Report to the Audit and Governance Committee

Report R~~r~~eference: AGC-006-2010/11 ~~C/ /2008~~

Date of meeting: 21 June 2010

Portfolio: Finance and Economic Development.

~~S~~Subject: Statutory Statement of Accounts 2009/10.

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Recommendations/Decisions Required:

That a report be submitted to the Council recommending that the Statutory Statement of Accounts for 2009/10 be adopted.

Executive Summary:

One of the key roles allocated to this Committee is to scrutinise the annual Statutory Statement of Accounts. All Members of the Council will have the opportunity to debate the Accounts at Full Council on 29 June and part of that debate will be to consider the recommendation of this Committee.

To assist Members with their consideration of the Accounts a full report follows together with the Accounts themselves.

Reasons for Proposed Decision:

The consideration of the draft Statutory Statement of Accounts falls within the Terms of Reference of this Committee. Officers have exercised their professional judgement and liaised closely with external experts and the External Auditor to produce the draft Statutory Statement. If Members are satisfied with the content of this report and the verbal responses to any questions raised, they are requested to recommend the draft Statutory Statement of Accounts for adoption by Full Council on 29 June.

Other Options for Action:

The Committee could decide that the accounts should be amended or expanded prior to them being presented to Full Council. Alternatively, the Committee could decide not to discharge this part of its terms of Reference and leave Full Council to scrutinise the Accounts.

Report:

1. The Accounts and Audit Regulations require Full Council or an Executive Committee to adopt the Council's Statement of Accounts before the end of June. The Council's constitution reserves the adoption of the Accounts to Full Council only. However, prior to

Council considering the accounts it is important that they have been subject to robust Member scrutiny. This Committee has scrutinised the Statement of Accounts for the previous three years.

2. The consideration of the Statement of Accounts is contained in the Terms of Reference of this Committee, the relevant parts being:

"

(h) To review financial statements, including the Council's Statement of Accounts, External Auditor's opinion and reports to members, and monitor management action in response to the issues raised by External Audit.

(i) Review, and challenge where necessary, the actions and judgements of Management, in relation to the Council's Statement of Accounts, paying particular attention to:

(i) critical accounting policies and practices, and any changes to them;

(ii) decisions requiring a major element of judgement;

(iii) the extent to which the financial statements are affected by any unusual transactions in the year and how they are disclosed;

(iv) significant adjustments resulting from the audit; and

(v) any material weakness in internal control reported by the Internal or External Auditor."

Changes to the Contents of the Statutory Statement for 2009/10

3. This section starts with an explanation of the mechanism for setting the rules that Local Authorities have to follow in producing their accounts. This is necessary as over a period of time there have been significant changes to the appearance and content of the accounts. Whilst there have been relatively few changes this year, it is worth repeating some of the information for the benefit of the new Members of the Committee and anyone who is coming afresh to these accounts.

4. The Chartered Institute of Public Finance and Accountancy (CIPFA) publishes a Statement of Recommended Practice (SORP) every year that Local Authorities are required to follow in producing their financial statements. Before the SORP is published the Accounting Standards Board (ASB) approves the document. In recent years the ASB has insisted that the SORP moves closer to Generally Agreed Accounting Practices (GAAP), so that public sector financial statements more closely resemble those prepared in the private sector.

5. In previous years the focus of the Statement of Accounts has been the Consolidated Revenue Account, which had the dual role of setting out the authority's financial performance and determining the net expenditure to be charged against Council Tax in the year. The new statements now required by the SORP disaggregate the Consolidated Revenue Account (and the old Statement of Total Movements on Reserves) to produce a set of statements which each have a single clear objective:

- Income and Expenditure Account – a summary of the resources generated and consumed by the authority in the year.

- Statement of the Movement on the General Fund Balance – a reconciliation showing how the balance of resources generated/consumed in the year links in with the statutory requirements for raising Council Tax.

- Statement of Total Recognised Gains and Losses – demonstration of how the movement in net worth in the Balance Sheet is identified to the Income and Expenditure Account surplus/deficit and to other unrealised gains and losses.

6. The above are described as core financial statements as all local authorities are required to produce them. There are two other core statements, the Balance Sheet and the Cashflow Statement. The Balance Sheet lists what the Council owns, what is owed to the Council and what the Council owes to others. The Cashflow Statement summarises the movements in assets, liabilities and capital that have taken place during the year and their effect on the Council's holdings of cash. Neither the Balance Sheet nor the Cashflow Statement required direct amendment to comply with the SORP.

Critical accounting policies and practices, and any changes to them

7. This has been a relatively quiet year with some small changes being introduced ahead of the full implementation next year of International Financial Reporting Standards (IFRS). There are few revised requirements in the SORP and no changes have been instituted by management. This helps make comparisons with last years accounts easier and a lengthy period of consistency would be welcomed. However, this will be prevented by the changes to comply with ~~International Financial Reporting Standards (~~IFRS~~)~~ and work is ongoing to manage this major project.

