

REPORT

CL 05 03-09

Committee	CIPFA/LASAAC LOCAL AUTHORITY CODE BOARD
Venue	Robert Street, London
Date	6 March 2009
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Subject	New Sections of Draft 2010 IFRS-Based 'Code'

Issue:	<p>To consider the IFRS-based Code of Practice on Local Authority Accounting, specifically in relation to:</p> <p><i>Principles already discussed</i></p> <p>(a) Retirement Benefit Plans</p> <p><i>No or limited changes to the SORP requirements</i></p> <p>(b) Employee Benefits - Introduction (c) Employee Benefits – Post Employment Benefits (d) Inventories (e) Work in Progress (Construction Contracts) (f) Revenue Recognition (g) Trade and other Receivables</p> <p><i>New material</i></p> <p>(h) Cash and Cash Equivalents (i) Biological Assets (Agriculture)</p>
Impact on guidance:	The Local Authority SORP is to be replaced from 2010/11; content will be included in the IFRS-Based Code of Practice on Local Authority Accounting
IAS/IFRS compliant?	Yes, except for the same interpretations as the i-FReM in respect of (c), (e) and additional interpretations in respect of (a), (d), (f) and (g)

IPSAS compliant?	Yes, except for the same interpretation as in the i-FReM in respect of (c).
SORP consistent?	Yes, except for differences in respect of (a), (c), (d), (h), and (i).
i-FreM consistent?	Yes, except for differences in respect of (a), (d), (f), and (g).
Impact on Taxation	No, except for (c); other possible impacts on taxation in (d) (e) and (i) are expected to be infrequent and insignificant.
Recommendation:	That the Board approves: <ul style="list-style-type: none"> (i) the proposed IAS/IFRS and IPSAS adaptations/ interpretations arising from the local authority context and SORP differences; and (ii) the attached sections of the draft IFRS-based Code of Practice on Local Authority Accounting.
Timing:	2010/11

DETAIL

Background

1. At its meeting held on 15 April 2008, CIPFA/LASAAC agreed the format and structure of the IFRS-based Code of Practice.
2. This report considers the sections of the draft IFRS-based Code of Practice on Local Authority Accounting listed above. The report considers these sections on an exceptions basis, with any differences from IAS / IFRS, IPSAS and the i-FReM highlighted for consideration. Differences from the SORP, and any possible impact on taxation are also highlighted for information. CIPFA/LASAAC is asked to consider and approve the sections of the draft IFRS-based Code, or suggest amendments.

Sections of the Code

Principles already discussed

(a) Retirement Benefit Plans

IAS/IFRS compliant?	Yes except that Pension Fund accounts for Police and Fire and Rescue Services are based on statutory requirements, and that a restriction is placed on the option to include pension liabilities in the financial statements.
IPSAS compliant?	N/A (no IPSAS yet on retirement benefit plans).

SORP consistent?	Yes, except for the additional requirement that the “the actuarial present value of promised retirement benefits” be disclosed.
i-FreM consistent?	Yes, with the exception that the i-FReM specifies the presentation of the pension liabilities whereas the Code retains the options set out in IAS 26.
Impact on Taxation	None.

3. IAS 26 does not require pension fund accounts to be prepared but specifies the requirements if they are prepared. The Code requires pension fund administering authorities for the LGPS schemes to prepare IAS 26 compliant Pension Fund Accounts. This is in line with the i-FReM, where the major pension schemes are required to report under IAS 26.

4. The Code requires Police and Fire and Rescue Service Authorities in England and Wales to prepare Pension Fund accounts based on statutory requirements. However, as these accounts are presented within the authority’s accounts rather than as separate entity accounts, it is arguable that they are outside the scope of IAS 26.

5. The requirements of IAS 26 are generally consistent with the existing SORP requirements, with one exception. IAS 26 requires pension liabilities to be disclosed in the pension fund accounts, with the SORP does not. Three options are permitted; inclusion in the financial statements, inclusion in the notes to the accounts, or by reference to an actuarial report. The Code permits all three options. The i-FReM interprets IAS 26 by removing the last two options and requires pension schemes to include the pension liabilities in the financial statement.

6. The Code does not include this interpretation, as the Secretariat feels that the practice of triennial valuations for the pension fund would lead to difficulties. IAS 26 permits the latest valuation to be used, even where this precedes the balance sheet date. With triennial valuations, it would be possible for assets to be valued as at the balance sheet date but liabilities to be valued at an earlier date – perhaps two years earlier. In these circumstances, the Secretariat believes disclosure in the notes to the accounts or by reference to the actuarial report would be more appropriate as the timing difference could be addressed. To achieve this, the Code requires that where pension liabilities are included in the financial statements, the valuations are at the balance sheet date.

No or limited changes to the SORP requirements

(b) Employee Benefits - Introduction

IAS/IFRS compliant?	Not applicable – introduces IAS 19 and contains definitions of terms common to the three substantive IAS 19 based sections of the Code on Benefits Payable During Employment, Termination Benefits and Postemployment Benefits.
IPSAS compliant?	As above.

