TYNE & WEAR FIRE AND RESCUE AUTHORITY **Item 11**

GOVERNANCE COMMITTEE MEETING: 22nd MARCH 2010

SUBJECT: INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

REPORT OF THE FINANCE OFFICER

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

1.0 Purpose of Report

1.1 To provide information to the Governance Committee on the implications of the need to comply with International Financial Reporting Standards (IFRS), the project outline and the necessary actions to enable the requirements to be met.

2.0 Reason for Decision

2.1 The Committee is recommended to note the report, the project outline set out in Appendix 1, and the necessary actions to enable the requirements to be met.

3.0 Background Information

3.1 As part of the Comprehensive Spending Review (CSR) 2007 the government announced that the 2008/2009 accounts were to be prepared using IFRS, adapted as necessary for the public sector, and its intention to publish the Whole of Government Accounts (WGA) on an IFRS basis for the first time for 2008/2009.

3.2 Following government consultation with its departments and the Financial Reporting Advisory Board (FRAB) on the technical work required in order to implement this change the transition was delayed until 2009/2010.

3.3 The main rationale for implementation of IFRS is as follows:

- To harmonise financial reporting in a world of cross-border trade and investment and increased globalisation, so that they are comparable and follow the same standards.
- To reflect the fact that, to date, over 100 countries have adopted or intend to adopt IFRS, and that the International Accounting Standards Board (IASB) expects that to increase to 150 countries by 2011.

3.4 The key dates for the implementation of IFRS in local government are:

- 1st April 2009 - IFRS transition date.

- July 2009 - consultation begins on the IFRS based accounting code for local government. This was finalised and published in December 2009.
- February / March 2010 - The first IFRS based budgets have been prepared for 2010/2011.
- 1st April 2010 - IFRS based accounting comes into effect for Local Government.
- 30th June, 2011 - the 2010/2011 Statement of Accounts will be IFRS compliant and will be reported to the Governance Committee.

4.0 Implications

4.1 The implementation of IFRS is complex and far reaching, and as such does not just affect the finance function of the Authority but impacts on some other key departments.

4.2 The resource required for successful implementation should not be underestimated, based on the recent experiences of the Health Service, who have had to implement IFRS a year earlier than local government.

4.3 Budget 2010/2011

The budget for 2010/2011 has been prepared so that it is IFRS compliant, as this will be the first year of full compliance by the Authority.

IFRS requirements mainly affect technical accounting treatments and the government has introduced legislation to ensure that the implementation of IFRS will not affect the Net Budget Requirement of the Authority.

4.4 With regard to the Statement of Accounts the scale of financial reporting increases significantly. When IFRS was implemented in the private sector their annual statement of accounts doubled in size and at least the same is expected for public sector bodies. This is due to the increased complexity of the accounts and the significant number of new and more detailed disclosures required under IFRS.

4.5 The first fully compliant IFRS based accounts for the Authority will be produced for the financial year 2010/2011; however IFRS requires that the previous year's accounts must also be IFRS compliant in order to show prior year comparisons. In order to achieve this position the Authority will need to include an opening transitional balance sheet as at 1st April 2009. This means that the 2008/2009 closing Balance Sheet will need to be restated to take into account the changes required under IFRS in order to be able to produce the comparative information required for the 2009/2010 accounting year. The work towards the production of the 2008/2009 restated balance sheet is currently ongoing but is progressing well.

In effect the accounts for 2009/2010 will need to be reported in the existing format as those for 2008/2009 (under the SORP 2009) and then they will also need to be re-stated on an IFRS compliant basis.

4.6 As mentioned above, under IFRS requirements, accounting policy changes, are retrospective. They are reflected in the opening balance sheet as if the authority had always accounted in accordance with IFRS. This affects the accounting treatment, in a number of key areas, and for the Authority the most notable areas affected are the accounting for:

- employee benefits;
- private finance initiatives;
- leases;
- assets.

4.7 The timetable for IFRS has been divided into three stages:

- Stage 1 – Restatement of the 2008/2009 transition balance sheet.
- Stage 2 – Full restatement of the 2009/2010 accounts.
- Stage 3 – Production of IFRS compliant accounts for 2010/2011.

