

AGENDA ITEM

## Corporate Affairs Committee

DATE: 24<sup>th</sup> SEPTEMBER 2008

STATEMENT OF ACCOUNTS 2007/2008

PAUL SLOCOMBE – DIRECTOR OF RESOURCES

### PURPOSE OF THE REPORT

1. The purpose of this report is for Members of the Corporate Affairs Committee to receive and approve the Middlesbrough Council Statement of Accounts 2007/2008. The approval of the Accounts by the Committee is intended to provide an opportunity for public scrutiny of the Council's financial statements and meet best practice requirements, as set out in the Audit Commission's Comprehensive Performance Assessment – Use of Resources.
2. The Statement of Accounts also includes the accounts for Teesside Pension Fund for which the Council is the Administering Authority.

### BACKGROUND

3. The Statement of Accounts is essentially a technical publication containing accounting statements that have been prepared in accordance with the Code of Practice on Local Authority Accounting in Great Britain and the Statutory Accounts and Audit Regulations. The Statement of Recommended Practice (SORP) further supports the accounting framework. The SORP is updated annually and specifies the accounting principles and practices required to prepare a Statement of Accounts, which present fairly the position of a local authority.

4. The key changes introduced by the recent SORPs include:
  - Establishment of a Revaluation Reserve with effect from 1<sup>st</sup> April 2007.
  - Fixed Asset Restatement Account and Capital Financing Account have been joined together to form the Capital Adjustment Account.
  - Local Authorities adoption of current reporting standards, dealing with the major changes in the accounting treatment of financial instruments covering areas such as soft loans, borrowing, financial guarantees and investments
  - Replacement of the Statement of Internal Control with an Annual Governance Statement
5. The main impact of the 2007 SORP for the Council was the detailed analysis required to ensure that the fixed assets Revaluation Reserve was established, maintained and reconciled on an individual asset basis with separate records for historic cost and revised current value now required for each asset.
6. Following significant changes in 2006/07 to the layout and accounting treatments, the Statement of Accounts now contains the following:
  - An Explanatory Forward
  - Annual Governance Statement
  - A Statement of Accounting Policies
  - Statement of Responsibilities for the Statement of Accounts
  - The Main Financial Statements comprising:
    - The Income and Expenditure Account
    - The Statement of Movement on General Fund Balances
    - Statement of Recognised Gains and Losses
    - Balance Sheet
    - Cash Flow Statement
  - Notes to the Main Financial Statements
  - Collection Fund and notes
  - Group Accounts
  - Teesside Pension Fund- Fund Account and Net Asset Summary

The purpose of each of the statements within the Accounts is as follows:

7. **Annual Governance Statement.** The Annual Governance Statement reports on the key financial controls and wider governance arrangements in operation within the Council. The Statement was presented to the Corporate Affairs Committee on the 28<sup>th</sup> May 2008.
8. **Income and Expenditure Account - Appendix A.** This is equivalent to a profit and loss account in a private sector companies accounts. It shows the income and expenditure of all the Council's functions, the net cost of Council services for the financial year and demonstrates how this has been funded (e.g. Government Grants, Non Domestic Rates and Council Tax). The format of the income and expenditure of the Council's services is presented using the Best Value Accounting Code of Practice (BVACOP) classification, again a statutory requirement. The main items of note are as follows:

Net operating expenditure – an increase of £6.4m over the previous year. This can be explained as a result of net inflation increase of £3.0m, an increase in the costs relating to Pension Fund £0.5m; an increase in the costs associated with equal pay settlements of £2.2m which are shown through the Income and Expenditure Account; an increase in depreciation and impairment charges and other smaller items of expenditure making up the balance.

9. **Statement of Movement on the General Fund Balance - Appendix B.** This statement discloses changes in the General Fund balance for council tax setting purposes in accordance with Generally Accepted Accounting Practice (UK GAAP) The inclusion of this statement reflects the importance of the movements in the general fund balance to a local authority as an aspect of the Council's financial stewardship. The adjustments summarised in this statement are either determined by statute or proper accounting practices.

