

## REPORT TO AUDIT AND PERFORMANCE REVIEW PANEL

Title: **Adoption of International Financial Reporting Standards (IFRS)**

Date: **18<sup>th</sup> February 2010**

Member reporting:

Contact officers: **Andrew Brooker, Richard Bunn**

### 1. SUMMARY

This report presents the draft transition balance sheet under IFRS, and other key areas for consideration by the Borough once IFRS is adopted as primary GAAP.

### 2. RECOMMENDATION

**The findings of this report are duly noted.**

What will be different for residents as a result of the adoption of IFRS?
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CIPFA has just issued the CODE for IFRS (replacing SORP 2009 under UK GAAP) and further guidance is still required. The expectation, however, is that the transition adjustments and any other changes necessary for ongoing IFRS reporting, will not impact the general fund.
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### 3 SUPPORTING INFORMATION

#### 3.1 Background

In accordance with Government regulations all local Governments will adopt IFRS from 1 April 2010. The first set of Financial Statements produced under IFRS will be for the year ending 31 March 2011 (2010/11). These accounts will also present a restated comparative year (2009/10) under IFRS. The start of the comparative period is the **transition date** for IFRS reporting which is 1 April 2009.

In line with LAAP Bulletin 80 the Borough has produced its draft transition Balance Sheet under IFRS (target date under the bulletin 31 December 2009). The Borough has produced this based on the current guidance available from CIPFA. As further guidance becomes available, the Borough will revalidate the draft adjustments and update the transition balance sheet accordingly.

### 3.2 Transition balance sheet – 1 April 2009

A draft transition balance sheet is attached as Appendix 1. The start point for this is the UK GAAP accounts presented in an IFRS format as shown in appendix 2.

The IFRS transition adjustments are as follows:

- **IAS 19 - Employee benefit accrual £4,724K**  
The Borough has included an accrual for employee benefits (principally holiday pay) in accordance with IAS 19. This accrual has been charged to a separate employee benefit reserve at the date of transition so that it does not impact the general fund.
- **IAS 40 - Investment properties**  
A £40K adjustment is required to eliminate the revaluation reserves relating to investment properties (under IFRS any changes in value are recognised in the income and expenditure account and then reversed out to the Capital Adjustment Account).
- **IAS 1 – Presentation of Financial Statements**  
A £25,780K adjustment to reclassify investments (bank deposits) as “cash and cash equivalents”. This adjustment relates to short term (less than 3 months maturity) low risk investments which under IFRS should be classified as “cash and cash equivalents”.
- **IAS 1 – Presentation of Financial Statements**  
A £545K adjustment to reclassify investments (other deposits) as “cash and cash equivalents” – as per above.
- **IAS 1 – Presentation of Financial Statements**  
The reported bank overdraft position of £12,405K (relating to unpresented cheques) will be included as part of borrowings, in line with best practice under IFRS.
- **IAS 20 - Accounting for Government Grants**  
Deferred grants and contributions of £35,483K have been transferred to the capital adjustment account in line with CIPFA guidance. The guidance essentially provides that grants are recognised in their entirety (once received and any conditions are met), rather than deferred and then recognised over the life of the asset.
- **IAS 20 - Accounting for Government Grants**  
Grants and contributions not yet applied of £21,691K have been reclassified from creditors to a separate “grants unapplied creditor” account in line with CIPFA guidance.

## **IFRS - impact on adoption as Primary GAAP**

The Borough will adopt IFRS as its primary GAAP from 1 April 2010. The main areas for consideration by the Borough are as follows:

### **Property plant and equipment (previously fixed assets)**

Key issues are as follows:

- IAS 16 requires revaluations to be at “fair value” rather than “market value”. CIPFA’s guidance suggests that the existing market values (at existing use) will essentially equate to fair value.
- The CODE will adopt the component accounting requirements of IAS 16. The Borough has not previously adopted component accounting. In accordance with CIPFA guidance this can be adopted prospectively from 1 April 2010.
- Impairments/revaluations are taken to the revaluation reserve where there is a balance on the revaluation reserve, thereafter they are recognised in the income & expenditure account. Previously under UK GAAP impairments were charged to the revaluation reserve or STRGL depending on their nature.

### **Investment properties**

Investment properties will be similarly revalued to “fair value”, however this will be on a “highest and best” use basis. Revaluation gains/losses on investment properties will be recognised in the income and expenditure account, these will then be reversed out of the general fund to the capital adjustment account. There is therefore no revaluation reserve for investment properties under IFRS.

*Current CIPFA guidance suggests that the existing “rolling 5 yearly valuations” for investment properties are likely to be insufficient for determining fair value under IFRS. The Borough will consider the practical issues around valuations during the next phase of this project and as further guidance is issued.*

### **Non current assets held for sale**

There are strict rules under IFRS regarding when an asset should be classified as held for sale. When these conditions are met the asset will be separately classified as such on the face of the balance sheet. The assets are measured at the lower of fair value and book value (rather than market value under UK GAAP). No depreciation is charged on these assets whilst they are classified as “held for sale”.

### **Leases**

The recognition and treatment of leases is essentially the same under IFRS as UK GAAP. IFRS is however more “principles based” rather than “rules based”, reflecting the substance of the agreement/transaction. This could lead to more finance leases being recognised under IFRS.

