

**CODE OF PRACTICE ON LOCAL  
AUTHORITY ACCOUNTING IN  
THE UNITED KINGDOM – A  
STATEMENT OF RECOMMENDED  
PRACTICE 2009**

**INVITATION TO COMMENT  
10 November 2008**

AT THE HEART OF  
PUBLIC SERVICES 

# INVITATION TO COMMENT

## 1 INTRODUCTION

- 1.1 Local authorities in the United Kingdom are required to keep their accounts in accordance with 'proper practices'. This is defined, for the purposes of local government legislation, as meaning compliance with the terms of the *Code of Practice on Local Authority Accounting in the United Kingdom*, prepared by the CIPFA/LASAAC Local Authority SORP Board (CIPFA/LASAAC). It is recognised by the Accounting Standards Board (ASB) as a Statement of Recommended Practice (SORP). The SORP is reviewed continuously and is updated annually.
- 1.2 This invitation to comment (ITC) sets out CIPFA/LASAAC's proposals for developing the current SORP with the resulting amendments to be included in a new edition of the SORP (2009 SORP) to apply to accounting periods commencing on or after 1 April 2009. The proposed developments are:
- (a) Adopting requirements for accounting for PFI schemes and similar arrangements that are consistent with the adaptation of IFRIC 12 *Service Concession Arrangements* contained in the Government's 2009/10 Financial Reporting Manual (FRM) and Whole of Government Accounts' requirements.
  - (b) Including more detailed and in some respects different requirements for accounting for council tax and national non-domestic rates in England, Scotland and Wales and rates in Northern Ireland.
  - (c) Removal of larger parishes and community councils from the list of bodies to which the SORP applies.
  - (d) Accounting for reorganised local authorities.
  - (e) Other minor amendments.

### **The consultation process**

- 1.3 Where CIPFA/LASAAC is interested in specific issues, consultation questions have been included in the ITC. However, CIPFA/LASAAC welcomes comments on any aspect of the draft SORP for 2009. In order to assess comments properly CIPFA/LASAAC would prefer respondents to support comments with clear accounting reasons and, where applicable, preferred alternatives. Questions on each issue raised in this ITC are included throughout the document. In addition, all the consultation questions are listed in a separate document, which can be downloaded, to help respondents to formulate their responses more conveniently.
- 1.4 In accordance with the ASB's Code of Practice on the Development of SORPs, responses to this Invitation to Comment will be regarded as on the public record unless confidentiality is specifically requested. Copies of all correspondence and an analysis of responses will be provided to the ASB.
- 1.5 A copy of the Exposure Draft 2009 SORP showing the amendments to the 2008 SORP and an extract of the ITC questions can be downloaded from the CIPFA website ([www.cipfa.org.uk/pt](http://www.cipfa.org.uk/pt)).

1.6 Responses are required by 8 February 2009 and may be sent to:

The Secretary  
CIPFA/LASAAC Local Authority SORP Board  
Policy and Technical Directorate  
CIPFA  
3 Robert Street  
London  
WC2N 6RL  
*Fax:* 020 7543 5695

*E-mail:* [sorp.responses@cipfa.org](mailto:sorp.responses@cipfa.org)

(For ease of handling, e-mailed responses, in Word document form, are preferred.)

- 2 ACCOUNTING FOR PRIVATE FINANCE INITIATIVE (PFI) AND SIMILAR CONTRACTS
- 2.1 Private Finance Initiative (PFI) and similar contracts are required in the current SORP to be accounted for under Application Note F *Private Finance Initiative and Similar Contracts* of FRS 5 *Substance of Transactions*. This will need to change as local authority accounts move to an IFRS basis. The Government and other entities covered by the Financial Reporting Manual (FReM) will be adopting IFRS in 2009/10. Local authorities will complete the move to IFRS in 2010/11.
- 2.2 Accounting for PFI arrangements was until recently a matter that was not covered specifically by an IFRS or an International Financial Reporting Interpretation Committee (IFRIC) 'interpretation' (which is equivalent to UITF Abstracts in UK GAAP). This changed with the issue of IFRIC 12 *Service Concession Arrangements*, which gives guidance on the accounting by operators for public-to-private service concession arrangements. In the 2009/10 FReM, which has already been issued, the guidance on accounting for PFI and similar schemes is based on IFRIC 12 but adapted to reflect public authority accounting requirements. The FReM guidance is consistent in most respects with the Discussion Paper on Service Concession Arrangements issued by the International Public Sector Accounting Standards Board (IPSASB) earlier this year.
- 2.3 CIPFA/LASAAC has reviewed the FReM requirements and believes it provides a sound and less complex basis for accounting for PFI and similar contracts. There are also the following compelling pragmatic reasons for adopting IFRS-based requirements in 2009/10 rather than in 2010/11 on full transition to IFRS:
- the upcoming requirement to supply information to the Government on PFI schemes in 2009/10 on a basis consistent with the FReM for WGA consolidation purposes
  - the announcement by CIPFA/LASAAC of its intention to prepare the 'Code' on the basis of IFRS from 2010/11.
- 2.4 The effect of these two factors is that in the absence of the proposed SORP amendment, authorities would need to account for their PFI schemes on two different bases in 2009/10: on an FRS 5 basis for inclusion in their statement of accounts; and on a FReM basis in order to provide the information to the Government that it needs to prepare its 2009/10 IFRS-based Whole of Government Accounts. CIPFA/LASAAC is therefore proposing that the 2009 SORP accounting requirements for PFI and similar contracts are based on IFRIC 12 as adapted by the Government's FReM.
- 2.5 If it were not for the above considerations CIPFA/LASAAC would not be proposing making the change to an IFRS-based approach in 2009/10 ahead of full adoption of IFRS in 2010/11 since it is not ideal to follow an IFRS-based approach selectively in one particular area in a SORP prepared under UK GAAP. Indeed, as a consequence, the ASB may need to comment on the matter in their statement of negative assurance or even qualify their statement.
- 2.6 A key difference between CIPFA/LASAAC's proposed requirements and the current SORP's FRS 5-based requirements, is the approach to determining whether the 'property' (eg school) used to deliver the PFI contract is 'on' or 'off' the balance sheet of the local authority. The current SORP, in accordance with FRS 5, follows a 'risks and rewards' approach to determine whether the authority or the operator has an ownership interest in the property, which is usually measured quantitatively in monetary terms using discounted cash flow techniques. Both IFRIC 12 and the FReM follow a simpler approach and seek to establish which

