Sunderland City Council

Item No. 10

AUDIT AND GOVERNANCE COMMITTEE 26 March 2010

International Financial Reporting Standards (IFRS) – Progress Report

Report of the Director of Financial Resources

1.0 Purpose of the Report

1.1 To provide Members of the Committee with an update on the Council's progress made towards compliance with International Financial Reporting Standards (IFRS) since the initial report was made to this Committee on 29th September 2009.

1.2 To set out the updated project outline (Appendix 1).

1.3 To identify the necessary actions and plans established to enable the requirements to be met.

2.0 Reason for the Decision

2.1 The Committee is recommended to note the report and the progress made to date.

3.0 Progress made to date

3.1 Budget 2010/2011

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

There are no budgetary implications as a result of technical accounting changes brought about by the convergence to IFRS for 2010/2011. All accounting changes that could impact upon the Council's budget and level of Council Tax are to be mitigated by government legislation. Preliminary work also confirms that the technical adjustments necessary to comply with IFRS will have a neutral impact upon the revenue budget for 2010/2011 in respect of the key areas of the Private Finance Initiative (PFI) schemes of which the Council has 2 such arrangements, leasing arrangements and the accrual in respect of employee benefits.

Members may recall that a budget of £25,000 was identified and agreed in order to help manage the full IFRS convergence process over the 3 year period and that this allocation would be used primarily to engage any specialist help that would be required. To date external assistance has been procured at a very modest cost and this budget will only be used where necessary to ensure the learning acquired is passed over to officers so that these elements can be managed internally going forward.

3.2 **Timetable for Compliance**

The workload and timetable for IFRS has been divided into three manageable phases reflecting the three financial years IFRS will impacts upon before becoming effective:

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

A detailed plan of actions and key tasks was drawn up to complete the work required in Phase 1, which it is estimated will be completed by the 31st March 2010.

The same process will be adopted for each Phase of the project in order to successfully complete the full convergence to IFRS.

3.3 **Phase 1 – Restatement of the 2008/2009 transition balance sheet**.

The key areas that require restatement have been identified and a detailed timetable has been established to ensure that Phase 1 is completed by 31st March 2010.

The key elements include:

- Private Finance Initiative (PFI).
- Council Tax
- National Non Domestic Rates
- Employee Benefits
- Equipment Leases
- Property Leases
- Assets
- Government Grants

3.3.1 Private Finance Initiative (PFI)

PriceWaterhouseCoopers (PWC) has been engaged to deliver the required accounting changes in respect of PFI because of the highly complex technical and specialist issues involved. All of the required information has been provided to them and it is envisaged that a report, which sets out the required accounting entries and the accounting model, that will enable all future accounting entries to be made will be provided so that this issue can be maintained in-house without further assistance from PWC. Completion is expected to be around by mid March 2010.

3.3.2 Council Tax

Currently the Council accounts for all of the Council Tax it receives regardless of whether it is retained by the Council or paid to a precepting authority. IFRS requires only the Council's share of the Council Tax income to be accounted for by the Council.

The restatement of the 2008/2009 balance sheet in respect of Council Tax has been completed. The calculation was based on guidance issued by CIPFA in mid January 2010.

3.3.3 National Non Domestic Rates (NNDR)

Similar to Council Tax, the Council currently accounts for all of the NNDR collected on behalf of central government. IFRS requires that the Council exclude from its accounts arrangements whereby it acts as an agent on behalf of another body.

The restatement of the 2008/2009 balance sheet in respect of NNDR has been completed. The calculation was based on guidance issued by CIPFA in mid January 2010.

3.3.4 Employee Benefits

Good progress has been made on this aspect.

There are two distinct groups of employees that the Council must consider using different valuation methodologies, i.e. teaching staff and non-teaching staff. Each group has different terms and conditions that impact on methodologies required for making an assessment of the value of untaken holiday entitlement and other employee benefits.

A formulaic approach based on guidance issued by CIPFA has been used for teaching staff.

For non-teaching staff a calculation has been made based on a sample of employees. The same sample has been used to calculate the value of untaken holidays, outstanding flexible working time and any outstanding time off in lieu.

3.3.5 Equipment Leases

The vehicle and equipment leases held by the Council are currently being reviewed by the Council's leasing advisers to ensure that they all comply with IFRS requirements. Although the criteria have not changed significantly, there have been some subtle changes. In particular, the removal and replacement of what was referred to as the 90% test with more qualitative tests around who has the risks and rewards of ownership. This work is also progressing well and a report is expected before the end of March 2010 for consideration by officers.

The agreement has been made within the terms of the current leasing contract therefore; there will be no additional costs to the Council in respect of this.

3.3.6 Property 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 Council 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 of the Council's property leases both where the Council acts as lessor and as lessee have been assessed under IFRS criteria. Currently, a small number of leases have been identified that may become finance leases under IFRS and these are currently being scrutinised further before making a final determination which may require some small technical accounting adjustments to the restated accounts.

3.3.7 Investment Property

Under IFRS the classification of assets will change. Assets previously referred to as Fixed Assets will be known as Property, Plant and Equipment. The main changes are in respect of a stricter definition 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 they are held solely to earn rentals or for capital appreciation, or both.

The Property Services Valuation Section are working closely with Financial Management Services to asses 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. This work is almost complete.

3.3.8 Government Grants

Under IFRS capital grants and contributions with no outstanding conditions on use will be recognised initially in the Comprehensive Income and Expenditure Statement (currently known as the Income and Expenditure Account). Any balances on the Government Grants Deferred Account must be transferred to the Capital Adjustment Account. It is anticipated that work in this area will be completed by the end of March 2010.

3.3.9 Summary

It is clear from the above that all issues affecting the restatement of the balance sheet are being dealt with and good progress is being made. The objective is to restate the balance sheet by 31st March 2010 and at this stage we are on target to achieve this completion date.

3.4 **Phase 2 – Full restatement of the 2009/2010 accounts.**

Procedures have been put in place to capture the required data to be able to draft IFRS compliant accounts for 2009/2010, which are to be prepared once the 2009/2010 accounts (which will be SORP 2009 compliant) have been audited in September 2010. The requirements have been incorporated into the 2009/2010 final accounts memo and detailed timetable to ensure the required information is made available as part of the 2009/2010 closedown process.

Embedding IFRS into the final accounts closure process at an early stage 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.

3.5 **Phase 3 – Production of IFRS compliant accounts for 2010/2011.**

The final stage of the convergence process will see production of the 2010/2011 statement of accounts under IFRS. A detailed timetable to achieve this stage of the process will be prepared in December 2010.

During this stage it is intended to provide detailed training for both members and officers on the specific requirements of IFRS to enable appropriate scrutiny of the revised statement of accounts presented to this Committee at its meeting on 30th June 2011.

4.0 General Issues

4.1 A project team has been established led by Financial Management Services. Directorates have responded well to requests for information and co-operation across all Directorates has been excellent.

4.2 The external auditor (Audit Commission) has been consulted throughout the process and to date their comments have been positive and helpful.

5.0 Conclusions

5.1 Progress to date has been good and within the detailed timetable set for Stage 1 of the process. No deviations from the timetable are expected at this time.

5.2 Regular progress reports are to be provided to Members and the Executive Management Team (EMT)

5.3 Awareness and specific training will be given to all relevant staff and members as part of the final stage of the project.

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

Audit and Governance Committee – IFRS report 29th September 2009
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