The following table summarises the general fund position shown in the Statement of accounts and reconciles it with the information included in the 2007/2008 Outturn report to Executive on the 27th May 2008.

<b>Movement in balances reported in the Outturn Report</b>	<b>£000</b>
Back Dated RSG transfer to earmarked reserve	2459
Balances set aside in the budget to cover potential CFL service pressures	752
Increase in balances at 31 March 2008, as a result of service savings as per statement in the May 2008 Executive Report	-489
Decrease in general balances during 2007/08	2,722
<b>Movement on the General Fund balance as per the Statement of Accounts</b>	<b>£000</b>
Opening Balance	8,199
Changes to the General Fund balance in year	2,722
Closing Balance General Fund during 2007/08	5,477

10. **Statement of Total Recognised Gains and Losses - Appendix C.** The principle reason for this statement is to bring together all the gains and losses that affect the Council's net worth, including the gains and losses from the revaluation of assets and the actuarial valuation of the pension fund which do not pass through the income and expenditure account.

11. **Balance Sheet - Appendix D.** This statement is important to the understanding of the local authority's financial position as at the 31<sup>st</sup> March 2008. It reports details of, the value of assets owned by the council, the level of creditors (amounts owed by the Council), the level of debtors (amounts owed to the Council) and the level of provisions and balances maintained by the Council. The main items of note are as follows:

Fixed Assets – these are assets owned by the authority which are used either in direct service provision or held for investment purposes. The value as at 31 March 2008 is £544m (March 2007 £473m). Fixed assets are revalued at least every five years with the valuation work being undertaken in-house by the Mouchel Valuation section or procured by external valuers. Other long-term investments and long term debtors relate to investments with a maturity date in excess of 12 months from the balance sheet date and debt outstanding on mortgages provided to third parties for the purchase of Council and private dwellings.

Current Assets – the main items included within this heading are debtors i.e. money owed to the Council as at 31 March 2008 and short-term investments. Investments have reduced by £11.154m over the year and the Council currently has £49.7m invested in other local authorities, a variety of banks and building societies. Debtors have decreased by £0.956m to £36.779m in the past year. This can mainly be explained by improved debt collection procedures.

Current liabilities – this is the amount of money owed by the Council to its suppliers and contractors which totalled £41.724m as at 31 March 2008 (£44.75m as at 31 March 2007). Improved processes for the payment of creditors can explain the main variance between the years.

Long term liabilities – this section is made up of several different items. Long term borrowing and the value of the pension liability makes up approximately 56% of the total. Long term borrowing (£100.6m) remains fairly static over the year as the Council has mainly used grants and contributions to fund capital expenditure. The Pension Liability amounts to £92.281m as at March 2008 (£126.030m March 2007). This is the value placed on the Council liability by the Pension Fund Actuary and is offset in the balance sheet by a corresponding credit on the Pension Reserve. The section on the Pension fund Accounts – paragraphs 15 to 18 below explains why the Council's liability reduced significantly.

Financed by – the total of all the items within this section is the value of the net worth of the Council. It shows the reserves and balances held as at 31 March 2008, and can be split between technical and earmarked reserves.

Technical Reserves - The two new technical reserves are the Restatement Reserve (£43.3m) and the Capital Adjustment Account (£269.7m), which are not cash backed. The Capital Adjustment Account records the consumption of the value of asset and deferred charges over the period that the authority benefits from the expenditure.

Earmarked Reserves – The Council's budget monitoring gives greater prominence to the level of cash-backed reserves in the form of the general fund balance and

earmarked reserves which are potentially useable to finance revenue and capital spending. The earmarked reserves (£11m) are linked directly to specific Council risks and programmes such as, Invest to Save/Change Programme and the Insurance Fund.

