

AUDIT COMMITTEE	AGENDA ITEM No. 5
9 FEBRUARY 2009	PUBLIC REPORT

Cabinet Member(s) responsible:	John Peach, Leader of the Council	
Contact Officer(s):	John Harrison, Director of Strategic Resources John Blair, Head of Strategic Finance	Tel. 01733 45 2398 Tel. 01733 38 4564

INTERNATIONAL FINANCIAL REPORTING STANDARDS

RECOMMENDATIONS	
FROM : Director of Strategic Resources	Deadline date : N/A
<ol style="list-style-type: none"> 1. To note the accounting changes required. 2. To note the timescale for implementation. 3. To support the transition to IFRS based accounts. 4. To note the potential impact on cash reserves and balances that will need to be managed through the MTFS. 5. To request regular update reports on implementation progress. 	

1. ORIGIN OF REPORT

- 1.1 The Chancellor's 2008 Budget announced that the annual financial statement of the Government Departments and other entities within the Public Sector will be prepared using International Financial Reporting Standards (IFRS).
- 1.2 For Local Government the accounts relating to 2010/11 need to be IFRS compliant, however as a result of 'IFRS 1 First time adoption of international reporting standards' the transition towards adopting IFRS in practice means the accounts as at the 1st April 2009 will need to be prepared in order to produce opening balances.
- 1.3 The move to IFRS is extremely complex and will have wide reaching implications not limited to the Council's finance function alone but throughout the Council's business activities.
- 1.4 This report is submitted by the Council's Section 151 Officer, the Director of Strategic Resources, being part of his statutory responsibilities.

2. PURPOSE AND REASON FOR REPORT

- 2.1 The purpose of this report is to brief the Committee on the IFRS transition, significant changes this is likely to bring to the Council's accounts, and the resource demand of this transitional task.
- 2.2 This report is for the Committee to consider under its Terms of Reference 2.8.1.5 (which forms part of the delegations for regulatory committee functions under Part 3, Section 2)

[Governance Support/Cabinet Officer to complete this section following liaison with Author] [Do NOT include any other text under this heading].

3. TIMESCALE

Is this a Major Policy Item / Statutory Plan?	NO	If Yes, date for relevant Cabinet Meeting	
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4. INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

BACKGROUND

- 4.1 International financial reporting standards (IFRS) are accounting standards issued by the International Accounting Standards Board (IASB). The term IFRS refers to the equivalent to UK GAAP, the set of 'Generally Accepted Accounting Principles' which the Council's accounts currently comply with.
- 4.2 As both business and financial markets become more global, the demand for a single international set of accounting standards has increased. One single set of standards aids the preparation, comparability and analysis of financial information for corporate entities.
- 4.3 The Chancellor's 2008 Budget announced the adoption of IFRS in the Public Sector, with the context being the need of government for "high value performance data in combination with appropriate financial data".

IMPLEMENTATION

- 4.4 Experience in the Private Sector has shown that the move to IFRS is both lengthy and complex and will involve not only the accountants, but internal auditors, human resources, ICT, surveyors, procurement and a range of other stakeholders.
- 4.5 IFRS adoption requires a rigorous methodology to ensure its strategic success. PwC note that the key milestones include:
- Implementing a suitable project structure with the different levels of the project and everyone's roles clearly defined;
 - Winning the involvement of all parties and convincing them of the strategic importance of the project for the organisation as a whole;
 - Tackling accounting policies to ensure that they comply with IFRS;
 - Planning the best possible use of human resources and finding new resources where necessary;
 - Defining and implementing a training plan for each category of participants affected by the project;
 - Adjusting information systems to meet the organisation's new needs and guarantee the best cost / benefit ratio of the change by providing broader, more consistent and reliable information;
 - Simulating IFRS financial statements before going live, to work out the best ways of communicating potential changes in performance trends;
 - Preparing the first financial statements in full compliance with IFRS, making sure that stakeholders understand the differences and there are no last minute surprises.

The impact of IFRS will also need to be considered when making strategic decisions during the transition period.

TECHNICAL CHANGES

- 4.6 There are a number of unique features of local authority accounting, not least the differences between Council Tax setting rules and accounting practice. These features may require CIPFA (Chartered Institute of Public Finance and Accountancy) to provide certain interpretations of IFRS in an IFRS-based code, but the track record of IFRS application in the government and NHS sectors shows that special interpretations for the public sector are rare.
- 4.7 Areas where IFRS is expected to present significant differences for local authorities:
- Fixed assets, where IFRS requires fixed assets to be held at 'fair value' as opposed to the current requirement for 'current value'

- Leases, where IFRS has a requirement for the leases of land and buildings to be accounted for and disclosed separately
- Defined benefit pension schemes, where there may be a potential change in accounting policy for actuarial gains and losses
- Joint ventures and associates – under IFRS a local authority only needs the power to influence another entity (rather than actually exercise it) for it to be treated as part of the group.

