AUDIT COMMITTEE	Brighton & Hove City Council **Agenda Item 84**

Subject:		**2009/10 Statements of Accounts and International Financial Reporting Standards (IFRS).**	
Date of Meeting:		**18th May 2010**	
Report of:		**Director of Finance & Resources**	
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Wards Affected:	All		

FOR GENERAL RELEASE

1 SUMMARY AND POLICY CONTEXT

1.1 This report provides the Audit Committee with information on the changes for the 2009/10 Statement of Accounts together with an update on the council's progress in implementing International financial reporting standards (IFRS) for the 2010/11 Statement of Accounts.

1.2 Implementation of IFRS will mean major changes to how we prepare and then present the accounts and so regular updates will be provided to the Committee on our progress towards achieving IFRS compliance.

2 RECOMMENDATION:

2.1 The Committee is recommended to note the changes for the 2009/10 Statement of Accounts

2.2 The Committee is recommended to note the implications for the council of the introduction of IFRS.

3 REASON FOR RECOMMENDATION

3.1 To ensure the Committee has up to date information on the changes that the council is required to make to its accounting practices to comply with the statutory frameworks for producing its accounts for both the 2009/10 and 2010/11 financial years.

4 BACKGROUND INFORMATION

4.1 Under the Accounts and Audit Regulations, the council's accounts must comply with proper practice. Local Government accounts are currently prepared using accounting principles based on UK Generally Accepted Accounting Practices (UKGAAP). Compliance with UK GAAP is currently achieved through the application of the "Code of Practice in Local Authority Accounting – A Statement of Recommended Practice" (the SORP).The SORP is published annually by the Chartered Institute of Public Finance and Accountancy (CIPFA).

4.2 In England and Wales, the SORP is part of the ‘proper practices’ requirements governing the preparation of an authority’s Statement of Accounts referred to in section 21 of the Local Government Act 2003, therefore we have a statutory duty to comply with the SORP requirements.

4.3 The 2009 SORP which relates to the financial year commencing on 1 April 2009 introduces a number of changes in accounting practice which the council needs to comply with. These changes are detailed in Section 5 below.

4.4 The move to IFRS for government bodies, for producing the Statement of Accounts and Whole of Government Accounts, was announced as part of the March 2007 HM Treasury Budget Report. Central Government and Health were required to adopt IFRS for their 2009/10 annual accounts (with comparatives for 2008/09). The adoption by Local Government will be required for annual accounts from the 2010/11 financial year (with comparatives for 2009/10).

4.5 The main reason for adopting IFRS is to bring benefits in consistency and comparability between financial reports in the global economy and to follow private sector best practice.

4.6 CIPFA has issued the first IFRS based Code of Practice on Local Authority Accounting which will apply to local authority budgets and accounts from 1st April 2010. Comparative analyses between the latest SORP and the IFRS based Code of Practice highlight a substantial number of differences where the move to IFRS will bring a number of accounting changes.

4.7 The impact of many of the IFRS’s will be presentational with new terminology and statements being introduced and a significant increase in the level of disclosure notes required. However, there are a number of IFRS’s which will have a significant impact on the accounts for 2010/11 and also the 2009/10 accounts with the early introduction of changes in accounting for Private Finance Initiatives (PFI’s).

5 2009/10 STATEMENTS OF ACCOUNTS

5.1 The 2009 SORP has introduced a number of changes that will need to be implemented for the 2009/10 accounts. The key issues which will affect the council’s financial statements are detailed below.

5.2 **Private Finance Initiatives (PFI) arrangements (IFRIC 12)**

5.2.1 Recognition and measurement of PFI and other similar arrangements are significantly different under IFRS than UK GAAP.

5.2.2 Currently the council has three PFI schemes (Schools PFI, Waste PFI and Library PFI). All three schemes pass the control tests under IFRS and the PFI properties used to deliver these PFI services will be required to be recognised on the council’s Balance Sheet together with a liability for the financing provided by the PFI provider.

5.2.3 Regulations have been put in place to ameliorate any impacts on authorities’ funding positions.

5.2.4 The change in PFI accounting will be implemented for the 2009/10 accounts under the 2009 Statement of Recommended Practice.

5.3 **Accounting for Council tax**

5.3.1 As a Billing Authority the council collects and distributes council tax on behalf of itself and other preceptors. The 2009 SORP concludes that billing authorities act as agents of major precepting authorities in collecting their attributable share of council tax and has introduced changes to the way the council accounts for Council tax.

5.3.2 Under the 2009 SORP only the billing authority's share of income and expenditure from the collection fund will be accounted for on the face of the financial statements, this differs from current practice, whereby all transactions resulting from the collection fund are included within the council's accounts.

