the 2016/17 code of practice on local authority accounting in the united kingdom

invitation to comment

the people
in public finance

invitation to comment

Introduction

1. Local authorities in the United Kingdom are required to keep their accounts in accordance with 'proper practices'. This includes, for the purposes of local government legislation, compliance with the terms of the *Code of Practice on Local Authority Accounting in the United Kingdom* (the Code), prepared by the CIPFA/LASAAC Local Authority Accounting Code Board (CIPFA/LASAAC). The Code is reviewed continuously and is issued annually.

2. Under the oversight of the Financial Reporting Advisory Board, CIPFA/LASAAC is in a position to issue mid-year updates to the Code. However, this will only be done in exceptional circumstances.

3. The edition of the Code that is applicable for a financial year is based on accounting standards in effect on 1 January prior to the start of the financial year. For the 2016/17 Code, this means that European Union (EU) adopted accounting standards with an effective date of 1 January 2016 or earlier will need to be taken into account.

4. This ITC sets out CIPFA/LASAAC's proposals for developing the new edition of the Code (the 2016/17 Code) to apply to accounting periods commencing on or after 1 April 2016 (Section B of this ITC). As there are a number of complex issues covered in this ITC it also contains an Executive Summary (Section A) which highlights the most significant issues which interested parties will need to consider.

5. The proposed developments for the 2016/17 Code are:

   (a) The measurement of the Highways Network Asset (transport infrastructure assets) at Depreciated Replacement Cost,
   (b) A review of the Accounting and Reporting by Pension Funds section of the Code,
   (c) Narrow Scope Amendments to International Financial Reporting Standards,
   (d) Augmentation of the Code's provisions on Concepts following the issue of the IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*
   (e) Legislative amendments, and
   (f) Other minor and drafting amendments.

6. This ITC also includes commentary on the adoption of IFRS 9 *Financial Instruments* and IFRS 15 *Revenue from Contracts with Customers* in future editions of the Code and seeks interested parties' views on whether there are likely to be any substantial application issues when they are adopted by the Code.

7. A separate consultation on the opportunities for improving the presentation of local authority financial statements is also available on the consultation pages of the CIPFA website. That consultation considers proposed changes to Sections 3.1 and 3.4 of the Code as does this consultation paper and therefore the same Exposure Draft (ED1) has been provided for both consultations.

The Consultation Process

8. Where CIPFA/LASAAC is interested in specific issues, consultation questions have been included in the ITC. However, CIPFA/LASAAC welcomes comments on any aspect of the draft 2016/17 Code. In order to assess comments properly CIPFA/LASAAC would prefer respondents to support comments with clear accounting reasons and, where applicable, preferred alternatives.

9. Responses to this Invitation to Comment will be regarded as on the public record and are required to be published on the CIPFA website unless confidentiality is specifically requested on the response form. If you require your response to be treated as confidential please indicate this clearly on the response itself. Copies of all correspondence and an analysis of responses will be provided to the Financial Reporting Advisory Board.

10. A copy of the Exposure Drafts of the 2016/17 Code in pdf format can be down-loaded from the CIPFA website.

11. To assist interested parties to respond to the consultation, a response form (in Word format) is attached. We would be grateful if respondents to the consultation could use this form as this will speed up the analysis.

12. Responses are required by **9 October 2015** and may be sent to:

The Secretary

CIPFA/LASAAC Local Authority Accounting Code Board

Policy and Standards Directorate

CIPFA

77 Mansell Street

London

E1 8AN

Fax: 020 7543 5695

(For ease of handling, e-mailed responses using the Word document form provided are preferred.)

SECTION A – EXECUTIVE SUMMARY

Introduction

13. This Invitation to Comment is predominantly focussed on the changes to the 2016/17 *Code of Practice on Local Authority Accounting in the United Kingdom* (the Code). The changes that are covered by the Code are those that arise as a result of CIPFA/LASAAC's development programme for the Code. The proposals for change include:

- Fundamental Changes to the Code as a result of **the move to measuring the Highways Network Asset** at Depreciated Replacement Cost in accordance with the measurement methodologies specified in the CIPFA *Code of Practice on Transport Infrastructure Assets*. This change was originally announced in the 2014/15 Code. It will see the creation of a new Highways Network Asset (a network of components of transport infrastructure assets) and includes specific recognition, measurement and derecognition policies for these assets.

- Changes as a result of **the review of Accounting and Reporting by Pension Funds section of the Code**. One of the most substantial changes included in the Code is the adaptation of the Code's adoption of IFRS 13 to bring the pension fund investments within the scope of the fair value measurement disclosures.

- A number of **narrow scope amendments** to International Financial Reporting Standards (IFRSs). These largely comprise clarifications of the provisions of individual standards. The Narrow Scope amendments include amendments to:

  - IAS 1 *Presentation of Financial Statements*, under the International Accounting Standard's Board Disclosure Initiative – although these changes are substantially made in response to overly prescriptive interpretations of the wording of IAS 1, CIPFA/LASAAC very much supports these changes as they should enable local authorities to ensure that they tell the most effective story within their financial statements.

  - IAS 19 *Employee Benefits*, Defined Benefit Plans: Employee Contributions – the options in these proposals are in line with the accounting policies already used by local authorities for employee contributions.

  - *Annual Improvements to IFRSs 2010 – 2012 Cycle* – the impact on local authority accounting and the changes proposed to the Code are summarised in Appendix A to this ITC. The changes proposed for the treatment of accumulated depreciation and impairment property, plant and equipment have led to CIPFA/LASAAC making its own changes for local authority circumstances in line with the normal approach used by local authorities.

