	Item no:	11

SUBJECT:	CHANGES TO THE 2006/07 ACCOUNTS
DECISION-MAKER:	AUDIT COMMITTEE
DATE OF DECISION:	8th FEBRUARY 2007
REPORT VERSION No:	2

FORWARD PLAN No: N/A **KEY DECISION?** N/A

STATEMENT OF CONFIDENTIALITY

NOT APPLICABLE

WARDS/COMMUNITIES AFFECTED:

NOT APPLICABLE

SUMMARY

There have been a number of changes to local authority accounting regulations which have a significant effect on the presentation of the Statement of Accounts from 2006/07.

The 2005/06 accounts have been reproduced at a high level in the new format required for 2006/07. This report shows how the 2005/06 accounts look in the new format and explains the main changes that have been implemented.

RECOMMENDATIONS:

(i) To note the changes in local authority accounting regulations and the effect they have on the Statement of Accounts.

REASONS FOR REPORT RECOMMENDATIONS

1. To assist the Audit Committee in their understanding of the Statement of Accounts and changes to local authority accounting regulations.

BACKGROUND

2. The Standards & Governance Committee has authority to approve the Council's annual Statement of Accounts. The 2006/07 accounts will be presented to the Audit Committee on 28th June, prior to approval by the Standards & Governance Committee on 29th June. The 2006/07 accounts will be in a different format from last year due to changes in local authority accounting regulations.

CONSULTATION

3. Not Applicable

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

4. Not to inform the Audit Committee of changes to the Statement of Accounts. However, this would not be helpful in understanding the changes to the accounts.

DETAIL

5 The annual Statement of Accounts is prepared in accordance with the Chartered Institute of Public Finance Accountants (CIPFA)'s Code of Practice on Local Authority Accounting (the SORP). Each year a new SORP is published to include changes to the way in which local authorities should prepare and present their accounts.

6. The 2006 SORP has introduced some significant changes which have a material effect on the way that the financial statements are presented. These changes are intended to make local government accounts more compliant with UK Generally Accepted Accounting Practice (UK GAAP), i.e. move them more towards accounting conventions adopted in the private sector.

7. The 2005/06 accounts have been reproduced in the new format, based on the limited guidance currently available. Detailed guidance on the new SORP will not be available until February/March 2007. The Audit Commission have reviewed the work done on the redrafted accounts prior to them being submitted to this meeting and are satisfied they are compliant with the regulations as currently published.

8. The key changes are:
   - Removal of the capital financing charge
   - The Consolidated Revenue Account (CRA) replaced with the Income and Expenditure Account
   - Changes to the HRA Statement
   - New Statement of Total Recognised Gains and Losses

9. **Removal of Capital Financing Charge**

The capital financing charge (also known as notional interest or asset rent) was intended to represent the cost of tying up resources in fixed assets. For 2005/06 the charge was 3.5%/4.95% of asset value depending on the type of asset. This was charged to each service based on the assets used in the provision of that service. The charge was then reversed out below the Net Cost of Services as it is a notional cost and does not form part of the Council Tax charge. The total Capital Financing Charge included in Net Cost Of Services for 2005/06 was £46M.

10. The 2006 SORP has removed the requirement to charge service revenue accounts with a capital financing charge. The effect of this is to reduce the Net Cost of Services by £46M, although there is no effect on the overall general fund balance because of the charge being reversed out below the line.

11. **Consolidated Revenue Account (CRA) replaced with the Income & Expenditure Account (I&E)**

Up until 2005/06 the CRA was the statement which brought together the day to day costs of running Council services, how it was financed and the surplus or deficit on the General Fund balance.

12. The CRA has now been replaced with the I&E. The I&E shows the Council's financial performance for the year and now includes some notional gains and losses, such as depreciation. Appendix 1 shows the I&E Account for 2005/06.

13. Therefore, the overall surplus or deficit on the I&E account will no longer be the same as the surplus or deficit on the General Fund balance, which is calculated by reference to which expenditure has a direct effect on Council Tax. For this reason, a supplementary statement is now required within the Statement of Accounts which shows the movement from the I&E account to the General Fund balance. This is shown in Appendix 2.