Leases of land where ownership does not pass should always be classified as an operating lease. For leases of “land and buildings”, IFRS requires that the “land” and “buildings” element are considered separately for classification purposes.

*The Borough currently has no finance leases and moving forward will continue with this policy.*

### **Embedded leases**

These are arrangements that do not take the legal form of a lease but which convey the right to use assets in return for a series of payments. Examples of such arrangements are outsourcing arrangements and managed service contracts that provide specific equipment.

*The Borough currently has no embedded leases. Looking forward the Borough will need to ensure that these are considered for major procurement contracts.*

### **Cash and cash equivalents**

“Cash and cash equivalents” will be separately classified on the face of the balance sheet. These are defined in IAS 7 as follows:

“cash comprises cash on hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value”

*In line with Price Waterhouse Coopers interpretation, the Borough will classify short-term investments as those falling due within three months.*

### **Government grants and other contributions**

CIPFA is currently working with HM treasury to agree a consistent approach across the two sectors with regard to accounting for Government and non-Government grants/contributions (including donated assets).

Notwithstanding the above, the initial guidance provided by CIPFA on this area is not in accordance with IAS 20 in terms of when the grant is recognised. IAS 20 requires the grant to be recognised over the period that the asset is used, matched with the depreciation charge, however, current CIPFA guidance suggests 100% recognition once conditions are met.

*This is a significant area for the Borough as it receives a high number of grants and other contributions (e.g. sect 106). The Borough will therefore review the position on Grants when further guidance is issued.*

### **Employee benefits accrual**

Under IFRS there is a specific requirement to include an employee benefits accrual. The accrual is made up of holiday pay and flexi time outstanding at 31 March. The

approach developed for calculating the accrual (for the transition balance sheet) will be consistently applied to subsequent periods.

Year on year movements of the holiday pay accrual will be recorded in the general fund and then reversed out to the separate employee reserve, thereby not impacting the general fund.

*The Borough will aim to provide employee benefit information from its "Trent" payroll system in coming years.*

### **Presentational issues including segmental reporting**

IFRS brings different terminology, a change in the presentation of the accounts and a number of new disclosures. In particular the requirements of IFRS 8 Operating Segments may result in significant additional disclosures in the accounts.

The Borough will consider the presentational and disclosure issues of IFRS during the next phase of the project and as further guidance is issued.

### **Next Steps**

The restatement of the transition balance sheet is a key milestone for the IFRS project. The Borough is now updating its future project plan to reflect the findings from this phase of the project. Key areas looking forward are as follows:

- Finalise IFRS accounting policies including any practical application issues (e.g. frequency of valuations for investment properties)
- Develop skeleton of IFRS accounts identifying new presentational and disclosure requirements.
- Restate 2009/10 under IFRS (the comparative year for the first set of IFRS accounts).



Royal Borough of Windsor and Maidenhead  
Restatement of transition balance sheet under IFRS

APPENDIX 2

	UK GAAP 31-Mar-09 £'000		UK GAAP in IFRS format 31-Mar-09 £'000
<b>Intangible assets</b>	5,601		
<b>Operational assets</b>			
Land and buildings	256,447		326,880
Vehicles, plant and equipment	2,371		5,601
Infrastructure assets	55,193	316,222	44,229
Community assets	2,211		206
		10,658	<b>376,916</b>
<b>Non operational assets</b>			
Investment properties	44,229		159
Assets under construction	10,658		23,439
Surplus assets held for disposal	1,425		41,325
<b>Total fixed assets</b>	<b>372,534</b>		<b>66,174</b>
<b>Fixed asset &amp; intangibles</b>	<b>378,135</b>		1,425
Long term investments	0		<b>444,515</b>
Long term debtors	206		
<b>Total Long term assets</b>	<b>378,341</b>		
<b>Current Assets</b>			
Stocks and work in progress	159		(7,692)
Debtors	23,439		(39,575)
Investments	41,325		(12,405)
Cash and bank balances	1,251		<b>(59,672)</b>
<b>Net current assets</b>	<b>66,174</b>		
<b>Total assets</b>	<b>444,515</b>		
<b>Current liabilities</b>			
Short term borrowings	(7,692)		(57,299)
Creditors	(39,575)		(553)
Cash overdrawn	(12,405)		(35,733)
<b>Net current liabilities</b>	<b>(59,672)</b>		(89,034)
<b>Total assets less current liabilities</b>	<b>384,843</b>		<b>(182,619)</b>
Long term borrowing >12 months	(57,299)		(57,299)
Government grants	(35,483)	(35,733)	(89,034)
Provisions	(553)		(553)
Deferred capital receipts	(250)		15,033
Defined benefit pension scheme liability	(89,034)		5,140
sub- long term liabilities	<b>(182,619)</b>		<b>202,224</b>
<b>Total assets less liabilities</b>	<b>202,224</b>		
<b>Financed by</b>			
Capital adjustment account	(268,782)		268,782
Revaluation reserve	(2,303)		2,303
Pensions reserve	89,034		(89,034)
Useable capital receipts	(1,850)		15,033
Earmarked reserves	(10,855)	(15,033)	15,033
Schools revenue reserve	(2,328)		5,140
Fund balances and reserves	(5,140)		<b>202,224</b>
	<b>(202,224)</b>		