8. The most significant changes have been to the way Council Tax and Non-Domestic Rates are accounted for. Previously, for Council Tax, the Income and Expenditure Account has just included the value of this Council's precept (the amount of money that the Council has budgeted to receive). Any amount of income above or below the precept level has previously been accounted for as part of the Collection Fund and has been allowed for in setting the next year's precept. From this year the income taken to the Income and Expenditure Account is this Council's share of Council Tax receipts, so any surplus or deficit on the Collection Fund is now included. The Balance Sheet treatment of outstanding Council Tax accounts as debtors has also changed. Previously all amounts that had been billed but not paid were shown as debtors of this Council. Now it is only this Council's share of the overall bill (approximately 10%) that is shown as Council Tax arrears. The remainder is shown as an amount due from other local authorities; on the basis that these authorities have been paid more in their precepts than this Council has collected from Council Tax payers. These changes are intended to better reflect the Council's position as acting as the collection agent for the other authorities.

9. Similarly to the way the Council acts as a collection agent for other authorities with Council Tax, it acts as a collection agent for central government with Non-Domestic Rates (NDR). Payments are made into a central government pool based on the assumed amounts to be collected from rate payers throughout the year. Historically all billed but unpaid NDR amounts have been included in the Balance Sheet as NDR Arrears. Now any outstanding amounts are included within amounts due to or from central government as they are part of any amount either owing to or from the NDR pool.

10. Another change worth mentioning is the inclusion for the first time on the Balance Sheet of an Accumulated Absences Account. This is to reflect flexitime and annual leave that has been earned in the year but remains untaken at the year end. As well as including a figure for this year it has been necessary to calculate the comparative figure for the

previous year.

11. An item that may attract more interest is the enhanced salaries disclosure. In addition to the previous disclosure by salary band information on the Council's top earners salaries, benefits and pensions is now required.

Decisions requiring a major element of judgement

12. In preparing a set of accounts at a point in time it is inevitable that some of the information required will not yet be available. The compression of the timetable for the preparation and approval of the accounts, from 30 September to 30 June, has exacerbated this problem. Where an issue is unclear it is far more likely to have been resolved six months after the year end than three. If an actual amount is uncertain an estimate is used. The estimate will be based on the assessment of information available at the time the accounts are closed. When the actual figures are determined any difference is usually accounted for in the following year. If the estimate was wrong by a material amount it would be necessary to consider re-stating the figures, this is extremely rare.

13. Last year the most significant loss shown in the accounts was one of £32 million for the impairment of some of the Council's properties. In order to keep asset values current, assets are revalued on a five-year rolling programme. The exception to this is Housing Revenue Account (HRA) properties that are revalued annually using the Beacon Method, a method that uses examples of a particular type of property and extrapolates for the whole population. Last year's revaluation saw a total reduction in gross book value of £139 million, of which £131 million related to HRA dwellings and garages.

14. The fall in values last year has been partially reversed by a near 10% increase this year, which has added £40 million to the value of council dwellings and garages. As in previous years, the valuations were conducted for the Council by the District Valuer using guidance issued by the Royal Institute of Chartered Surveyors. This exercise clearly requires a major element of judgement and the Council's Estates and Valuation Service check the valuations provided by the District Valuer to ensure that a proper and rigorous process has been followed and that the valuations are reasonable. The increase in value is significant but needs to be seen in the context of the overall value of fixed assets on the balance sheet of £655 million.

15. In these reports in previous years I have commented on the movement in the pension liability in the next section, as it could be seen as an unusual transaction. However, the significant increase in the liability this year has made clear the element of judgement exercised by the actuary in establishing the pension figures. The largest creditor on the Balance Sheet is the Council's liability to the pension fund. The Balance Sheet shows that the pension liability for the Council has increased in the year from £41.5 million to £56.5 million. The value of the scheme assets has increased substantially during the year but changes in the actuarial assumptions used have increased the projected liabilities by even more. The future value of the schemes liabilities is discounted back to a present day value using an interest rate based on bond yields and the reduced bond yield has increased the value of the liabilities. It is hoped that as normality returns to financial markets a higher bond yield in future will lead to a reduction in the liabilities.

16. The following table is included to illustrate how the overall deficit has fluctuated over time, in part due to changes in asset values but also due to the judgements made by the scheme actuary (Mercer).