12. **Cash Flow Statement - Appendix E.** This Statement explains the movement in the Council's cash balances over the year and summarises the inflows and outflows of cash with third parties. The other main Statements are produced on an accruals basis, whereby income and expenditure are matched to the period to which they relate whether or not it has been paid or received. This Statement has any non-cash accounting adjustments and accruals removed and displays the situation relating to actual cash received from third parties and actual cash paid to third parties
13. **Collection Fund.** This statement has no equivalent in the private sector. It is required by statute and shows the transactions the Council has undertaken in relation to Non-Domestic Rates and Council Tax income. The information within the collection fund statement is consolidated into the Income and Expenditure Account under sources of finance.
14. **Group Accounts.** The authority conducts some of its activities through partnerships and separate undertakings. The SORP requires the production of Group Accounts to take account of these relationships in order to provide a full picture of the Council's overall financial position.
15. **Teesside Pension Fund Accounts.** The Pension Fund Accounts show the contributions to the Council's Pension Fund for employees employed by the 60+ contributing bodies during 2007/08, together with the pensions and other benefits paid from it, movements in investments during the year and the financial position of the fund as at 31 March 2008.
16. The 2007/2008 year was a positive year for Teesside Pension Fund, continuing the upward trend since the downturn of 2003 when the fund's total value dropped to £962 million. The total value of the fund rose by £33 million in the year to £2,048 million, a modest increase of 1.6% in the year, and 113% over the 5 years since 2003.
17. The increase in the fund occurred despite a fall in the market value of investments of £65 million (2006/2007 – increase of £90 million), due to the fall in equity values in the fourth quarter of the year. The Fund was protected to some extent from the sell-off in the fourth quarter by its heavy weighting in cash, accumulated to take advantage of better buying opportunities.
18. The Fund's actuaries, Barnett Waddingham, completed the latest triennial valuation of the Fund and this showed that the Fund has made progress since the last one was carried out in 2004, with the overall funding level increasing from 84% to 98% funded.
19. Attached to this report are extracts from the audited Statement of Accounts providing details of the main accounting financial statements. A copy of the full

statement has been made available to all members of the Corporate Affairs Committee. A copy of the full statement has been deposited within the Members Library. In addition a copy of the accounts will be made available on the Council's Internet site, once the External Auditor has signed the document.

20. A combined Annual Report / Summary of Accounts has been produced for 2007/08. The report includes performance information and summary financial data and which will be published in the Middlesbrough News (See Appendix F)

### **External Consultation**

21. Notice was given in the local press for any interested person to inspect, and make copies of, The Statement of Accounts and other documents between 21 July and 15 August 2008. Interested persons have been able to question the Auditor about the accounts and make objections to the same with effect from 18 August 2008 until the completion of the audit.
22. The Statements have been subject to external audit - Deloitte, which commenced on 4th August and was completed on 8th September. A statement (ISA+260) will be produced which details any unadjusted misstatements found during the course of the audit. The auditors have not identified any material changes required to the Statements.
23. The Statement of Accounts has had the following alterations made from the draft presented to members in June 2008, which are mainly presentational matters, which ensure complete compliance with revised Statement Of Recommended Practice (SORP) requirements and Best Value Accounting Code of Practice (BVACOP).

	<b>Alteration</b>	<b>Reason</b>
1	Transfer amounts for: Building Schools for the Future HR Initiatives and Equal Pay Repayment of Capital Grants mis-classified as reserves to provisions.	Review of provisions to ensure compliance with FRS12.
2	An asset was disposed of that remained on the Fixed Asset Register at the end of the year	Ensures compliance with SORP.
3	Note 46 Contingent Liabilities / Assets: The note on Equal Pay Claims has been expanded to include the tribunal decision on APT&C and protection.	Improved disclosure

24. The Building Schools for the Future and HR Initiatives & Equal Pay reserves in the above table (row 1) had been re-classified previously on the advice from the former external auditors. They are now to be classified as provisions and will remain as provisions from now on.

25. There are no major issues raised by the External Auditor - Deloitte and there was significant progress in the production of the 2007/2008 Statement of Accounts. The draft and final Statements have been produced well within the timetable and the quality of the working papers has again improved.
26. The preparation of the Statement of Accounts has been undertaken in accordance with an internal quality assurance framework to ensure the accounts are prepared in accordance with the SORP and other relevant legislation.

