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CONSTITUTION COMMITTEE – 28 SEPTEMBER 2011

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

STATEMENT OF ACCOUNTS 2010/11

PURPOSE

1. The purpose of this report is to:
   a) present the 2010/11 Statement of Accounts, attached as Appendix A to this report, for approval.
   b) to inform the Committee of the key issues within the accounts, and
   c) to report the key findings from the external audit of the accounts

BACKGROUND

2. The Accounts and Audit regulations were amended in March 2011 to require all authorities to formally approve their accounts by the end of September following the end of the financial year. In the past, the requirement was for the accounts to be formally approved by the end of June.

3. The change has been introduced to align the approval process more closely with the procedures applying elsewhere in the public and private sectors. It will mean that members are now being asked to formally approve the accounts after, rather than before, the findings of the audit are known.

4. The accounts are required to be published by 30 September with the auditor's opinion as required by the Accounts and Audit regulations.

5. A copy of our external auditors, PricewaterhouseCoopers (PwC), report on the accounts is attached as Appendix B. The draft letter of representation is attached as Appendix C. The auditor anticipates issuing an unqualified audit opinion.

6. The Corporate Governance Committee will consider the auditors report at its meeting on the 26th September 2011. The auditor is required to communicate the results of the audit to those charged with governance prior to certifying the financial statements. Comments from that meeting will be reported to the Constitution Committee.

7. The Statement of Accounts for 2010/11 are prepared under the International Financial Reporting Standards (IFRS) based Code of Practice on Local Authority

Accounting for the first time. This is part of a wider public sector move to international accounting standards. The NHS and Central Government adopted IFRS in 2009/10. Local authority accounts were previously prepared in accordance with UK accounting standards and the Statement of Recommended Practice (SORP).

STATEMENT OF ACCOUNTS

8. The Statement of Accounts are accompanied by the Annual Governance Statement signed by the Chief Executive and Leader of the County Council This statement sets out the purpose of the system of internal control, how it operates in the County Council and how its effectiveness has been reviewed. This statement was considered by the Corporate Governance Committee on 13 May 2011 and the Committee approved the statement and the method used to evidence it.

9. A report setting out the provisional revenue budget outturn was considered by Cabinet on 14 June 2011 and by the Budget and Performance Monitoring Scrutiny Panel on 20 June 2011. The main issues are set out below.

Revised Format of the Accounts - IFRS

10. On first time adoption, IFRS requires the previous SORP based 2008/9 balance sheet and 2009/10 Statement of Accounts to be restated on an IFRS basis to provide comparative figures. As a result the balance sheet and associated notes exceptionally show 3 years accounts for 2010/11.

The main changes for the County Council are:

11. A new presentation for the Primary Statements – summarised below:

IFRS	Contains	SORP Equivalent
Movement in Reserves Statement (MIRS)	Shows all movements in usable and unusable reserves. Key statement showing movement of the General County Fund (includes schools balances) for the year.	Statement of Movement on the General County Fund Balance (SMGCFB)
Comprehensive Income & Expenditure Statement (CIES)	Shows the Surplus/Deficit on the provision of services. Combines the SORP I&E and STRGL.	Income and Expenditure Account (I&E) Statement of Total Gains and Losses (STRGL)
Balance Sheet	Shows the total assets and liabilities of the Council. Presentational changes to the SORP including new headings	Balance Sheet
Cash Flow Statement	Shows the cash flows in/out of the Council – presentational changes to the SORP	Cash Flow Statement

12. Property, Plant and Equipment (PPE) – this is the new IFRS name for fixed assets on the balance sheet. IFRS has an increased emphasis on component accounting compared with the SORP – this recognises that an asset may include different

components with different useful economic lives and should be depreciated and valued separately. The fixed asset register has been reviewed to ensure that this requirement is met. Other changes include a new heading on the balance sheet for Asset Held for Sale, within the Current Assets section. This contains those assets that are actively being marketed and expected to sell within 12 months.

13. Leases – there is a stricter definition of what constitutes an operating lease as opposed to a finance lease. The previous tests have been replaced with a combination of eight harder tests meaning that some leases previously accounted for as an operating lease are now reclassified as a finance lease. Finance leases are required to be recognised as an asset on the Council's balance sheet matched by a liability to pay the lease payments. The asset is then subject to regular valuations, depreciation and capital financing, although statutory regulations have been implemented to reverse out any financial effect.

