

Response ID ANON-Y9BZ-FPYU-J

Submitted to Consultation on the Future of the IFRS 9 Statutory Override
Submitted on 2022-09-09 10:03:32

Introduction

1 What is your name?

Name:
Mark Catlow

2 What is your email address?

Email:
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3 What is your organisation?

Organisation:
Chichester District Council

Background

Scope of the consultation

Matters for consideration

Questions

1 In your view, what should the future of the IFRS 9 override be post March 2023 [elapse/extend/make permanent]? Please set out your rationale.

Make permanent

In your view, what should the future of the IFRS 9 override be post March 2023 [elapse/extend/make permanent]? Please set out your rationale.:

The Council's view is that the addition of a further source of revenue uncertainty and risk at this time would be unwelcome and would necessitate further revenue resource being diverted from funding front line services to mitigate fair value risk.

For this reason, the Council prefers that the override is made permanent. The conditions that justified the override still exist and our experience over the last few years (see Q10) have demonstrated the need for the override to remain. Further, making the statutory override permanent would have the added benefit of releasing the risk reserve (see Qs 2&4 below) for investment in council services, or to address immediate concerns regarding inflationary cost pressures.

2 Please describe any financial consequences for your authority if the statutory override is allowed to elapse from 31 March 2023?

Please describe any financial consequences for your authority if the statutory override is allowed to elapse from 31 March 2023?:

The Council intends to hold around £45m in external pooled fund investments at the end of 2022/23. These are financed entirely by internal cash resources.

The funds have been carefully selected to diversify risk and, as a further mitigation, the Council employs a fair value risk reserve which would be used to absorb some fair value movements if the override is removed.

Whilst it would be hoped that, over time, fair values will increase to provide downside risk cover, this is not the case at present and our experience over the last few years proves the adage that values can go down as well as up.

If the override were allowed to lapse on 31.3.2023, any negative fair value movements would be charged to the risk reserve in the first instance, but council tax-payer funds would not be isolated using the reserve as funds would need to be diverted to reinstate a suitable balance as part of future budget periods.

3 What are the advantages and disadvantages of investing in pooled investment funds for your LA?

What are the advantages and disadvantages of investing in pooled investment funds for your LA? :

The Council first invested in external pooled funds in 2016.

Since that date, these investments have generated over £5m of revenue to support front line services. Further detail of this is provided in our response to

Q10.

This return is significantly greater than that available through this period from term deposits and direct investments with third parties such as local authorities and banks.

This income has supported the provision of important front-line services through the last six years and has helped the Council maintain services through the pandemic and post-pandemic periods.

Alongside the revenue return, we feel that pooled fund investments are more diversified and are at less risk of individual default than direct investments or deposits, particularly given the potential for bail-in of Local Authority investments in the banking sector.

As to disadvantages, we have identified the following:

1. The implementation of IFRS9 has led to significant local funds being diverted from services to provide for the potential that fair value movements will, ultimately, be charged to the Council's General Fund; The council has currently set aside £1.4m of funds to cover such losses and may need to supplement that further by the end of the current financial year.

2. The Treasury function is becoming increasingly complex, especially given the changes to the 2021 CIPFA Treasury Code.

3. The requirement for MIDIF2 accreditation can be time consuming and bureaucratic; and,

4. The systems required to monitor and record these investments are often expensive and therefore difficult to justify for a local authority.

4 How would removing the statutory override change your current approach to investing in pooled investment funds?

How would removing the statutory override change your current approach to investing in pooled investment funds?:

We would continue to invest in external pooled funds as we believe that they are an appropriate vehicle for long term treasury investment. If the override were removed, we would need to divert resources from front line services to mitigate the risk of fair value movements.

To illustrate the resources that would need to be reserved, the following are our calculated reserve values based on our likely investment portfolio as at 31.3.2023.

Risk that loss in any one year would exceed reserve Reserve needed – resources taken from front line services

1 in 5 £1,852,000

1 in 7 £2,271,000

1 in 10 £2,822,000

1 in 20 £3,616,000

5 Assuming the statutory override elapses March 2023, what impact might this change have on your audit process?

Assuming the statutory override elapses March 2023, what impact might this change have on your audit process?:

We cannot speak for our auditor on this point however we don't see how the removal of an override would increase the complexity of the audit of the Council's accounts.

