumptions than the other options appear to support.** **For example a failure to meet the terms and conditions for the receipt of City Deal funds would not automatically mean that the full advance becomes repayable. Nor does the statutory guidance specifically require that the advance repayments move to an asset life or depreciation basis in the event of funding stream failure. The application of part 2 paragraph 43 in the event of a change in the profile or amount of the income stream could be clarified.** |
| 41 | Do you agree with the statutory guidance as it relates to varying the period of any repayment and the annual repayments amounts? If no, please provide reasons. | Yes | **Generally CIPFA agrees that the ability to vary the advance repayment, where it is prudent, is supported.****As noted above however there is concern that paragraphs 39 & 48 (no change to advance repayments period if the asset life increases or decreases) may create pressure and an undesirable incentive to take an optimistic view of asset life from the outset.** **Additionally part 2 paragraph 47 appears to be more flexible and less prescriptive in the variation allowed under the funding/income method as opposed to the asset life or depreciation methods.** |
| 42 | Do you agree with the statutory guidance as it relates to accounting for the repayment of loans fund advances? If no, please provide reasons. | Yes | **With reference to previous comments relating to clarity on application of statutory mitigation, part 2 paragraph 49 could potentially specify that the historical cost elements of depreciation and impairment charged to the General Fund should be transferred to the Capital Adjustment Account (Cr the General Fund Dr the CAA).** |
| *Policy on prudent repayment and disclosure of sums committed - paragraphs 50 to 55*Accounting standards require a local authority to disclose their policy on depreciation. A statutory adjustment is currently made to the statutory Annual Accounts replacing depreciation with the statutory loans fund advance repayment. The new statutory arrangement for the repayment of loans fund advances requires a determination by the authority as to repayment. Local authorities are required to articulate their policy for prudent repayment. The statutory guidance requires a local authority to disclose their policy for determining its statutory loans fund advance repayment within the statutory Annual Accounts.Loans fund repayments represent a liability to repay in future periods, similar to lease repayments or borrowing. The statutory guidance therefore requires disclosure in the statutory Annual Accounts of the value of outstanding advances at each financial period end, together with an analysis of the value of repayments due in future periods. The disclosure requires the analysis to be in 5-year periods. |
| 43 | Do you agree that a local authority’s policy on loan fund repayments should be included in the statutory Annual Accounts?If no, please provide reasons. | No | **We consider that as one of the substantial adjustments in the adjustments between accounting basis and the funding basis line it would be useful for a local authority in Scotland to set out briefly that it has complied with the statutory requirements for loans fund repayments in its summary of accounting policies, the authority will choose the level and relevant narrative description to meet the needs of its users.**  **We are not certain that it would benefit the users of local authority financial statements if this is specified in statutory guidance. There is no such requirement in the English statutory guidance on the Minimum Revenue Provision.** |
| 44 | Do you agree that a disclosure note on loans fund balance, together with an analysis of repayments due in future periods should be included in the statutory Annual Accounts?If no, please provide reasons. | No | **The Scottish Government will be aware that following the CIPFA/LASAAC Local Authority Accounting Code Board (CIPFA/LASAAC) Telling the Story review that there is a need to avoid adding clutter to local authority financial statements.****We are not clear what benefits the user of local authority financial statements in Scotland might derive from the inclusion of these disclosures.** **Compliance with the requirements of the new statutory guidance will be provided by the assurance on the statutory adjustment relating to the repayment of the loan.** **CIPFA/LASAAC has focussed on streamlining the disclosures relating to the statutory adjustments; these proposals would add further detail to this area.**  |
| 45 | Any other comments? | No Comment |  |
| *Any other comments you wish to make on the proposals?*  |