

## Part 4 (Wales)

# Accounting Guidance for Local Councils with Income or Expenditure exceeding £1million

## Proper practices

- 4.1 Local Councils, governed by the Local Government Acts and with a turnover in excess of £1 million per annum (larger local councils), are “local government bodies” according to Regulation 2(1) of the Accounts and Audit (Wales) Regulations 2005 (as amended).
- 4.2 The regulations require<sup>1</sup> all local government bodies ‘to prepare, in accordance with proper practices in relation to accounts, a statement of accounts each year...’.
- 4.3 From 2009/10 the CIPFA/LASAAC SoRP Board has disappplied the SoRP for larger local councils. The SoRP no longer applies to the preparation of annual statements of accounts for larger local councils in Wales
- 4.4 The Local Authorities (Capital Finance and Accounting)(Wales) Regulations 2003 (as amended) define Governance and Accountability for Local Councils: A Practitioners’ Guide 2008 (Wales) and its successor publications (‘the guidance’) as proper practices for community councils in Wales. For financial years commencing on or after 1 April 2009, the ‘proper practices in relation to accounts’ guiding larger local councils in the preparation of the annual statement of accounts are found in Part 4 of the guidance. All authorities to which section 21 of the Local Government Act 2003 applies that are required to prepare a Statement of Accounts by the regulations therefore have a statutory duty to comply with these proper practices.
- 4.5 This guidance is designed to assist larger local councils to prepare statements of accounts in accordance with ‘proper practices’, that is, the relevant professional standards which, given the scale of a council’s activities, are applicable.
- 4.6 The guidance is based on the provisions of the Accounting Standards Board’s Financial Reporting Standard for Smaller Entities effective April 2008 (FRSSE 2008)<sup>2</sup> and its successor publications. By following the guidance, larger local councils will therefore follow generally accepted accounting practices. Councils should note that the guidance takes precedence over the requirements of the FRSSE. However, in the event of any ambiguity in the guidance, it should be read as being consistent with the FRSSE.
- 4.7 By adopting and applying the guidance, larger local councils become exempt from applying more complex accounting standards such as Statements of Recommended Accounting Practice (SoRP), Codes of Practice on Accounting, other Financial Reporting Standards (FRS including IFRS) and Urgent Issues Task Force (UITF) Abstracts.
- 4.8 Councils should note that this guidance will be updated when the International Financial Reporting Standard – IFRS for Small and Medium Size Entities – is developed and issued.

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<sup>1</sup> Regulation 7 of the Accounts and Audit (Wales) Regulations 2005 (as amended)

<sup>2</sup> Available from <http://www.frc.org.uk/asb/technical/frsse.cfm>

## ***Applying the guidance***

- 4.9 The guidance in this Part should be applied to all accounting periods commencing on or after 1 April 2009. Local councils operating below the £1 million annual turnover threshold ('smaller local councils') continue to complete an annual return and are not required to prepare and submit accounts in accordance with this Part 4.
- 4.10 In the event of conflict between this guidance and any statutory requirement, the statutory requirement shall represent the proper practices to be applied
- 4.11 Section A below covers general principles and accounting concepts for the accounts. Section B describes the statements of accounts in greater detail and the form of their presentation.

## **Calculating income and expenditure**

- 4.12 In order to determine, in line with the regulations, whether you need to prepare a statement of accounts in accordance with Regulation 7(3), it is necessary to determine if your council's income or expenditure exceed £1 million. To establish income and expenditure for this purpose, councils should calculate their income and expenditure on an accruals basis as shown in part 3 of this guide.

## ***Transition arrangements***

- 4.13 In the first year of adoption of this guidance as opposed to the preparation and presentation of financial statements in accordance with the CIPFA SoRP the following approach should be adopted:
- a clear statement should be included within the note on the basis of preparation that the accounts have been prepared for the first time following the guidance. The statement should explain that the format of the statements has changed and that the comparative period has been restated in the newly adopted format;
  - Details of any changes in accounting policy arising in accordance with paragraph 4.25 of this guidance;
  - Such matters should be accounted for as a Prior Period Adjustment in accordance with paragraph 2.15 of the FRSSE with disclosure at the foot of the Statement of Total Recognised Gains and Losses;
  - The existing Capital Adjustment Account should be renamed the Capital Financing Account; and
  - Where the council opts to retain the book amounts in respect of tangible fixed assets under paragraph 4. The balance on the revaluation reserve should be transferred to the Capital Financing Account.