14. For 2005/06 there was a deficit on the General Fund balance of £2.5M. The I&E now shows a deficit for 2005/06 of £15.0M. The following table shows the explanations for the change:

	£M
Deficit reported in CRA	**2.5**
Depreciation and other capital accounting no longer reversed out	28.4
Repayment of Debt taken out	(5.1)
Revenue financing of Capital taken out	(4.4)
Movement on Pension Reserve taken out	9.2
Loss on Disposal of Fixed Assets	0.1
Amortisation of Deferred Grants	(1.1)
Transfer from Earmarked Reserves	(14.7)
Other Accounting Adjustments	0.2
Deficit reported in I&E	**15.0**

15. Previously, capital accounting entries such as depreciation were shown within the Net Cost of Services and then reversed out within Net Operating Expenditure so as to eliminate any effect on the reported surplus or deficit. In the new Income & Expenditure Account these entries are no longer reversed out and so the bottom line surplus/deficit on the Income & Expenditure Account includes notional costs such as depreciation. This has the effect of worsening the reported deficit. However this does not have any impact on the General Fund balance or the amount to be raised from Council Tax.

16. Other accounting entries such as the financing of capital expenditure from revenue sources and the repayment of the Council's long term borrowing were previously included as costs in the Consolidated Revenue Account. These are now excluded from the Income & Expenditure Account and are instead reported in the Statement of Movement on the General Fund Balance. This has the effect of improving the surplus/deficit position on the I&E Account, but has no impact on the General Fund balance or the amount to be raised from Council Tax.

17. In 2005/06 the Council paid an employer's contribution of £15.4M into Hampshire County Council's Pension Fund, based on the contribution rate determined by the Fund's Actuary. However, the Council is required to account for retirement benefits in the Net Cost of Services at the time that employees earn their future entitlement. For 2005/06 this was valued at £19.4M. In addition, the Council must also record the net increase or decrease in the notional value of the Council's share of the pension fund assets. For 2005/06 this was a decrease of £5.2M. Therefore, the total cost reported within Net Operating Expenditure for 2005/06 was £24.6M. As the actual amount paid over to Hampshire was only £15.4M, the difference (£9.2M) was shown as a credit below Net Operating Expenditure. In the new Income & Expenditure Account, the credit of £9.2M is excluded and therefore the I&E account includes the full amount of £24.6M. The difference of £9.2M is now shown in the Statement of Movement on the General Fund Balance. This has the effect of worsening the deficit position. Again there is no impact on the General Fund balance or the amount to be raised from Council Tax.

18. It should be noted that work is currently underway in assessing the useful lives of all the Council's properties. This will enable depreciation to be charged on many more assets than had been previously. This will therefore increase the depreciation costs being charged to the I&E and therefore the deficit that will be reported in the 2006/07 Statement of Accounts is likely to be significantly higher than is shown in this report. However, as depreciation is a notional charge, this will have no effect on Council Tax.

19. **Changes to the HRA Statement**

The changes to the HRA statement are similar to the I&E account in that the HRA statement now includes some notional gains and losses. Therefore there is a supplementary statement required showing the movement from the deficit or surplus on the HRA statement to the HRA balance calculated under previous rules.

20. **Statement of Total Recognised Gains and Losses (STRGL)**

This new statement (shown in Appendix 3) replaces the Statement of Total Movement on Reserves and brings together all the gains and losses of the Council for the year. The statement shows the aggregate increase in the Council's net worth, which includes:

- Surplus/Deficit on the I&E
- Surplus/Deficit on revaluation of fixed assets
- Actuarial Gains/Losses on pension fund assets/liabilities

FINANCIAL/RESOURCE IMPLICATIONS

21. The changes to the Statement of Accounts do not have any real financial implications in terms of balances available or Council Tax. They deal primarily with the treatment of notional costs.

Property

22. There are no specific property implications arising from this report

Other

LEGAL IMPLICATIONS

Statutory power to undertake proposals in the report:

Accounts and Audit Regulations 2003

Other Legal Implications:

POLICY FRAMEWORK IMPLICATIONS

The Statement of Accounts is prepared in accordance with CIPFA's code of Practice on Local Authority Accounting in the UK.

SUPPORTING DOCUMENTATION

Appendices

1.	Income & Expenditure Account
2.	Statement of Movement on the General Fund Balance
3.	Statement of Total Recognised Gains & Losses

Documents In Members' Rooms

1.	None

Background Documents

Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
None	

Background documents available for inspection at:

REPORT OF: Executive Director Resources

AUTHOR: Name: Rob Carr Tel: 023 80 83 2885

E-mail: Rob.carr@southampton.gov.uk

File Name: Changes to Accounts S&G Report v2