party controls the property by applying a few key tests. A crucial test is whether it reverts to the public authority at the end of the service concession period, with reversion being indicative that the property should be carried on the local authority's balance sheet.

- 2.7 Whether the property reverts to the authority at the end of the PFI contract is also one of the factors taken into account currently in deciding whether it should be carried on the authority's balance sheet, but in this case it is as just one type of risk and reward along with others that are assessed to determine the party that bears the greater share of risk and reward.
- 2.8 Overwhelmingly in local authority PFI contracts the PFI property reverts to the authority at end of the contract for nil or negligible additional consideration, but in most cases the PFI property is not being carried on the authority's balance sheet. It seems likely that on adoption of accounting requirements based on the FReM most PFI properties that are not currently being carried on local authorities' balance sheets would be required to be recognised 'on balance sheet' along with a liability representing the obligation of the authority to pay for the property.
- 2.9 This would result not only in the recognition of the PFI property and a liability representing the obligation of the authority to pay for the property, but also the need to determine the amount that would have been charged to revenue since inception under the new accounting policy and compare it with the amount that was charged under the previous accounting policy. In turn, the effect on the General Fund Balance would need to be determined. CIPFA has been discussing with Government officials in the four jurisdictions the need to consider whether legislation to ameliorate any effect the change might have on budget requirement is needed. Discussions are progressing and changes to regulations/statutory guidance to address the issue have already been made in England and Wales. PFI schemes have not been used in Northern Ireland and regulation/statutory guidance appears to be unnecessary.
- 2.10 With regard to Scotland, consideration of whether regulation/statutory guidance might be needed to ameliorate any affect the change might have on budget requirements has been complicated by the need to clarify how the legislation regarding local authority borrowing powers applies to on balance sheet PFI contract related liabilities. This in turn affects whether Loan Fund accounting would or would not apply to PFI related liabilities. This matter is the subject of a separate public consultation that is being undertaken by LASAAC. The closing date for responses was 17 October 2008. The outcome of the LASAAC consultation and any conclusions reached by LASAAC will be considered by CIPFA/LASAAC in reaching its conclusions on the matter.
- 2.11 As explained above, CIPFA/LASAAC's reason for proposing to adopt an IFRS-based approach to accounting for PFI before full transition to IFRS in 2010/11 is pragmatic and aimed at reducing the overall burden on authorities. Discussions will however proceed with officials and other stakeholders to assess whether 'early adoption' might cause unexpected consequences. If having seen the detail within the ITC for the SORP and/or regulations/statutory guidance or proposed regulations/statutory guidance, points of concern remain or become evident, respondents are asked to raise them in their responses. CIPFA/LASAAC will then have regard to these issues in finalising the SORP.
- 2.12 The proposed FReM-based requirements for PFI and similar schemes are contained in Appendix E of the accompanying SORP Exposure Draft; and the Regulations/Statutory Guidance that has been issued for England and Wales is attached at Appendix A of this ITC.

### **Accounting for private finance initiative (PFI) and similar contracts**

- Q1 Do you agree with the proposals to base the accounting requirements for PFI and similar contracts on the FReM from 1 April 2009? If you do not agree please give reasons.
- Q2 Do you agree that if, as discussions progress and events unfold, CIPFA/LASAAC concluded that the adoption of FReM-based accounting requirements for PFI would risk adverse impact on budget requirements and taxation, it should not proceed with implementing the proposal in 2009/10?
- Q3 Do you have any comments on the detail of the section on accounting for PFI and similar contracts of the 2009 Exposure Draft SORP?

### **3 ACCOUNTING FOR NNDR AND COUNCIL TAX IN THE CORE FINANCIAL STATEMENTS IN ENGLAND, SCOTLAND AND WALES**

- 3.1 The issue of whether billing authorities in England act as agent rather than principal when collecting the element of council tax required to meet major preceptors' precepts has been raised with CIPFA/LASAAC by the Audit Commission, which said:

*"The billing authority is in our view merely an agent of the major preceptors, which means that it should include in its accounts only its share of debtors and creditors of the Collection Fund and the preceptors should do likewise."*

- 3.2 Following this comment, CIPFA raised the question of whether billing authorities act as agent rather than principal with practitioners and stakeholders as part of the recent 'Back to Basics' consultation on the local authority statement of accounts. The results were that:

- (a) 85% of respondents agreed that CIPFA/LASAAC should explore with CLG and the devolved administrations billing authorities' accounting for NNDR on an agency basis
- (b) 80% of respondents said that council tax collected on behalf of major preceptors by billing authorities should be accounted for on an agency basis in England
- (c) 100% of respondents said council tax should be accounted for by billing authorities as 'principal' in Wales.

