

## BVACOP 2008

### Consultation on Proposed Changes to the Section 2: The Definition of Total Cost

#### INTRODUCTION

- 1 CIPFA is committed to keeping BVACOP up to date by reviewing it each year and developing it in response to:
  - changes in the external environment, including legislative changes and changes in the SORP<sup>1</sup>; and
  - suggestions made for the improvement or clarification of specific issues.
  
- 2 An earlier consultation proposed amending the dates to which BVACOP applied, with the intention of aligning future editions of BVACOP with financial years, after a transition period. Responses to this consultation supported the proposal, and BVACOP 2008 will (subject to approval) commence this process. This consultation paper therefore puts forward the changes proposed to the BVACOP definition of 'Total Cost' that will be mandatory for authorities in preparing financial information for the following:
  - 2008/09 Performance Indicators
  - 2008/09 Statements of Accounts
  - 2009/10 Budgets
  - 2009 Performance Plans, Improvement Plans or Summaries
  - 2009/10 Performance Indicators
  - 2009/10 Statements of Accounts
  
- 3 The main proposed changes to Section 2: The Definition of Total Cost relate to:
  - **Revenue Expenditure Funded from Capital under Statute** – the 2008 SORP replaced the concept of deferred charges with a revised accounting treatment for revenue expenditure funded from capital under statute. This term covers expenditure that legislation allows to be classified as capital for funding purposes when it does not result in the expenditure being carried on the Balance Sheet as a fixed asset, for example improvement grants. It is proposed that these amounts are charged to the relevant service revenue accounts. As a consequence of this change in accounting treatment, it is also proposed that expenditure is recorded in the subjective group in the Recommended Standard Subjective Analysis to which the expenditure relates rather than in group 8 Depreciation and Impairment Losses.

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<sup>1</sup> Code of Practice on Local Authority Accounting in the United Kingdom, A Statement of Recommended Practice (produced each year by the CIPFA/LASAAC Joint Committee)

- **Trading Accounts and Trading Operations** – BVACOP provides guidance on accounting for trading accounts and trading operations. It is proposed to extend this guidance in relation to charges made by local authorities for providing trading companies with services, supplies, work and facilities. It is also proposed to remove continuing compulsory competitive tendering (CCT) arrangements from the list of trading operations run by local authorities.
  - **Costs associated with abortive capital projects** – the SORP does not allow costs associated with abortive capital projects to be capitalised; instead the costs must be charged to the Income and Expenditure Account. It is proposed to clarify the accounting treatment for these costs by requiring them to be charged to the relevant Service Revenue Account.
- 4 The consultation on the 2009 SORP is expected to incorporate the IFRS-based accounting treatment for PFI arrangements. Whilst this will not alter the definition of total cost, it would lead to expenditure under a PFI scheme being classified under different groups in the Recommended Standard Subjective Analysis, and would result in different charges to Service Revenue Accounts.
- 5 CIPFA would welcome comments and feedback on any aspect of this consultation paper or BVACOP generally but the questions at the end of this consultation paper on the proposed change may assist respondents.

#### **Responding to the Consultation**

- 6 Responses to this consultation paper should be sent preferably by email (paul.mason@cipfa.org) to:

Paul Mason  
CIPFA  
3 Robert Street  
London WC2N 6RL

To arrive no later than noon on **31 December 2008**.

- 7 During the consultation period, any questions or queries about the changes proposed should be directed to Paul Mason on:

Telephone 0207 543 5691  
Or e-mail paul.mason@cipfa.org

## **CONSULTATION ON SECTION 2: THE DEFINITION OF TOTAL COST IN THE PROPOSED 2008 BVACOP**

### THE PURPOSE OF 'TOTAL COST'

- 8 'Total cost' is a key BVACOP concept. It was established to provide a consistent basis for all statutory financial disclosures in relation to Best Value including Performance Plans in England and Improvement Plans in Wales, and performance indicators. Total cost must also be used for reporting the cost of services in the Income and Expenditure Account.

