performance in public services

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Local Government Pension Funds: Accounting update

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This session will cover:

- Changes to example pension fund accounts for 2016/17

- Current developments

CIPFA performance in public services

2016/17 example accounts

Main changes are:

- Management costs
- IFRS 13

Management costs guidance

2014 guidance was re-published in June 2016 following extensive consultation with practitioners and stakeholders

Incorporated into example accounts for 2016/17

Aims to build on the general principles established in 2014 with:

- more detailed accounting guidance
- worked examples for practitioners

Guidance only – recommended, but not mandated by Code

Management expenses

Suggested disclosure note

Note 11: Management expenses

2015/16		2016/17
£000		£000
3,948	Administrative costs	4,248
9,215	Investment management expenses	8,137
845	Oversight and governance costs	885
14,008		**13,270**

Investment costs

Suggested disclosure note

Note 11 a: Investment management expenses

2015/16 £000		2016/17 £000
835	Transaction costs	987
5,975	Management fees	4,520
2,215	Performance related fees	2,415
190	Custody fees	215
9,215		**8,137**

No further analysis of administrative, oversight and governance or transaction costs in example accounts as these are not significant for most LG pension funds

Investment costs - recognition

Cost is defined as “ an amount that has to be paid to buy or obtain something”...and a **liability** as “ being legally responsible for something”…

- Code does not permit netting off costs against income
- The Guidance reinforces this for LGPS accounting by grossing up investment costs and income
- Requires liaison with Fund Managers to identify fees/costs deducted at source
- Be careful not to end up accounting for costs that were never your responsibility to pay in the first place!

Back to basics – consider:

- Am I legally responsibility for these costs?
- What is the corresponding entry in the fund manager’s accounts?
- Am I carrying the risks associated with these investments?
- Do I have control over whether or not these costs are incurred?

IFRS 13 Fair value measurement

Fair value underpins many IFRS and the Code **BUT** inconsistent or unclear requirements have led to a lack of comparability between financial information

IFRS 13 aims to provide a consistent definition of fair value based on

...the **"highest and best price"**...that can be obtained in the **"most advantageous market",** with additional disclosures to explain the valuation techniques applied

Adopted as a Code requirement for principal authorities from 2015/16, and for LGPS from 2016/17

LGPS and Fair Value

All pension fund investments are revalued every year with the change in value taken to the Fund Account

↓

Current assets and liabilities are valued at amortised cost, and outside the scope of IFRS 13

↓

IFRS 13 has limited impact as there should be no difference between "carrying value" and "fair value" for **most** LGPS assets and liabilities

↓

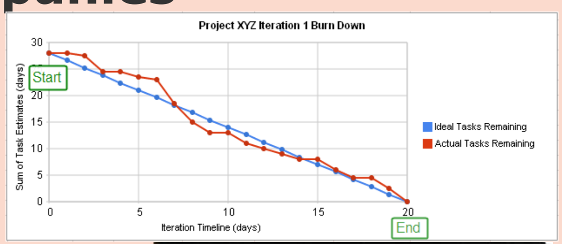
But there are some specific scenarios where IFRS13 might apply if the LGPS has directly held property, artefacts or shares

3 specific areas where IFRS 13 might apply

Directly held land and property

Consider whether a higher price could be obtained by amalgamating adjacent sites, removing covenants or changing current use

Shares in unquoted companies



Usually valued on a going concern basis BUT if company has saleable assets (stock, buildings, equipment or intellectual property) a breakup valuation may achieve a higher price

Art and Antiques

Basis of valuation should be specialist auction sale NOT house clearance or out of date insurance value

IFRS 13 - Extra disclosures required

Extended scope:

- Valuation method for each asset class
- Analysis by level 1,2,3 hierarchy

New disclosures:

- Narrative and quantitative assessment of sensitivity to changes in valuation methods and market conditions
- Any transfers between levels of fair value hierarchy
- For level 3 measurements
  - Quantitative information on significant unobservable inputs
  - Reconciliation of opening to closing balances showing movements in year
- Distinguish unrealised gains/losses from realised gains/losses in the Fund Account

Other changes

- Aligned investment asset classification with Pension SoRP 2015
- Note 16c – level 1 to 3 hierarchy amended to exclude loans & receivables
- Separate disclosure of members allowances, audit fees and taxation where significant AND costs can be separately identified
- Key management personnel disclosure now required

Key management personnel compensation – who and what

Who?

