AUDIT & GOVERNANCE COMMITTEE

28th June 2012

Report of the Director of Finance

DRAFT ANNUAL STATEMENT OF ACCOUNTS & REPORT 2011/12

EXEMPT INFORMATION

None

PURPOSE

To receive the Draft Statement of Accounts (the Statement) for the financial year ended 31st March 2012.

RECOMMENDATION

That Members review the Annual Statement of Accounts 2011/12.

EXECUTIVE SUMMARY

Current legislation, detailed in Accounts and Audit (England) Regulations 2011, requires the Council to prepare a Draft Statement of Accounts by 30th June each year (approved by the Chief Finance Officer), a Committee of the Council to approve the Statement by 30th September and for the Council to publish the Statement together with the Auditors opinion by 30th September 2012.

The draft accounts, once signed by the Executive Director Corporate Services, will be issued to the External Auditor on or before 30th June in compliance with the regulations, and are subject to the normal External Audit review by the Audit Commission.

Although there is now no formal requirement for this Committee to approve the accounts prior to audit, it is considered best practice that members have the opportunity to review the accounts. The Draft 2011/12 Statement of Accounts (subject to audit) are being prepared and will be circulated prior to the meeting.

This Committee will be required to formally approve the final Statement of Accounts by the 30th September 2012, following the receipt of the External Auditors 'Report to those charged with Governance' on the accounts.

Key issues affecting the 2011/12 accounts / accounting process are detailed within the report.

RESOURCE IMPLICATIONS

For 2011/12, a revenue budget underspend for the General Fund of £0.9m is reported with an increase in General Fund closing balances of £210k. The Housing Revenue Account reports an underspend of £79k with a reduction in Housing Revenue Account closing balances of £0.6m.

It should be noted that the Medium Term Financial Strategy identified required balances of £4.2m (at 1st April 2012) compared to the draft actual closing balances of £4.7m - additional balances of £509k. For the HRA balances of £4.7m were forecast at 1st April 2012 compared to the actual balances of £4.5m - fewer balances of £221k. Balances above the minimum will be required to provide additional funds for uncertainties regarding future Government funding arrangements.

The outturn for the 2011/12 capital programme identifies an underspend of £1.604m against the approved budget of £6.769m (actual spend £5.165m - no change since Provisional Outturn). However, it has been approved that £1.489m of scheme spend be re-profiled into 2012/13. This will result in an overall underspend of £115k for the 2011/12 capital programme.

LEGAL / RISK IMPLICATIONS

Current legislation, detailed in Accounts and Audit (England) Regulations 2011, requires a Committee of the Council to approve the Statement by 30th September 2012 and for the Council to publish the Statement together with the Auditors opinion by 30th September 2012.

REPORT AUTHOR

Stefan Garner, Director of Finance

LIST OF BACKGROUND PAPERS

Capital Outturn Report 2011/12 - Cabinet, 13h June 2012
Provisional Outturn Report 2011/12 - Cabinet, 13th June 2012

BACKGROUND INFORMATION

Prior to 2010/11 Local Authorities were required to prepare their accounts using accounting policies based on UK Generally Accepted Accounting Practice (UK GAAP) and in accordance with the *Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice* (the SORP) prepared by the Chartered Institute of Public Finance and Accountancy (CIPFA). It was announced in the 2007 Budget (as amended) that International Financial Reporting Standards (IFRS) would be used for the production of accounts from 2010/11 onwards following a transition period.

The SORP was based on UK Generally Accepted Accounting Principles (GAAP) but modified for local government where legislative requirements demand different treatments to UK GAAP. This was to ensure that there were arrangements in place to mitigate the potential effect upon Council Tax of certain transactions and to recognise the unusual nature of local authority funding.

From 2010/11 there is no longer a Local Authority SORP produced by CIPFA. Instead, there is a Code of Practice on Local Authority Accounting prepared by CIPFA under the guidance of the Financial Resources Advisory Board (FRAB), which is the independent body responsible for overseeing the development of financial reporting within the UK public sector.

An updated Code of Practice applicable for 2011/12 was issued by CIPFA in January 2011 and the changes reflected in this review must now be incorporated into the Council's 2011/12 accounts, together with relevant changes to accounting policies.

The Code is based on International Financial Reporting Standards (IFRS), and has been developed by the CIPFA/LASAAC Code Board overseen by the Financial Reporting Advisory Board. It is based on approved accounting standards issued by the International Accounting Standards Board and interpretations of the International Financial Reporting Interpretations Committee, except where these are inconsistent with specific statutory requirements.