  - *Annual Improvements to IFRSs 2012 – 2014 Cycle* – the majority of these changes will not impact on local authority financial reporting: see Appendix B.

  - IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* – Clarification of Acceptable Methods of Depreciation and Amortisation – these changes apply to local authorities though CIPFA/LASAAC considers that local authorities do not use the depreciation and amortisation methods prohibited by the amendments to the standard.

- IFRS 11 *Joint Arrangements* – Accounting for Interests in Joint Operations – this technical change applies to local authorities – ie that an acquirer of an interest that meets the definition of a business is required to apply all of the principles of business combinations in IFRS 3 (with the exception of the principles that conflict with guidance in IFRS 11).

- IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011), Sale or Contribution of Assets Between an Investor and its Associate or Joint Venture. Although this change will apply to local authorities it is unlikely to be a regular transaction for local authorities (and may actually) not be adopted by the European Union in time for the effective date of the 2016/17 Code.

- IAS 27 *Separate Financial Statements* (2011), Equity Method in Separate Financial Statements, CIPFA/LASAAC considers that this change should not be applied to local authorities to maintain the reliability of the local authority single entity financial statements.

▪ **Augmentation of the Code's provisions on Concepts (section 2.1) following the issue of the IPSASB Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities** - the changes proposed include:

  - improvements to the objectives of the local authority financial statements

  - further provisions on the users of local authority financial statements ie that the primary users are service recipients and resource providers, and

  - further commentary for the public sector context that clarifies that information should not be excluded because it is complex.

▪ **Legislative Changes** – the legislative changes include:

  - Amendments due to the **Local Audit and Accountability Act 2014** and **the Accounts and Audit Regulations for English Authorities**, the new Act and Regulations will mean changes to the relevant references throughout the Code but also to the narrative reporting requirements in the Code. However, the principles set out in the Code for the part of the Regulations that require that the narrative report "must include comment by the authority on its financial performance and economy, efficiency and effectiveness in its use of resources over the financial year" will also be confirmed in guidance issued by CIPFA following the consultation.

  - Amendments due to **the Local Government (Accounts and Audit) Regulations (Northern Ireland)** – these update the factual references in the Code.

  - Amendments resulting from new statutory guidance (Finance Circular 4/2015) issued by the Scottish Government on **Accounting for Equal Pay and Severance.**

14. This ITC also includes a high level overview of **two new standards anticipated to apply to future editions of the Code** ie IFRS 15 *Revenue from Contracts with Customers (*anticipated to apply to the 2018/19 Code) and IFRS 9 *Financial*

Instruments (anticipated to apply to 2018/19 Code). CIPFA/LASAAC does not consider that there are any issues where application of the Code should require specific adaptation for IFRS 15. Application issues may arise for IFRS 9. However, CIPFA/LASAAC is seeking interested parties' views on the application of IFRS 9 to financial instruments held by local authorities.

15. A separate consultation which will lead to fundamental changes to the Code *Telling the Story – Consultation on Improving the Presentation of Local Authority Financial Statements* is being issued at the same time as this consultation. This uses the same Exposure Draft for the changes to sections 3.1 and 3.4 of the Code. The consultation will be available on www.cipfa.org/tellingthestory2016.

Full List of Questions on the Exposure Drafts of the 2016/17 Code

The Measurement of the Highways Network Asset

Q1	Do you agree with the proposed new Section 4.11 and the proposed amendments to section 4.1 of the Code for the definition, recognition and scope of the Highways Network Asset? If not, why not? What alternatives do you suggest?
Q2	Do you agree with the proposed new Section 4.11 and the proposed amendments to section 4.1 of the Code for the measurement of the Highways Network Asset? If not, why not? What alternatives do you suggest?
Q3	Do you agree with the proposed new Section 4.11 and the proposed amendments to section 4.1 of the Code for the derecognition of components of the Highways Network Asset? If not, why not? What alternatives do you suggest?
Q4	Do you agree with the transitional provisions in the Code for the move to measurement of the Highways Network Asset at DRC? If not, why not? What alternatives do you suggest?

The Review of the Accounting and Reporting by Pension Fund Section of the Code

Q5	Do you agree with the proposed amendments to the (Pension) Fund Account in Section 6.5 of the Code? If not, why not? What alternatives do you suggest?
Q6	Do you agree with the proposed amendments to the (Pension) Net Assets Statement in Section 6.5 of the Code? If not, why not? What alternatives do you suggest?
Q7	Do you agree that the Code should adapt IFRS 13 *Fair Value Measurement* and remove the scope exclusion for section 6.5 of the Code for disclosures? If not, why not? What alternatives do you suggest?
Q8	Do you consider that the Code should only include option A for the reporting of the Actuarial Present Value of Promised Retirement Benefits or should all three options be retained? Please set out the costs and benefits of your preferred option for the users and preparers of pension fund financial statements.

Q9 Do you agree that the Code should include a recommendation to disclose transaction costs for investment management per the proposals in paragraph 6.5.5.1 v) of the Exposure Draft of the Code? If not, why not? What alternatives do you suggest?

Q10 Do you agree with the addition of the Annex to section 6.5 which includes an overview of how the remaining sections and chapters of the Code apply to local authority pension funds? If not, why not? What alternatives do you suggest?