5.4 **Accounting for NNDR**

5.4.1 The 2009 SORP confirms that the collection of National Non-Domestic Rates (NNDR) is carried out by authorities as an agent activity on behalf of central government and should be accounted for accordingly.

5.4.2 Under the 2009 SORP the NNDR taxpayers' debtor and creditor balances and impairment allowance for doubtful debts are not Balance Sheet items of the billing authority since it acts as an agent of the Government when collecting NNDR. This differs from current practice where NNDR taxpayers' debtor and creditor balances and an impairment allowance for doubtful debts would have been included on the council's balance sheet.

5.5 **Senior Officers remuneration**

5.5.1 Regulation 4 of the Accounts and Audit (Amendment No.2) Regulations (England) 2009 [SI 2009 No. 3322)] introduces a new legal requirement to increase transparency and accountability in Local Government for reporting remuneration of senior officers.

5.5.2 The new requirements are intended to ensure comparable remuneration disclosure for all senior staff within local authorities and guarantee the same level of openness and transparency as central government and the private sector and comes into force on 31 March 2010 (except where a duty of confidentiality exists).

5.5.3 With effect from the 2009/10 financial year, the statement of accounts must be accompanied by a note of the number of employees whose remuneration fell in each bracket of a scale in multiples of £5,000 starting with £50,000. The amended disclosures are subject to the duty of confidentiality referred to above.

5.5.4 The amended Regulations introduce a new requirement to disclose individual remuneration details as follows:

- For senior employees whose salary is £50,000 or more per year but less than £150,000, they must be listed individually by way of job title only.
- For senior employees whose salary is £150,000 or more per year must also be identified by name.

A definition of senior employee is provided in the amended regulations and will include the Chief Executive, identified by job title and name, together with directors who report directly to the chief executive or hold a statutory post, identified by job title.

6 THE INTRODUCTION OF IFRS.

6.1 The implementation of IFRS is being managed as a project by the council. This project has been ongoing for several months. A Project Board has been established and a Project Manager appointed. A Project Initiation Document has been agreed and detailed project plans have been compiled and put in place to meet the statutory deadlines for producing the 2010/11 accounts within the statutory timeframes. Progress against the project plan is on track and significant progress is being made.

6.2 There are a number of areas which will have significant impact for the 2010/11 accounts following the implementation of IFRS. Individual working groups have been established to consider and implement the necessary changes, both in accounting and system and processes terms. The significant areas of change under IFRS are discussed below.

6.3 **Leases (IAS 17)**

6.3.1 The recognition and measurement of leasing arrangements are changing with the likelihood that more leasing arrangements will have to be included on the council's Balance Sheet.

6.3.2 All existing leases (where the council is either lessee or lessor) are in the process of being reviewed with the potential need to reclassify leases. For accounting purposes there are two types of leases; finance leases and operating leases. Leases will need to be classified as either operating leases or financial leases with the associated accounting treatment being different for each

6.3.3 Whilst the reclassification of leases does not change the amount of money the council receives under a lease, IFRS has complex effects on the accounting treatment of income from leases which may have a potential adverse financial impact on the council's flexibility to apply resources from leases income to meet expenditure. Regulations are in place to delay this impact and as such will only apply to any new leases entered into by the council with effect from 1 April 2010.

6.3.4 The quantitative test, used under the SORP to recognise leases, no longer applies with more emphasis being placed on substance over form and the need to establish whether the risks and obligations of full ownership of an asset have passed over to the council by virtue of the lease agreement.

6.3.5 IFRS also requires the separation of land and building elements of property leases with the land element treated as an operational lease and buildings potentially treated as a finance lease. The potential impact of this would involve bringing the asset onto the council's Balance Sheet together with a corresponding liability.

6.3.6 IFRS introduces the concept of 'lease type arrangements' also referred to as 'Embedded Leases'. This requires assessment of whether any contract may involve the use of an asset, if a contract effectively gives the council 'control' over the use of an asset then this would involve bringing the asset onto the council's Balance Sheet.

6.3.7 There are resources implications in ensuring all leases have been recognised and accounted for correctly. The council has currently employed an external temporary resource to assist officers with this work.

6.4 **Employee Benefits (IAS 19)**

6.4.1 Under IFRS there is a requirement to accrue for the cost of employee benefits to be accounted for in the year in which the benefit is earned by the employee. This will include both untaken annual leave and accrued flexi hours at the year end.

