PART A

| | |
|---|---|
| **Report to:** | Audit Committee |
| **Date of meeting:** | 13th March 2013 |
| **Report of:** | Head of Strategic Finance |
| **Title:** | Grant Thornton Update |

1.0 **SUMMARY**

1.1 Attached is a general up date regarding national developments and specific issues relevant to Watford.

2.0 **RECOMMENDATIONS**

2.1 That the Committee considers the attached paper and the response from the Head of Strategic Finance.

**Contact Officer:**
For further information on this report please contact: Bernard Clarke, Head of Strategic Finance, telephone extension: 8189 email: bernard.clarke@watford.gov.uk

3.0 **RESPONSE TO ATTACHED PAPER**

3.1 Grant Thornton (on Page 5 of attached report) refer to discussions regarding lease agreements for the Harlequin and Charter Place. These discussions were instigated by the Council and concerns potential changes to the current financial arrangements with Capital Shopping Centres (CSC) and has been necessitated by changes in accounting methodology through International Financial Reporting Standards (IFRS)

3.2 Simplistically, as far as IFRS is concerned there are two types of 'lease arrangement'—a finance lease and an operational lease. For local authorities there is a significant difference between the two whereby if any financial arrangement is determined to be a finance lease then any income generated has to be classified as a capital receipt. If however a lease is agreed to be an operating lease then the income is classified as revenue income. Current agreements for the Harlequin (INTU) Centre have allowed all income to be treated as revenue. In seeking to reach agreement on the redevelopment of Charter Place, CSC has requested current agreements should be amended.

3.3 It is vitally important therefore that the structure of any amended agreement does not change the current situation whereby all income is treated as revenue. Should this not be the case and any of the considerable rental income be treated as a finance lease (and hence become a capital receipt) then the Council would have a rather large hole in its revenue budget. Discussions with Grant Thornton are ongoing.

3.4 Also on Page 5 of attached Paper reference is made to advice regarding the treatment of Growing Places Funding at the Health Campus. This discussion was again instigated by the Council and could potentially have a significant effect upon revenue budgets. Accountancy treatment is again the 'villain of the piece'. The Council would wish to borrow £6m from the Local Enterprise Partnership (LEP) to help fund infrastructure works at the Health Campus. Under accounting rules the Council would need to make provision for the repayment of the loan through a 'Minimum Revenue Provision' (MRP) in its annual budget. The loan (in actual fact two loans of £3m) needs to be repaid back within 5 years of their having been taken up.

3.5 The need to make an annual provision is not necessary however if it can be demonstrated that a return on the up front investment is relatively certain within the five year period. The financial arrangements with our Health Campus partner, Kier, is seeking to ensure that the £6m Growing Places funding will be prioritised in any future dividends.

3.6 Grant Thornton also refer (on Page7) to the recently introduced retention of business rates. The Council has received forecasts of the effects upon Watford. The most recent in February 2013 from the DCLG seemed to suggest that the Council would be better off under the new system. The DCLG did not fully take into account the potential for business rate appeals currently outstanding with the Valuation Office. Any increased 'yield' from business rates would also be dependent upon the annual uplift to business rates (2.6%, RPI). There is strong pressure upon the Chancellor of the Exchequer in his 20th March Budget to actually freeze any increase in business rates. The Council's MTFS has been cautious therefore and assumed no benefit (or shortfall) in business rate income in 2013 onwards. It is anticipated that before planning the 2014/2015 Budget that further modelling will take place.

3.7 Grant Thornton has highlighted (on Page 8) the fact that Municipal Mutual Insurance has announced it can no longer guarantee a solvent run off. This has been anticipated by Watford for the past two years. The Statement of Accounts for both 2010/2011 and 2011/2012 (Page 74) has highlighted this likelihood as a Contingent Liability. The Council currently has outstanding claims from potential litigants of £348k and dates back over a decade and may not be settled. Nevertheless, the Council's general reserves has included £100k as cover should this £348k be fully realised. I will discuss with Grant Thornton as part of Final Accounts closure for 2012/2013 whether this £100k needs to be moved from reserves into the 'provisions' section of the Balance Sheet.

3.8 Grant Thornton's update also refers to six reports produced by the Audit Commission (Pages 9 to 12 refer) and asks 'have you considered them'? The simple answer is NO. Part of the concerns of local government was that councils were required to follow the Audit Commission's agenda rather than manage their own affairs. There seemed to be a presumption that local councils (particularly small district councils) had a staff resource retained to consider regular reports produced by 'technicians' within the Commission. The demise of the Commission was generally welcomed in large areas of local government and has had the effect of considerably reducing external audit fees. The most substantial issues within these reports are reflected within the way Watford conducts its business and prepares its financial planning. Many of the issues have been reflected within Grant Thornton's own reports on issues such as financial resilience and value for money. The latest report on improving Council Governance is currently being studied as I would intend to report the Annual Governance Statement to the Audit Committee at its June meeting.

3.9 Page 12 of the attached document refers to preparation for closure of the 2012/2013 final accounts. In terms of specific questions: I do not believe there are any key risks in preparing the financial statements for 2012/2013, there has been no major changes in staff resource and financial figures are looking very comfortable at the present time. Timetables have been produced and meetings held with Grant Thornton. So far, so good.

3.10 Finally, on Page 12, the issue of Reserves is highlighted. The Audit Committee has considered this in the past (as indeed has the Budget Panel). The Council actually highlights a number of different reserves and explains why they are necessary. At paragraph 3.7 earlier reference has been made to the insurance reserve which has now 'come into play' and has effectively been fully justified.' In setting the budget the report provides a separate section upon the Council's holding of reserves prior to agreeing a council Tax. Watford, in my view, has an exceptionally transparent process where reserves are concerned.

## 4.0 IMPLICATIONS

### 4.1 Financial Issues

The Head of Strategic Finance comments that the up date from Grant Thornton is an extremely useful aide memoire and has effectively confirmed that all financial implications have been reflected within current Council plans and Statement of Accounts.

4.2 **Legal Issues** (Monitoring Officer)

The Head of Legal and Property Services comments that there are no legal implications arising directly out of this report.

4..3 **Potential Risks**

| Potential Risk | Likelihood | Impact | Overall score |
|---|---|---|---|
| That the Council will fail to anticipate future financial pressures. | 1 | 4 | 4 |

4.4 **Staffing**

None Directly

4.5 **Accommodation**

None Directly

**Appendix 1: Grant Thornton Update**