### REVENUE EXPENDITURE FUNDED FROM CAPITAL UNDER STATUTE

- 9 Before the 2008 SORP, expenditure that legislation allowed to be classified as capital for funding purposes when it did not result in the expenditure being carried on the Balance Sheet as a fixed asset was classed as a deferred charge. Deferred charges were initially recognised in the Balance Sheet, and then amortised to the Income and Expenditure Account. In recent years, this amortisation has taken place in the year in which the expenditure was incurred, with the result that no deferred charges were carried on the Balance Sheet.
- 10 The 2008 SORP has taken the next logical step in accounting for this expenditure in accordance with proper accounting practice. The concept of deferred charges has been replaced by revenue expenditure funded from capital under statute. Such expenditure is now to be treated in accordance with proper practice and charged to the Income and Expenditure Account. It is proposed that these amounts are charged to the relevant service revenue accounts. As a consequence of this change in accounting treatment, it is also proposed that expenditure is recorded in the subjective group in the Recommended Standard Subjective Analysis to which the expenditure relates rather than in group 8 Depreciation and Impairment Losses.

### TRADING ACCOUNTS AND TRADING OPERATIONS

- 11 BVACOP provides guidance on accounting for trading accounts and trading operations. The guidance covers the identification of trading accounts and operations, disclosure requirements and the treatment of significant balances on trading accounts for services provided internally. It is proposed to extend this guidance in relation to charges local authorities may make for providing legally separate trading companies with services, supplies, work and facilities. The guidance would recommend authorities consider charging companies with contributions to the corporate and democratic core and to non-distributed costs, and where they do so, recommend they ensure that charges to trading companies are based on total cost plus contributions to corporate and democratic core (CDC) costs and non-distributed costs (NDC).
- 12 BVACOP has previously identified six main types of trading operation that may be run by authorities. One of these types was continuing compulsory competitive tendering (CCT) arrangements. As the legislation regarding CCT was repealed a number of years ago and any continuing arrangements will have been subsequently re-tendered, it is proposed to remove this type of operation from

the list identified in BVACOP.

#### COSTS ASSOCIATED WITH ABORTIVE CAPITAL PROJECTS

- 13 The SORP does not allow costs associated with abortive capital projects to be capitalised; instead the costs must be charged to the Income and Expenditure Account. This accounting treatment has been required for a number of years, but recently questions of how such costs should be accounted for under total cost have arisen. It is proposed to clarify the accounting treatment for these costs by requiring them to be charged to the relevant Service Revenue Account.

#### INTRODUCTION OF IFRS-BASED ACCOUNTING FOR PFI ARRANGEMENTS

- 14 It is expected that the consultation on the 2009 SORP will incorporate the IFRS-based accounting treatment for PFI arrangements. This would bring most assets on to the Balance Sheet, along with a related liability. The payments made under the arrangement would need to be split into three elements – repayment of the liability (not charged to the Income and Expenditure Account), financing charge (interest – charged to a corporate account) and the service charge (charged to the service revenue account). In addition, the Service Revenue Account would be charged with depreciation, which would be reversed in the Statement of Movement on the General Fund Balance and replaced by a provision to repay the liability (e.g. MRP in England and Wales). Currently payments for supplies and services under a PFI arrangement are included in Group 4 Supplies and Services of the Recommended Standard Subjective Analysis. If the new arrangements are approved as part of the 2009 SORP, then from 1 April 2009 only the service charge element of the payment would be included in this group. Depreciation would be included in Group 8 Depreciation and Impairment Losses, and the interest element would be included in Group 10 Capital Financing Costs (Not Included in the Net Cost of Services).

#### INVITATION TO COMMENT QUESTIONS

Q1	Do you agree that revenue expenditure funded from capital under statute should be included in the definition of total cost?
Q2	Do you agree that continuing compulsory competitive tendering (CCT) arrangements are no longer applicable for local authorities?
Q3	Do you agree that costs associated with abortive capital projects should be charged to the relevant Service Revenue Account?
Q4	Do you agree that if the 2009 SORP introduces the IFRS-based accounting arrangements for PFI schemes, the various elements of the payments made will need to be accounted for as set out in paragraph 14 of this consultation paper and Chapter 9, Section 4 of the proposed BVACOP?