Q11 Do you agree that the Exposure Draft of section 6.5 of the Code appropriately provides for the requirements for the reporting of Scottish pension funds? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IAS 1 *Presentation of Financial Statements*, Disclosure Initiative

Q12 Do you agree with the approach to the adoption of the Amendments to IAS 1 (Disclosure Initiative) in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IAS 19 *Employee Benefits*, Defined Benefit Plans: Employee Contributions

Q13 Do you agree with the approach to the adoption of IAS 19 *Employee Benefits* (Defined Benefit Plans: Employee Contributions) in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: Annual Improvements to IFRSs 2010 – 2012 Cycle

Q14 Do you agree with the approach to the adoption of the Annual Improvements to IFRS 2010 - 2012 Cycle in the Code? If not, why not? What alternatives do you suggest?

Annual Improvements to IFRSs 2012 - 2014 Cycle

Q15 Do you agree with the approach to the adoption of the Annual Improvements to IFRS 2012 - 2014 Cycle in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*, Clarification of Acceptable Methods of Depreciation and Amortisation

Q16 Do you agree with the approach to the adoption of the Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IFRS 11 *Joint Arrangements*, Accounting for Acquisitions of Interests in Joint Operations

Q17 Do you agree with the approach to the adoption of the Amendments to IFRS 11 *Joint Arrangements,* Accounting for Acquisitions of Interests in Joint Operations in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011), Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

Q18 Do you agree with the approach to the adoption of the Amendments to IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011) - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture in the Code? If not, why not? What alternatives do you suggest?

Augmentation of the Code's Provisions on Concepts - The IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*

Q19 Do you agree with the approach to the amendments to section 2.1 of the Code based on the IPSAB Conceptual Framework? If not, why not? What alternatives do you suggest?

The Local Audit and Accountability Act 2014 and the Accounts and Audit Regulations 2015 (English Authorities)

Q20 Do you agree with the proposed amendments to Chapter 1 of the Code for the application of the Code to the relevant authorities covered by the Accounts and Audit Regulations 2015? If not, why not? What alternatives do you suggest?

Q21 Do you agree with the approach to the proposed amendments to Section 3.1 of the Code for the narrative statement for local authorities in England? If not, why not? What alternatives do you suggest?

Q22 Do you consider that there are any other areas of Narrative Reporting which ought to be stipulated in the Code? Please provide reasons for your response.

Q23 Do you agree with the proposed amendments to Section 3.4 of the Code as a result of the application of the Accounts and Audit Regulations 2015 to the provisions of Code for English local authorities? If not, why not? What alternatives do you suggest?

Q24 Do you agree with the proposed amendments to Section 3.4 of the Code as a result of the application of the Accounts and Audit Regulations 2015 to the provisions of the Code for English local authorities? If not, why not? What alternatives do you suggest?

The Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015

Q25 Do you agree with the proposed amendments to the Code for the Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015? If not, why not? What alternatives do you suggest?

Minor Amendments

Q26 Do you agree with the proposed amendments to the Code to reflect the new Statutory Guidance on Equal Pay and Severance for Scottish Authorities? If not, why not? What alternatives do you suggest?

Further Guidance

Q27 Are there any areas within the Code where additional guidance or improvements to the Code would be helpful? Please support your answer by giving details of the difficulties being experienced.

Future Editions of the Code – Application of IFRS 15 *Revenue Recognition for Contracts with Customers* and IFRS 9 *Financial Instruments*

IFRS 15 *Revenue for Contracts with Customers*

Q28 Do you agree with CIPFA/LASAAC's early views that there are no substantial issues that would require interpretation or adaptation in the Code for local authorities for the adoption of IFRS 15 *Revenue for Contracts with Customers*? If not, why not? Please give reasons for your response.

IFRS 9 *Financial Instruments*

Q29 Do you consider that there will be any particular application issues for the adoption of IFRS 9 *Financial Instruments* with regard to the financial instruments held by local authorities? Please set out what you consider these issues will be and the potential impact on adoption of the standard by the Code.

SECTION B – 2016/17 CODE – DETAILED DISCUSSION

The Measurement of the Highways Network Asset (ED2)

Introduction

16. CIPFA/LASAAC confirmed in the 2014/15 Code its intention to move to the measurement of transport infrastructure assets in accordance with methodologies specified by the *Code of Practice on Transport Infrastructure Assets* (Transport Code) in the 2016/17 Code[1] ie measurement at a Depreciated Replacement Cost (DRC) base. The proposed new requirements for the Accounting Code are included principally in a new Section 4.11 (the Highways Network Asset) with consequential amendments to Section 4.1 (Property, Plant and Equipment). This proposed change in accounting policy extends the current adaptation of IAS 16 in section 4.1 of the Code to withdraw the option to measure the carrying amount of this class of assets at historical cost.

17. The Transport Code is intended to serve as best practice guidance for those who are responsible for the management of infrastructure assets and as a tool for those who audit their performance. A central principle that underpins the Code is that the same data should be capable of serving the needs of asset management, financial management, budgeting and financial reporting.

18. As items of property plant and equipment, the 2016/17 Accounting Code draft clarifies that the recognition, measurement and derecognition principles follow the requirements of the Accounting Code for that class of assets unless the accounting policies state otherwise. However, the drafting of the Code follows the approach used for Heritage Assets and has established a separate section for the Highways Network Asset, to include provisions for the specific accounting policies and disclosures required for the asset.

Scope

19. Transport Infrastructure Assets are items of property, plant and equipment in the 2015/16 Code, included within the infrastructure class of assets. With the help of the Project Implementation Steering Group[2] (PISG) CIPFA/LASAAC is considering whether the remaining items within infrastructure assets can be measured effectively at current value. However, this work will not be completed for the 2016/17 Code.

