CARDIFF COUNCIL
CYNGOR DINAS CAERDYDD

AUDIT COMMITTEE: 27 MARCH 2017

STATEMENT OF ACCOUNTS 2017/18 – ACCOUNTING POLICIES AND FUTURE REGULATORY CHANGES

REPORT OF CORPORATE DIRECTOR RESOURCES

AGENDA ITEM: 5.2

Reason for this Report

The Audit Committee terms of reference set out the responsibility for reviewing the financial statements prepared by the authority.

This report has been prepared to provide Audit Committee Members with:-

A. The draft accounting policies on which the Statement of Accounts for 2017/18 will be based, along with the key areas in the accounts where estimates and assumptions are used in preparation of the accounts.
B. The key changes expected to be implemented for the 2017/18 accounts arising from the 2017/18 CIPFA Code of Practice (the Code) and our own internal review:-
C. Potential changes in the Code in 2018/19 and beyond that are likely to have the most impact on the accounts.
D. An update of regulatory changes following amendments by Welsh Government to regulations that govern the production of the Accounts.

Background

Councils are required to prepare the Accounts using a Code of Practice developed by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Code is based on International Financial Reporting Standards (IFRSs) and sets out the minimum requirements for financial statements.

The Council's Statement of Accounts for 2016/17 was considered by Audit Committee in June and September 2017. It is a technical document, which relies on information received from many Directorates; relies on technical expertise and capacity in order to meet tight timescales for preparation and makes previously recommended improvements. Preparation and audit of the accounts needs to consider the significant assumptions required and materiality of their impact to users of the accounts.

During 2015, CIPFA undertook a consultation ('Telling the Story'), which aimed to review non-essential or historic items included within Local Authority Statement of Accounts and to better explain the financial statements. Attached at Appendix 1 is a guide produced by CIPFA on Understanding Local Authority Financial Statements, which may be useful information to members of the Committee to support their role.

The key timescales in relation to the 2017/18 accounts are shown in the table below:-

Date (Last Working Day)	Item
From 15 June 2018 onwards	Submission of accounts for External Audit
26 June 2018	Draft Statement of Accounts presented to Audit Committee
29 June 2018	Draft Statement of Accounts signed off by Corporate Director Resources
2 July 2018	Accounts open for public inspection for 20 working days
27 July 2018	Public inspection ends
23 August 2018	Receipt of all external audit queries
18 September 2018	Draft Audited accounts presented to Audit Committee
27 September 2018 (TBC)	Final Audited accounts and accompanying disclosures presented to Full Council for approval and sign off
28 September 2018	Publication of Statement of Accounts

The Council continues to work closely with Wales Audit Office (WAO) on a process of continual improvement, including considering materiality of transactions, simplifying wording, removing or adding narrative where this better explains the Council's performance or figures included in the accounts.

A - Draft Accounting Policies 2017/18 and Significant Assumptions used in the Accounts

The Council's draft 2017/18 accounting policies are included, at Appendix 2. CIPFA has encouraged Councils to simplify wording and the content of accounting policies, some of which may have been in place for a number of years. We continue to do so in the draft however there are no changes made that would impact on the reporting of financial performance historically or in the future. The policies remain unchanged. A summary of the main amendments to the policies are shown below:

Accounting Policies Section	Change
General Principles	Included new section on the accounting convention adopted in the accounts and confirmed the accounts are prepared on a going concern basis i.e the Council will continue to operate in the foreseeable future
Assets	Separated disclosure of policies for Heritage assets from Property Plant & Equipment assets
Investment Property	Additional disclosure including types of assets included in the investment property classification. This follows the recommendation by WAO as part of the 2015/16 accounts matters to consider. A review of assets held in this category has been concluded and reviewed by WAO. Whilst categorisation will allways involves an element of judgement, the majority of assets will remain as initially classified, with others that have the characteristics of community asset transfers, to be shown as surplus assets

Assets Held for Sale	Inclusion in the policy of the four criteria considered for assets to be included within this category
Revaluation of assets	Inclusion of future proposed revaluation timescales for assets where valuations are undertaken

The Council is also required to highlight areas of the accounts where assumptions and estimates have to be made. e.g. in the valuation of fixed assets. The proposed significant assumptions used in 2017/18 for disclosure in the accounts are included in Appendix 3. Changes in assumptions and different assumptions could have a significant impact on the values included in the accounts, but are often purely an accounting exercise and changes will have no impact on the level of Council Tax / Rent payable, as they are required to be reversed.

Following a review, two assumptions listed below have been removed from those disclosed in previous years, with the rationale also highlighted. All other assumptions remain largely unchanged.

Previous Significant Assumption	**Reason for removal**
Manually determined debtors or creditors	Assumptions are normally based on evidenced data.
Employee leave benefits accrual accrued at the end of the year	Assumptions are now based on more robust data of leave from Council IT systems

Amendments to the narrative for accounting policies and assumptions have been considered and agreed with Wales Audit Office.

B - Changes in the 2017/18 Code

The main changes in the 2017/18 code are to:-

- specify the minimum requirements for inclusion in the 'Narrative Report' including financial and non financial data about Council performance. These are statutory requirements in England but not yet in Wales
- clarify accounting policies and encourage simplification as well as consideration of relevance and materiality.