	2009/10 £'m	2008/09 £'m	2007/08 £'m	2006/07 £'m	2005/06 £'m
Liabilities	(139.2)	(102.3)	(120.3)	(111.2)	(111.7)
Assets	82.7	60.8	76.9	82.4	76.7
Deficit	(56.5)	(41.5)	(43.4)	(28.8)	(35.0)

17. The inclusion of this amount in the Balance Sheet shows the extent of the authority's liability if the pension fund was to close on 31 March ~~2009~~2010. It does not mean that this full liability will have to be paid over to the pension fund in the near future.

18. ~~18.~~ There are no other areas in the Statement of Accounts to bring to Members attention as having required a major element of judgement. Where it has been necessary to exercise judgement in the interpretation of the SORP advice has been sought from CIPFA and staff have liaised closely with both the External Audit Manager and other Essex authorities.

The extent to which the financial statements are affected by any unusual transactions in the year and how they are disclosed

19. The most unusual transaction during the year was a substantial VAT refund which has been disclosed as an Exceptional Item. This relates to ~~over declared~~ VAT which has subsequently been ruled 'over-declared' and interest on output tax charged on supplies of sporting services between 1 January 1990 and 31 March 1994. A number of authorities across the country have made similar claims and Members may have seen them described in the press as "Fleming Claims". The claim produced a net benefit of £1.2 million.

20. Another unusual item is the Council's investments that are currently held as part of the administration of the Heritable Bank. This was reported last year as the passing of an amendment to the capital financing regulations to encourage the deferment of the impact of investment impairments to 2010/11 was unusual.

21. The creditor progress report issued by the Heritable administrators (Ernst & Young) on 28 January 2010 increased the projected return to creditors from 80p in the £ to 85p in the £. This is consistent with the improved return seen during the year, as 35p was returned which was more than double the anticipated 15p. Therefore, the accounts include an impairment based on recovering 85p in the £. In normal circumstances the impairment would be charged to the Income and Expenditure Account and impact on the General Fund Balance. However, in view of the overall uncertainty about the timing and ultimate levels of recovery from the various administrations, the previous government encouraged authorities to postpone until 2010-11 the impact on budget calculations of the impairments. The full impact of the impairment was allowed for in setting the Council's budgets for 2010/11.

22. The improvement in the anticipated outcome and the better return in year have combined to reduce the carrying value of the impairment on the Balance Sheet from £711,000 to £466,000. In calculating the impairment the Council has followed the Local Authority Accounting Panel Bulletin 82, update number 2, issued in May 2010. This anticipates the administration will conclude in 2012 and further dividends will be 20p during 2010/11, 20p during 2011/12 and a final 10p during 2012/13. How this is dealt with in subsequent periods will depend on the ultimate level of recoveries from the administration.

23. A transaction that requires the approval of the Secretary of State must be seen as unusual, even though it is in line with Council policy. Prior to the last triennial valuation of the Pension Fund the Council had anticipated an increase in the deficit on the fund and a corresponding increase in contributions being required from employers to fund it. In order to fund these additional contributions £2.5 million was moved from the Usable Capital Receipts Reserve to a Pension Deficit Reserve with the intention of applying to the Secretary of State for capitalisation directions. Pension contributions would normally be treated as revenue expenditure but where a particular item would have a severe impact on the revenue account local authorities are able to seek authority from the Secretary of State to treat the expenditure as capital and meet it from capital resources rather than revenue.

24. Since 2005/06 the Council has applied each year to the Secretary of State for capitalisation

directions. Full directions have been obtained for all years other than 2006/07 when directions were issued for only 57% of the amounts requested. The amounts capitalised in the 2009/10 accounts are £644,000 (£662,000 in 2008/09) General Fund and £302,000 (£310,000 in 2008/09) Housing Revenue Account (HRA).

Significant adjustments resulting from the audit

25. It is always hoped that there will be no significant adjustments arising from the audit. However, given the issues outlined above the possibility of a significant adjustment cannot be ruled out. Any adjustments that are made to the draft Statement of Accounts will be reported back to this Committee.

26. The difficulties in producing such a complex Statement of Accounts in a short period of time have already been mentioned above. The accounts that follow are complete, other than the Cashflow Statement and associated notes, but are subject to an ongoing checking process and Members will be advised of any amendments at the meeting. Once complete, the Cashflow Statement will be issued as a supplementary paper.

Any material weakness in internal control reported by the Internal or External Auditor

27. To date no material weaknesses have been reported, if any such weaknesses are discovered they will also be reported to this Committee.

Resource Implications:

The Accounts set out the resource implications of the Authorities activities for 2009/10. The recommendation of the Accounts to Full Council does not in itself have any resource implications.

Legal and Governance Implications:

Full Council must approve the Accounts before the end of June and as part of the overall governance framework the Accounts should be subject to robust Member scrutiny prior to their approval.

Safer, Cleaner and Greener Implications:

There are no environmental implications.

Consultation Undertaken:

None.

Background Papers:

None.

Impact Assessments:

There are no equalities or risk management impacts.