- 3.3 In the light of the Audit Commission's comment and the outcome of the 'Back to Basics' consultation, CIPFA/LASAAC has undertaken a review of how NNDR and council tax should be accounted for in authorities' core financial statements in England, Scotland and Wales.

#### **Principal versus agent – impact on accounting**

- 3.4 A key factor in determining the appropriate accounting treatment of NNDR and council tax is whether the billing authority acts as principal or agent. The significance of whether a billing authority acts as principal or agent is that:

- (a) If a billing authority acts as a principal:

- its income would be the gross income accruing for the year, including in the case of council tax, the amount arising in respect of major preceptors' precepts
- debtors and the impairment allowance for doubtful debts would be carried wholly on the billing authority's balance sheet.

(b) If a billing authority acts as an agent:

- NNDR collected for the Government would not be the billing authority's income and the billing authority would not carry the NNDR debtors and impairment allowance for doubtful debts on its balance sheet
- council tax collected for major preceptors would not be the billing authority's income and a proportion of council tax debtors and the impairment allowance for doubtful debts would be carried on the balance sheets of the major preceptors.

3.5 Under UK GAAP in order for an entity to account for income as principal it should have exposure to the significant risks and rewards associated with the income. The tables below assess whether the billing authority acts as agent rather than principal when collecting NNDR and council tax to meet major preceptors' precepts by examining exposure to three key risks and rewards. In CIPFA/LASAAC's view, these assessments would remain unchanged on adoption of IFRS in 2010/11 and therefore further IFRS related changes in 2010/11 would not be required.

### National non-domestic rates in England, Scotland and Wales

Table 1

<b>Do billing authorities in England, Scotland and Wales act as agent rather than principal when collecting NNDR?</b>		
<b>Characteristic indicating acts as an agent</b>	<b>Arrangement in operation</b>	<b>Indicates is an agent?</b>
No exposure to risks associated with 'selling price'	The Government sets the NNDR charge by deciding the Uniform Business Rate or 'multiplier'. The billing authority is not exposed to risk eg an increase or decrease in the amount it is responsible for collecting does not result in any more or less NNDR income for the billing authority since all the proceeds are paid to the Government (except indirectly by the size of the overall NNDR national pool being different).	<b>YES</b>
No exposure to credit risk	The billing authority does not bear the credit risk since billing authorities are allowed to offset bad debts written off and the movement in the impairment allowance for doubtful debts in calculating the amount they are required to pay into the NNDR national pool.	<b>YES</b>

The income earned is 'predetermined' eg a fixed fee per transaction or stated percentage of the amount billed	The amount the billing authority earns is predetermined: it receives only an agent's fee (cost of collection allowance).	<b>YES</b>
---	--	------------

## Council tax in England

Table 2

<b>Do billing authorities in England act as agent rather than principal when collecting council tax arising in respect of major preceptors' precepts?</b>		
<b>Characteristic indicating acts as an agent</b>	<b>Arrangement in operation</b>	<b>Indicates is an agent?</b>
No exposure to risks associated with 'selling price'	In England the billing authority maintains a Collection Fund which is credited with council tax income. The billing authority and major preceptors share the council tax income in proportion to their council tax precept or demand and are exposed proportionately to the risk that actual income is less or more than that anticipated when the precepts and demands were set. The billing authority is not exposed to the 'selling price' risk associated with the amounts collected on behalf of major preceptors.	<b>YES</b>
No exposure to credit risk	The billing authority does not assume any credit risk in respect of the share of council tax income relating to major preceptors' precepts. When calculating the surplus or deficit on the Collection Fund, bad debts written off and the movement in the impairment allowance for doubtful debts relating to the major preceptors' precepts are borne by the major preceptors themselves.	<b>YES</b>
The income earned is 'predetermined' eg a fixed fee per transaction or stated percentage of the amount billed	The amount of income the billing authority receives in respect of council tax raised to meet major preceptors' precepts is predetermined as nil since the whole council tax income accruing in respect of major preceptors' precepts is paid over to the major preceptors.	<b>YES</b>

3.6 A matter that applies only to England is that the council tax income included in the Income and Expenditure Account is not the accrued income for the year but rather the amount the Collection Fund regulations require to be included in the General Fund ie the council tax precept or demand for the year plus or minus the authority's share of the previous year's Collection Fund surplus or deficit. In recent years the SORP has established a methodology for accounting for such situations, which is that the GAAP-based income or expenditure is included in the Income and Expenditure Account and the difference between this amount and the amount that statute requires to be included in the General Fund is accounted for as a movement on reserves and included as a reconciling item in the Statement of Movement on the General Fund Balance.

### Council tax in Wales

Table 3

<b>Do billing authorities in Wales act as agent rather than principal when collecting council tax arising in respect of major preceptors' precepts?</b>		
<b>Characteristic indicating acts as agent</b>	<b>Arrangement in operation</b>	<b>Indicates is an agent?</b>
No exposure to risks associated with 'selling price'	In Wales major preceptors receive the exact amount of their precept and therefore the billing authority bears the selling price risk associated with the council tax raised to meet a major preceptor's precept.	<b>NO</b>
No exposure to credit risk	The billing authority bears the whole credit risk in respect of the share of council tax billings relating to major preceptors since the major preceptor receives its exact precept irrespective of the level of bad and doubtful debts experienced by the billing authority.	<b>NO</b>
The income earned is 'predetermined' eg a fixed fee per transaction or a stated percentage of the amount billed	A billing authority experiences a gain or loss of a non-predetermined amount in respect of council tax raised to meet major preceptors' precepts since it gains or loses by the amount by which the income that accrues is more or less than that estimated when precepts were set.	<b>NO</b>

### Council tax in Scotland

3.7 In Scotland there are no major preceptors with which to share council tax income. Amounts paid out by billing authorities to other bodies all take the form of levies on the authority (some of which are called 'requisitions' in Scotland) and which are fixed amounts.