The Code does not contain any significant changes which will affect the Council's Statement of Accounts for 2017/18, however there are a number of minor amendments that will be made including:-

- continuing to look at opportunities to improve content and to include additional disclosures on a best practice basis in the Narrative Report
- reviewing of the pension fund tables
- adding table to financial instruments to aid understanding with figures in the balance sheet
- reviewing tables, comparative figures and formatting
- implementing WAO and other feedback

C- Potential changes to the Code 2018/19 onwards

The main change in the code for 2018/19 relates to the incorporation of International Financial Reporting Standard (IFRS) 9 - Financial Instruments. This was developed largely as a response to the global financial crisis, is long and complex and is designed to cover sophisticated financial instruments often used in financial markets. Although aimed largely at improving transparency and decision-making in financial institutions, it will also impact on the accounts. It applies to financial instrument assets only and for the Council this would currently include its treasury investments, equity holdings in companies, and any loans provided. Whilst complex, the main considerations required by the Code are:-

- Determining the reason for owning the asset e.g. strategic or commercial; trading; generate future income streams?
- Review of contractual cash flows, financial performance and expected future returns
- Classification into one of the following three categories, with any movements in valuation reflected as shown in the table below:-

Category	**Valuation Method**
Amortised Cost	Historic cost adjusted for any expected credit losses, defaults or discounts
Fair Value through profit and loss	Fair Value (year-end market price) with all realized or unrealized gains or losses taken to income and expenditure each year
Fair Value through other comprehensive income	Fair value with gains or losses taken to a financial instrument revaluation reserve until the asset is disposed of

- Increased disclosure requirements, reviewing and explaining valuation methods and judgements made
- Regular assessment of credit risk or impairment
- Dependent on assessment of credit risk, consider recognition of impairment over lifetime (expected loss) rather than only accounting for it when incurred i.e. at an earlier stage rather than when disposed of.

IFRS 9 changes go hand in hand with recent changes in the prudential code and treasury management code and ultimately are aimed to ensure that local authorities are clear as to what financial assets they are holding, what the risks are, why they are holding them and ensuring changes in value / recoverability are reflected in the accounts and at an early stage.

The Council already includes significant disclosures about the financial instruments it holds in the Statement of Accounts. From an initial review of assets currently held, they are not complex or not deemed primarily held for a commercial or trading basis to generate income for the Council. Accordingly the changes are not expected to have a significant accounting or any financial impact on the Council based on its current holding of financial assets, but it will need to be a consideration in the approach to future transactions or changes in policy.

The current approach to providing a fair value for accounting purposes for the Council's interest in Cardiff Bus and any movements in value is likely to remain unchanged as are the risks in using those figures for a commercial purpose without understanding the assumptions used. Any changes in fair value are expected to be reversed to a financial instrument revaluation reserve as is currently the case. However these are not expected to have a significant financial impact on the Council based on its current holding of financial assets.

Further work is required during the next twelve months in conjunction with the Council's Treasury advisors and WAO, to ensure we meet these new accounting requirements, consider materiality and any statutory overrides being considered by government.

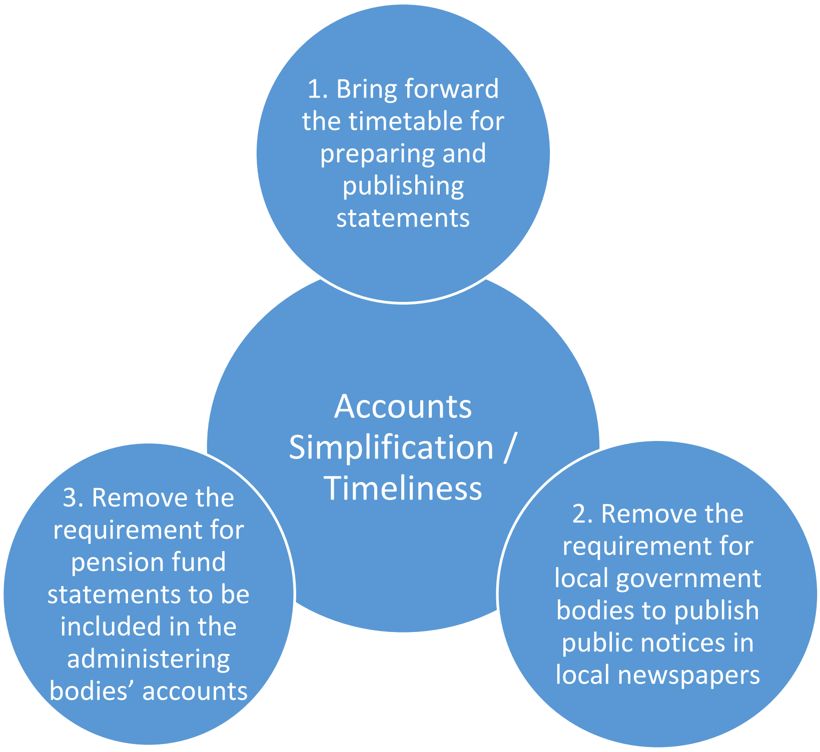
Looking further ahead to 2019/20, the Code will incorporate the requirements of International Financial Reporting Standard 16 – Leases. This will remove the existing classification of operating and finance leases covering buildings, equipment etc and their different accounting treatments. It will require that all leases with a term over a year are recorded as assets and liabilities unless the underlying asset is of low value.