14. Employee Benefits – IFRS requires the cost of annual leave not taken by the year end to be accrued as a liability on the balance sheet. This affects all employees including teachers who work term time. CIPFA have produced a proforma for calculating the liability for teachers. For non teaching employees a sampling approach was undertaken for 2008/9, 2009/10 and 2010/11 as the records are mainly paper based. In future years it is intended that a full data collection will be taken following the introduction of Oracle HR self service. As part of the IFRS changes, the Council have implemented a consistent annual leave year for all employees across the Council to coincide with the financial year. Prior to this there were more than six different leave years. Accounting regulations have been introduced to ensure the accrued charge is not charged to council tax. The reversal is held in the bottom half of the balance sheet under Short Term Accumulating Compensated Absences Adjustment Account. The total at 31 March 2011 was £12.2m. (31 March 2011 £12.3m).

15. Government Grants and Contributions – IFRS requires that all grants are now credited immediately to the CIES unless conditions requiring repayment remain outstanding the year end. Capital grants are no longer deferred and matched to expenditure meaning that the Government Grants and Contributions Deferred Account has been removed. Capital grants and contributions received in advance are now shown in a new Capital Grants Receipts in Advance account on the balance sheet. Revenue grants received in advance where no conditions exist for repayment are now restated and treated as earmarked revenue reserves. Where conditions exist at the balance sheet they are either treated as receipts in advance or short term creditors (where repayment is required).

16. Cash and Cash equivalents – IFRS has extended the definition of cash on the balance sheet to also include short term highly liquid investments that are readily convertible to known amounts of cash. Using the CIPFA guidance short term deposits of less than 3 months have been reclassified as cash equivalents on the balance sheet.

17. Notes to the Accounts – IFRS requires a greater level of supporting notes to assist the readers of the accounts compared with the SORP. Significant new notes include extended balance sheet disclosures for creditors and debtors, summary

details of the total costs of the termination of employee contracts during the year, assumptions made about the future in terms of estimates in the accounts and estimates of the impact of accounting standards that have been issued but not yet adopted. The accounts have therefore increased in size by approximately 40%.

Movement in Reserves Statement (MIRS)

18. The General County Fund balance shows whether the Council has under or over spent against the Council Tax that it raised for the year, taking into account the use of reserves built up in the past and contributions to reserves earmarked for future purposes. Note 9 to the accounts, shows that overall the General County Fund remains at £9m in 2010/11 after approved carry forwards, the same as in 2009/10.

19. The policy on the County Fund has been to maintain balances in line with the inherent risks faced by the County Council. The required level of reserves is kept under review during the year and a more formal assessment is undertaken at the time the Medium Term Financial Strategy (MTFS) is rolled forward. The policy will be to continue to maintain a level of County Fund consistent with the overall financial environment and the level of the County Fund is currently within the target range of 2 to 3% of net expenditure (excluding schools). The balance of £9m represents 2.6% of net expenditure for 2011/12.

20. Overall earmarked cash backed revenue revenues (excluding schools) have increased from £62.9m in 2009/10 to £86.5m at the end of 2010/11 – see note 9 to the accounts. This is mainly as a result of contributions to the Insurance Reserve, Waste Strategy implementation reserve, PCT/Public Health in Leicestershire reserve and the new Transitional Grant Aided Fund reserve. Further details are provided below:

    - Insurance reserve £11.6m. To meet future claims to enable the Council to meet the excesses not covered by external insurers. The levels are recommended by independent advisors. As set out in the MTFS the reserve was increased by £3.5m during 2010/11 mainly to meet potential liabilities arising from Municipal Mutual Insurance Ltd that is subject to a run-off of claims following liquidation in 1992. The level of this reserve will be kept under review during 2011/12 to take account of the MMI run-off position.

    - Waste strategy implementation £6.1m. From the waste underspend, £1.9m has been transferred to this reserve to improve recycling and household waste sites at Melton, Lount and Kibworth and to upgrade the transfer station at Whetstone.