## Conclusions

- 3.8 As a result of its review of accounting for NNDR and council tax in the core financial statements in England, Scotland and Wales, which is summarised in the tables above, CIPFA/LASAAC proposes the following.

### *NNDR income in England, Scotland and Wales (Table 1)*

A billing authority:

- (a) Should not include income in its Income and Expenditure Account for the NNDR it collects from taxpayers.
- (b) Should not include NNDR taxpayer debtor and creditor balances in its balance sheet.
- (c) Should include a creditor in its balance sheet for NNDR cash collected from taxpayers at the balance sheet date but not yet paid to the Government ('national pool') or a debtor for cash overpaid to the Government.
- (d) Should not include in the Cash Flow Statement as 'revenue activities' the cash received from NNDR debtors and payments into the national pool but should rather include the difference between the two amounts as an increase or decrease in other liquid resources.

Proposals (b) to (d) represent a significant change from the accounting policies currently followed by billing authorities in England, Scotland and Wales.

### *Council tax income in England (Table 2)*

- (e) A billing authority should not include any income in its Income and Expenditure Account for the council tax income relating to major preceptors' precepts.
- (f) For both billing authorities and major preceptors the council tax income credited to the Income and Expenditure Accounts should be their accrued council tax income for the year and the difference between this and the amount required by the Collection Fund regulations to be included in the General Fund should be included as a reconciling item in the Statement of Movement on the General Fund Balance.
- (g) Council tax debtor and creditor balances are not wholly assets and liabilities of the billing authority but should be carried in the relevant proportions on the balance sheets of the billing authority and major preceptors.
- (h) Relevant proportions of the net cash collected from council tax debtors belong to the major preceptors and that at the balance sheet date creditors or debtors should be recognised by the billing authority for cash not yet paid or overpaid respectively to major preceptors.
- (i) Major preceptors should recognise a debtor or creditor for the net cash collected on their behalf by the billing authority from council tax debtors and creditors but not yet paid to them, or overpaid, at the balance sheet date.
- (j) A billing authority should not include in the Cash Flow Statement as a 'revenue activity' the share of cash received from council tax payers attributable to major preceptors or the amounts paid to major preceptors as precepts (including the adjusting payment or receipt in respect of the previous year's surplus or deficit on the Collection Fund). Rather the difference between the two amounts should be included as an increase or decrease in 'other liquid resources'.
- (k) A major preceptor should include in its Cash Flow Statement as a 'revenue activity' the amount it receives from the billing authority in the form of

precept (including the receipt/payment for the previous year's Collection Fund surplus or deficit). The difference between this amount and its share of cash received by the billing authority from council tax debtors should be included as an increase or decrease in 'other liquid resources'.

Proposals (f) to (k) represent a significant change from the accounting policies currently followed by authorities in England.

*Council tax income in Wales (Table 3)*

- (l) The billing authority should include the whole accrued council tax income for the year in its Income and Expenditure Account including the amounts raised to cover major preceptors' (ie Police Authorities') precepts. The police authority precept should be shown as expenditure.
- (m) The billing authority should carry the council taxpayers' debtor and creditor balances including amounts relating to the major preceptor precepts in its balance sheet.

The practices followed by billing authorities in Wales varies with regard to proposal (l) with some billing authorities showing their council tax income net of the police authority precept. It is understood that all billing authorities in Wales already follow proposal (m).

**Council Tax Income in Scotland**

- (n) The billing authority should include the whole accrued council tax income for the year in its Income and Expenditure Account.
- (o) The billing authority should carry the council taxpayers' debtor and creditor balances in its balance sheet.

It is understood that all authorities in Scotland already follow the Exposure Draft SORP's proposals, which in effect would formalise in the SORP current practice.

**Accounting for NNDR and council tax in the core financial statements in England, Scotland and Wales**

*National non-domestic rates*

Q4 Do you agree that in England, Scotland and Wales billing authorities act as agents of their respective jurisdictions' Governments when collecting NNDR?

Q5 Do you agree that a billing authority:

- (a) Should not include income in its Income and Expenditure Account for the NNDR it collects from taxpayers?
- (b) Should not include NNDR taxpayer debtor and creditor balances in its balance sheet?
- (c) Should include a creditor in its balance sheet for NNDR cash collected from taxpayers at the balance sheet date but not yet paid to the Government ('national pool') or a debtor for cash overpaid to the Government?

If you disagree, please indicate the element(s) with which you disagree and your preferred treatment.