A detailed timetable has been established for Stage 1 linked to the key changes as identified in paragraph 4.6. Stage 1 is progressing well, and a brief description of the effect of each element and its progress to date is given below.

4.8 Stage 1 - Employee Benefits

International Accounting Standard (IAS) 19 deals with employee benefits where they are material. If material, accruals must be created at the end of the financial year for:

- Holiday pay earned but not yet taken.
- Flexi-time balances.
- Time off in lieu.
- Injury and early retirement benefits.

Identifying this information has not been straight forward as currently the payroll system does not hold this type of information and not all employees have the same holiday year. Work in this area has commenced with good progress being made so far..

For information, the calculation is to be based on a random sample of employees; the same sample will be used for calculating the value of untaken holidays, outstanding flexible working and time off in lieu. Injury and early retirement benefits will be dealt with on a case by case basis. The external auditor has agreed to the approach being adopted in addressing the requirements in this area.

4.9 Stage 1 - Private Finance Initiatives

Property used in a Private Finance Initiative (PFI) arrangement will be recognised as an asset of the authority if it passes the International Financial Reporting Interpretations Committee (IFRIC) 12 control tests. These tests include:

- The local authority controls or regulates what services the operator must provide within the property, to whom it must provide them, at what price and where.
- The local authority controls, through ownership, beneficial entitlement or otherwise, a significant residual interest in the property at the end of the term of the arrangement.
- Where the property is used for its entire life, and there is little or no residual interest, the arrangement would still fall within the scope of IFRIC12 where the authority controls or regulates the service provided.

It is anticipated that the Authority's PFI arrangement will pass the control tests of IFRIC12 and therefore will need to be accounted for as assets of the Authority.

The new PFI reporting arrangements will be introduced as part of the SORP 2009, a year earlier than anticipated. Detailed guidance has now been released and this issue is being dealt with outside of the other IFRS areas as the Authority will need to report PFI accounting compliant with IFRS guidelines for the 2009/2010 accounts.

Due to the highly complex nature of PFI accounting, external support has been engaged from PriceWaterhouseCoopers (PWC) at a modest cost in order to comply with this aspect of the IFRS reporting changes.

Work is almost complete on this issue and it is envisaged that a report, which will include the required accounting entries and the accounting model will enable all future accounting entries to be made without further assistance from PWC. This work is expected to be completed before the end of March 2010.

4.10 Stage 1 - Leases

The main change between accounting for leases under IAS17 as compared to SSAP21 is that leases on land and property are accounted for separately as leases on land and leases on buildings. Under the previous regime using SSAP21 there was no such separation. This change may lead to some leases being reclassified as finance leases under the new guidelines. The implications of this, for the Authority, are that all property leases will need to be reviewed and analysed between land and buildings.

This has required property, legal and finance staff to work closely together to ensure compliance with the IFRS reporting and accounting requirements. All property leases have now been identified and evaluated under IFRS criteria to establish the correct accounting treatment, with one building lease becoming a finance lease. There are no revenue implications from this change.

The vehicle and equipment leases held by the Authority
Are currently being reviewed by the Authority's leasing advisers at no cost to ensure all comply with IFRS requirements. This work is also progressing well and a report is expected before the end of March for consideration by officers.

4.11 Stage 1 - Assets

IAS16 requires items of property, plant, and equipment, with a cost that is significant in relation to the total cost of the item to be depreciated separately. This requirement means that assets also need to be split into individual components. CIPFA have announced that there will be no requirement to split existing assets, so only those acquired or re-valued from 1st April 2010 onwards will initially have to follow the new requirements. This change, however, represents a significant one for the Authority particularly in the way it will have to value its assets, and property staff will be most affected by these new requirements.

Also, IFRS gives stricter definitions of surplus assets and investment properties. Assets may only be classed as 'assets held for sale', if they are being actively marketed and the sale is expected within the next 12 months. Assets can only be classified as investment property if it is held solely to earn rentals or for capital appreciation, or both.

The Property Services Valuation Section of the lead authority are working closely with finance staff to assess the correct categorisation of assets under IFRS. Good progress has been made and it is anticipated that the majority of assets currently included as investment property will require transfer into property assets.