The Code also draws on approved accounting standards issued by the International Public Sector Accounting Standards Board and the UK Accounting Standards Board where these provide additional guidance. The latest edition of the Code applies for accounting periods commencing on or after 1 April 2011. It supersedes the 2010/11 Code.

The CIPFA/LASAAC Code Board overseen by the Financial Reporting Advisory Board also issued a mid-year update to the Code to provide accounting guidance on regulations issued and on other legislative developments since the original code was issued.

In England and Wales, the Code is part of the 'proper practices' requirements governing the preparation of an authority's Statement of Accounts referred to in section 21(2) of the Local Government Act 2003. All English authorities to which section 21 applies and that are required to prepare a Statement of Accounts by the Accounts and Audit Regulations under section 27 of the Audit Commission Act 1998, therefore have a statutory duty to comply with the Code's requirements.

The 2011/12 Code introduces some changes in accounting practice which the council needs to comply with. These changes are detailed in below.

CHANGES IN ACCOUNTING POLICY FOR 2011/12

The need for changes in accounting policy can arise from:

(i) changes that are mandatory under the annual IFRS based *Code of Practice on Local Authority Accounting* and require a new or revised accounting policy to be adopted by all local authorities;

(ii) changes within the overall framework of the *Code of Practice* but where the policy to be adopted is discretionary and is dependent upon interpretation of local circumstances.

The changes required to the Council's accounting policies for 2011/12 therefore arise from an updated IFRS based *Code of Practice on Local Authority Accounting* issued by CIPFA in January 2011.

In addition a code update to this was subsequently issued to reflect a number of developments to statutory accounting or disclosure requirements which have taken place since the 2011/12 Code was published.

Many of the changes reflected in the 2011/12 code & code update do have to be incorporated into the Council's accounts but do not necessarily impact on its accounting policies. This is because the changes are principally around additional or changed disclosure notes, points of clarification and additional guidance etc.

Changes to the *Code of Practice* that impact on Council's Accounting Policies in 2011/12 are therefore minimal and relate to Heritage Assets.

Main changes to the Code of Practice on Local Authority Accounting Code (The Code) for 2011/12

Following the significant changes in Local Authority Accounting last year, 2011/12 is a year of consolidation with relatively few new requirements. The new requirements are summarised below:

- Heritage Assets
- Exit Packages
- Community Infrastructure Levy and Business Rates Supplements
- Related Party Disclosures
- Financial Instruments

1. Heritage Assets

The only change to the Council's accounting policies necessitated by the changes to the accounting framework relates to heritage assets.

FRS30 has now been adopted in the Code and there is a new chapter 4.10 in the Code. There is a new class of assets to be disclosed called Heritage assets, to be shown (at valuation - with exceptions) on the balance sheet for the first time.

The impact was already assessed and disclosed as part of the 2010-11 Accounts. A new category will be included in the financial statements & assets have been reviewed against the criteria of heritage assets. This is a change in accounting policy and as such will need to be treated retrospectively and lead to a need to restate the 10/11 Balance Sheet.

Heritage assets are assets which are intended to be preserved in trust for future generations because of their historical, artistic, scientific, technological, geophysical or environmental qualities that are held and maintained principally for their contribution to knowledge and culture. Examples include; historical buildings such as the Castle, archaeological sites, military and scientific equipment of historical importance, civic regalia, medals, museum collections and works of art.

Community assets, (including parks (excluding archaeological sites); cemeteries and crematoria (land only); and allotments where there are restrictions on alternative uses) are not heritage assets, but are accounted for as property, plant and equipment.

The Code also permits, but does not require, authorities to adopt the measurement and disclosure requirements within FRS 30 for community assets.

Heritage assets should be carried at valuation but may be carried at historical cost where it is not practicable to establish a valuation and historical cost information is available.

Where there is no information available on either cost or value, and the cost of obtaining the information outweighs the benefits to the users of the financial statements, there is no requirement to recognise heritage assets on the Balance Sheet. There should, however, be appropriate disclosure of the types of heritage asset held.

Officers have compiled a comprehensive an inventory, based on the historical cost or historic valuations of heritage assets. Whilst the Council was reluctant, at a time of budget pressures, to engage the services of a professional valuer to update the required information, it was considered appropriate to seek updated valuations for the significant assets held (under a value for money approach). Therefore, the Assay office were requested to value the significant items of Civic Regalia and an external valuer engaged to provide replacement cost values for statues within the borough.

