

HAMPSHIRE COUNTY COUNCIL**Report**

Committee/Panel:	Audit Committee
Date:	29 September 2010
Title:	International Financial Reporting Standards Implementation – Project Update
Reference:	2007
Report From:	County Treasurer

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1. Summary

- 1.1. This report provides an update to the Audit Committee following the report on 25 March 2010 regarding the required implementation of International Financial Reporting Standards (IFRS) for the financial year 2010/11. It sets out the developments that have taken place in terms of standards and guidance as well as outlining progress made to date with the project.

2. Contextual Information

- 2.1. Following a consultation process, the Code of Practice for 2010/11 was issued by CIPFA/LASAAC in December 2009. This required local government accounting to come fully in line with IFRS accounting for the financial year 2010/11. In addition, the presentation of the financial statements for 2009/10 required an early introduction of IFRS for PFI and related contracts. These changes affect a number of the Council's business processes and systems, most notably valuation processes for property assets, lease arrangements, some small changes in SAP Asset and changes to accounting adjustments and the presentation of accounts.
- 2.2. As such this change is not simply a finance issue as it has wider implications for the organisation. It encompasses many of the practices of the Council from procurement to staffing. The project is being co-ordinated from within County Treasurer's Department but requires buy in and considerable amounts of work from other departments of the Council. Corporate Finance staff have been and continue to work closely with colleagues from PBRsIT, especially in Property Services and Hampshire Transport Management in relation to leases and asset classifications, and in IT Services in relation to SAP Asset.
- 2.3. The County Council is well placed to meet the requirements. Following the Audit Commission's assessment in November 2009 that the Council was on

track with its implementation plan (green traffic light) a further assessment in July 2010 came to the same conclusion. The project plan has been updated to reflect further developments and can be seen in Appendix C.

3. Guidance

- 3.1. At this stage the guidance notes which advise accounting professionals on how to implement the Code of Practice for 2010/11 have not yet been released. The normal timescale for these is for publication prior to the end of December. However, transition guidance has been placed on the CIPFA website to assist Councils in understanding the implications of the transition to IFRS accounting. These do not take the place of the guidance notes as they do not provide practical examples, yet they have proven to assist in calculations, for example of the employee benefits accrual.

4. Early transition elements

- 4.1. One element of IFRS accounting has been introduced earlier than the overall 2010/11 target in order to reflect the Government's timetable for introducing Whole of Government Accounts. This involved a change to accounting for private finance initiatives (PFIs) and similarly structured service concession arrangements.
- 4.2. Where contracts met the specific criteria of service concessions, to provide assets and services to an authority, those assets were required to be brought onto the authority's balance sheet. Following a review of contracts, it was determined that the Council had two such arrangements, the Hampshire Waste Disposal Contract and the new Street Lighting PFI.
- 4.3. As the Street Lighting PFI had been only recently signed at the end of the financial year 2009/10 and no assets had as yet been provided, there were no assets at that stage to bring onto the balance sheet. The notes to the financial statements were required to disclose the expected levels of capital, interest and service payments for the remainder of the contract. This was made possible by using the detailed contract financial model drawn up by external financial advisers in collaboration with finance staff working in the Environment Department. This information will be used in 2010/11 and future years to assist in determining the value of assets to be brought onto the balance sheet and the offsetting liability for paying capital amounts for those assets.
- 4.4. The long standing Hampshire Waste Disposal Contract was also determined, following work with Southampton and Portsmouth City Councils and external financial advisers, to meet the definition of a service concession. Considerable work was undertaken to model the contract from its start date in 1997 and to split capital and interest payments from service costs. These were then allocated to the three collaborating authorities and relevant adjustments have been made in the 2009/10 accounts as well as the restated 2008/09 comparable accounts. In addition, the notes to the accounts include the expected future values of capital, interest and service costs for the remainder of the contract.

5. Progress for 2010/11 Statement of Accounts

Statement Format

- 5.1. Changes to the presentation of the accounts have been assessed and are being incorporated within systems in preparation for the process of producing the 2010/11 financial statements. The 2008/09 balance sheet and the main 2009/10 accounts have been restated as far as possible at this stage, including all the adjustments which have been calculated to date. These are included as appendices D-F to this report, also to demonstrate the new format of the balance sheet, comprehensive income & expenditure statement and the new statement of movement on reserves.

Notes to the Accounts

- 5.2. Under IFRS the notes to the accounts have changed and become more complex in some areas. Ongoing assessment of these changes is taking place in order to ensure that processes are in place before the end of March 2010/11 to collect the relevant information for completion of new notes. Some of the information for 2009/10 comparable notes has already been collected, other aspects will be adjusted as part of the overall 2009/10 restatement. Prior to the end of 2010/11 it will be important to ensure that the format and presentation of these notes is correct and that they feed appropriately into or from the main statements as required.

5.3. Employee Benefits

- 5.4. Surveys of non-teaching staff across the Council have been carried out to determine the average level of annual leave and flexi-leave carried forward at the end of March 2009 and March 2010 in order to restate the 2008/09 and 2009/10 accounts. Taking into account different working practices across the authority, there is a low average level of leave carried forward for non-teaching staff with an estimated value of just under £2 million for 2008/09 and £2.6 million for 2009/10. This represents 0.61% and 0.78% respectively of the Council's total pay costs for non-teaching staff.
- 5.5. For teaching staff the guidance for calculating the value of leave has been revised since the report on 25 March 2010. This has significantly reduced the estimated value of the accrual required to £14.7 million for 2008/09 and £17.8 million for 2009/10 representing approximately 3.51% and 4.1% respectively of the total annual pay costs for teaching staff.
- 5.6. Whilst the accrual for teaching staff benefits represents a material amount, the value of non-teaching staff benefits is not considered significant enough to warrant an entry into the accounts. However it is likely that the Council will be required to continue to conduct an annual review of this figure to ensure that it does not reach a material level.
- 5.7. As noted previously in reports to the Audit Committee, any accrual in the Balance Sheet for employee benefits is purely an accounting adjustment. As such it will not impact upon the General Fund and will instead be offset by a contribution from an Employee Benefits Adjustment Account. This adjustment for the teaching staff accrual has been included in the restated accounts attached.

