AGENDA
ITEM 10

Report to: Audit Committee

Date of meeting: 16th March 2011

Report of: Senior Accountant

Title: Update on the progress of the IFRS restatement

1 SUMMARY

1.1 This report follows on from the Implementation of International Financial Reporting Standards report dated 13th January 2010 and updates the Audit Committee about the progress the Council has made in restating the accounts following the introduction of International Financial Reporting Standards (IFRS) to local government. It highlights for Members:

- What has been done to date by officers (3.1)
- What are the major substantive changes (3.2)
- What effects it will have on the authority (3.3)

2 RECOMMENDATIONS

2.1 That the Committee notes the report and periodically monitors the progress of the implementation of IFRS in the Council by way of future reports to Committee

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3 PROGRESS

3.1 What has been done to date by officers?

3.1.1 A considerable amount of work has already been undertaken by officers in ensuring that the Council is IFRS compliant by the agreed date. This work includes:

- **Project & Officer Groups -** In the early stages the councils' formed a project group which has now been replaced by an officer group from the Finance and Property departments who meet every two months to monitor the progress of IFRS issues.
- **Discussed progress** on the implementation of IFRS with the Councils' Internal and External Auditors and sought their advice and clarification on technical issues.

- **Identified the substantive changes** and the work related to those changes
- **Listed the journals that are necessary in order to restate** the opening balance sheet as at 1st April 2009 and 31st March 2010.
- **Drafted a new IFRS compliant skeleton set of accounts for 2010/11** which includes the restated balances as at 1st April 2009 and 31st March 2010. Also, reviewed and adjusted the notes in the accounts that need to be changed due to the introduction of IFRS. The restatement of opening balances will be reviewed by the external auditors in March 2011.
- **Listed what information is necessary to complete the statement of accounts for 2010/11** and informed all staff what information we require and the deadline for returning that information.

3.2 **What are the Major Substantive Changes?**

3.2.1 The major accounting adjustments resulting from the implementation of IFRS are listed below:

- **Reconsidering the classification of investment assets** – IFRS requires Investment property to be held solely for capital appreciation or income generation. If there is any partial service reason for retaining the asset it must be considered operational and would require to be depreciated. The added difficulty is that the restated IFRS balance sheet would have to be amended retrospectively for different accounting treatment required.
- **Identifying the property leases of the Council and establishing the category of the lease, into either finance or operational lease.** The current work by both Councils has identified approximately 150 assets which are held on lease for 15 years or less, and these due to the length are all operational leases. 35 leases of 16 years to 50 years have been evaluated against a criteria to assess and establish the party which has the risks and rewards of ownership. With regard to the longer leases in excess of 50 years 90 leases have been considered most of which are for ground leases
- **Identifying leases on Vehicles Plant and equipment and establishing the category of the lease, into either finance or operational lease –** approximately 50 leases have been assessed
- **Collecting data related to employee benefits that have been earned but not taken,** and therefore need to be accounted for as accruals. IFRS requires costs to be recorded in the contractual year, and this means that if leave is carried forward the cost of leave needs to be taken out of the year it will be taken and passed back as a cost into the year it relates to. Data needs to be collected of untaken leave in respect of carry forward leave, sick leave, and maternity leave, also banked leave at TRDC
- **Considering the requirements for component accounting** which is required where an asset has different elements and those elements have different economic lives. For example, Watford Town Hall may be made up of several components (eg building, land, roof, windows, lifts) which have different economic lives and therefore the depreciation will be calculated on each individual component to give a more accurate assessment of depreciation for the asset as a whole.

- **Reviewing the deferred grants** and making adjustment depending on whether the grants have conditions attached. Where no conditions are attached the grants will no longer be amortised over the life of the asset they fund.
- **New Final Accounting statements including the restatement of previous statements into an IFRS format** – The current Financial accounting statements have had format amendments, the balance sheet presentation will be slightly different and the comprehensive Income and Expenditure account will include the Statement of Total Gains and Losses. Changes also apply the movement on reserves, the cash flow, some of the terminology and the notes in the accounts. Examples of the updated set of 2010/11 Statement of Accounts are attached in Appendix 1.