## **Section A: General requirements and accounting principles**

### ***The structure of the accounts***

- 4.14 Local councils that exceed the turnover threshold should follow this guidance. When preparing their financial statements, practitioners must recognise that not all of the elements do apply to the local councils given their statutory framework, powers, duties and functions.
- 4.15 The financial statements subject to audit should consist of the following:
- an annual report<sup>3</sup>;
  - an annual governance statement;
  - a statement of responsibilities for the statement of accounts;
  - a statement of accounting policies;
  - an income and expenditure account;
  - a statement of movement of reserves;
  - a statement of total recognised gains and losses<sup>4</sup>;
  - a balance sheet;
  - notes to the accounts; and
  - the external auditor's report.
- 4.16 The Accounts and Audit (Wales) Regulations require a statement of internal control, prepared in accordance with proper practices, to be included with the financial statements. This requirement is met by including the annual governance statement with the financial statements. Assembly Government guidance<sup>5</sup> identifies this practitioners' guide as the source of appropriate professional guidance on proper practice in relation to internal control, details of which may be found in Part 2 above.
- 4.17 A large local council should add such additional information or statements as are necessary to ensure that the financial statements presents fairly its financial position and transactions. Councils should note that the Accounts and Audit (Wales) Regulations require certain information to be disclosed. Further information is provided at paragraph 4.111.
- 4.18 The FRSSE requires a directors' report to accompany the statement of accounts. To meet this requirement, larger local councils should provide an annual report on its activities during the reporting year. The annual report is to be approved by the council.
- 4.19 The annual report should include such additional information to enable the user of the accounts to gain a better understanding of any matters set out in the accounts. Practitioners should note the external auditor's opinion does not cover the annual report. Auditors will, however, check that it meets minimum disclosure requirements and will check for consistency between financial information presented in the annual report and within the council's financial statements.

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<sup>3</sup> The annual report is not covered by the auditor's certificate. However, financial information contained in the annual report must be consistent with the financial statements and notes.

<sup>4</sup> Only required if gains and losses (for example from the revaluation of assets) are not recognised in the I&E account.

<sup>5</sup> Welsh Assembly Government Guidance on the Accounts and Audit (Wales) Regulations 2005 issued April 2005

- 4.20 The FRSSSE while recommending the voluntary disclosure of cash flow information states that this is not a mandatory requirement. Councils may prepare a cash flow statement if they wish to.
- 4.21 All accounts and notes, including the cash flow statement if reported, should present both current and preceding accounting period information.
- 4.22 Where a council is the sole managing trustee for a trust fund, including charitable trusts, a separate trust fund revenue account and balance sheet should be disclosed by means of a note to the financial statements.
- 4.23 Local councils should use discretion in providing additional information over and above that required by proper practice that may be of interest to the users of the account, for example, if the council runs leisure or cultural services, car parks etc. Such information must be provided separately from the accounting statements, preferably within the annual report, and clearly excluded from those statements that are subject to the auditor's opinion and report.
- 4.24 Local councils should note however that if additional information is published with the financial statements it will be reviewed by the auditor in the same way as the annual report to check consistency with the audited financial statements.

## ***Accounting Principles and Policies***

- 4.25 The financial statements state that they have been prepared in accordance with this guidance and should include:
- a description of each material accounting policy (see below);
  - a statement (if necessary) detailing any changes to the accounting policies from one period to another, including reasons for change and an analysis of the financial effect of the change; and
  - where the effect of a change to an estimation technique is material, a description of the change and where practicable the effect on the result for the current period.
- 4.26 When preparing the financial statements local councils should have regard to the following accounting principles:

**Going Concern:** Local councils carry out their functions as a going concern. Any material uncertainties about this presumption are disclosed.

**Prudence:** Local councils determine any amount of any item on a prudent basis. That is to exercise a degree of caution when making estimates under conditions of uncertainty so that assets are not overstated and liabilities not understated.

**Accruals:** The financial statements are prepared on an accruals basis. All income and expenditure relating to the financial period to which the accounts relate is taken into account without regard to the date of payment or receipt.

**Relevance:** The financial statements provide information about the council's financial performance that is useful for assessing the stewardship of public funds and for making economic decisions.

**Consistency:** Consistent accounting policies are applied both within the accounting period and between accounting periods. Where accounting policies are changed, the reason and effect are separately disclosed.

**Reliability:** The financial information provided is reliable and:

- reflects the substance of the transactions and other events that have taken place;
- is free from deliberate or systematic bias;
- is free from material error;
- is complete within the bounds of materiality; and
- under conditions of uncertainty, is prudently prepared.

**Comparability:** The statements of account are prepared with consistent and adequate disclosure to allow comparability.

**Understandability:** All reasonable efforts are taken in preparing financial statements to ensure they are as easy to understand as possible.

**Materiality:** An item of information is material if its mis-statement or omission might reasonably be expected to influence assessments of stewardship and economic decisions, or comparisons with other entities, based upon the financial statements.

- 4.27 Accounting policies and estimation techniques shall be consistent with the FRSSE and applied consistently within the same accounts and from one financial period to the next. If there is a material change in accounting policy the amounts for the current and corresponding periods shall be restated on the basis of the new policies by making prior period adjustments.
- 4.28 Prior period adjustments shall be made by restating the comparative figures for the proceeding year and adjusting the opening balances of reserves accordingly. Where a statement of total recognised gains and losses has been prepared the cumulative amount should also be noted at the foot of the current period.