## **FUTURE ACCOUNTING DEVELOPMENTS**

27. Internationally a number of accountancy regulatory bodies have agreed to a convergence of accounting standards and practices globally to enable easier comparison of accounts across countries. Local Government accounts are moving to a standard known as International Financial Reporting Standards (IFRS). This has, and will, lead to significant changes to the format and accounting practices for local government. Due to the significant work involved in moving to IFRS compliance the changes have been taking place over a number of years.

## **ROLE OF THE CORPORATE AFFAIRS COMMITTEE**

28. The Corporate Affairs Committee has a role to ensure that the quality control procedures are in place to ensure that the Statement of Accounts submitted for audit is of the appropriate standard. Given the complex technical nature of the accounts the Committee is not expected to be able to review the accounts in detail. However it should consider the following:
  - The key accounting policies
  - Assurances about the financial systems that have provided the figures for the accounts;
  - The quality control arrangements over the preparation of the accounts by the Director of Resources and his staff;
  - Key judgments in preparing the accounts;
  - Any issues raised by the External Auditors - Deloitte that have to be resolved.
  - Question any significant changes from the previous year
29. As noted earlier in this report, the format of the Statement of Accounts is heavily prescribed by a range of regulations and reporting arrangements. However, it is important that they are understandable and meaningful to all stakeholders. Although constrained by regulations and reporting standards, the Council is always looking to improve the content and format of the Statement of Accounts. Members' comments on how the Accounts and explanatory information could be improved in the future are therefore welcome.

## OPTION APPRAISAL/RISK ASSESSMENT

30. Risk:

Risk	Category	Implications
The Council's accounts are significantly incorrect, incomplete or misstated and are "qualified" by the External auditor	Legal, CPA	The Council's Use of Resources CPA score could not be above a 1.
The Statement of Accounts is not approved by 30 September 2008	Legal, Reputation, CPA	There is a statutory requirement for the Statement of Accounts to be approved by 30 September. Failure to do so would result in external criticism and would limit progress on CPA.

## FINANCIAL, LEGAL AND WARD IMPLICATIONS

31. Overall the accounts show a sound financial position for the Council with the level of balances being in line with the Council's Medium Term Financial Plan.
32. The application of sound financial management across all services was reflected in the final outturn for the year with a net saving compared to budget of £485,000 (0%).
33. Actual capital spend in the year was £34.2m, compared with a budget of £39.6m. Expenditure during the year was mainly funded from grants (59%), from usable capital receipts (18%), from borrowing (12%), from revenue contributions (2%) and from capital contributions (9%). The percentage of spend achieved compared to the budget represented 86.4%.

## RECOMMENDATIONS

34. It is recommended that:

Members approve the final 2007/2008 Statement of Accounts.

## REASONS

35. The purpose of the Statement of Accounts is to present the overall financial position of the Council at 31 March 2008 in accordance with guidance produced by CIPFA.
36. The recommendation is supported by the requirement to comply with the 2004 Accounts and Audit Regulations, which require the audited Statement of Accounts to be approved by the 30th September 2008.



37. The SORP requires that the Director of Resources to sign and date the Accounts under a statement that the accounts present fairly the financial position of the authority at the accounting date and its income and expenditure for the year then ended.
38. The Accounts and Audit Regulations also require the Statement of Accounts to be signed and dated by the presiding member of the Corporate Affairs Committee meeting at which the accounts are approved.

## **BACKGROUND PAPERS**

The following papers were used in the preparation of the report: -

- Code of Practice on Local Authority Accounting in the UK – SORP 2007.
- Draft Statement of Accounts 2007/2008
- Draft Statement of Accounts Report to Corporate Affairs Committee 26th June 2008
- Annual Governance Statement Report to Corporate Affairs Committee 28th May 2008
- 2007/2008 Outturn report to Executive on the 27th May 2008.

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