20. The scope of the new transport infrastructure class of assets has been included in the new section 4.11 of the Accounting Code under the definitions section. Section 4.1 has been amended to remove the Highways Network Asset from the scope of section 4.1. This new class of assets draws on the categorisation of the components of the Highways Network Asset described in more detail in the Transport Code (Table 4.1). CIPFA/LASAAC also proposes that it would be clearer for the users of local authority financial statements if the network of assets described in the Transport Code is described as the Highways Network Asset as this is a more commonly understood term. For clarity the Code describes this as having the same meaning of the network of assets specified in the *Code of Practice on Transport Infrastructure Assets.*

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[1] In this Section of the ITC the 2016/17 Code will be referred to as the 2016/17 Accounting Code to clearly differentiate between this and the Transport Code.

[2] The Project Implementation Steering Group is the Group responsible for the development of the Transport Code.

Recognition

21. CIPFA/LASAAC is of the view that the network should be treated as a single asset because of the nature of the flow of the economic benefits and service potential in a networked asset and the difficulty in clearly and fully separating the individual flows. Also the elements that make up the network (eg structures (bridges), street lighting and traffic management) all exist for a single purpose ie to secure the effective and safe management of the traffic using the network, they are all maintained from this one objective and are largely inalienable. Other public sector entities that hold transport infrastructure assets at current cost (eg the Highways Agency and Transport Scotland) also use this approach.

22. CIPFA/LASAAC is also of the view that transport infrastructure assets should be recognised as a separate class of assets on the face of the balance sheet. This is due to the materiality of this class of asset and the different accounting policies the Code will prescribe for it.

Measurement

23. The 2015/16 Accounting Code described infrastructure assets as “inalienable”. This would include the Highways Network Asset within that class of assets, meaning that rights are not able to be transferred and there is no prospect of sale or alternative use. It also states that expenditure is only recoverable by continued use of the asset created.

24. The draft 2016/17 Accounting Code stipulates that the Highways Network Asset must follow the methodologies specified in the Transport Code. The Transport Code uses the same definition of DRC as the Accounting Code. However, the draft of the Accounting Code stipulates that the specifications of annual depreciation should be drawn from the provisions in the Transport Code.

25. This method of estimating annual depreciation for carriageways and structures is based on the definition of an asset as an inalienable asset ie the authority will hold and use the asset throughout its economic life and therefore the economic life of the asset will be the same as the useful life. It also assumes that the performance of the asset is maintained by replacement of its service potential when it has been worn out (hence the definition of annual depreciation).

26. The Transport Code therefore estimates the consumption of the economic benefits and service potential embodied in the asset or component using the definition of annual depreciation in the Transport Code. The specification of annual depreciation in the Transport Code is: the depreciation amount allocated each year, which in certain cases may be estimated by the aggregate cost of all the capital replacements/reinstatements needed to restore its service potential over the life cycle, spread over the estimated number of years in the cycle.

27. This approach is therefore an interpretation of IAS 16 for a Network of Assets where large parts of its service potential are maintained on an annual basis by replacement of expenditure. This approach is similar to the approach in the FReM which describes the consumption of the assets ie Annual Depreciation as being the “*… the value of the service potential replaced through the maintenance programme plus, or minus, any adjustment resulting from the annual condition survey*” (2015/16 FReM paragraph 7.1.20). This approach to depreciation has

been included in the Transport Code[3] since its inception as the PISG considers this to be the best measure of the annual consumption of service potential of the Highways Network Asset.

28. There are some components of the Highways Network Asset, for example, modular footways (see Transport Code paragraph 9.9.5), where annual depreciation is measured in almost the same way as the FReM as this is the best estimate of the service potential consumed in the year. Thus the Accounting Code cross refers to the Transport Code for the estimation of annual depreciation to ensure that it best meets the estimation processes for the relevant component/category of the Highways Network Asset.

Measurement of Changes in Condition

29. The Guidance and supporting tools for the measurement of transport infrastructure assets, including UK Pavement Management Systems (known as UKPMS[4]), use the definition for annual depreciation and the specific definitions for each asset type for the calculation of annual depreciation. Condition is used as a proxy for age in order to establish where the assets sit on the depreciation line (ie per paragraph 8.5.5.1 of the Transport Code for carriageways). However, the gradient of the line which measures the annual depreciation does not change. In line with the Transport Code, the actual deterioration of the asset between years is not compared to the annual depreciation as this data is not currently readily available for authorities. It is, however, included in the measurement of accumulated depreciation. If the estimated age of the asset changes (up or down) by more than expected this impact is assumed to be a revaluation movement per paragraphs 4.1.2.34 to 4.1.2.36 of the Accounting Code and not a direct annual charge to the Comprehensive Income and Expenditure Statement (CIES).

30. This approach differs from that normally taken for property, plant and equipment where changes in condition would be reflected in the formal revaluations undertaken by qualified valuers and thus be included as part of a depreciation charge to the CIES. Further changes in condition would not be reflected until the next formal valuation in accordance with the requirements of the Accounting Code for frequency of valuations unless indications of impairment exist.

31. This means that condition for the measurement of the Highways Network Asset will be reflected in the financial statements (the balance sheet) by means of an annual assessment of condition. The movements in the value of the asset due to condition will be by means of revaluation gains or losses and not reflected in charges for depreciation. Impairment events would be accounted for in accordance with the requirements of the Accounting Code.