## ***Accounting for Grants***

- 4.29 Revenue grants and subsidies should be credited to revenue accounts and accrual is only made for amounts known to be receivable at the end of the accounting period.
- 4.30 A government grant should not be taken to the income and expenditure account unless the conditions for its receipt have been met and there is reasonable assurance that it will be received.
- 4.31 Where the acquisition of a fixed asset is financed either wholly or in part by a government grant or other contribution, the amount of the grant or contribution should be deducted from the purchase price of the asset.
- 4.32 Larger local councils previously adopting a policy of accounting for grants as deferred assets which are amortised over the useful life of the related asset by taking annual contributions to revenue may:
- Apply any unamortized grant balance against the depreciated value of the asset and depreciate the adjusted asset value over the remaining life of the asset, restating the opening balances accordingly; or
  - Continue with a policy of depreciating the gross value of the asset and releasing the associated capital grant as previously. Councils opting for this approach must make full disclosure in their accounting policies and identify in a note to the balance sheet any assets and grants subject to this treatment.
- 4.33 Where a larger local council opts to continue to defer government grants in its balance sheets and amortise them on the same basis as the associated asset that amortisation should be reversed out of the income and expenditure account as follows:

- Insertion of an additional line below the Net Operating Surplus or Deficit for Year “Reversal of government grant amortisation”; and
- By processing the following journal:

Credit: Capital Financing Account

Debit: General Fund “Reversal of government grant amortisation”

## **Fixed Assets**

- 4.34 Expenditure on tangible fixed assets shall be measured at cost and then written down to its recoverable amount if necessary. Assets are defined as rights or other access to future economic benefit controlled by a local council as a result of past transactions or events. Other than for investment property, the option of revaluing assets, although permitted by the FRSSE, is not recommended.
- 4.35 All expenditure on the acquisition, creation or enhancement<sup>6</sup> of fixed assets above a *de minimus* level should be recognised on a consistent basis and capitalised on an accruals basis in the accounts. Councils must set an appropriate *de minimus* level for each category of asset and review this level from time to time.
- 4.36 Fixed assets are to be classified between:
- research and development, intangible assets and goodwill;
  - tangible fixed assets;
  - investments (in companies) and investment properties.

Councils are likely to only have tangible fixed assets (land & buildings, vehicle and plant) and some may hold investment properties. No specific sub-division into type of fixed assets is required. However if Councils consider that users of the financial statements should be provided with further information, a sub division of tangible fixed assets between land & buildings; vehicles & plant; and non-operational assets by way of a note to the accounts is suggested.

- 4.37 Tangible fixed assets should be recorded at historic cost and written down to a recoverable amount if less. In the event of the rare occurrence where historic cost is not known, the book value of an asset may be estimated by the Members of the council on the basis of professional guidance. Assets valued in this way must be individually identified in asset registers and in the notes to the accounts.
- 4.38 For the first accounting period for which this guidance is applied, if a larger local council does not adopt an accounting policy of revaluation of tangible fixed assets but the carrying amount of its tangible fixed assets reflects previous revaluations and impairment it may:
- retain the book amounts. In these circumstances the council shall disclose the fact that the transitional provisions in paragraph 19.3 of the FRSSE are being followed and that the valuation has not been updated and give the date of the last valuation; or

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<sup>6</sup> Not all subsequent expenditure on assets is capital expenditure. Practitioners are directed to paragraph 6.22 of the FRSSE 2008 which describes the only conditions under which subsequent expenditure may be capitalised and thus qualify as capital expenditure.

- restate the carrying amount of the tangible fixed assets to historical cost (less restated accumulated depreciation) as a change in accounting policy.

## ***Investments***

- 4.39 Where held, investments should be disclosed in the balance sheet at historic cost. The market value of investments at the balance sheet date should be disclosed in a note to the accounts supported by an investments register. Realised gains are taken to the income and expenditure account as they occur. Provision should be made for any diminution in value of investments.
- 4.40 Where investment properties are held, these must be disclosed on the balance sheet within Fixed Assets at market valuations. Because of the inherent risk of such investments for local councils, investment property valuations must be made at frequent intervals, at least annually.

## ***Depreciation***

- 4.41 All tangible fixed assets (other than investment properties) should be depreciated over their useful economic life on an appropriate basis. Land is regarded as having an unlimited life and is therefore not depreciated. Investment properties are not depreciated except where held on a lease with an unexpired term is 20 years or less.
- 4.42 The notes to the accounts should disclose the depreciation method applied and the useful economic lives of the assets.
- 4.43 For fixed assets other than non-depreciable land and non-operational investment properties, the only ground for not charging depreciation is that the depreciation charge is immaterial.
- 4.44 For simplicity, it is suggested that depreciation is provided by the straight line method. This writes off the cost of the relevant assets in equal instalments over their useful lives. However Councils should consider whether other more appropriate methods should be adopted depending on their circumstances. Any changes to depreciation methods or periods must be disclosed in the accounting policies and highlighted in notes in the year of change.
- 4.45 Depreciation should be charged to the income and expenditure account.
- 4.46 However, larger local councils must also meet the requirement contained in paragraph 3 of Schedule 1 to the Local Government Act 2003. This requires that where a larger local council meets any expenditure by borrowing, it shall in each financial year debit the 'appropriate amount' to the account from which that expenditure would otherwise fall to be met.
- 4.47 The 'appropriate amount' is a sum equivalent to an instalment of principal and interest combined such that if paid annually it would secure the payment of interest at the due rate on the outstanding principal together with the repayment of the principal not later than the end of the fixed period. The appropriate amount should be debited to the Income and Expenditure account with an offsetting credit to the Capital Financing account.
- 4.48 The effect of the statutory requirement is that the council's income and expenditure account will be debited each year with actual depreciation and any annual loan interest charges as well as the statutory cost of an annual instalment of debt plus interest within the 'appropriate amount'. Therefore, in order that taxpayers are not