Such assets need to be valued, depreciated (where the Heritage Asset has a finite useful economic life) and reviewed on a regular basis for evidence of impairment losses.

A disclosure has been included which shows the value and type of Heritage Assets held by the Authority, together with a balance sheet movement reconciliation.

An accounting policy for the acquisition, preservation, management and disposal of Heritage Assets is required.

A review of our current assets held has taken place to re-categorise assets that meet the definition for a heritage asset. Discussions have also taken place with various service managers to ensure all assets that could be captured under the definition have been identified and are included on the Council's balance sheet.

Identified heritage assets will be held on the Council's balance sheet using uplifted insurance valuations. This has resulted in a significant increase in the non current assets value held on the balance sheet for 2011/12.

As this is a retrospective change in accounting policy, the comparative figures for the 2010/11 Statement of Accounts have been restated.

2. Exit Packages

The 2011/12 Code introduces a requirement to report summary information in relation to exit packages (e.g. redundancy).

A new note has been included on the number of staff exit packages agreed (grouped in rising bands of £20,000 up to £100,000, and bands of £50,000 thereafter), analysed between redundancies and other departures.
The note also discloses the total cost of packages agreed in each band.
Bands have been combined where this is necessary to ensure that individual exit packages cannot be identified (except where disclosure of payments to the individuals is required elsewhere under regulations).

Exit packages include compulsory (where applicable) and voluntary redundancy costs, pension contributions in respect of added years, ex-gratia payments and other departure costs.

3. Community Infrastructure Levy and Business Rates Supplements

The 2011/12 Code provides guidance on accounting for income from the Community Infrastructure Levy (CIL) and Business Rate Supplements.

The Council has not exercised the power to charge supplemental business rate charges (this power was introduced 1 April 2010).

The Council do not currently have a CIL in place (this power was introduced 6 April 2010).

4. Related Party Disclosures

There has been some clarification and change to the definitions of 'related party' and 'close members of the family' of a related party.

Related party transactions are ones which are not arm's length due to one party to a transaction being able to control or exert significant influence over the other.

The 2011/12 Code amends the related party disclosures required in respect of central government departments, government agencies, NHS bodies and other local authorities. Additional guidance on the definition of a related party is also included. New definitions of IAS 24 are included - this is extra guidance and does not represent a change.

The disclosure for government is reduced and the normal disclosure requirements do not apply. For central government departments, government agencies, NHS bodies and other local authorities, the Council has disclosed: The name of the government (i.e. UK Government) and the fact that the government exerts significant influence through legislation and grant funding. The following information in sufficient detail enables users of the entity's financial statements to understand the effect of related party transactions on its financial statements: a) the nature and amount of each individually significant transaction, and b) for other transactions that are collectively, but not individually, significant, a qualitative or quantitative indication of their extent.

5. Financial Instruments

The 2011/12 Code incorporates minor changes to the disclosures of the nature and extent of risks arising from financial instruments. Additional disclosures are also required where the level of soft loans granted by an authority is material.

Soft loans are loans advanced by the Council to third parties at interest rates below the prevailing market rate. The Council does not have any soft loans.

The 2011/12 Code clarifies that financial instrument disclosures are required in respect of leases and PFI, PPP and similar schemes.

Changes include reduced disclosures in respect of financial assets that are neither past due nor impaired, and clarification of the disclosures required in respect of collateral and other credit enhancements obtained.

6. Accounting for Joint Ventures

The Code gives clarification that where an Authority is a party to a joint venture, does not have joint control of that joint venture but does have significant influence, the interest in the joint venture should be accounted for as if it were an associate in line with IAS 31. It also includes additional guidance on the accounts of transfers of functions between public sector bodies. The Council does not have any joint ventures.

7. Code Clarifications

The 2011/12 Code clarifies the requirements in a number of areas where uncertainty was identified in the 2010/11 Code.

SIGNIFICANT TRANSACTIONS IN 2011/12

The following major transactions have occurred during the year that will have significant impact on the Financial Statements:

1. HRA Self Financing

With effect from 1st April 2012 the HRA subsidy system was abolished and replaced with a new system of self financing. Under the new system the council was required to take on additional debt totalling £44.668million. This payment was made to central government on 28th March 2012 and has been shown as an extraordinary payment in the HRA accounts for 2011/12 in accordance with guidance issued in Local Authority Accounting Panel (LAAP) Bulletin 92. The debt will appear in the balance sheet.