3.3 **What effects will it have on the Authority?**

- **Accounting adjustments**
  The accounting impact of IFRS on the council will be mitigated as the government has allowed adjustments to the 2009/10 accounts to be reversed in the Council's Reserves' to ensure council tax payers are not adversely affected by the restatment exercise. The major change has been on leases but the impact is likely to be minimal going forward as the Council has been proactive in ensuring that new leases are operating leases, thereby ensuring rent receivable is treated as revenue receipts rather than capital receipts. The other major changes are also unlikely to have a major impact on the Council going forward.
- **Leases**
  The major impact will be in considering leases, as the income or expenditure (I&E) relating to finance leases will be treated as capital income or expenditure (principle) and revenue income or expenditure (interest) rather than just revenue income or expenditure. In order to minimise the future effects of this change, the Legal and Property departments are aware of the changes and are therefore careful in drafting lease agreements (as the lessor) and ensuring where possible the lease agreements are drafted as operating leases and do not transfer the risks and rewards of ownership to the lessee.
- **Classification of property assets**
  The rules regarding classification of assets between operational and non operational has changed and new asset groups added (surplus assets & assets held for sale). The impact of this change is immaterial.
- **Annual leave and TOIL carried forward**
  The accrual for annual leave and TOIL carried forward has been mitigated in the restated 2009/10 accounts. The movement in 2010/11 onwards should not be materially different. HR are aware of this accounting adjustment and both Finance and HR will review the accrual annually to ensure the accrual movement does not have a materially adverse affect on the Council.
- **Grants deferred**
  Accounting for government and non government grants in the I&E will no longer be amortised over the life of the asset they fund.

Where there are no conditions attached they will be credited to the revenue accounts in the year they are received. This will have a positive short term impact on the I&E, but this is a technical accounting entry and will have no affect on Council Tax.

- **Componentisation**
  This will not have a material impact on the council as there are few operational assets above the deminimis level. The assets will be considered for componentisation as and when they are revalued as part of the five year rolling programme and so the effect will be spread over five years and may result in some immaterial additional depreciation in the short term.
- **Staff**
  The IFRS restatement has involved significant additional work over the last year. Technical Finance and Property staff have been on several IFRS seminars and workshops over the last year to ensure the Council has sufficient knowledge of the IFRS restatement process and are fully prepared for the new reporting standards. Also, other Finance and non Finance staff will receive training on IFRS as part of the year end training for 2010/11
- **Systems**
  The New Financial Management system is IFRS compliant and the integrated fixed asset module is being upgraded in March 2011 to ensure it is also IFRS compliant.
- **Financial Impact on Councils General Fund**
  The impact on the General fund for 2009/10 has been mitigated as new capital finance regulations have been produced by the government which prevent the new rules affecting the costs being borne by the Council taxpayer. Key staff are also aware of the IFRS leasing rules and this should help mitigate any future issues resulting from finance leases.

4 CONCLUSIONS

4.1 International Financial Reporting Standards (IFRS) is a statutory accounting requirement from 2009-10, and will require the restatement of the balances as at 1 April 2009 and 31 March 2010 into the IFRS format. A summary of the adjusted 2009/10 balances are attached in Appendix 2.

4.2 The implementation of IFRS has involved Officers in significant additional work. The impact on the authority's statement of accounts will be significant but the impact on the Council's general fund will be mitigated for past transactions and will only impact on ongoing leases.

5 IMPLICATIONS

5.1 **Financial Issues**
The implementation is currently achieved by the use of existing resources.

5.2 **Legal Issues**
The legal implications are contained within the body of the report.

5.3 **Potential Risks**

Potential Risk	Likelihood	Impact	Overall score
Failure to accurately identify changes to be made to accounts	2	3	6
Failure to meet timetable	2	3	6
Insufficient resources to implement	1	3	3
Financial Impact on Council	1	3	3
Those risks scoring 9 or above are considered significant and will need specific attention in project management. They will also be added to the service's Risk Register.			

5.4 **Staffing**

None Directly

5.5 **Accommodation**

None Directly

5.6 **Community Safety**

None Directly

5.7 **Sustainability**

None Directly