4.12 Stage 2 – Full restatement of the 2009/2010 accounts

Procedures have been put in place to capture the required data, mainly around employee benefits to enable the restatement of the 2009/2010 Statement of Accounts. This requirement has been incorporated into the 2009/2010 final accounts detailed timetable.

Embedding IFRS into the final accounts closure process early will ensure the timely and accurate provision of information in the future.

The timescale for restating the 2009/2010 Statement of Accounts is set out in Appendix 1.

4.13 Phase 3 – Production of IFRS compliant accounts for 2010/2011

The final stage of the convergence process will be to produce the 2010/2011 Statement of Accounts in accordance with IFRS. A detailed timetable to achieve this stage of the process will be prepared by December 2010 and will be reported to this Committee.

This stage will include detailed training for both elected and co-opted members and officers on the specific requirements of IFRS.

4.14 General Issues

Having examined other sectors who have implemented IFRS, the key elements for a successful transition are planning, people, systems, timetabling and effective communication.

These wider issues are fully set out in turn below:

a) Planning and Project Outline
Early planning is critical to the success of this project. An initial project outline has been produced and is set out at Appendix 1 for information and sets out the key stages for the successful implementation of IFRS. From this, a more detailed project plan has been developed with critical path analysis and key milestones.

b) Project Team Membership
The project team is led by a senior manager from within Technical Accountancy which forms part of the Financial Management Section of the lead authority.
Senior or appropriate managers have been identified from within the following areas of the lead authority:
- Legal Services (Leasing / Assets)
- Property Services Valuation Section (key role in Leasing / Assets)
- HR (key role in Staff Benefits)
- Financial Resources (SAP system developments)

c) Initial impact Assessment / Timetable
In line with best practice an initial impact assessment was carried out and formed part of the Project Outline which was initially drafted in August 2009. Most of the impact of converging to IFRS has been outlined in this report as the Authority is affected by most of the changes brought about by implementing IFRS.

At this stage, the level of external assistance has been limited to specialist technical assistance around the PFI aspect of IFRS. It is difficult to identify whether further external assistance will be required for Stage 2 and 3 of the process.

The Authority is already aware that some Authorities have already employed additional staff and/or consultants to assist with the management and implementation work identified and there is no shortage of firms ready to offer help in this area.

This Authority's approach is to ensure that we acquire the right expertise at the right time and then build up our knowledge by being actively involved in the process. At this stage it is premature to set out any additional resources required, however, this will be reviewed on a regular basis.

d) Awareness and Training (Communication)
Regular update reports will be provided to this Committee, throughout all three stages of the project. Training will also be provided to members as appropriate but especially to this Committee, whose role it is to receive and approve the accounts.

Relevant staff at various levels will also benefit from some general awareness training on this issue and it is further proposed that more detailed specialist training will be required for those areas more affected by the change in the reporting requirements such as property, finance and HR.

5.0 Conclusions

5.1 PFI accounting changes must be implemented in time for the 2009/2010 accounts and will need an element of external specialist input.

5.2 The Authority must be able to comply with reporting under IFRS in time for its 2010/2011 accounts with comparable accounts produced for 2009/2010.

5.3 A project team is in existence consisting of the appropriate officers from those key services identified in paragraph 4.14(b) above.

5.4 A clear project plan to manage Stage 1 of the IFRS transition has been developed from the Project Outline set out in Appendix 1. This will also be used as a firm basis for a detailed project plan for Stage 2 and 3, which will be developed with input from the project team ensuring that the Authority complies fully with the IFRS requirements.

5.5 Regular progress reports are to be provided to the Senior Management Team.

5.6 The need for external consultants / additional staff resources will be reviewed on an ongoing basis. Before any arrangements are entered into, assessment will be made to ensure the optimum use of the resource that also facilitates knowledge transfer to key staff.

5.7 Awareness and specific training will need to be considered for all relevant staff and members as appropriate.

6.0 Recommendation

6.1 The Committee is recommended to note the report and the project outline set out in Appendix 1.

7.0 Background Papers

Statement of Recommended Practice 2009 (SORP2009)
Draft IFRS Based Code of Practice on Local Authority Accounting in the United Kingdom
Local Authority Accounting Panel (LAAP) Bulletin 81 – Implementation of IFRS