2. Municipal Mutual Insurance (MMI)

Contingent Liability: Following a Supreme Court decision handed down on 28th March 2012, if Municipal Mutual Insurance (MMI) are unable to foresee a position in which future investment income net of operating expenses would be adequate to achieve payment of agreed claims in full then appropriate alternative arrangements, which might involve the triggering of the Scheme of Arrangement (SOA), would be made. Under the SOA, the Council could be liable to pay a levy up to the value of claims paid since 1993. The value of claims paid amounts to £250k.

3. **The Impact of the Recession**

Impairment of Investments

The accounting requirements for impairing investments (such as investments placed with Icelandic Banks) have been made in line with CIPFA guidance with the change in impairment included in the surplus or deficit on the Income and Expenditure Account in line with advice and information from the administrators.

Following a capitalisation direction of up to £4m approved by the Government which allowed the Council to capitalise £3.386m in 2009/10 relating to the impact of the impairment of investments on the General Fund, an improvement in the recovery rates for two of the banks (KSF & Heritable) is anticipated which has led to a fall in impairment levels.

With regard to the investment with Glitnir, On 28 October 2011 the Icelandic Supreme Court ruled that UK local authorities' claims in the administrations of Glitnir qualified as priority claims under Icelandic bankruptcy legislation, confirming the earlier decision of the Reykjavik District Court.

The position as to the status of interest on UK local authorities' deposits maturing between 6 October 2008 and 22 April 2009 has also been fully resolved for Glitnir depositors meaning that the value of the Councils' claims is equal to the value of the original deposit plus interest accrued to 22 April 2009 or, if earlier, the maturity date.

After the decision of the Icelandic Supreme Court had been delivered, the Winding Up Board of Glitnir made a distribution proposal to priority creditors. This was accepted by all UK local authorities and implemented on 16 March 2012. Under the terms of the distribution proposal, payment of each claim (measured in ISK terms as at 22 April 2009) was made in a basket of currencies with conversions made using Central Bank of Iceland selling rates as at 22 April 2009. The distribution currencies were Icelandic kroner, Euros, US dollars, pounds sterling, and Norwegian kroner. The weightings for the distribution currencies were determined based on the currencies of the adjusted assets held by Glitnir as at 30 September 2011.

The amounts received by the Council in currencies other than Icelandic kroner were converted into sterling when received – with the Council receiving £2.6m directly into its bank account on 16 March 2012 (from an anticipated £3.2m). The Council has therefore accounted for the final amount of any impairment charge by comparing the carrying value of the impaired deposit with the sum of the amount actually received in sterling and from conversion of Euro, US dollar and Norwegian kroner receipts.

The balance (c. £0.6m) is held in Icelandic kroner amounts that have been distributed by the Glitnir Winding Up Board but held in an escrow account in Iceland because, under the applicable currency controls operating in Iceland, the permission of the Central Bank of Iceland is required to release Icelandic kroner payments held within the Icelandic banking system. The money held in the Glitnir Winding Up Board escrow account is, however, earning interest for the benefit of local authorities at a rate of 3.4%.

4. Changes to the Accounts

Whenever changes to accounting principles are made it is necessary to produce comparable figures for the previous year on the new basis – therefore changes to the 2011/12 accounts have been mirrored in re-stated accounts for 2010/11 to allow for like for like comparisons.

The changes have had a material impact on individual figures within the Balance Sheet and the associated disclosure notes. However, the changes mean that the Movement in Reserves Statement**,** Comprehensive Income and Expenditure Account, Cashflow Statement and level of opening balances remain unaffected.

The Council's accounts for 2011/12 consist of the following:

- **Core Financial Statements:**

  - **Movement in Reserves Statement**: shows the movement in the year on the different reserves held by the Authority, analysed into 'usable reserves' (i.e. those that can be applied to fund expenditure or reduce local taxation) and other reserves. The Surplus or (Deficit) on the Provision of Services line shows the true economic cost of providing the Authority's services. These are different from the statutory amounts required to be charged to the General Fund Balance and the Housing Revenue Account for council tax setting and dwellings rent setting purposes.

  - **Comprehensive Income & Expenditure Account:** shows the accounting cost in the year of providing services in accordance with generally accepted accounting practices, rather than the amount to be funded from taxation. Authorities raise taxation to cover expenditure in accordance with regulations; this may be different from the accounting cost. The taxation position is shown in the Movement in Reserves Statement.

  - **Balance Sheet:** shows the value as at the Balance Sheet date of the assets and liabilities recognised by the Authority. The net assets of the authority (assets less liabilities) are matched by the reserves held by the authority.