affected by this double charge to the precept, larger local councils must make the necessary adjustments to their financial statements.

- 4.49 In order to reach an accurate Net Surplus or Deficit for the Year (see 4.92 below) larger local councils must each year reverse out from the income and expenditure account:
- the annual depreciation charge; and,
  - any actual loan interest paid.
- 4.50 These amounts should be credited to the Income and Expenditure account and debited to the Capital Financing Account. The Capital Financing Account will show the net cumulative effect of these offsetting adjustments. The annual reversal of depreciation is required whether the council borrows or not.
- 4.51 Practitioners are reminded that the duty to make a minimum revenue provision (MRP) contained in Regulation 21(1) of the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 does not apply to any community council. Regulation 21(2) states that a community council may charge to a revenue account any amount in respect of the financing of capital expenditure incurred by the community council in that year.

## ***Impairments***

- 4.52 Where a larger local council continues to adopt a policy of carrying tangible fixed assets at valuation the adjustment line in the Income and Expenditure account “Reversal of annual depreciation charge” should be renamed “Reversal of annual depreciation charge and impairments”
- 4.53 Where an impairment is charged to the income and expenditure account its impact should be reversed as follows:
- Debit Capital Financing Account
- Credit General fund: Reversal of annual depreciation charge and impairments
- 4.54 Any reversal of impairments in subsequent years should similarly be reversed.

## ***Leasing***

- 4.55 Leases take two forms. Finance leases are leases where substantially all of the risks of ownership are transferred to the council, Operating leases are defined as any lease that is not a finance lease. If, at the inception of a lease, the present value of the minimum lease payments, including an initial payment, amounts to substantially all (i.e. normally 90% or more) of the fair value of the asset subject to lease, it is presumed to be a finance lease.
- 4.56 A finance lease should be recognised on the balance sheet as an asset and also as an obligation to pay future rentals. At the inception of the lease the sum to be recorded both as an asset and a liability shall normally be the fair value of the asset. An asset held under a finance lease should be depreciated over the shorter of the lease term and its useful life.
- 4.57 The finance charge under a finance lease should be allocated to each accounting period over the lease term and a straight line method is reasonable,

- 4.58 Operating lease rentals should be charged to revenue on a straight line basis over the lease term whether or not this matches actual payments.
- 4.59 Hire purchase contracts which have the characteristics of a finance lease should be accounted for as a finance lease. Other hire purchase contracts should be treated as operating leases.

### ***Stock and Work In Progress (WIP)***

- 4.60 Stock and WIP should be included at the lower of cost or net realisable value.

### ***Short Term Investments***

- 4.61 Investments which will or may mature during the following financial year should be included in the balance sheet at the lower of cost or net realisable value.

### ***Debtors***

- 4.62 Debtors should be stated net of a provision for bad and doubtful debts where one is necessary. The note to the accounts should analyse debtors (with previous accounting period comparatives) analysed as to amounts falling due within one year and over one year. The following subdivision is suggested:

Trading debtor amounts falling due under one year  
Trading debtor amounts falling due after one year

Sundry Debtors

(Less: Provision for bad and doubtful debts)

= Subtotal Trading and Sundry Debtors

HM Revenue & Customs (VAT)

Cash with Officers

### ***Cash at Bank and In Hand***

- 4.63 Cash at bank should include current and deposit accounts as well as short-term investments such as building society and similar accounts. Cash in hand is the value of all petty cash floats.

### ***Creditors***

- 4.64 Trading creditors and the value of HM Revenue and Customs creditor should be identified in the supporting note, with VAT and payroll deductions (Income Tax, Employees and Employers NI) amounts due separately disclosed.
- 4.65 Amounts received by way of development contributions that are held on a conditional basis and may be repayable if not used for the purpose provided are not to be treated as reserves, but accounted as receipts in advance and included with creditors.

### ***Other short term liabilities***

- 4.66 Short term liabilities should include the current portion of long term debt – the capital amount of loans outstanding repayable within the next financial year.

## **Long Term Liabilities**

- 4.67 Long Term Borrowing: For those local councils that have taken out loans to finance capital expenditure a note to the accounts showing the nature of the borrowing and an analysis of the maturity profile is required. For ease of reading this may be presented in a table within the note identifying borrowing due to be repaid within one year, one to two years, two to five years and over ten years. The current portion of long term debt should be shown as a current liability.