SORP consistent?	As above.
i-FReM Consistent?	As above
Impact on Taxation	As above

7. This section provides an introduction to the requirements of IAS 19, as the scope of this standard goes beyond that of the equivalent UK standard (FRS 17) and that of the SORP. As an introduction, this section does not include any accounting requirements.

(c) Employee Benefits – Postemployment Benefits

IAS/IFRS compliant?	Yes, except for: <ul style="list-style-type: none"> (a) The use of the 'corridor approach' is not permitted. (b) The Code requires the Teachers' pension schemes and the LGPS in the case of minor non-principal authorities to be accounted for as if they are defined contribution schemes. (c) The Code has adopted the term 'entity combination' in accordance with <i>IPSAS 25</i> Employment Benefits rather than the IAS 19 terminology of 'business combination'. (d) The Code interprets "sufficient regularity" in respect of the valuation of pension liabilities.
IPSAS compliant?	Yes, except for: <ul style="list-style-type: none"> (a) The use of the 'corridor approach' is not permitted. (b) The Code requires the Teachers' pension schemes and the LGPS in the case of minor non-principal authorities to be accounted for as if they are defined contribution schemes. (c) The Code interprets "sufficient regularity" in respect of the valuation of pension liabilities.
SORP consistent?	Yes except for the change in classification of the Northern Ireland Local Government Officers Superannuation Scheme (NILGOSS) to one that is required to be accounted for on a defined benefit basis.
i-FReM consistent?	Yes
Impact on Taxation	No impact on taxation would be expected in England, Scotland and Wales. In Northern Ireland the change from a defined contribution basis of accounting to a defined benefit basis of accounting would impact on taxation without the introduction of similar legislation to that in force in England, Scotland and Wales, which requires the

pension costs charged to the General Fund to be *"the amount payable for the year in accordance with statutory requirements governing the particular pension schemes or funds in which the authority participates."*

8. IAS 19 and IPSAS 25 permit the use of the 'corridor approach', where actuarial gains and losses falling outside an agreed 'corridor' are recognised in the Income and Expenditure Account. The Code, in line with the i-FReM, does not permit this approach to be used.

9. The Teachers' pension Schemes for England and Wales and Scotland, which provide defined benefit pensions to employees, has been classified by the Code as one where participating authorities shall account for their participation as if it were a defined contribution scheme. Similarly for the Local Government Pension Scheme the Code requires the participation of minor non-principal authorities in the scheme to be accounted for as if it were a defined contribution scheme unless contributions are set on the basis of the authority's specific circumstances.

10. IAS 19 requires the present value of the defined benefit obligation and fair value of any plan assets to be determined with *"sufficient regularity"*. An interpretation of the minimum requirements with respect to this is included in the Code.

11. The SORP classifies the Northern Ireland Local Government Officers Superannuation Scheme (NILGOSS) as a scheme to be accounted for as if it were a defined contribution scheme. The scheme does not meet the criteria in IAS 19 to be classified as such a scheme, and under the Code, the scheme is classified as a defined benefits scheme.

12. Without a regulation similar to that in England, Wales and Scotland (where the amount chargeable to the General Fund for providing pension benefits for employees is the amount payable for the year in accordance with the statutory requirements) there would be an impact on taxation. The need for legislation on the matter for Northern Ireland is being considered by the Northern Ireland Department of the Environment.

(d) Inventories

IAS/IFRS compliant?	Yes, except for adoption of two additional specific measurement requirements from IPSAS 12
IPSAS compliant?	Yes
SORP consistent?	Yes, except for adoption of two additional specific measurement requirements from IPSAS 12 and the measurement of inventories purchased on deferred settlement terms
i-FReM consistent?	Yes, except for adoption of two additional specific measurement requirements from IPSAS 12

Impact on Taxation	Adoption of IFRS may lead to items being recognised in different periods to the SORP, but this is expected to occur infrequently and be insignificant.
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13. The draft Code and the i-FReM follow IAS 2, with inventories being measured at the lower of cost and net realisable value. In addition the draft Code adopts two additional measurements for inventories from IPSAS 12: *'inventories acquired through a non-exchange transaction their cost shall be measured at their fair value as at the date of acquisition'* and *'inventories shall be measured at the lower of cost and current replacement cost where they are held for distribution at no charge or for a nominal charge; or consumption in the production process of goods to be distributed at no charge or for a nominal charge'*. These two additional measurements for inventories are not covered in the SORP but are relevant to local government, and are intended to produce better estimates than IAS 2 in these circumstances; for example following IAS 2 for non-exchange transactions could result in inventories being carried at a nil or nominal amount.

14. The draft Code requires the financing element of inventories purchased on deferred settlement terms to be recognised in order to reflect the substance of the transaction. The SORP is silent on this issue although the measurement is implicit in FRS 26.