Whilst this is expected to have no direct financial impact, significant work will need to be undertaken to ensure existing lease type arrangements across the Council are identified, and accurately recorded. This will need to include a review of existing and creation of new processes for managing and recording existing and new lease arrangements. This will need to be led by Finance and supported by Directorates.

D - Accounts and Audit Regulations

Between 14 November 2016 and 6 February 2017, the Welsh Government (WG) consulted on proposed changes to the Accounts and Audit Regulations that would apply to Local Government Bodies.

The three main proposals will come into force on 14 March 2018 and will apply to financial years ending on or after 31 March 2018.



The first change is to bring forward the timetable for preparing, auditing and publishing the statements of accounts. The aim is to:-

- bring them into line with other parts of the public sector
- enhance the accountability of authorities and the usefulness / timeliness of accounts

- assist larger relevant bodies' own financial management by providing earlier assurance of the previous year's financial outturn
- free up finance staff time to look at in-year issues, rather than spending a significant part of the year considering the preparation and support for audit of the previous financial year

The table below shows the required deadlines to be met.

	Accounts	2017/18	2018/19	2019/20	2020/21
22 county and county borough councils & their committees	Prepare and sign by S151	30 June	15 June	15 June	31 May
	Publish following audit and Council approval	30 Sept	15 Sept	15 Sept	31 July

The Council supported the change, whilst recognising the impact on its own staff and external parties from whom information is required for its preparation. The Council currently aims to provide a Statement of Accounts for audit on 15 June. Consideration of changes in process to bring forward the Council's preparation timetable by at least two weeks will need to take place by 2020/21 with gradual improvements in timetable proposed over the next few years. This must be done at the same time as meeting the challenge of an increasingly complex statement of accounts as well as planned changes in the Code outlined previously. The approach to this will need to be a combination of streamlining processes, allocation of additional technical capacity, working closely with auditors as well as considering changes in approach or systems that support earlier preparation.

The significant impact will be on the timing of the external audit of the accounts which will require a fundamental change in approach to audit. Accordingly the regulations propose a phased approach to allow external auditors to make adequate provision for the revised timetable through their business planning processes. Any such revised approach will also need to take into account materiality and also the impact on local authority resources.

In order to meet the timescales above, the Council and any other bodies charged with governance will need to consider carefully the timing of meetings and potentially responsibility for approving them in the short term and longer term. This includes the timing of Council meetings to approve the accounts and also Audit Committee for scrutiny of the Accounts. This exercise will need to be undertaken in the next few months and reported back to audit committee as part of a future report for the Accounts.

<u>The second change</u> of the regulation relates to the requirement to publish a notice stating when their accounts are available for public inspection and for completion of audit. This was stipulated to be done by advertisement in one or more local newspapers circulating in the area of the body concerned. The revised regulations are less specific and accept that alternative media such as the Council's website can now also be used to make users of the accounts aware of the period of public inspection.

<u>The third change</u> is that the requirement to include the Pension Fund statements in the Statement of Accounts of the administering body has been removed. The requirement to set a date for inspection, publicise the audit, for the S151 officer to sign, for those charged with governance to authorise, approve and certify the accounts, the need for an audit certificate and audit opinion remain unchanged. However the Council will need to consider how a standalone set of pension fund accounts will be approved as part of the

responsibilities for those charged with governance of the pension fund. One option is to include the Pension Fund Accounts within the *Annual Report* document which is currently required to be published by 1 December each year at the latest. Another option is to align the timetable of the pension fund annual report and accounts with the main administering authority statements. Further clarification has been sought from the WG and the Council will work with WAO to develop locally agreed arrangements to meet responsibilities for the pension fund statement of accounts.

Reasons for Recommendations

To inform Audit Committee of the key changes impacting on the Council and Pension Fund Statement of Accounts for 2017/18 and changes expected in the medium term.

Legal Implications

There are no direct legal implications as a result of this report.

Financial Implications

The changes outlined in this report particularly beyond 2017/18 are likely to require additional workload on the part of the local authority finance function and directorates. Consideration of the cost and benefit of all changes will need to be undertaken as part of implementation particularly in respect of the materiality of the impact of the requirements.

Recommendations

Audit Committee are requested to note :-

- the draft accounting policies and assumptions to be used in preparing the statement of accounts for 207/18 and beyond
- the changes to governance requirements for the current and future years accounts

CHRISTINE SALTER
CORPORATE DIRECTOR RESOURCES
15 MARCH 2018

The following Appendices are attached:

Appendix 1 – CIPFA Guide – Understanding Local Authority Financial Statements
Appendix 2 – Draft Accounting Policies 2017/18
Appendix 3 – Draft significant assumptions and estimates used in preparing the Accounts