## **Reserves**

- 4.68 Reserves are the net worth of the council at the accounting date. Reserves should only include amounts held by the council as development contributions where such contributions are unconditional.
- 4.69 The disclosure of reserves reflects the historic financial position as at the end of the accounting period. Further analysis by local councils into designated or undesignated reserves is optional and should only be presented as note to the accounts.

### **Capital Financing Account**

- 4.70 The Capital Financing Account is a non-distributable reserve used to hold the adjusting balances between annual depreciation and the statutory annual 'appropriate charge' for borrowing.

### **Revaluation Reserve**

- 4.71 The revaluation reserve is a non-distributable reserve used to hold the adjusting balances arising from the revaluation of assets. Where a council adopts a policy of carrying tangible fixed assets at a valuation, an annual adjustment should be made to the Revaluation Reserve in respect of the difference between the actual depreciation charge and the historical cost depreciation as follows:

Debit; Revaluation reserve

Credit: Capital Financing Account

For the excess of the actual depreciation charge compared with the historical cost depreciation.

### **Usable Capital Receipts Reserve**

- 4.72 Where a council disposes of an asset during the year, the proceeds of which are a capital receipt under the local Authorities (Capital Finance and Accounting)(Wales) Regulations 2003, the resultant gain or loss will be reported in the Income and Expenditure account. This amount should then be reversed out of the general fund as follows:

- Insert an additional line below the Net Operating Surplus or Deficit for the Year for "reversal of Gains and Losses"; and
- Process the following journals:

Debit: general Fund "Reversal of Gains and losses"

Credit: Usable Capital Receipts Reserve  
With the proceeds of sale; and

Debit: Capital Financing Account  
Credit: General Fund "Reversal of Gains and Losses"  
With the carrying value of the asset disposed

- 4.73 Where a larger local council acquires tangible fixed assets that it proposes to fund from usable capital receipts, an adjustment should be made by debiting the Usable Capital Receipts Reserve and crediting the Capital Financing Account. This adjustment should be reported in the Statement of Movements in Reserves

## ***Pensions***

- 4.74 Section 10 of the FRSSSE covers the accounting requirements for entities operating either direct contributions or defined benefits pension schemes and deals with matters of recognition, valuation and presentation as well as measurement.
- 4.75 The Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 (SI 2003/3239) (the 2003 Regulations) establish the principle that it is the actual contributions and payments in relation to retirement benefits, as required by the relevant Regulations that must be taken into account for the purpose of determining revenue (taxation) requirements.
- 4.76 Employees of local councils are usually members of the Local Government Pensions Scheme, a statutory scheme, which provides members with defined benefits (retirement lump sums and pensions) related to pay and service. As such councils should account for the retirement benefits on that basis.
- 4.77 However, although the Local Government Pensions Scheme (LGPS) is a defined benefits scheme, it may not always be possible to identify clearly and specifically the share of the underlying assets and liabilities of the particular scheme that relate to a larger local council's employees. It may therefore not be possible to determine a fair value of the scheme attributable to the Council's employees. This would occur, for example, where the scheme actuary groups a number of smaller admitted bodies together and determines a common contribution rate.
- 4.78 Councils are expected to obtain the best information available in relation to meeting accounting standards. The cost of obtaining information is not a barrier. In the event that information is available from the pension scheme actuary valuing the council's share of the pension scheme assets and liabilities, then this information must be applied in the preparation of the accounts.
- 4.79 If a fair valuation is not possible, larger local councils should account for pensions on a defined contributions basis (see 4.84 below).

### **Defined benefit schemes**

- 4.80 Where a fair valuation is possible, larger local councils should follow the requirements of section 10 and Appendix II of the FRSSSE and the statutory requirements set out in the 2003 Regulations.
- 4.81 Larger local councils following the requirements of this guidance must charge to the income and expenditure account an amount equal to the retirement benefits payments and contributions to pension funds which are payable for that year in accordance with statutory requirements of the 2003 Regulations.

4.82 This means that a number of adjustments must be made to proper practice accounting as set out in FRSSE.

4.83 Where a larger local council participates in a defined benefit pension scheme for which its share of assets and liabilities can be identified:

- A Pension Reserve should be included in the Reserves section of the balance sheet. The Pensions Reserve is an adjustment account that manages the effects of FRS17 changes made to the income and expenditure account against the statutory requirements for meeting the cost of retirement benefits from local taxes. It also absorbs the impact of actuarial gains and losses. It will normally balance exactly the pensions liability carried in the top half of the Balance Sheet. The movement on the pensions liability calculated as set out in the FRSSE needs to be reconciled to the pensions costs required to be made for council tax purposes by appropriations to or from the Pensions Reserve;
- An additional line in the Income and Expenditure account should be included between the Net Operating Surplus/Deficit for the Year and the Net Surplus/Deficit for the Year (to General Fund) described as Pension fund adjustment;
- Amounts included in the Income and Expenditure account in respect of the pension fund in accordance with the FRSSE (current service costs, past service costs, settlements, interest cost & expected return on assets) should be reversed out and replaced with the contributions payable by the council for the year as follows:

**Amounts included in the I&E**

Debit Pension Reserve

Credit Pension fund adjustment

**Contributions payable**

Debit Pension fund adjustment

Credit Pension Reserve

**Defined contribution schemes**

4.84 The cost of a defined contribution scheme (or of a defined benefits scheme where a fair valuation is not possible) is equal to the contributions payable to the scheme for the accounting period and should be recognised in the income and expenditure account. In addition, the following disclosures should be made in a note to the Income and expenditure account:

- the nature of the scheme
- the cost for the period
- any outstanding or prepaid contributions at the balance sheet date.