  - **Cash Flow Statement:** shows the changes in cash and cash equivalents of the Authority during the reporting period. The statement shows how the Authority generates and uses cash and cash equivalents by classifying cash flows as operating, investing and financing activities.

- **Supplementary Statements:**

  - **Housing Revenue Account:** reflects the statutory requirement to maintain a separate account for Council Housing.

  - **The Collection Fund:** shows the non-domestic rates and council tax income collected on behalf of Staffordshire County Council, the Police Authority, the Fire & Rescue Authority and this Council's General Fund.

These accounting statements are supported by appropriate notes to the accounts including the Statement of Accounting Policies - this provides details of the framework within which the Council's accounts are prepared and published.

GENERAL FUND, HOUSING REVENUE ACCOUNT & CAPITAL OUTTURN

Below are details of the outturn fund balances for the General Fund and the Housing Revenue Account together with a summary of the outturn position on Capital Expenditure for the year.

GENERAL FUND

When compared to the final approved budget (which reflects decisions made by members during the financial year) an under-spend of £0.9m is reported, £195k more than reported in the provisional outturn report.

Closing General Fund balances as at 31st March 2012 were £4.7m:

General Fund Balances Movement 2011/12	Final Outturn £'000	Projected Outturn £'000
Balances B/fwd.	4,511	4,511
Approved Budget transfer To / (From) balances	(699)	(699)
Approved Budget Changes during year	0	0
Outturn variance - Surplus	909	714
Balance C/fwd.	**4,721**	**4,526**

The main changes since the provisional outturn was prepared are due to:

- Net additional income arising from the reduced impairment of Icelandic deposits following an improvement in the forecast financial position and repayment of the funds held with Icelandic Bank Glitnir, £342k; offset by
- A reduction in recharges to the Housing Revenue Account following finalisation of year end costs, £82k;
- The inclusion of costs associated with the pensions liability for West Midlands Councils staff, £42k.

In addition to these, the remainder of the favourable outturn variance of £909k is mainly attributable to savings made in the following areas:

- write back of unspent/redundant reserves, £156k;
- a net reduction in the joint waste management arrangement of £146k (including unexpected income from bulky waste of £27k);
- vacancy allowance & IFRS Contingency budget not required to be released, £75k
- vacant posts within Environmental Health, £92k

It should be noted that the Medium Term Financial Strategy identified balances of £4.2m (at 1st April 2012) compared to the draft actual closing balances of £4.7m - the additional balances of £509k above this minimum will be required to provide additional funds for uncertainties regarding future Government funding arrangements.

Members should be aware that any unplanned call on the above balance could adversely affect the Authority's ability to resource activity within the Medium Term Financial Strategy period.

HOUSING REVENUE ACCOUNT

The Housing Revenue Account (HRA) is underspent against the approved budget for the year by £79k, £232k less than reported in the provisional outturn report. The Housing Revenue Account balances as at 31st March 2012 were £4.5m.

HRA Balances Movement 2011/12	Final Outturn £'000	Projected Outturn £'000
Balances B/fwd.	5,087	5,087
Approved Budget	(679)	(679)
Approved Budget Changes during year	0	0
Outturn variance - Surplus	79	311
Balance C/fwd.	**4,487**	**4,719**

The change since the provisional outturn was prepared is mainly due to:

- An increase in the pension costs associated with the conclusion of the Housing Repairs contract, £300k (total cost of £569k); offset by

- A reduction in recharges to the Housing Revenue Account following finalisation of year end costs, £82k;

In addition to these, the remainder of the outturn variance surplus of £79k shown above is mainly attributable to the following areas:

- Higher payments Under Subsidy System, £158k; offset by :

  - Lower Debt / Capital Charges from the General Fund, £339k;

  - Council House Rents income higher than budget due to a quicker turnaround of void properties reducing overall void levels, £139k;

  - Savings in Repairs & Maintenance costs across multiple contracts, £78k.

It should be noted that the Medium Term Financial Strategy identified balances of £4.7m (at 1st April 2012) compared to the draft actual closing balances of £4.5m, means fewer balances of £221k.

CAPITAL OUTTURN

The outturn for the 2011/12 capital programme identifies an underspend of £1.604m against the approved budget of £6.769m (actual spend £5.165m - no change since Provisional Outturn). However, it has been approved that £1.489m of scheme spend be re-profiled into 2012/13. This will result in an overall underspend of £115k for the 2011/12 capital programme.

Full details are contained within the Capital Outturn Report reported to Cabinet on 13th June 2012.

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