Measurement - The Treatment of Accumulated Depreciation and Impairment

32. The normal approach for local authorities to the treatment of accumulated depreciation and impairment for property, plant and equipment under IAS 16 is that local authorities follow the option to eliminate accumulated depreciation and impairment when an asset is revalued. This is because these measures are accounting estimates of changes in value relating to the consumption of assets whose cumulative effect is confirmed or contested by a formal valuation reflecting

[3] The Code of Practice on Transport Infrastructure Assets was subsequently subject to review and consultation in 2013 and therefore there is 2013 version of the Transport Code.
[4] UKPMS (UK Pavement Management Systems) is the asset management system used to estimate the Gross Replacement Cost, Depreciated Replacement Cost and the annual depreciation charge of carriageways.

the actual condition of the property at the valuation date. The depreciation and impairment estimates are therefore made redundant by the valuation.

33. CIPFA/LASAAC considers that the information generated for the measurement of Highways Network will be better presented following the option in IAS 16 where accumulated depreciation and impairment is not eliminated (written out) on revaluation of the asset. Instead CIPFA/LASAAC proposes adapting IAS 16 so that accumulated depreciation and impairment will need to be adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account accumulated impairment losses.

34. Accumulated depreciation is estimated by the various supporting materials (ie toolkits and calculators) and on the basis of the amount of the asset that has been consumed at the reporting date.

Derecognition

35. The draft of the 2016/17 Accounting Code stipulates that the requirements for derecognition will follow the requirements of the Accounting Code for property, plant and equipment. In addition, the cost of a replaced part, e.g. surface of a road, shall be used as an estimate of the value of the part it has replaced. This is also supported by the methodology in the Transport Code in which the performance of this network is such that the service potential of the network is replaced as parts are worn out as assessed by the professional judgement of engineers. Where authorities can measure the Gross Replacement Cost or Accumulated Depreciation of the replaced part more accurately they are permitted to do so. This differs from the usual approach where local authorities use this cost as an indication of what the cost of the replaced part was at the time the asset was acquired.

36. The draft of the 2016/17 Accounting Code also requires that authorities assume that on replacement the asset has reached the end of its useful/economic life and/or has been fully utilised. Where authorities can measurably assess that this is not the case they are permitted not to treat the asset as being at the end of its useful life.

Disclosures

37. CIPFA/LASAAC's proposal to measure the Highways Network Asset on the face of the balance sheet also means that disclosures for the Network will be made separately from the other classes of property, plant and equipment. The disclosures included in the new section 4.11 are the same disclosures included in the Code for property, plant and equipment as applied to the new measurement requirements for the Highways Network Asset.

Transition

38. CIPFA/LASAAC has confirmed in both the 2014/15 and 2015/16 Accounting Codes that the move to the measurement of transport infrastructure assets (the Highways Network Asset) is a change in accounting policy which should be treated in accordance with Section 3.3 and therefore the 2016/17 Code will require full retrospective restatement for the new measurement requirements.

39. The revaluation reserve will be substantially increased on application of the new measurement requirements and local authorities will need to establish the difference between the depreciated historical cost (DHC) carrying amount for transport infrastructure assets and the carrying amount at DRC from 1 April 2015

ie to establish the third balance sheet for this change in accounting policy. CIPFA/LASAAC understands from anecdotal evidence that it might be difficult to split the new opening (DHC) balance for transport infrastructure assets from the previous infrastructure assets class within property, plant and equipment and therefore has allowed a transitional approach for the estimation of the split.

The Measurement of the Highways Network Asset

Q1	Do you agree with the proposed new Section 4.11 and the proposed amendments to section 4.1 of the Code for the definition, recognition and scope of the Highways Network Asset? If not, why not? What alternatives do you suggest?
Q2	Do you agree with the proposed new Section 4.11 and the proposed amendments to section 4.1 of the Code for the measurement of the Highways Network Asset? If not, why not? What alternatives do you suggest?
Q3	Do you agree with the proposed new Section 4.11 and the proposed amendments to section 4.1 of the Code for the derecognition of components of the Highways Network Asset? If not, why not? What alternatives do you suggest?
Q4	Do you agree with the transitional provisions in the Code for the move to measurement of the Highways Network Asset at DRC? If not, why not? What alternatives do you suggest?

The Review of the Accounting and Reporting by Pension Fund Section of the Code (ED3)

Background to the review

40. CIPFA/LASAAC set out in the ITC for the 2015/16 Code that it intended to review the reporting requirements of section 6.5 of the Code (Accounting and Reporting by Pension Funds). This review was timed to coincide with the issue of the new *Financial Reports of Pension Schemes, A Statement of Recommended Practice* (2015) (2015 Pension SORP). The ITC requested interested parties' views on any issues that they considered needed to be included in the review. CIPFA/LASAAC received a small number of responses and the issues raised are considered in the paragraphs below.

41. In addition, as the financial statements (the Fund Account and the Statement of Net Assets) were based on the previous Pension SORP CIPFA/LASAAC reviewed the Statements against the requirements in the 2015 Pension SORP, subject to consideration for local authority pension fund circumstances.

42. As is set out in Section 6.5 of the 2015/16 and preceding Codes CIPFA/LASAAC has concluded that the statutory requirement for administering authorities to prepare pension fund annual reports does not change the requirement for them to include pension fund accounts in their Statements of Accounts. This is with the exception of Scottish Administering Authorities where the statutory position is such that local authorities in Scotland are required to publish separate financial statements for local government pension funds. CIPFA/LASAAC's view remains that the pension fund financial statements of administering authorities should be

provided separately from local authority financial statements, but that, this would require statutory support which is not currently available in England and Wales. CIPFA/LASAAC's review outlined below is notwithstanding this position.