## ***Revenue expenditure funded from capital under statute (REFCUS)***

- 4.85 Section 16 of the Local Government Act 2003 provides that the Welsh Assembly Government may:
- (a) by regulations provide that expenditure of local authorities shall be treated as being, or as not being, capital expenditure; and
  - (b) by direction provide that expenditure of a particular local authority shall be treated as being, or as not being, capital expenditure.
- 4.86 A capitalisation direction enables specific revenue expenditure to be treated as capital expenditure. Instead of charging it to revenue it may be funded from borrowed money or capital receipts
- 4.87 An additional line should be included in the Income & Expenditure Account below “Net Operating Surplus or Deficit for the Year” entitled “Revenue expenditure funded from capital under statute”.
- 4.88 Where there are revenue items included within the Income & Expenditure that are to be funded from capital under statute these should be adjusted as follows:
- Debit: Capital Financing Account
- Credit: General Fund “REFCUS”.

## ***Post Balance Sheet Events***

- 4.89 Post balance sheet events whether favourable or unfavourable are identified as either adjusting or non adjusting events. Adjusting events are those that provide evidence of conditions that existed at the balance sheet date. Non-adjusting events are those that are indicative of conditions that arose after the balance sheet date.
- 4.90 Councils should adjust the amounts recognised in the accounts to reflect adjusting events after the balance sheet date.
- 4.91 Councils should not adjust the accounts for non-adjusting events after the balance sheet date. However if the event is material it should be disclosed by way of a note identifying the nature of the event and an estimate of its financial effect if it can be made, or a statement otherwise.

## ***Related Party Transactions***

- 4.92 Two or more parties are related if at any time during the accounting period:
- One party has a direct or indirect control of the other party; or
  - The parties are subject to common control from the same source; or
  - One party has significant influence over the financial and operating policies of the other party.
- 4.93 Where a council purchases, sells, transfers goods and other assets or liabilities, renders or receives services or provides or receives financial support to or from a

related party of a material nature such transactions must be disclosed. Transactions with members of the council or with companies controlled by them should be disclosed.

- 4.94 Disclosure of pension contributions and employees salaries, transactions with utility companies and government departments and agencies are not required to be reported as related party transactions.

### ***Signing and Approval of the Accounts***

- 4.95 The financial statements should be prepared and approved in accordance with Regulations 8 and 9 of the Accounts and Audit (Wales) Regulations 2005 as amended and be signed and certified by the responsible financial officer and submitted for approval by the council in accordance with the regulations.

## **Section B: The Statements of Account**

### ***General Disclosure Requirements***

- 4.96 The financial statements should state that they have been prepared on the basis of this guidance. Any departure from the guidance so that the statements present fairly should be disclosed and the reasons for the departure identified together with an explanation of how the position shown in the financial statements is different as a result of the departure.
- 4.97 The financial statements shall include:
- a description of each material accounting policy followed;
  - details of any changes to the accounting policies followed in the preceding period, and in addition to the disclosures necessary for prior period adjustment, a brief explanation of why each accounting policy is more appropriate and where practicable a indication of the effect on the current accounting period;
  - where the effect of a change to an estimation technique is material, a description of the change and where practicable an indication of the effect on the results of the current accounting period;
  - disclosure of any material uncertainties as to the going concern presumption should be disclosed; and
  - comparative amounts from previous accounting periods for every item disclosed in the balance sheet, income and expenditure accounts and notes to the financial statements, with the exception of details of additions and disposals etc of fixed assets and their cumulative depreciation.

### ***Annual Report***

- 4.98 The FRSSE requires the preparation of an annual report along with the financial statements. This formal annual report, is a useful means of presenting detailed financial information in the context of the council's operating environment. Larger local councils should prepare an annual report along with their financial statements
- 4.99 Councils which include an annual report should note that it will not be subject to detailed audit review although auditors will report by exception any inconsistency with the financial statements. Preparers of financial statements should ensure that there is internal consistency throughout before presenting the financial statements to the council for approval. The annual report should be approved by the council and signed by the Chair accordingly.
- 4.100 The annual report should be an easily understandable guide to the most significant matters reported in the financial statements. It should provide an explanation in overall terms of the council's financial position, and assist in the interpretation of the financial statements. It should also contain a commentary on principal activities of the council, the major influences affecting the council's income and expenditure during the year and information on the financial needs and resources of the council.
- 4.101 Where the council prepares an annual report, the following disclosures should be included::
- a description of the principal activities of the council;
  - details of the Members of the council; and

- a statement describing the policy adopted in relation to disabled people (only required if over 250 employees).