- Q6 Do you agree with CIPFA/LASAAC's proposals for including NNDR cash flows in the Cash Flow Statement?
- Q7 Do you have any comments on or suggestions for amending paragraphs 3.65e to 3.65j of the consultation SORP Exposure Draft, which cover NNDR? If so, please give them. It would be helpful if reasons are given and alternatives suggested for matters with which you disagree.
- Council tax (England)*
- Q8 Do you agree that in England a billing authority acts as an agent of its major preceptors when collecting the element of council tax relating to the major preceptors' council tax precepts?
- Q9 Do you agree that:
- (a) A billing authority should not include any income in its Income and Expenditure Account for the council tax income relating to major preceptors' precepts?
  - (b) For both billing authorities and major preceptors the council tax income credited to the Income and Expenditure Accounts should be their accrued council tax income for the year and that the difference between this and the amount required by the Collection Fund regulations to be included in the General Fund should be included as a reconciling item in the Statement of Movement on the General Fund Balance?
  - (c) Council tax debtor and creditor balances are not wholly assets and liabilities of the billing authority but should be carried in the relevant proportions on the balance sheets of the billing authority and major preceptors?
  - (d) Relevant proportions of the net cash collected from council tax debtors belongs to the major preceptors and that at the balance sheet date creditors or debtors should be recognised by the billing authority for cash not yet paid or overpaid respectively to major preceptors?
  - (e) Major preceptors should recognise a debtor or creditor for the net cash collected on their behalf by the billing authority from council tax debtors and creditors but not yet paid to them, or overpaid, at the balance sheet date?
- If you disagree, please indicate the element(s) with which you disagree and your preferred treatment.
- Q10 Do you agree with CIPFA/LASAAC's proposals for including council tax cash flows in the Cash Flow Statement?
- Q11 Do you have any comments on or suggestions for amending paragraphs 3.24a to 3.24p of the consultation SORP Exposure Draft, which cover council tax income in England? If so please give them. It would be helpful if reasons are given and alternatives suggested for matters with which you disagree.
- Council tax (Wales)*
- Q12 Do you agree that in Wales a billing authority acts as principal when collecting the element of council tax relating to the major preceptors' council tax precepts?

- Q13 Do you agree that a billing authority in Wales:
- (a) Should include the whole accrued council tax income for the year in its Income and Expenditure Account, including the amounts raised to cover major preceptors' (ie Police Authorities') precepts?
  - (b) Should carry the council taxpayers' debtor and creditor balances, including amounts relating to the major preceptor precepts, in its balance sheet?
- If you disagree, please indicate the element(s) with which you disagree and your preferred treatment.
- Q14 Do you agree with CIPFA/LASAAC's proposals for including council tax cash flows in the Cash Flow Statement?
- Q15 Do you have any comments on or suggestions for amending paragraphs 3.24r to 3.24u of the consultation SORP Exposure Draft, which cover council tax income in Wales? If so, please give them. It would be helpful if reasons are given and alternatives suggested for matters with which you disagree.
- Council tax (Scotland)*
- Q16 Do you have any comments on or suggestions for amending paragraph 3.24q of the consultation SORP Exposure Draft, which covers council tax income in Scotland? If so, please give them. It would be helpful if reasons are given and alternatives suggested for matters with which you disagree

#### 4 ACCOUNTING FOR RATES IN THE CORE FINANCIAL STATEMENTS IN NORTHERN IRELAND

- 4.1 In Northern Ireland the property tax is called rates and is levied on both domestic and non-domestic properties. Rates are collected by the Land and Property Services Agency, an executive agency of the Department of Finance and Personnel. The Land and Property Services Agency is clearly acting as an agent so the relevant question is not whether it acts as an agent or principal but whether the rate income it collects belongs to the Government or the local authority for the area. The main features of the rates system in Northern Ireland are:
- (a) As part of the budget setting process, district councils fix the rate for the next financial year that it estimates is needed to meet its budget requirement in terms of a penny rate product. This rate is based on both domestic and non-domestic properties and is levied at an amount in the pound. In addition there is regional rate set by the Government at an amount in the pound.
  - (b) Rates are collected from ratepayers by the Land and Property Services Agency.
  - (c) Similar to a major preceptor in England, an authority receives rate monies during the year in instalments (like a 'precept') from the Land and Property Services Agency based on an estimate of the income made when the rate was set. It also receives or pays an adjusting amount from or to the Land and Property Services Agency after the year end. This adjustment takes into account new properties, changes in valuations and write-offs of bad debts by means of a recalculation using a "final penny

product" rather than the "estimated penny product" used to set the rate. However, no amount is included in the adjustment in respect of an impairment allowance for doubtful debts.

- (d) Authorities do not include rates debtors in their Balance Sheets.
  - (e) Authorities include in their balance sheet as a debtor or creditor the 'final penny rate product' adjustment for the year notified by the Land and Property Services Agency so the amount of rate income included in the Income and Expenditure Account for the year is the amount receivable for the year from the Land and Property Services Agency.
- 4.2 The situation in Northern Ireland is different from both England and Wales and is not as clear-cut. Since no amount is included for impairment allowance for doubtful debts, the rate income receivable, unlike a major preceptor's council tax income in England, is not the accrued income for the year but a statutorily determined amount. Unlike in the case of a major preceptor in Wales, the authority does not receive a predetermined monetary amount; rather it receives an amount that will not be exactly the amount estimated when the budget was set since the actual penny rate product will be different from the estimated penny rate product.
- 4.3 In CIPFA/LASAAC's view, since the income receivable by local authorities is not the accrued rate income but a statutorily determined amount, the substance of the arrangement is that the local rate income accrues to the Government and authorities receive their 'rate income' from the Government in a similar way to which authorities in England receive redistributed NNDR.
- 4.4 The above accounting analysis is also consistent with the tenor of the legislation. The Rates (Northern Ireland) Order 1977 says under sections 9 and 34:

***"Levying of rates"***

*9 –(1) A regional rate and a district rate shall be levied by the Department in every district as if they were items of a single rate.*

*(2) For all purposes, including the purposes of section 4 of the Crown Debts (Ireland) Act 1781, the whole of the rate comprised of the terms mentioned in paragraph (1) shall be a debt due to the Crown."*

***"Payments to district councils on account of district rates"***

*34 –(1) The Department shall, in respect of each year, pay to each district council in accordance with regulations a sum equal to the product of a district rate made by the council for the year.*

*(2) The sum payable under this Article shall be charged on and issued out of the Consolidated Fund, and for the purposes of providing for such issues the Department may borrow money."*

**Conclusions**

- 4.5 As a result of its review of accounting for rates in the core financial statements in Northern Ireland, CIPFA/LASAAC proposes that:
- (a) The income credited to the Income and Expenditure Account in respect of rates for the year should be the amount receivable for the year from the Land and Property Services Agency.
  - (b) A debtor or creditor for the 'actual penny rate product' adjustment for the year that will be made by the Land and Property Services Agency in the following year should be included in the balance sheet.

It is understood that all authorities in Northern Ireland already follow the Exposure Draft SORP's proposals, which in effect would formalise in the SORP current practice.

#### **Accounting for rates in the core financial statements in Northern Ireland**

Q17 Do you agree that the income credited to the Income and Expenditure Account in respect of rates for the year should be the amount receivable for the year from the Land and Property Services Agency?

Q18 Do you agree that a debtor or creditor for the 'actual penny rate product' adjustment for the year that will be made by the Land and Property Services Agency in the following year should be included as a debtor or creditor?

#### **5 REMOVAL OF LARGER PARISH COUNCILS AND COMMUNITY COUNCILS FROM THE APPLICATION OF THE SORP**

5.1 The SORP is currently applicable to larger parish councils in England and larger community councils in Wales. The number of such larger councils is about 40. In England, these councils are ones that do not meet the requirements to be classified as 'smaller relevant authorities' because their gross income or expenditure (whichever is the higher) for the year concerned is, or for either of the two immediately preceding years was, £1 million or more. In Wales the concept of 'smaller relevant authority' has not been adopted but a similar '£1 million or more' threshold is applied to community councils. In addition, in Wales community councils with income or expenditure above £200,000 have the option to prepare their financial statements in accordance with the SORP.

5.2 One of the responses to the 2008 SORP was from the National Association of Local Councils (NALC), which raised the matter of whether the SORP should be applied to any parish council. Some of the reasons given by NALC why the present time was perfect to remove the whole of the parish council sector from the application of the SORP were:

- the expected removal of the Best Value Duty from all Parish and Town Councils in England (it has never applied in Wales), which would significantly reduce the number of councils to which the SORP applies (this has now been implemented)
- the Government initiative to de-regulate smaller bodies wherever possible
- the fact that Whole of Government Accounts will exclude the financial results of parish councils
- the higher thresholds applicable to lighter touch reporting approach in the private sector under the ASB's Financial Reporting Standard for Smaller Entities (FRSSE), which for example includes £6.5million 'turnover'.

5.3 One important additional reason to consider removing the application of the SORP not mentioned by NALC, is the planned adoption of an IFRS-based Code in 2010/11 and the burden of making the transition that this would place on a small entity like a parish or community council.

- 5.4 All parish councils in England and Community Councils in Wales are required by the two jurisdictions' respective Accounts and Audit Regulations to follow 'proper practices'. However, for all parishes and community councils, except the 40 or so larger ones, proper practices are not contained in the SORP but in *Governance and Accountability for Local Councils A Practitioners' Guide 2008 Edition (England)* and *Governance and Accountability for Local Councils: A practitioners' Guide 2008 (Wales)*. The Guide for England is prepared and maintained by the Joint Practitioners Advisory Group (JPAG) whose membership includes representatives of the Audit Commission, CLG, NALC, Society of Local Council Clerks, CIPFA, Wales Audit Office, Welsh Assembly Government and One Voice Wales. The Guide for Wales is prepared and maintained by the Local Council Audit Liaison Group (LCALG) whose membership includes representatives of the Wales Audit Office, the Assembly Government, One Voice Wales, the Society of Local Council Clerks, and auditors.
- 5.5 CIPFA/LASAAC finds the above arguments for removing the whole of the parish and community council sector from the application of the SORP persuasive and proposes that this should be implemented if an appropriate alternative source of 'proper practices' becomes available to take its place. Such a source of 'proper practices' is being developed by JPAG. The guidance is expected to draw on the FRSSE and is planned to be issued as an exposure draft for public consultation in Autumn 2008 and approved for publication in early 2009 as additional sections of *Governance and Accountability for Local Councils A Practitioners' Guide 2008 Edition (England)* and *Governance and Accountability for Local Councils: A Practitioners' Guide 2008 (Wales)* respectively.
- 5.6 CIPFA/LASAAC has consulted with stakeholders and has concluded that no amendment to legislation would be required to remove the parish and community council sector from the application of the SORP in England. A change to regulation in Wales is required to reflect this change and the matter is under consideration. In CIPFA/LASAAC's view, the change could be made by amending paragraphs 1.7 and 1.8 of the SORP as follows:
- 1.7** In England and Wales, the SORP is part of the 'proper practices' requirements governing the preparation of an authority's Statement of Accounts referred to in section 21 of the Local Government Act 2003. All authorities to which section 21 applies that are required to prepare a Statement of Accounts by the Accounts and Audit Regulations under section 27 of the Audit Commission Act 1998 or section 39 of the Public Audit (Wales) Act 2004, except larger parishes and larger community councils, therefore have a statutory duty to comply with SORP requirements. The SORP no longer applies to larger parish and community councils. From 1 April 2009 the 'proper practices' requirements governing the preparation of these bodies' accounts are contained in *Governance and Accountability for Local Councils A Practitioners' Guide 2008 Edition (England)* and *Governance and Accountability for Local Councils: A Practitioners' Guide 2008 (Wales)*.
- 1.8** In practice this definition includes principal councils, police authorities, fire and rescue authorities, the Greater London Authority and its functional bodies, ~~and the larger parish and community councils~~. More specialised bodies should check against the definitions to decide whether they are covered. It is expected that bodies covered by the Accounts and Audit Regulations requirements to prepare a Statement of