- “chief officers, elected members….having authority and responsibility for planning, directing and controlling the activities….” [Code 3.9.2.2]

What?

- Compensation includes:
  a) Short-term employee benefits eg pay, NI, annual leave
  b) Post-employment benefits eg pension
  c) Other long-term post-employment benefits
  d) Termination benefits
  e) Share-based payments
- Disclose in total and for each category
  - No names required

Key management compensation –in practice

Element	Officers	Members	Measurement
S/t benefits	Pay etc	N/A	IAS 19
Post-employment	Pensions	Pensions?	IAS 19
Other l/t benefits	Unlikely	N/A	IAS 19
Termination benefits	Potentially	N/A	IAS 19
Share-based pay'ts	Unlikely	N/A	IFRS 2

Action:
- Identify KMP early
- Identify possible benefits
- Engage actuary

Current developments

- Faster closedown
- IFRS 9 Financial Instruments

Faster Closedown

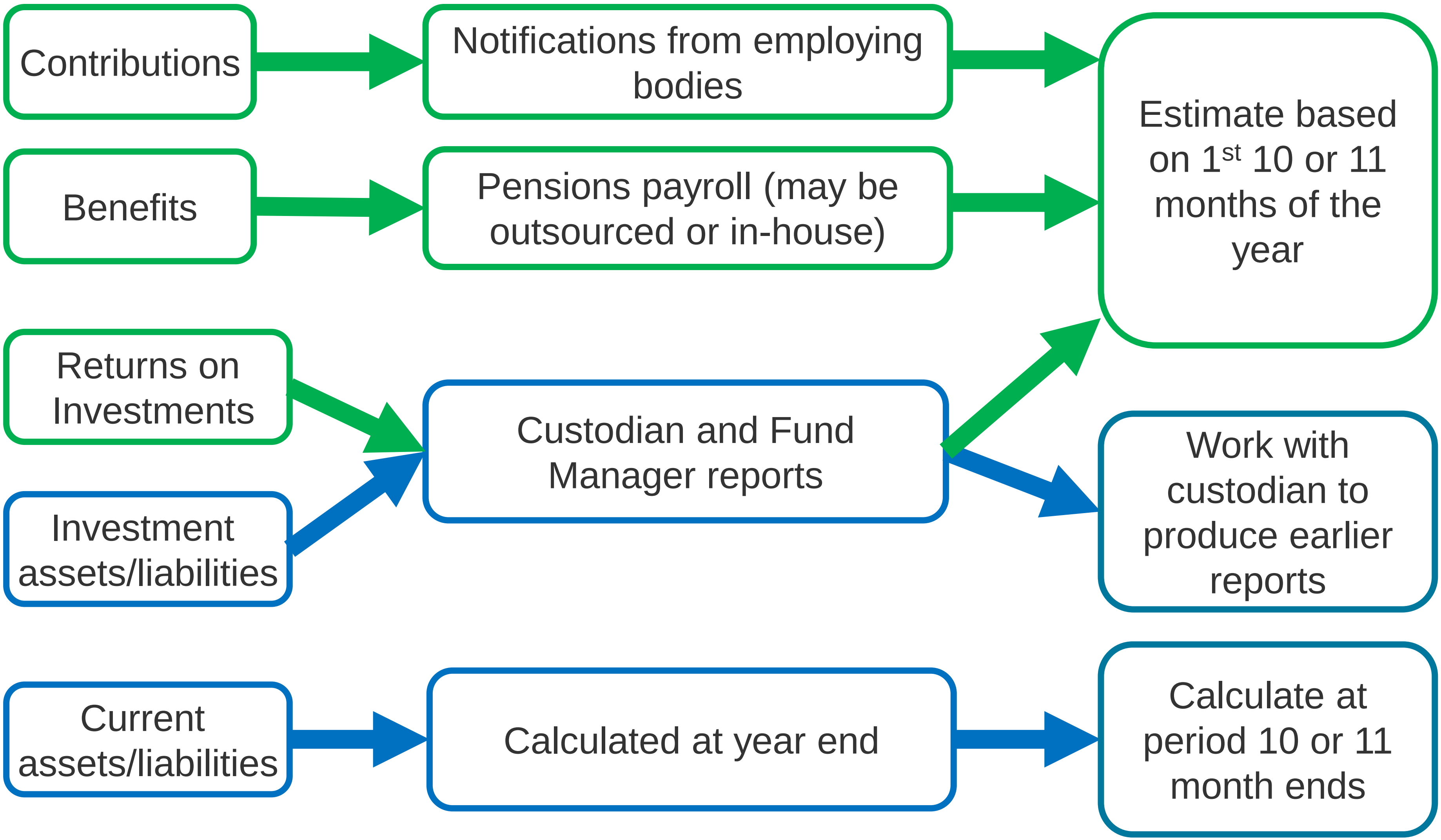
Why bother?