6.4.2 Under UKGAAP, there has not been a requirement to previously accrue for annual leave and flexi leave not taken in the financial year to which it relates and the council, in common with most local authorities, currently makes no year end provision for accrued leave in the accounts. The collation of these balances as at 31st March, for non schools staff, is being obtained from service managers as part of the accounts closure process. The provision in respect of schools staff will be calculated using a formula supplied by CIPFA.

6.4.3 Regulations have been put in place to ameliorate any impacts on authorities' funding positions.

6.5 **Fixed Assets**

6.5.1 IFRS introduces some significant changes to the way Property, Plant and Equipment (previously known as Fixed Assets) will need to be accounted for.

Component Accounting.

6.5.2 IFRS introduces component accounting. There is no formal definition of a component although IFRS requires each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item to be depreciated separately. The council will be required to account for material components of assets as they are replaced rather than having a single valuation for the whole asset. For example, lifts or roofs of buildings may need to be accounted for separately.

6.5.3 The council will need to collect additional information regarding its capital programme to be able to derecognise replaced components and this is likely to have implications for the council's asset management system. These issues are being considered by financial services staff in conjunction with property professionals with potential resource impacts in terms of more valuations needed and changes to systems and accounting treatment;

Valuation Methods

6.5.4 IFRS introduces changes to the valuation methods of assets with property assets valued at fair value; infrastructure assets, community assets, assets under construction and plant and equipment valued at historic cost and council dwellings valued at existing use value (investment properties and assets held for resale are discussed below). Future valuations can continue to be made on a minimum five year cycle, as is currently the case under SORP, but if an asset experiences significant and volatile change in fair value that results in a material difference, then annual valuations are required. Impairment reviews must be made each year. These issues are being considered by financial services staff in conjunction with property professionals with potential resource impacts in terms of more valuations needed and changes to systems and accounting treatment;

Investment Property (IAS 40)

6.5.5 Under IFRS, there are changes in the valuation of investment properties with these assets being carried at fair value rather than the lower of net current replacement cost or net realisable value. There is also a tighter definition of investment properties under IFRS which may lead to some reclassification of assets; in addition, investment properties are to be valued each year (rather than on a five year rolling basis) which has a resource impact for the council.

Intangible Assets (IAS 38)

6.5.6 IFRS introduces new rules for valuing and capitalising intangible assets. IFRS recognises a wider range of intangible assets and internally generated intangible assets are capitalised where the recognition criteria are met; these changes may result in the recognition of more intangible assets.

Non-current Assets Held for Sale and Discontinued Operations

6.5.7 Under IFRS, assets classified as held for sale are measured at the lower of their carrying amount or fair value and are subject to depreciation. There will be implications for the council's asset management system. There is also a tighter definition of non current assets held for sale under IFRS which may lead to some reclassification of assets.

6.6 **Group Accounts (IAS 27, 28, 31, IFRS 3)**

6.6.1 A new definition of a subsidiary or associate is introduced under IFRS and is based around the power to control or significant influence. The definition of joint ventures covers jointly controlled entities, assets or operations. All partnership arrangements across the council will need to be reviewed to assess whether any fall under the IFRS definitions.

7 FINANCIAL & OTHER IMPLICATIONS

Financial Implications

7.1 Impact on Budgets and Council Tax

Whilst some of the changes introduced by IFRS will give rise to a change in the net expenditure reported each year, any impact on Council Tax will be mitigated through statutory accounting adjustments.

Finance Officer Consulted: Melanie Bloom Date: 19 April 2010

Legal Implications*:*

7.2 The recommendations in part 2 above are proper for the Audit Committee to consider and to note. Under the Accounts and Audit Regulations 2003, it is the responsibility of the Audit Committee to approve the council's statement of accounts (SoA).

Lawyer consulted: Oliver Dixon *Date: 21 April 2010*

Equalities Implications*:*

7.3 There are no equalities implications arising directly from this report.

Sustainability Implications*:*

7.4 There are no direct environmental implications arising from this report.

Crime & Disorder Implications*:*

7.5 There are no direct implications for the prevention of crime and disorder arising from this report.

Risk and Opportunity Management Implications:

7.6 Risks in relation to the accuracy of the financial statements are considered as part of the statutory accounts process.

Corporate / Citywide Implications:

7.7 The quality of a public authority's financial statements is of reputational importance and where the auditor gives an unqualified opinion, citizens, partners and other stakeholders can be assured that the statements present fairly the financial position of the authority. The quality and accuracy of the Statement of Accounts also impacts on the council's score under the Comprehensive Area Assessment framework.

SUPPORTING DOCUMENTATION

Appendices

None

Documents in Members' Rooms

None

Background Documents

None