Accounts but not by the definition of proper practices in section 21 of the Local Government Act 2003 will adopt the SORP as a source of proper practices, unless adoption is ruled out by legislation or a more specialised accounting code applies to them.

5.7 The CLG and Welsh Assembly Government provide guidance to their respective Accounts and Audits Regulations that gives their interpretation of which documents contain the 'proper practices' to be followed with regard to the preparation of accounts. Therefore, in CIPFA/LASAAC's view, it would be appropriate to formally obtain confirmation from CLG and the Welsh Assembly Government, that they agree that the SORP should no longer be the source of 'proper practices' and that they confirm that their interpretation of which documents contain 'proper practices' from 1 April 2009 will be *Governance and Accountability for Local Councils A Practitioners' Guide 2008 Edition (England)* and *Governance and Accountability for Local Councils: A Practitioners' Guide 2008 (Wales)* respectively.

5.8 There is one further substantive reference to parish and community councils in paragraph 3.76 of the SORP, which concerns the applicability of defined benefit pension accounting to certain pension arrangements including those:

"(c) for town, parish and community councils and other minor non-principal authorities such as internal drainage boards preparing their accounts in accordance with the SORP, the local government pension scheme, unless contributions are set on the basis of the authority's specific circumstances."

CIPFA/LASAAC proposes that the reference to "town, parish and community councils" in paragraph 3.76 of the SORP should also be removed as a consequential amendment.

5.9 The SORP currently refers to "internal drainage boards" (IDBs) in paragraph 3.76. CIPFA/LASAAC also proposes to remove this reference since the SORP is no longer the source of 'proper practices'. There is now specialised guidance that is recognised as the source of non-statutory proper practices for the preparation of IDB financial statements.

#### **Removal of larger parish and community councils from the application of the SORP**

Q19 Do you agree that the larger parish and community councils should be removed from the application of the SORP if an appropriate alternative source of 'proper practices' becomes available to take its place for the 2009/10 year of account?

Q20 Do you agree that in England the Joint Practice Advisory Group and the Local Authority Audit Liaison Group in Wales, which are currently the bodies that prepare the non-statutory 'proper practices' guidance for the preparation of accounts by all local and community councils except the 40 or so larger parish and community councils, are the appropriate bodies to prepare guidance for the larger parishes and community councils? If not, please give your reasons and preferred alternative.

Q21 Do you agree that paragraph 3.76 of the SORP should be amended to delete references to *“town, parish and community councils”* and *“internal drainage boards”*?

## 6 ACCOUNTING FOR REORGANISED LOCAL AUTHORITIES

- 6.1 A number of local government reorganisations will take effect on 1 April 2009. This raises the questions of how to account for such reorganisations. CIPFA/LASAAC therefore proposes to provide guidance in this area in the 2009 SORP.
- 6.2 Under UK GAAP there are two methods for accounting for transfers of the whole or part of an entity – acquisition accounting and merger accounting. Under acquisition accounting, assets and liabilities are transferred at fair value at the transfer date, and the difference between any consideration given and the net assets or liabilities is treated as goodwill. Under merger accounting, the assets and liabilities of the entities (or parts of the entities) are simply added together to provide the opening balance sheet position.
- 6.3 The central government Financial Reporting Manual – and therefore the Whole of Government Accounts – views such transfers of function as “machinery of government” changes. Reorganisations are accounted for in the same manner as a group restructuring using merger accounting. CIPFA/LASAAC considers that the same rationale also applies to local government reorganisation, as these are not changes that the authorities themselves can effect, but require legislation.
- 6.4 The 2009 SORP Exposure Draft therefore proposes that authorities account for local government reorganisation in the same manner as a group restructuring. Authorities subject to local government reorganisation will reflect the transfer of assets and liabilities and the consequential changes to reserves in a restated opening balance sheet. Assets and liabilities will be transferred at their carrying amount at the transfer date (effectively the closing balance sheet immediately prior to the reorganisation – 31 March 2009 for reorganisations taking effect on 1 April 2009). The transfers will need to be reported in the Statement of Total Recognised Gains and Losses and the notes to the accounts. However, gains or losses on the transfer of assets and liabilities will not be reported through the Income and Expenditure Account.

### **Accounting for reorganised local authorities**

Q22 Do you agree that local government reorganisation should be treated as a “machinery of government” change, and accounted for in the same manner as a group restructuring using merger accounting?

Q23 Do you agree that transfers should be reported in a restated opening balance sheet, and not through the Income and Expenditure Account?