4.102 The annual report should be concise and restricted to significant matters. It should include such items that are likely to be significant to the understanding of the financial statements such as:

- an explanation of which statements follow, their purpose and the relationship between them;
- a comparison of expenditure in the year with the original budget for the accounting period, and an explanation of significant variations from it;
- a brief note of any major fixed asset acquisitions and disposals or material liabilities incurred;
- an explanation of any material and unusual charge or credit in the accounts;
- any significant change in accounting policies. The reason for the change, and the effect on the accounts, should be explained;
- any major change in statutory functions which has a significant impact on the accounts. In addition, a comment on planned future developments in service delivery, including a summary of revenue and capital investment plans, distinguishing between expenditure intended to maintain existing levels of service provision and that intended to expand existing services or develop new services;
- a brief note of the council's current borrowing facilities and capital borrowing, outlining the purpose and impact of financing transactions entered into during the year; and
- a summary of the council's internal and external sources of funds available to meet its capital expenditure plans and other financial commitments.

## ***Annual Governance Statement***

4.103 Regulation 4 of the Accounts and Audit (Wales) Regulations requires each council to conduct an annual review of the effectiveness of its system of internal control. Once complete the council must report its findings by including a statement on internal control, prepared in accordance with proper practices, with its annual accounting statements.

4.104 Part 2 of this guidance is recognised by the Welsh Assembly Government as a source of proper practice and requires the production of an annual governance statement. Therefore the financial statements should include the annual governance statement. The annual governance statement should contain:

- an acknowledgement of council's responsibility for ensuring there is a sound system of internal control;
- an indication of the level of assurance that a system of internal control can provide;
- a brief description of the key elements of the internal control environment;
- a brief description of the process that has been applied in maintaining and reviewing the effectiveness of the system of internal control, including some comment on the role of the council and any committee charged with an overview

of the council's governance arrangements, internal audit and any other assurance mechanisms; and

- an outline of the actions taken, or proposed, to deal with significant internal control issues.

4.105 The statement should be signed by the chair of the council and the chief executive officer or clerk of the council. The minimum amount of disclosure required in the annual governance statement is the same as that contained in the annual return used by smaller local councils (See part 2 of the Practitioners' Guide guide) Larger councils may wish to apply the guidance contained in the joint CIPFA/SOLACE framework - Delivering Good Governance in Local Government.

### ***The Statement of Responsibilities for the Accounts***

4.106 The statement of responsibilities should:

- acknowledge the council's responsibilities for the proper administration of its financial affairs and the appointment of a responsible financial officer (RFO);
- acknowledge the council is required to manage its affairs to secure economic, efficient and effective use of its resources;
- set out the RFO's responsibilities for the preparation of the accounts, the selection and application of appropriate accounting policies, for estimation techniques and compliance with generally accepted accounting practice, the maintenance of proper records and steps taken to prevent and detect irregularities; and
- the statement should be signed and dated by the responsible finance officer

### ***Statement of Accounting Policies and Estimation Techniques***

4.107 The statement should include the following:

- an acknowledgement that the accounts have been prepared in accordance with proper accounting practices and this guidance;
- the fundamental accounting concepts and estimation techniques used in the preparation of the financial statements (accruals, relevance, consistency, reliability, comparability, understandability, materiality, and going concern);
- for fixed assets, the basis of recognition, initial measurement, valuation, depreciation and disposal of each class of tangible fixed assets;
- the accrual of income and expenditure;
- the treatment of contingent liabilities and contingent assets;
- the basis on which stocks are included in the accounts;
- the accounting treatment for capital receipts;
- the accounting treatment for grants and contributions;
- the accounting treatment for leases and other similar instruments;
- the recognition and treatment of provisions and other liabilities;

- the recognition and treatment of balances and earmarked and general reserves;
- the accounting treatment for pensions;
- the reporting of contingent liabilities and contingent assets;
- the accounting treatment for post balance sheet events;
- exceptional items, extraordinary items and prior period adjustments; and
- the accounting treatment of acquired or discontinued operations.

4.108 If other material accounting policies are adopted and applied these should also be fully disclosed here.

### ***The Income and Expenditure Account***

4.109 The income and expenditure account should include information for both current and prior year accounting periods.

4.110 Revenue arises from precepts, grants, rents, interest and other investment income, delivering services and sundry activities.