4.8 The following table illustrates some further differences

Significant	Some	Minor
Increased disclosures *	Tangible fixed assets	Inventories
First time adoption	Investment property	Provisions
PFI – Private Finance Initiative	Intangible assets	Government grants
Leases	Presentation of financial statements	Revenue
Operating Segments	Cash flow statement	Post balance sheet events
Infrastructure assets	Accounting policies	Tax
	Employee benefits	Foreign exchange rates
	Related party transactions	Financial instruments.
	Business combinations	
	Group Accounts	

* financial statements in the listed sector increased in size by 60%

ISSUES

- 4.9 As highlighted above the transition to IFRS based accounts is a highly complex area, involving the expertise outside, as well as within, the Council's finance function.
- 4.10 The timings for the adoption of IFRS places competing demands on projects like Manor Drive Plc, the restructure of Operations Directorate, and the overall redundancy process, all currently being undertaken at the Council.
- 4.11 Experience in the other sectors have highlighted difficulties in
- sourcing original contract details for leases and larger schemes like PFI
 - lack of knowledge and expertise through dependence on consultants
 - lack of project team to progress the task
 - lack of capacity for the task, noting this is not something for current staff to do on top of their 'day job'
 - consideration given to moving budgeting and planning to IFRS basis to avoid dual accounting systems
 - consideration to the potential impacts on cash, reserves, and balances through the retrospective application (IFRS1) where 'catch-up' accounting entries may be required.

ACTIONS

- 4.12 The implementation will be managed as a project by the Corporate Accounting Manager and will also report regularly to Audit Committee.
- 4.13 Although the council's 2010/11 accounts will be the first to be prepared on an IFRS basis, there will be a number of key tasks to be undertaken prior to that time. These include.
- restating the 2009/10 accounts on an IFRS basis;

- the opening balances at 1 April 2009 will need to be on an IFRS basis
- Whole of Government Accounts (WGA) will be on an IFRS basis from 2009/10; and
- The impact on budgets, the council tax, our systems and staff training are all areas which need to be considered.

4.14 It is recognised that in the private sector, introduction of IFRS was most successful where key stakeholders other than finance were also involved at an early stage. PwC are leading a workshop in February to investigate the impact of IFRS which will involve all the key stakeholders. Following the workshop PwC will produce an impact report detailing the implications.

4.15 In the private sector, 70% of the effort of the IFRS transition was seen to be in restating the balance sheet to be on an IFRS basis.

4.16 Shown at Annex 1 are some of the key actions that will need to be considered. In some instances it may not be possible to make substantial progress until further guidance is provided.

4.17 It is important that we engage with our external auditors throughout the transition period in order to establish any audit trail or working paper expectations, materiality considerations, preliminary views on accounting treatment, audit timetable and arrangements for ongoing communication.

5. CONSULTATION

No consultations are being considered for this item as this is a statutory change.

6. ANTICIPATED OUTCOMES

As set out in the report.

7. REASONS FOR RECOMMENDATIONS

The recommendations are made to advise the Committee of the transition to IFRS, to highlight the demands and pressures placed on the Council's resources, and ensure involvement of the Committee in this process.

8. ALTERNATIVE OPTIONS CONSIDERED

The Statement of Accounts will be required to be prepared in accordance with the IFRS by 2010/11, and this report sets out the main themes required in to ensure the satisfactory production of the Statement of Accounts. The options are therefore limited in order for the accounts to be prepared to the regulatory deadline and specification.

9. IMPLICATIONS

9.1 The implications arising from this report are to consider, in advance, the processes required in the transition to IFRS based accounts.

9.2 To provide the Committee the opportunity to consider the role and requirements of the Council to meet the transition to IFRS based accounts.

10. BACKGROUND DOCUMENTS

Used to prepare this report, in accordance with the Local Government (Access to Information) Act 1985)

PwC, IFRS and local authorities, More than just numbers

PwC, International Financial Reporting Standards, What is IFRS? Your questions answered

PwC, Inside IFRS, Helping you make the transition (various issues)

ACTIONS TO BE CONSIDERED

Managing the IFRS conversion project
<ul style="list-style-type: none"> • Create a Project Board to oversee the implementation • Develop a working group of staff, utilising all affected services
<ul style="list-style-type: none"> • Inform Audit Committee of potential implications of IFRS and regularly report to committee on progress made • Increase awareness at Corporate Management Team level
<ul style="list-style-type: none"> • Review staffing resources and the current level of skills and any conflicting commitments • Review any training needed to help facilitate the introduction of IFRS
Internal and External Reporting
<ul style="list-style-type: none"> • Review any strategic financial implications such as impact on estimates • Any impact on measured performance against council ambitions.
<ul style="list-style-type: none"> • Gain an understanding on what the likely impact will be on the presentation of the income and expenditure statement and balance sheet. • Address any changes required due to new disclosure requirements
<ul style="list-style-type: none"> • Develop any changes needed to internal communications and management information.
<ul style="list-style-type: none"> • Establish ways in which to enhance the information published in such documents as the annual report
Data, systems, processes and controls
<ul style="list-style-type: none"> • Establish how the required information is to be gathered in order to enable the transition • Establish controls over data quality and data capture
<ul style="list-style-type: none"> • Identify any system enhancements needed to meet any additional requirements under IFRS
<ul style="list-style-type: none"> • Identify any other changes occurring across the authority which may need to be integrated with IFRS • Process changes and controls – documentation compliant with corporate governance requirements

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