Fund Account

43. CIPFA/LASAAC has compared the Pensions Fund Account in the Code to the 2015 Pension SORP and considered that there were no fundamental omissions. However, it has proposed a number of minor changes to improve the presentation of the account for the users of the pension fund and the understandability of the Code's provisions for pension fund accounts preparers.

44. Paragraph 6.5.2.5 of the 2015/16 Code sets out that to ensure comparability between different local authority pension fund disclosures the investment income analysis or sub classification should be based on that of the Pension SORP and to maintain this comparability CIPFA/LASAAC therefore proposes updating the analysis in line with the 2015 Pension SORP where this is consistent with the reporting requirements of local authority pension fund financial reporting. This is not substantially different from the current requirements. Where local authorities have any material investment income outside these classifications this would be included in the "Other" category and disclosed as relevant under the Code's provisions on IAS 1 to report material transactions.

45. The 2015 Pension SORP also includes two classifications which are further analysed by appropriate sub classifications ie "transfers in from other pension funds" and "payments to and on account of leavers". The CIPFA example financial accounts[5] present similar sub classifications in the notes to the accounts. CIPFA/LASAAC therefore recommends that for added certainty for accounts preparers and to improve comparability and consistency these sub classifications are included in the Fund Account.

46. CIPFA/LASAAC also proposes adding two sub totals included in the 2015 Pension SORP to improve the understandability of the (pension) fund account.

Net Assets Statement

47. CIPFA/LASAAC has also reviewed the net assets statement against the one in the 2015 Pension SORP and has concluded that there are no fundamental omissions. Again using the rationale for comparability in paragraph 6.5.2.5 CIPFA/LASAAC has updated the investment assets classification to more closely align with that of the 2015 Pension SORP. This has required minor changes to the Statement.

Accounting Policies and Disclosures

48. CIPFA/LASAAC would reiterate its comments from the consultation on the 2015/16 Code that the framework for reporting pension funds in the Code is robust as it relies not only on IAS 26 *Accounting for Retirement Benefit Plans* but also the full accounting framework in the Code ie EU adopted IFRS (as it applies to pension funds). There is one area where CIPFA/LASAAC considers that improvement might be made ie fair value measurement disclosures.

Fair Value Measurement Disclosures

[5] Included in the *Local Government Pension Scheme Fund Accounts 2014/15, Example Accounts and Disclosure Checklist*, CIPFA December 2014

49. The adoption of IFRS 13 *Fair Value Measurement* in the Code includes a scope exclusion for section 6.5 for disclosures of retirement benefit plan investments measured at fair value, this reflecting the scope exclusion for IAS 26 in IFRS 13. CIPFA/LASAAC was concerned not to make the reporting requirements of IFRS 13 more onerous for local authorities than IFRS and this was particularly important under the Improving the Presentation of the Local Authority Financial Statements agenda. However, the review highlighted that the 2015 Pension SORP has adopted a form of fair value disclosures similar to that of IFRS 13. Perhaps more importantly the 2015 Pension SORP discusses the objectives of the users of the Pension Fund Financial Statements and indicates that these users are concerned about investment performance and fair value disclosures are an important element of demonstrating this to users.

50. CIPFA/LASAAC would note that there are other elements of the IFRS-based Code that apply to pension fund accounts that would mean that local authorities would need to consider the use of fair value disclosures in the financial statements. Firstly, the pension funds would have to report under paragraphs 3.4.2.83 on future and other sources of estimation uncertainty at the end of the reporting period that have a significant risk of resulting in a material adjustment for assets and liabilities in the next financial year. The IFRS 13 fair value disclosure structure would be the best means available of reporting such risks.

51. Secondly, paragraph 3.4.2.40 c) of the Code requires administering authorities to provide sufficient additional disclosures when compliance with the specific requirements in the Code is insufficient to enable users to understand the impact of particular transactions and other events and conditions on the authority's financial position and financial performance. Again the fair value disclosures are likely to mitigate against the risk of the administering authority providing insufficient information in the pension fund financial statements. This is the approach CIPFA will take in its guidance on the 2015/16 pension fund financial statements. However, CIPFA/LASAAC is of the view that it would provide more certainty and be clearer for accounts preparers if the Code clearly stipulated these requirements and therefore such proposals are included in the 2016/17 Code Exposure Draft. CIPFA/LASAAC proposes adapting the reporting requirements of IFRS 13 to include fair value disclosure requirements for pension fund investments in the 2016/17 Code.

Actuarial Present Value of Promised Retirement Benefits

52. IAS 26 gives three options for the presentation of the actuarial present value of promised retirement benefits. Paragraph 6.5.2.8 and 6.5.2.9 of the Code confirms how these are to be applied by administering authorities – the three options are included in the Exposure Draft of proposed amendments to the Code. CIPFA/LASAAC has since the 2013/14 Code considered Option A to be the preferred option. However, it has retained options B and C.

53. One of the respondents to the consultation on the 2015/16 Code suggested as this was CIPA/LASAAC's preferred option that this option only should be prescribed in the Code. CIPFA/LASAAC has yet to be convinced of any arguments to move to this position but would seek interested parties' views on whether they consider that such a move would be useful to the readers of pension fund financial statements and what would be the benefits and costs of such a move.