4.111 It is recommended that the analysis of income and expenditure should contain a summary of the main fund raising and spending areas:

#### **Income**

Precept  
 Grants received  
 Rental income, interest and investment income  
 Charges made for services  
 Other income or contributions

#### **Expenditure**

*Direct Service Costs*  
 Salaries and Wages  
 Grant-aid expenditure  
 Other costs

*Democratic, Management and Civic Costs*  
 Salaries & wages  
 Other costs

#### **Exceptional Items (if any)**

Gains or losses on disposal of fixed assets

#### **Net Operating Surplus or Deficit for Year**

Reversal of annual depreciation charge (usually a Cr)  
 Statutory charge for capital ('the appropriate amount') (Dr)

#### **Net Surplus or Deficit for Year (to General Fund)**

### **Disclosure Notes to the I & E Accounts**

1. An analysis of grants received. Grants may be received from other local authorities. The nature and the amount of grants received should be identified where material.
2. Information about the Pension Scheme offered to employees identifying the administering authority, the nature of the scheme, the cost for the period and the amount of any outstanding or prepaid contributions at the balance sheet date.
3. Disclosure of remuneration of staff earning over £60,000 per annum in bands of £10,000 with current year and previous year numbers of employees<sup>7</sup>.
4. Audit fees and expenses
5. Related party transactions: Councils should disclose related party transactions that are material to the Council's accounts including:
  - the name of related parties;
  - a description of the relationship;
  - the amounts involved;
  - any other elements of the transaction necessary for an understanding of the financial statements;
  - the amounts due to or from related parties at the balance sheet date and any provisions for doubtful debts at that date; and
  - any amounts written off in the accounting period in respect of debts due from related parties.
6. Details of adjustment for depreciation and calculation of the 'appropriate amount.
7. Overheads including depreciation should be included within other costs under Democratic, Management and Civic Costs. A note to the accounts should provide an analysis of these costs into the principal components.

### ***The Statement of Movement of Reserves***

- 4.112 This statement reconciles the change in reserves between accounting periods.
- 4.113 It is anticipated that this statement will be provided in columnar form showing each separate reserve, as reported on the balance sheet, and the net movements during the year that reconcile the opening balance to the closing balance. Supporting this table should be detailed reconciliations in respect of those reserves where this is not already provided elsewhere in the accounts. For example; Capital Financing Account, Earmarked reserves, Usable Capital Receipts Reserve. Where the detail is elsewhere in the accounts this should be cross referenced from the statement.

### ***The Statement of Total Recognised Gains and Losses***

- 4.114 Where it is prepared, the presentation of a statement of total recognised gains and losses should have the same prominence as the income and expenditure account. The statement should include all gains and losses that are not included in the income and expenditure account such as surplus or deficit arising on revaluation of fixed assets.
- 4.115 In the case of local councils who account for assets on an historic cost basis and account for pensions on a defined contribution basis it is likely that all gains and

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<sup>7</sup> This is a requirement of regulation 7(2) of the Accounts and Audit (Wales) Regulations 2005 as amended.

losses will have been recognised in the income and expenditure account and therefore this statement will not be required.

4.116 If required, the format of the statements is:

- Surplus or deficit on the income and expenditure account
- Surplus or deficit on the revaluation of fixed assets
- Actuarial gains or losses on pension fund assets or liabilities (not required for councils accounting for pension funds on a defined contribution basis)
- Any other gains or losses.

4.117 Current accounting period and prior period comparatives are required.

## ***The Balance Sheet***

### **+ Intangible Assets (if any)**

### **+Fixed Assets**

Land and Buildings  
Vehicles and Plant  
Non – operational assets

### **+Current Assets**

Stock and Work in Progress  
Debtors and Prepayments  
Short term Investments  
Cash at bank and in hand

### **-Current Liabilities**

Creditors and receipts in advance  
Current portion of long term debt

### **=Net Current Assets**

### **=Total Assets less Current Liabilities**

### **-Long Term Borrowing**

### **=Total Assets less liabilities**

### **= Reserves**

Usable capital receipts reserves  
Revaluation Reserve (if used)  
Capital Financing account  
Earmarked Revenue Reserves  
General Reserves

## **Disclosure Notes to the Balance Sheet**

1. Post balance sheet events: Disclosure of any material non adjusting post balance sheet event is required and should include the nature of the event and estimate of its financial effect, or a statement that such an estimate cannot be made
2. Tangible Fixed Assets and Depreciation: The notes to the accounts should disclose;
  - the cost or valuation at the beginning of the accounting period
  - the effect of any revaluation made during the accounting period
  - acquisitions made during the accounting period
  - disposals made during the accounting period.

The accounts should also disclose:

- the cumulative amount of depreciation at the beginning of the accounting period,
- the amount of any depreciation during the accounting period
- the amount of any adjustments made on disposal during the accounting period
- the amount of any other adjustments made during the accounting period

Note: Investment properties are not depreciated

3. Leases:
  - Finance Leases: Assets held under finance leases can either be aggregated with other fixed assets owned by the council along with the accumulated depreciation or be disclosed separately. If disclosed in aggregate the net amount of assets held under finance leases and the amount of depreciation allocated should be separately disclosed. In addition the amount of future obligations related to finance leases should be disclosed
  - Operating Leases: The note should disclose the payments which the council is committed to make during the next year analysed between those in which the commitment expires within that year, in the second to fifth years inclusive and over five years from the balance sheet date, showing separately the commitments in respect of leases of land and buildings and other operating leases.

## ***The Auditor's Report***

- 4.118 The external auditor will report in accordance with the Auditor General's Code of Audit and Inspection Practice and in accordance with guidance issued by the Auditor General.