

The move to international financial reporting standards – a briefing for local government bodies

Background

- 1 The Financial Statement and Budget report, published on 21 March 2007, stated that:

‘The annual financial statements of government departments and other entities in the public sector are currently prepared using accounting policies based on UK Generally Accepted Accounting Practice (UKGAAP). In order to bring benefits in consistency and comparability between financial reports in the global economy and to follow private sector best practice, this Budget announces that from the first year of the Comprehensive Spending Review (CSR) period these accounts will be prepared using International Financial Reporting Standards (IFRS) adapted as necessary for the public sector.’

- 2 The Commission welcomes the adoption of IFRS, as it reinforces the drive to improve financial reporting and enhance accountability for public money.

- 3 The timetable announced by the Government suggests that from 2008/09 all public sector bodies, including local government bodies, will be expected to prepare their accounts in accordance with IFRS. However, the timetable for the transition to IFRS in local government has yet to be confirmed and is currently the subject of discussion between the Treasury, the Department for Communities and Local Government (CLG) and the Chartered Institute of Public Finance and Accountancy/Local Authority (Scotland) Accounts Advisory Committee (CIPFA/LASAAC). We are also in discussion with those bodies about how the development of a new local government Statement of



Recommended Practice (SORP), or equivalent, should be taken forward and we will work closely with these key stakeholders to support that process over the next year.

- 4 The move to IFRS in local government is still, therefore, at an early stage. However, the adoption of IFRS will have significant implications for the way in which local government bodies prepare their annual financial statements. It also poses challenges for standard-setters and auditors. The Audit Commission is committed to helping local government bodies keep up to date with these developments. This is, therefore, the first of what will be a series of briefings, aimed at the preparers of accounts, which will address developments in the application of IFRS.

What are the implications for you?

- 5 CIPFA is currently analysing the key differences between the SORP and IFRS and this will be considered by CIPFA/LASAAC in June 2007. More details on the proposed CIPFA/LASAAC approach can be found in its report dated 16 April 2007, which is available on the CIPFA website. However, what is clear is that, as a minimum, the 2008/09 whole of government account (WGA) will be prepared in accordance with IFRS, so local government bodies will be required to prepare their 2008/09 WGA consolidation packs in accordance with IFRS.
- 6 The actual size of the task is difficult to assess until CIPFA/LASAAC have completed their analysis. However, changes to the local government SORP in recent years have gone a considerable way towards aligning it with current UKGAAP. These changes will help to mitigate the impact of the changes to IFRS.
- 7 Work on the development of an IFRS-based Financial Reporting Manual for central government bodies is at an advanced stage and a draft is to be issued for consultation in the summer. The Commission, through its membership of the Financial Reporting Advisory Board (FRAB), which advises the Treasury and the devolved administrations in Scotland and Wales on financial accounting and reporting issues, has been closely involved in this process and is thus well aware of the technical and practical issues involved. We believe that this work forms a useful basis for developing an equivalent accounting framework for local government.

- 8 The impact of the move to IFRS will vary from body to body, depending on materiality and local circumstances. However, in the Commission's view, the treatment of leases and private finance initiative (PFI) schemes in particular could have material implications for many bodies.
- 9 While the International Accounting Standards Board has issued guidance on accounting for PFI, that guidance only applies to the operators of PFI rather than to the public sector partner. Accordingly, it will be necessary to develop additional guidance for the public sector. But most commentators agree that under international standards most PFI schemes are likely to come onto the balance sheet. Again, the practical financial implications of such a change will need to be thought through.
- 10 There is also a potentially significant increase in the number of disclosures required by IFRS which, again, may increase the amount of work required to ensure compliance. CIPFA will be consulting with the Treasury in the coming months on the extent of the disclosures required in the public sector, using as a basis the work on disclosures in central government and the health service that is already underway.
- 11 We are also discussing with the Treasury, CLG and CIPFA/LASAAC the form of guidance for the initial transition from UKGAAP to IFRS. This will be based on IFRS 1: *First Time Adoption of International Financial Reporting Standards* and its related guidance, but is likely to be adapted for the local government context.

The way forward

- 12 The Commission itself is developing its response to the challenges posed by the transition to IFRS. In doing so, we are working with our partner firms who can draw on their experience in the transition to IFRS in the private sector. We are also working closely with the National Audit Office and the other national audit agencies in the UK to pool our expertise to ensure as smooth a transition as possible.



- 13 Both Australia and New Zealand have already adopted IFRS for their public services and, through our contacts with our sister agencies in these countries, we can also learn from and build on their experiences.
- 14 We will be providing training for our auditors so that they are able to inform and comment on local government bodies' arrangements for the transition to IFRS, as they are developed.
- 15 All the experience from the private sector and internationally suggests that an early start and good planning is essential to a smooth transition. It is in everyone's interests that the transition to IFRS is successful and the Commission and its appointed auditors are committed to helping local government bodies through this process. Future briefings in this series will be designed to keep you informed of key developments and their implications.

For further information on the work of the Commission please contact:
Audit Commission, 1st Floor, Millbank Tower, Millbank, London SW1P 4HQ
Tel: 020 7828 1212 Fax 020 7976 6187 Textphone (minicom): 020 7630 0421
www.audit-commission.gov.uk