Administrative/Management Expenses

54. Interested parties will be aware that there has been a great deal of public scrutiny about investment management expenses across sectors. In particular,

there has been scrutiny of investment management expenses in the Local Government Pension Scheme (LGPS) culminating in the Department for Communities and Local Government (DCLG) Call for Evidence on the future structure of the LGPS launched in 2013. CIPFA in its response stressed the need for a comprehensive, reliable and robust data set to underpin the type of information necessary to achieve reform prepared on a comparable basis.

55. The 2015 Pension SORP also prioritises the reporting of transaction costs within the pension fund financial statements and it recommends direct transaction costs should be analysed for each significant asset class disclosed in the investment reconciliation table. CIPFA/LASAAC is of the view that a similar approach in the Code would enable local authorities to report transaction costs transparently. This would also allow greater scrutiny and comparison with other pension funds as the disclosure is a recommendation in the 2015 Pension SORP. The Exposure Draft of section 6.5 includes a new recommended disclosure requirement at paragraph 6.5.5.1 v) based on the 2015 Pension SORP disclosure.

Overview of Application of the Code's Accounting Policies to Pension Funds

56. A number of commentators have in the past considered that it is sometimes difficult to understand the relationship of the reporting requirements of other sections of the Code with section 6.5 of the Code. These comments have asked for more commentary on this issue in Section 6.5 itself. CIPFA/LASAAC therefore proposes adding an Annex with a table that provides an overview of how the other sections of the Code apply to pension funds.

Scottish Reporting Requirements for Pension Funds

57. An audit body commented that the review of section 6.5 should include consideration that Scottish pension fund financial statements are published in a separate document. Therefore a paragraph has been included in Section 6.5 (paragraph 6.5.3.2) to emphasise this issue and the new table in the Annex to section 6.5 identifies when different arrangements are likely to apply to Scottish Pension Fund Abstracts of Accounts. Section 6.5 also includes updated references to the new Statutory Guidance on the Pension Funds included in Scottish Government Finance Circular 6/2015.

The Review of the Accounting and Reporting by Pension Fund Section of the Code	
Q5	Do you agree with the proposed amendments to the (Pension) Fund Account in Section 6.5 of the Code? If not, why not? What alternatives do you suggest?
Q6	Do you agree with the proposed amendments to the (Pension) Net Assets Statement in Section 6.5 of the Code? If not, why not? What alternatives do you suggest?
Q7	Do you agree that the Code should adapt IFRS 13 *Fair Value Measurement* and remove the scope exclusion for section 6.5 of the Code for disclosures? If not, why not? What alternatives do you suggest?

Q8	Do you consider that the Code should only include option A for the reporting of the Actuarial Present Value of Promised Retirement Benefits or should all three options be retained? Please set out the costs and benefits of your preferred option for the users and preparers of pension fund financial statements.
Q9	Do you agree that the Code should include a recommendation to disclose transaction costs for investment management per the proposals in paragraph 6.5.5.1 v) of the Exposure Draft of the Code? If not, why not? What alternatives do you suggest?
Q10	Do you agree with the addition of the Annex to section 6.5 which includes an overview of how the remaining sections and chapters of the Code apply to local authority pension funds? If not, why not? What alternatives do you suggest?
Q11	Do you agree that the Exposure Draft of section 6.5 of the Code appropriately provides for the requirements for the reporting of Scottish pension funds? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IAS 1 *Presentation of Financial* Statements, Disclosure Initiative (ED1)

Introduction and Background

58. In December 2014 the IASB issued a set of amendments to IAS 1 *Presentation of Financial Statements* as a first step in its Disclosure Initiative. The amendments clarify, rather than significantly change, existing IAS 1 requirements. In most cases the proposed amendments respond to overly prescriptive interpretations of the wording in IAS 1. CIPFA/LASAAC considers that these amendments are particularly helpful to support its improving the presentation of the local authority financial statements review.

59. The amendments to the Code for local authorities relate to the areas itemised below.

Materiality

60. The amendments to IAS 1 clarify that an authority must not reduce the understandability of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions.

61. The amendments to IAS 1 also clarify that when a standard requires a specific disclosure that materiality considerations do still apply and confirms that this is the case even if the standard uses the term “as a minimum” (the Code already applies this policy in specific cases but CIPFA/LASAAC considers that it is useful to be explicit following the IAS 1 amendments).

Order of the notes

62. The amendments affirm that local authorities have flexibility as to the order in which they present the notes to financial statements, but also emphasise that understandability and comparability should be considered by an entity when

deciding on that order. The amendments give examples of the systematic ordering of notes.

Disaggregation and Subtotals

63. The amendments to IAS 1 clarify that line items in the balance sheet may be disaggregated and also set out requirements for subtotals. The amendments also remove the wording “as a minimum” from paragraph 3.4.2.59 the Code as the intention of this amendment to IAS 1 was to address the possible misconception that this wording prevents local authorities from aggregating the line items specified in that paragraph if those specified line items are immaterial.

Accounting Policies

64. There are minor changes to the description of accounting policies. IAS 1 no longer refers to a “summary of” significant accounting policies.

Presentation of Items of Other Comprehensive Income and Expenditure Arising from Equity Accounted Investments in Joint Ventures and Associates.

65. The amendments also clarify that the share of Other Comprehensive Income and Expenditure of associates and joint ventures accounted for using the equity method must be presented classified between those items that will or will not be subsequently reclassified to profit or loss.