## 7 OTHER MINOR CHANGES

### **Financial reporting standards**

- 7.1 No new Financial Reporting Standards (FRSs) or UITF Abstracts have been issued since 30 September 2007. There has been a minor amendment to FRS 20 *Share-*

*based Payment* to clarify accounting for cancellation of share options by the employer; and a minor amendment to *FRS 25 Financial Instruments: Presentation* relating to the equity/liabilities classification of certain puttable financial instruments issued by an entity that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation. Neither amendment affects entities like local authorities that do not issue equity instruments. It is proposed that no amendment is made to the SORP in respect of these amendments.

- 7.2 A new development in accounting standards setting is that the International Accounting Standards Board (IASB) under its 'annual improvement process' issued in May 2008 *Improvements to IFRSs*, which made minor amendments to a number of IFRSs. The ASB has issued a Financial Reporting Exposure Draft (FRED) *Improvements to Financial Reporting Standards* in response. The proposals set out in the FRED implement into UK converged standards the IASB *Improvements to IFRS* and make consequential amendments to UK FRS arising from IFRS and also proposes minor amendments which have been identified to apply to UK FRS only. The closing date for comments on the FRED was 27 September 2008. The consultation responses are currently being considered by the ASB and the FRS had not been issued at the date of issuing the 2009 SORP ITC. However, the FRS is expected to be issued shortly.
- 7.3 The annual improvement processes of both the ASB and IFRS are intended to be used for minor and uncontroversial amendments in order to clarify rather than change standards. In CIPFA/LASAAC's view, the proposals in the FRED would have little if any impact on the 2009 SORP and in turn on local authority accounting. The FRED can be viewed by clicking the following link:
- <http://www.frc.org.uk/images/uploaded/documents/FRED%20Web%20optimized%20FINAL.pdf>
- 7.4 CIPFA/LASAAC proposes that if (as expected) *Improvements to Financial Reporting Standards* is issued shortly as an FRS, it should consider further whether there are any matters that could usefully be included as minor clarifying amendments in the 2009 SORP.

### **Unapplied grants reserve**

- 7.5 A stakeholder has suggested that the reference to the 'unapplied grant reserve' referred to in SORP paragraph 3.103 is no longer appropriate. The stakeholder suggested that 'unapplied grant reserve' be amended to 'unapplied grant account'. The change is in line with recent SORP naming conventions, eg the change of name of the now defunct Fixed Asset Restatement Reserve to Fixed Asset Restatement Account a few years ago, as well as the naming of the recently established Capital Adjustment Account. CIPFA/LASAAC proposes that paragraph 3.103 is amended as follows:

**3.103** In Wales the Major Repairs Allowance should be credited to an unapplied grant reserveaccount when it becomes receivable. When the reserveaccount is applied to new expenditure, the authority should consider whether it would be relevant to transfer the amount to Government Grants Deferred – otherwise it will be credited to the Capital Adjustment Account.

**Other minor changes**

*Financial reporting standards*

Q24 Do you agree that there are no financial reporting standards developments that need to be included in amendments to the SORP?

Q25 Do you agree that if *Improvements to Financial Reporting Standards* is issued shortly as an FRS, CIPFA/LASAAC should consider further whether there are any matters that could usefully be included as minor clarifying amendments in the 2009 SORP?

*Unapplied grants reserve*

Q26 Do you agree with changing the name of the unapplied grant reserve to unapplied grant account?

8 MATTERS NOT COVERED BY THE 2009 SORP INVITATION TO COMMENT

8.1 If you consider that there are additional amendments that need to be made to the 2009 SORP, CIPFA/LASAAC would be pleased to consider these.

**Matters not covered by the 2009 SORP invitation to comment**

Q27 Do you consider that there are additional amendments that need to be made to the 2009 SORP? If so, please give details of the matter.

## APPENDIX A

### REGULATIONS/STATUTORY GUIDANCE THAT HAS BEEN ISSUED FOR ENGLAND AND WALES REGARDING FINANCE LEASES AND PFI

#### Capital finance regulations

- 1 Very similar changes have been made to the Capital Finance and Accounting Regulations of both England and Wales. Rather than setting out detailed provisions in their respective regulations for determining the Minimum Revenue Provision for the year, the new requirement is for the authority to determine an amount of minimum revenue provision "*which it considers to be prudent*".
- 2 'Statutory guidance' on what would constitute a prudent Minimum Revenue Provision for the year is set in statutory instrument 2008/414 for England and statutory instrument 200/588 (W59) for Wales. Paragraph 20 of the statutory guidance for both England and Wales, which deals with Finance Leases and PFI, is identical for England and Wales and say:

***"FINANCE LEASES AND PFI***

*20. In the case of finance leases and on balance-sheet PFI contracts, the MRP requirement would be regarded as met by a charge equal to the element of the rent/charge that goes to write down the balance sheet liability. Thus, Option 3 will apply in modified form."*

- 3 The 'informal commentary' on the statutory guidance at paragraphs 40 of the England and paragraph 39 of the Wales documents also comment on the statutory guidance in identical terms. The England paragraph is shown below:

***"FINANCE LEASES AND PFI [paragraph 20]***

*40. The effect of the guidance here is to ensure that the combined impact of the finance charge and MRP for finance leases and on-balance sheet PFI schemes is equal to the rental or service charge payable for the year. This will ensure that, if the impending move to International Financial Reporting Standards in local government has the effect of bringing more PFI schemes on balance sheet, there will be no effect on the charge to the revenue account. However, the Department will, if necessary, issue further guidance when the accounting implications of that change become clearer."*