- provides more timely and relevant information to stakeholders
- statutory requirement in England
- allows time to adapt processes for next year based on lessons learn because audit concludes earlier
- early programme builds in capacity to deal with emerging issues
- once bedded in drives efficiency and continual improvement
- frees up resources to focus on added value
- staff motivation improved

What this means in practice

- ✓ Better planning and organisation
  - Begin with the end in mind – plan backwards
- ✓ Practice in-year – quarterly closedown
- ✓ Share the workload
- ✓ Prioritise closedown so deadlines are achieved
- ✓ Streamline and automate processes
  - align ledger reporting to Code
  - close on estimates
- ✓ Manage the audit process
  - clear working papers
  - in-built and demonstrable QA
- ✓ Quicker production of annual report

Estimation techniques

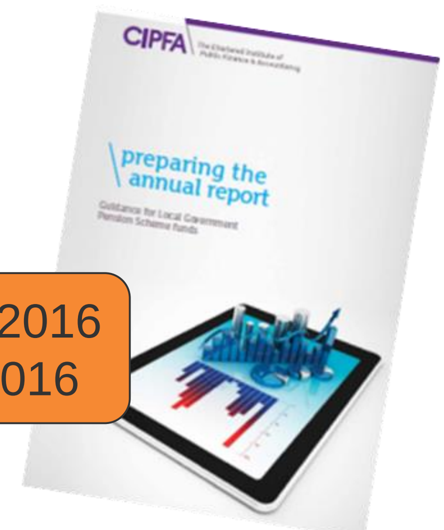


Annual report publication

- ✓ Start early
- ✓ De-couple strategic documents and financial years
- ✓ Use CIPFA guidance to identify what you want, from whom and when
- ✓ Ensure documents needed are kept up to date
- ✓ Allow time for Member/s151 input and approval

Draft to audit 1 May 2015
Published 18 May 2015

Draft to audit 9 April 2016
Published 14 July 2016



IFRS 9 Financial Instruments

Approved by IASB July 2014:

- New classification categories for financial instruments
- Simplified hedge fund accounting
- Current methods of accounting for realised/unrealised gains and losses to be replaced with an annual charge for expected credit loss impairments
- Some additional disclosure requirements

Current expectation is that IFRS 9 will be adopted as a Code requirement for 2018/19

IFRS 9 – expected credit losses

Accounting will move from an "incurred loss" to an "expected loss" basis, reflected as an annual charge in the accounts

This earlier recognition of **possible** (as opposed to **actual**) impairments will be recognised based on:

- Current credit risk
- Any significant increase in credit risk expected over the next 12 months
- Any objective evidence of impairment

This process will be based on annual reviews at each balance sheet date and will require:

- Exercise of judgement by senior management
- Advice from experts (fund managers)
- Record keeping to track losses as they are recognised in the accounts

Any questions?

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