It would however increase financial risk and uncertainty reflected in the auditors VFM assessment and this may increase the fees payable by local authorities for this work

6 Assuming that the statutory override is continued beyond March 2023, do think it should be time-limited or permanent? Please set out your rationale.

Permanent

(a) Assuming that the statutory override is continued beyond March 2023, do think it should be time-limited or permanent? Please set out your rationale.:

As set out in our response to Q1, we feel certainty is important to financial planning. Adding a new financial risk to a local authority's financial position when it is not absolutely necessary does not feel like a rational choice.

For this reason, our view is that the override should be made permanent. This would also enable the current risk reserve to be released for investment in service provision.

We do not understand why maintaining the IFRS9 override would reduce the credibility of local authority accounting. The Council's comprehensive income statement is maintained on an IFRS9 basis and users of the financial statements can already judge the risk carried by the Council in terms of financial instruments.

We also do not understand why the IFRS9 override should be any different to the multiple other overrides which have existed for many years, and which do not seem to be subject to the same handwringing about credibility that this override has been subjected to.

7 If you think the statutory override should be time-limited, what do you consider the appropriate length of time it should be extended?

If you think the statutory override should be time-limited, what do you consider the appropriate length of time it should be extended?:

n/a

8 If applicable, has your authority taken steps to reduce its exposure to the risks associated with pooled investment funds ahead of the statutory override potentially ending 31 March 2023? Please provide details.

Not Answered

If applicable, has your authority taken steps to reduce its exposure to the risks associated with pooled investment funds ahead of the statutory override potentially ending 31 March 2023? Please provide details. :

The council has taken steps to reduce the risk - please refer to the answers for Q2&4

9 If your authority has not taken steps to reduce its exposure to risks from pooled investment funds, please set out the rationale for this.

Not applicable

If your authority has not taken steps to reduce its exposure to risks from pooled investment funds, please set out the rationale for this.:

10 Do you agree that by not recognising the fair value movement of pooled investment funds this reduces effective risk management and potentially creates future risks? Please provide details.

Do you agree that by not recognising the fair value movement of pooled investment funds this reduces effective risk management and potentially creates future risks? Please provide details.:

Disagree

Do you agree that by not recognising the fair value movement of pooled investment funds this reduces effective risk management and potentially creates future risks? Please provide details.:

No we do not agree.

The governance and risk management framework to be applied is established by the CIPFA Code of Treasury Management and the framework applies whether the override exists or not.

The focus should not be on carried gain or loss, it should be on ensuring that Local Authorities are making robust decisions about their capacity to carry external fund investments over the long term without being forced to sell them and crystallize gains or losses at a time not of their choosing.

If the override is removed, we wonder if this could also influence robust risk management. It may then be open to a local authority to build into its financial plans an assumption on gains from investments likely over a suitable period – effectively incorporating risk into financial projections that the current statutory override eliminates

11 What is the fair value of your authorities pooled investment fund investments as at 31 March 2022?

What is the fair value of your authorities pooled investment fund investments as at 31 March 2022?:

£34m

12 Please set out the value of the gains/losses from your authorities investments in pooled investment funds for 2019/20, 2020/21, 2021/22 recognised under proper practices. Please give both absolute value and as percentage movement for each year.

Please set out the value of the gains/losses from your authorities investments in pooled investment funds for 2019/20, 2020/21, 2021/22 recognised under proper practices. Please give both absolute value and as percentage movement for each year.:

We assume you are referring to the gain/ loss as of 31 March for each year.

2019/20 2020/21 2021/22

Portfolio £34,000,000 £34,000,000 £34,000,000

Gain (Loss)(£3,947,330) £2,880,256 £1,362,338

Gain (loss) % (11.6%) 8.4% 4%

For information and to present a complete picture of the contribution external fund income has made to supporting local budgets and services, the table below provides the total revenue recognised for each of the relevant years. These sums represent approximately 5% of the Council's net cost of services for each year.

2019/20 2020/21 2021/22

External Fund Revenue £897,000 £1,071,648 £1,093,894

13 What is the balance on the unusable reserve as created by the statutory override as at March 2022?

What is the balance on the unusable reserve as created by the statutory override as at March 2022?:

£6,491 Dr

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