    - PCT/ Public Health £3.9m. The Primary Care Trust (PCT) agreed to transfer £3.9m to the County Council at the end of 2010/11. This has been used to fund 2010/11 County Council expenditure relating to the Leicestershire Together Staying Healthy Strategy to make progress towards health related targets within the theme of creating a healthier Leicestershire. The resulting underspend has been allocated to an earmarked reserve to fund future partnership work.

- Transitional Grant Aided Fund £5m. Reserve set aside to ease the transition of Children's and Youth Offending services that are affected by the reduction in specific grants.

21. Reserves are held for other reasons, including:-

    - Reconfiguration of services. Under the change management programme, the County Council is in the process of making major changes to the way services are delivered. With increasing focus on efficiency this programme of reconfiguration will continue and accelerate. With many of these projects significant up front investment is required. This will include severance costs, project management and ICT. The change management reserve consists of £2.9m for organisational change projects and £9.6m for invest to save projects and other MTFS issues.

    - Renewals – To enable services to plan and finance an effective programme of vehicle and equipment replacement. These reserves are a mechanism to smooth expenditure on asset replacement so that a sensible replacement programme can be achieved.

22. Schools balances have increased from £16.2m in 2009/10 to £17.3m at the end of 2010/11.

<u>Comprehensive Income and Expenditure Statement (CIES)</u>

23. The Service classification within the Income and Expenditure Account is presented in line with CIPFA's Best Value Accounting Code of Practice and thus is not comparable to the format of the council budget.

24. It should also be noted that the CIES cannot be directly compared to the outturn underspend reported to members. This is because the financial accounts comply with various reporting standards whereas the management accounts are compiled on a slightly different basis. The key differences relate to the way depreciation, impairment, reserves and provisions are reported.

25. The CIES shows a surplus of £137m for 2010/11 (£59m deficit 2009/10). This is mainly as a result of the Governments announcement that public service pensions would be up-rated in line with the Consumer Prices Index (CPI) rather than the Retail Prices Index (RPI). As a consequence of this, all future pension benefits that have already been earned are expected to be lower than previously estimated, resulting in a 'past service' gain of £124.3m being credited to the Income and Expenditure account. This has no overall impact on the balance on the General County Fund as statute requires the entry to be reversed out in the Movement in Reserves Statement (MIRS).

26. The explanatory foreword explains the outturn in the context of the Council's budget. In summary, the County Council (excluding schools grant) underspent by a net £0.8m after allowing for carry forwards and approved transfers to reserves

Balance Sheet

27. The balance sheet shows net assets have increased from £67.7m at 31 March 2010 to £416.4m as at 31 March 2011. The main reason for the increase is a significant reduction in the net pension liability from £654.3m at 31 March 2010 to £330.1m at 31 March 2011. The balance represents all pension entitlements that have been earned to date but which are not yet in payment.The reduction is primarily related to the government's switch from RPI to CPI for public sector pension indexation referred to earlier.

28. Four Industrial Properties have been recategorised as finance leases as part of the transition to IFRS. The leases meet the definition of a finance lease as defined by IAS17. The leases have been added to Land and Buildings (PPE) on the balance sheet together with a finance lease liability. PPE has increased by £1.3m and finance lease liabilities by £1.8m as a result.

Pension Fund Accounts

29. These accounts include a copy of the County Council's pension fund accounts.

30. The last available triennial actuarial valuation of the pension fund showed that at 31 March 2010 the fund's assets covered 80% of its liabilities. This funding level was a decrease on the 93% position of the 2007 valuation and this was primarily due to the lower-than-expected investment returns achieved in the three year period. Over the period investment returns were virtually zero – with two sharply negative years being offset by a major rally in 2009/10 – but this was significantly below the c.6% which is assumed within the 2007 actuarial valuation. This underperformance put significant upward pressure onto the contribution rates of employing bodies but these were contained somewhat for tax raising bodies by using a smoothing mechanism and by the use of a 20 year deficit-spreading period.

RECOMMENDATION

31. The Committee is recommended to approve the Statement of Accounts for 2010/11.

BACKGROUND PAPERS

None.

CIRCULATION UNDER THE LOCAL ISSUES ALERT PROCEDURE

None.

EQUAL OPPORTUNITIES IMPLICATIONS

None.

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