15. CIPFA/LASAAC are asked to note that the account to be used to record inventories acquired through a non-exchange transaction, in the final version of the Code will depend upon the work that is currently being undertaken by HM Treasury and CIPFA with regard to the accounting and presentation of non-exchange transactions under IAS 2 and IPSAS 23. An oral update of this work will be given at item 8 on this agenda.

(e) Work in Progress (Construction Contracts)

IAS/IFRS compliant?	Yes, except for the expansion to the scope and definition of construction contracts, and clarification of when expected losses shall be recognised, from IPSAS 11
IPSAS compliant?	Yes
SORP consistent?	Yes
i-FReM consistent?	Yes
Impact on Taxation	Adoption of IFRS may lead to items being recognised in different periods to the SORP, but this is expected to occur infrequently and be insignificant.

16. The draft Code and the i-FReM follow IAS 11. The draft Code includes 'cost based' and 'non-commercial contracts' within the scope of construction contracts which also include 'binding arrangements' within its definition. These adaptations which follow IPSAS 11 are relevant to local government, and are intended to cover the scope and types of construction contracts that may occur in the public sector.

17. The draft Code adopts IPSAS 11 in respect of recognition of expected losses, which makes it clear that the requirement to recognise an expected deficit on a contract immediately it becomes probable that contract costs will exceed total contract revenues applies only to contracts in which it is intended at **inception** of the contract that contract costs are to be fully recovered from the parties to that contract.

(f) Revenue Recognition

IAS/IFRS compliant?	Yes, except for the interpretation of IAS 39 in respect of the measurement of revenue arising from non-exchange transactions
IPSAS compliant?	Yes
SORP consistent?	Yes
i-FReM consistent?	Yes, except for the interpretation of IAS 39 in respect of the measurement of revenue arising from non-exchange transactions
Impact on Taxation	No impact on taxation

18. The draft Code and i-FReM follow IAS 18 in respect of revenue recognition. The draft Code follows IPSAS 9 and the relevant elements of IPSAS 23.

19. The draft Code includes an interpretation of IAS 39, which has a direct impact on the measurement of revenue, where revenue arising from non-exchange transactions (i.e. council tax) shall be measured at the full amount receivable. This is because, for non-exchange transactions, there can be no difference between the delivery and payment dates; IPSAS 23 reflects this by not requiring taxation revenue to be discounted. This interpretation follows the SORP; the i-FReM is silent on this issue.

(g) Trade and other Receivables

IAS/IFRS compliant?	Yes, except for the interpretation of IAS 39 in respect of the measurement of trade and other receivables arising from non-exchange transactions
IPSAS compliant?	Yes
SORP consistent?	Yes
i-FReM consistent?	Yes, except for the interpretation of IAS 39 in respect of the measurement of trade and other receivables arising from non-exchange transactions
Impact on Taxation	No impact on taxation

20. The draft Code follows IAS 18 in respect of trade and other receivables. The draft Code follows IPSAS 9 and the relevant elements of IPSAS 23. The i-FReM does not specifically deal with trade and other receivables but does cover income recognition, where IAS 18 is applied in full.

21. As in (f) above, the draft Code includes an interpretation of IAS 39, in terms of the measurement of trade and other receivables.

New material

(h) Cash and Cash Equivalents

IAS/IFRS compliant?	Yes
IPSAS compliant?	Yes
SORP consistent?	Yes, except for the movement of 'cash' in the balance sheet and cash flow position includes cash equivalents
i-FReM consistent?	Yes
Impact on Taxation	No impact on taxation

22. The draft Code implements the requirements of IAS 7 and IPSAS 2 in full with no adaptations or interpretations. The accounting requirements in the draft Code are therefore consistent with those in the i-FReM.

23. The draft Code includes cash equivalents within the movement of 'cash' in the balance sheet and cash flow position. The SORP does not include cash equivalents within the movement of 'cash', and is likely to classify such items as short-term investments on the balance sheet and management of liquid resources on the cash flow statement.

(i) Biological Assets (Agriculture)

IAS/IFRS compliant?	Yes
IPSAS compliant?	N/A (no IPSAS yet on biological assets)
SORP consistent?	N/A – new requirement
i-FReM consistent?	Yes
Impact on Taxation	In theory the measurement of biological assets held for agricultural purposes at fair value through profit or loss could result in increases or decreases to the General Fund. In practice, authorities will only hold such assets exceptionally, and any impact on taxation is expected to be immaterial.

24. Whilst IAS 41 is only expected to apply to local authorities in exceptional cases, the draft Code requires, in line with the i-FReM, that it is applied in full. The draft Code clarifies, again in line with the i-FReM, that biological assets that are not held for agricultural purposes are not subject to IAS 41.

25. This is a new requirement in the IFRS-based Code, as there is no equivalent treatment in UK GAAP and hence the matter is not covered by the SORP.

Recommendation

26. The Board is requested to approve:

- (i) the proposed IAS / IFRS and IPSAS adaptations / interpretations arising from the local authority context and differences from the i-FReM; and
- (ii) the sections of the draft Code of Practice on Local Authority Accounting covering the above sections.