

AUDIT COMMITTEE

29 MARCH 2011

INTERNATIONAL FINANCIAL REPORTING STANDARDS UPDATE

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Summary

This report advises Members of the progress being made to comply with the requirements of the new International Financial Reporting Standards (IFRS).

1. Budget and Policy Framework

- 1.1 In accordance with the terms of reference, consideration of changes to financial rules, new accounting standards and changes to the reporting framework are matters for this committee.

2. Background

- 2.1 All council's accounts were previously prepared using UK Generally Accepted Accounting Practice (UK GAAP). This is converging with International Financial reporting and will eventually disappear. This process has already occurred within the private sector and central government and the NHS were required to be IFRS compliant for 2009/2010. This requirement applies to local authority accounts from 1 April 2010, which also includes comparative data for 2009/2010.
- 2.2 In December 2010, Members of this committee were advised of the changes required to the accounts following the introduction of IFRS and the progress in restating the 2009/2010 Financial Statements. Members also agreed to an increase in the de minimis level in relation to accounting policies for the production of the Statement of Accounts for capital expenditure to £25,000.
- 2.3 The Audit Committee requested a report back to this meeting following the audit of the restated financial statements, including reference to the increase in the de minimis level.

3. Restatement of the 2009/2010 Financial Statements

- 3.1 The core financial statements, in IFRS format, comprise:
- Comprehensive Income and Expenditure Account;
 - Movement in Reserves Statement;
 - Balance Sheet and
 - Cash Flow Statement.

- 3.2 The restated financial statements for 2009/2010 are reviewed by external auditors to ensure compliance with IFRS. However, a formal opinion is not given as this will be incorporated within the audited 2010/2011 accounts. The reviewed financial statements will form the basis of the IFRS compliant Statement of Accounts for 2010/2011 and future years. In addition to these core financial statements there are a number of additional or expanded disclosures in the notes to the accounts e.g. employee severance payments, related parties, movement in non-current assets etc., and a small number of previous disclosures have been removed. The majority of these, although increasing the workload in preparation of the accounts, are relatively straightforward and the relevant data is available.
- 3.3 At the time of writing this report our external auditors, PKF, are still in the process of reviewing the financial statements and an update will be given at this meeting. As indicated at the last meeting of this Committee, IFRS has introduced a considerable number of changes to the way local authorities record and present their financial information and Members were advised of those areas where the most significant changes would occur. The following areas are still being discussed between officers and PKF and, hopefully, any outstanding issues will be resolved by the time this committee meets:
- 'Componentisation' of non-current assets;
 - Treatment of 'embedded leases';
 - Reclassification and valuation of some fixed (now non-current) assets and
 - Treatment of capital grants and contributions.
- 3.4 Unsurprisingly, a recent survey by the Audit Commission has identified componentisation, leases and valuation of property, plant and equipment as the areas which are giving local authorities the most significant reporting issues. For Members' information the Audit Commission survey is attached as Appendix A to this report. Appendix 1 to that document covers the significant reporting issues that were outstanding at the time of the survey.
- 3.5 With regard to the increase in the de minimis level for IFRS capital accounting purposes, this has removed the requirement to treat vehicles used in the grounds maintenance contract, for example, as the Council's assets and the associated detailed record keeping that entails. In addition it should minimise the number of finance leases which require separate treatment in the accounts under IFRS.
- 3.6 The latest guidance on the accounting treatment of different types of schools under IFRS indicates that local authorities should not include those schools as assets in their accounts where they have no direct control over service provision. For Medway, this would result in the removal, as at 1 April 2010, of two primary schools and eight secondary schools with a total value of approximately £115 million. A further secondary school, with a value of £17 million, will be removed during 2010/2011. The new academies on existing sites will remain in the Council's accounts until the new buildings are complete and handed over to the Academy Trust. This approach has been agreed with PKF. For comparison purposes, the total valuation for schools as at 1 April 2010 was some £412 million.

4. Accounting Policies

- 4.1 Part of the transition to IFRS involves review and updating of the Council's accounting policies. The accounting statements will, be prepared in accordance with the Code which is based on approved International Financial Reporting Standards and the Council's Accounting Policies will follow these standards wherever practicable.
- 4.2 A revised set of draft Accounting Policies is attached at Appendix B for Members' approval. These may be subject to review during the preparation of the 2010/2011 accounts and any changes will be subject to members' approval.

5. Financial and Legal Implications

- 5.1 To date there has been no additional cost in adopting IFRS, however, there is a possibility that external support may be required, for example, specialist valuations of property components etc.
- 5.2 The Code of Practice on Local Authority Accounting in the United Kingdom sets out the proper accounting practices required by section 21 (2) of the Local Government Act 2003. These proper practices apply to Statement of Accounts prepared in accordance with the statutory framework established by the Accounts and Audit Regulations 2003

6. Risk Management

- 6.1 Failure to implement IFRS will affect on the quality of the 2010/2011 accounts and the audit of these statements possibly leading to a qualified audit opinion.
- 6.2 The recent resignation of a key member of staff may affect the preparation of the 2010/2011 Statement of Accounts in accordance with IFRS.

7. Recommendation

- 7.1 Members note the progress to date in implementing IFRS as outlined in Section 3
- 7.2 Members agree the draft Accounting Policies set out in Appendix B.

Background papers

IFRS Update report to Audit Committee 21 December 2010

CIPFA Code of Practice on Local authority Accounting in the United Kingdom 2010/11.

CIPFA Code of Practice Guidance Notes

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