Grants and Contributions

- 5.8. The Code requires a change to the method of accounting for grants and contributions. Rather than capitalising those grants and contributions received for capital purposes and amortising them over the life of the relevant asset to offset the effects of asset depreciation, instead the income will be recognised in year in the comprehensive income and expenditure statement. Only if the grant or contribution was made with conditions attached to it that have not yet been met or which make it likely that the grant or contribution will need to be repaid, will the balance remain on the balance sheet as a liability.
- 5.9. In order to meet this requirement, work is underway to determine whether any of the material grants and contributions currently held on the balance sheet have such conditions attached. This is considered unlikely and the restatement of the comprehensive income and expenditure account and balance sheet have been initially prepared on the basis that no deferred grants and contributions will be retained on the balance sheet as liabilities.

Leases

- 5.10. Significant work has been carried out to identify all the existing lease arrangements of the Council. These have been assessed against the indicative criteria included in the Code to determine whether they are operating or finance leases. The overarching principle against which to assess the leases is where the risks and rewards of the assets lie, regardless of the legal arrangements of a contract.
- 5.11. Of the original list of just over 1000 property leases held at 31 March 2009, a shortlist of 120 leases was further analysed against the criteria for finance leases. This has involved close work with the Property Services team within PBRISIT to carry out in depth investigation into the lease agreements, the use of the assets and the values of those assets. Current estimates are that 3 leases meet the criteria and are material enough to impact on the presentation of the accounts. Final stages of determining the adjustments to the accounts for these leases are underway.
- 5.12. Following this, work will be carried out to assess new leases in 2009/10 and 2010/11 against the criteria for finance leases. It is not expected that there will be many if any of these as the majority of leases are for shorter periods than the life of the asset or for land only.
- 5.13. Work is also being undertaken to assess vehicle leases in terms of the criteria for finance leases. It appears unlikely at this stage that any of the vehicle leases will meet this criteria and they will therefore continue to be accounted for as operating leases.
- 5.14. Ongoing consideration is also being given to the contracts of the Council to assess whether they might contain embedded leases. As yet there have been no embedded leases identified.

Investment Property and Assets Held for Sale

- 5.15. Work has been carried out in collaboration between Property Services and Corporate Finance to assess whether any of the assets held at the end of

2008/09 should be properly classified as Investment Property or Assets Held for Sale. A small number of Assets Held for Sale have been identified and the necessary adjustments to the accounts have been made in the restated 2008/09 balance sheet. Work is continuing to assess the value of the Investment Properties which have been identified. This task will also be carried out for the assets held at the end of 2009/10 in order to restate the 2009/10 balance sheet.

Systems

- 5.16. Some small system changes have been identified for SAP Asset and discussions have taken place with Corporate Solutions and SAP representatives on how to implement these. Testing and developments in this area will be taking place shortly. It does not appear that SAP will be able to carry out or automate the necessary calculations for the transactions to deal with finance leases. It is expected that this work will be completed manually.

6. Future work

- 6.1. Much of the work to restate the 2008/09 balance sheet has now been completed with a small number of calculations still required. Once completed the next milestone will be to restate the whole of the 2009/10 accounts by the end of December 2010, ready for review by the external auditors and inclusion in the 2010/11 accounts.
- 6.2. Overall this ongoing work will be completed in accordance with the project plan, drawing on external advice where necessary and keeping the external auditor informed.

7. Recommendation

- 7.1. That the Audit Committee note the progress made and the work still required for the successful implementation of the IFRS Code of Practice.
- 7.2. That a further report on IFRS implementation be considered by the Audit Committee in March 2011.

CORPORATE OR LEGAL INFORMATION:**Links to the Corporate Strategy**

Hampshire safer and more secure for all:	no
Corporate Improvement plan link number (if appropriate):	
Maximising well-being:	no
Corporate Improvement plan link number (if appropriate):	
Enhancing our quality of place:	no
Corporate Improvement plan link number (if appropriate):	

Other Significant Links

Links to previous Member decisions:		
<u>Title</u>	<u>Reference</u>	<u>Date</u>
Implementing International Financial Reporting Standards	918	1 September 2009
Implementing International Financial Reporting Standards – Project Update	1393	25 March 2010
Direct links to specific legislation or Government Directives		
<u>Title</u>	<u>Date</u>	
The Code of Practice on Local Authority Accounting in the UK 2010/11 (Based on International Financial Reporting Standards)	December 2009	

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

<u>Document</u>	<u>Location</u>
None	

IMPACT ASSESSMENTS:

1. Equalities Impact Assessment:

- 1.1. Equality objectives are not considered to be adversely affected by the proposals in this report.

2. Impact on Crime and Disorder:

- 2.1. The proposals in this report are not considered to have any direct impact on the prevention of crime.

3. Climate Change:

- a) How does what is being proposed impact on our carbon footprint / energy consumption?

No specific proposals.

- b) How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

No specific proposals affecting adaptation to climate change.