CITY OF CARDIFF COUNCIL
CYNGOR DINAS CAERDYDD

AUDIT COMMITTEE: 22 MARCH 2016

ACCOUNTING POLICIES UPDATE

REPORT OF CORPORATE DIRECTOR RESOURCES

AGENDA ITEM: 4.2

Reason for this Report

1. The Audit Committee Terms of Reference sets out their responsibility for reviewing the financial statements prepared by the authority.

2. This report has been prepared to provide Audit Committee Members with an update on changes to accounting policies included in the 2015/16 CIPFA Code of Practice (the Code) and potential impact for the Council's Statement of Accounts. It will also highlight future Code updates that are likely to have a significant impact on the accounts.

Background

3. The Code of Practice is based on International Financial Reporting Standards (IFRSs), and is developed by the CIPFA/LASAAC Code Board under the oversight of the Financial Reporting Advisory Board. The Code has been prepared on the basis of accounting standards and interpretations in effect for accounting periods commenting before 1 January 2015.

4. There are a number of changes within the Code that will have little or no effect on the Council's Statement of Accounts. This report will focus on the key accounting changes to the Code that will impact upon the Councils accounts. A copy of the Council's draft 2015/16 accounting policies is included, for information, at Appendix 1.

IFRS 13 Fair Value Measurement

5. The most significant change within the 2015/16 Code is the application of IFRS 13 *Fair Value Measurement* of property, plant and equipment in local government. CIPFA/LASAAC deferred adoption of IFRS 13 to the 2015/16 financial year to allow time to review the concepts which underpin its measurement requirements and their relevance in the public sector.

6. CIPFA/LASAAC are of the view that the definition of fair value in IFRS 13 is not the most appropriate measurement base for operational property, plant and equipment in the public sector. Service potential is of primary interest when managing public

sector assets, therefore the measurement of ‘Current Value’ will continue for operational assets.

7. However, the 2015/16 Code introduces the concept of valuation of surplus assets and investment properties for accounting purposes on the basis of ‘Fair Value’ and requires any valuations to be based on the basis of ‘highest and best use’. This is the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date.

8. In respect of surplus assets, the Council adopted a fair value approach, in 2014/15, for reasons set out previously in its accounting policies. This was deemed to give a fairer indication of the value of assets not used in service delivery. The change in the Code affirms our existing approach and supports our original deviation from the accounting approach previously recommended.

9. The Council’s investment properties were revalued during 2014/15 and professional valuation advice deems that the Council’s approach to valuation of these assets already considers the revised fair value requirements. Whilst a high level review will be undertaken during 2015/16 to determine that the valuations previously provided have not changed materially, the next full revaluation of investment properties is to take place in 2016/17 in accordance with the rolling programme of revaluations.

Forthcoming changes to the Code

10. The 2015/16 Code includes confirmation of changes to forthcoming editions of the Code, including adoption of the measurement requirement of the *Code of Practice on Transport/Infrastructure Assets* in the 2016/17 Code. These changes are likely to require significant additional workload on the part of the local authority finance function and directorates at a time of significant financial pressures. 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.

Highway Network Infrastructure Assets

11. Although the change in measurement of the Highway Network Infrastructure Asset will not be implemented until the 2016/17 Code, there will be a significant impact on the balance sheet and comprehensive income & expenditure (CI&E) accounts and, therefore, it is important that those responsible for governance are made aware of the changes and its potential impact.

12. The Highway Network Infrastructure Asset includes land, carriageways, footways, cycle tracks, structures, street lighting, street furniture and traffic management systems. It is the most valuable asset that the Council holds and operates, in terms of replacement cost. However, local authority accounts do not currently reflect the true value of the asset, its condition, its cost in providing services and the implications of not maintaining it in the short and long term.

13. From 2016/17, the asset will need to be measured at Depreciated Replacement Cost (DRC), rather than Depreciated Historic Cost (DHC), and will also be a disclosed as a separate class of asset on the balance sheet. The move to DRC will

significantly change the balance sheet and increase depreciation charges to the CI&E. There will be no requirement to restate balances in relation to 2015/16.

14. There are a number of reasons for the change to DRC, including:

- Whole of Government Accounts – deemed that nationwide assets were understated by over £200 billion largely due to the valuation of infrastructure assets.
- Leads to better financial and asset management.
- Better reflects cost of replacing an asset in its current condition.
- More realistic valuation basis than historic cost, which is extremely dated.
- Consistent with the key principles of the Infrastructure Code.

15. These changes aim to address the following:

- Increase visibility and impact of infrastructure assets in delivery of Council services.
- Nationally a perception that not enough spent on maintaining infrastructure assets, with the impact of not maintaining assets now resulting in more expense later.
- Lack of consistent data on quantities, condition of such assets, maintenance backlogs and true cost of holding such assets
- Data held in disparate systems or not held at all.
- The only infrastructure assets held in the Council accounts are those where expenditure has been incurred since a certain date in the 1990s. They are measured at historic costs and do not reflect true value, condition or use in service delivery.
- Lack of information to improve service delivery and resource allocation in line with Asset Management Plans.

16. The City Operations Directorate has been providing asset valuation and condition data for the National Whole of Government Accounts project. It has been working with the County Surveyors Society Wales Highway Asset Management Group to review the information held, how it is held, and professional assumptions made. The Whole of Government Accounts return for 2014/15 included a Gross Replacement cost for Highway Network assets of c £2.3 billion for Cardiff, which would double the valuation of all non-current assets currently included in the Statement of Accounts.

17. The pre-requisites for preparing for the upcoming change include:

- Highways, Transport, Finance and Audit officers involved at an early stage and sufficient resource available to deliver requirements.
- Ensuring financial information generated for asset management is robust, consistent and fit for purpose e.g. Gross Replacement Cost, current condition, professional assumptions, inventory and asset lives.
- Data is available in a form that can be used to inform the Statement of Accounts Systems and processes exist that can be audited, maintained and updated with all relevant information provided by professionals in their field.
- Consideration of materiality and cost versus value added in the provision and collection of information
- Early support from external audit where needed.

Telling the Story Consultation

18. During 2015, CIPFA undertook a consultation on ‘Telling the Story’, which aimed to review clutter within Local Authority Statement of Accounts and better explain the financial statements. It is not yet known exactly when the findings of the consultation will impact upon the Code, however it is possible that they will be introduced in the 2016/17 version of the Code.

19. The key change under consideration is a change from reporting the net cost of services, within the CI&ES, on a Service Reporting Code of Practice (SERCOP) basis to the recognised management reporting structure of each authority. The consequence will be a deviation from standardised reporting of income and expenditure across all local authorities. To support this change, it is intended to introduce a new ‘Expenditure & Funding Analysis’ note to the accounts, which will provide a reconciliation of the figures contained within the CI&ES and those reported as part of each authority’s final management accounts for the year. Furthermore, a simplification of the Movements in Reserves Statement and a significant change to the contents of the segmental reporting note is under consideration.

20. In support of CIPFA’s simplification agenda, the Council is currently undertaking a review of its Statement of Accounts, with the intention of removing immaterial disclosures and superfluous narrative and information.

Reasons for Recommendations

21. To ensure the Audit Committee are aware of the implications of accounting policy changes on the Council’s Statement of Accounts.

Legal Implications

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

Financial Implications

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

Recommendations

24. That the update in respect of accounting policies be noted.

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14 MARCH 2016