Narrow Scope Amendments: IAS 1 Presentation of Financial Statements, Disclosure Initiative

Q12 Do you agree with the approach to the adoption of the Amendments to IAS 1 (Disclosure Initiative) in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IAS 19 Employee Benefits, Defined Benefit Plans: Employee Contributions

Introduction and Background

66. In November 2013 the IASB issued its amendments to IAS 19 *Employee Benefits* (Defined Benefit Plans: Employee Contributions). The amendments to this standard were discussed in the consultation on the 2015/16 Code. However, the IAS 19 amendments did not legally come into force until 12 January 2015 and this was after the effective date for adoption of new or amended standards in the 2015/16 Code ie 1 January 2015. The proposed amendments were therefore not included in the 2015/16 Code.

67. IAS 19 requires contributions from employees or third parties to be considered when accounting for defined benefit plans. It requires that such contributions that are linked to service are attributed to periods of service as a reduction of service cost (ie as a negative benefit). Therefore, contributions from employees or third parties reduce the ultimate cost of a defined benefit and should therefore be accounted for consistently with the accounting for the defined benefit. This amendment to the standard will apply to local authorities.

68. It offers two options for this and the second option is most applicable to the accounting requirements for employee contributions ie if the amount of the contributions is independent of years of service an authority is permitted to recognise such contributions as a reduction in the service cost in the period in which the related service is rendered, instead of attributing a proportion of the contributions to the periods of service over which a reduction of contributions was earned. CIPFA/LASAAC considers that this is consistent with the approach of local authorities and therefore does not consider that there will be a significant change in accounting practice for local authorities.

69. The 2015/16 Code does not include the original paragraph (paragraph 93 of IAS 19) which is subject to amendment and relates to the accounting treatment for employee contributions. However, for the avoidance of doubt, reference will be made in paragraph 6.4.1.1 to these amendments to IAS 19 that this will apply in the 2016/17 Code.

> Narrow Scope Amendments: IAS 19 *Employee Benefits*, Defined Benefit Plans: Employee Contributions
>
> Q13 Do you agree with the approach to the adoption of IAS 19 *Employee Benefits* (Defined Benefit Plans: Employee Contributions) in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: *Annual Improvements to IFRSs 2010 – 2012 Cycle* (EDs 1, 2, 4 and 8)

70. The IASB carries out cyclical work to identify and implement improvements in IFRSs. It issued the *Annual Improvements to IFRSs 2010 – 2012 Cycle* in November 2013 and amendments were included in the Exposure Drafts of the 2015/16 Code. However, they did not come legally in to force until 12 January 2015 and this was after the effective date for adoption of new or amended standards in the 2015/16 Code ie 1 January 2015. The proposed amendments are therefore not included in the 2015/16 Code.

71. The proposed amendments to the Code are set out in Appendix A to this ITC and in the relevant Exposure Drafts.

72. One particular area of note in the Annual Improvements is the treatment of accumulated depreciation and impairment as an amendment to IAS 16 *Property, Plant and Equipment*. The amendments prescribe the treatment of accumulated depreciation under which:

"… *the gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset… The accumulated depreciation at the date of the revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account accumulated impairment losses*."

73. CIPFA/LASAAC is content that this treatment is appropriate for measurement bases for which DRC is estimated as information is available for both gross and net carrying values and this information is supported by appropriate evidence and as such includes this option for the treatment for accumulated depreciation and impairment for the new Highways Network Asset. However, CIPFA/LASAAC considers that adjustments to the gross carrying amounts would, however, be

counterintuitive for local authority valuations as these values are certified by the valuer.

74. CIPFA/LASAAC is also concerned that some classes of assets for local authorities include both DRC and non DRC valuations and considers that it would not be useful to the reader of local authority financial statements to include classes of assets where both treatments of accumulated depreciation would be used. As it considers that local authorities normally use the elimination method CIPFA/LASAAC considers that the non-elimination method for the treatment of accumulated depreciation and impairment should be withdrawn for property, plant and equipment (except for the Highways Network Asset). This is an adaptation of IAS 16.

Narrow Scope Amendments: Annual Improvements to IFRSs 2010 – 2012 Cycle	
Q14	Do you agree with the approach to the adoption of the Annual Improvements to IFRS 2010 - 2012 Cycle in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: *Annual Improvement to IFRSs 2012 – 2014 Cycle*

75. The IASB issued the *Annual Improvements to IFRSs 2012 – 2014* Cycle in September. Appendix B to the ITC includes a summary of its application to local authorities. There are no anticipated changes to the Code for this set of Annual Improvements.

Annual Improvements to IFRSs 2012 -2014 Cycle	
Q15	Do you agree with the approach to the adoption of the Annual Improvements to IFRS 2012 - 2014 Cycle in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets,* Clarification of Acceptable Methods of Depreciation and Amortisation

76. In May 2014 the IASB issued amendments to IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets.*

77. The amendments to IAS 16 clarify that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. CIPFA/LASAAC considers that this principle can also be applied to service potential embodied in an asset following the Code’s approach to the adoption of IAS 16. CIPFA/LASAAC considers that although local authorities may very occasionally use income methods to value assets they do not depreciate assets on the basis of revenue-based methods and therefore this should not be a change in accounting policy for local authorities.

78. The amendments to IAS 38 clarify that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset. This presumption, however, can be rebutted in certain limited circumstances. Again, CIPFA/LASAAC does not consider that this should lead to a change in accounting policy for local authorities.

79. The amended IFRS paragraphs to which these narrow scope amendments apply were not included in the Code (and therefore where necessary the Code would anticipate direct reference to the standard). As these two amendments are not likely to bring about a change in accounting policy for local authorities CIPFA/LASAAC does not consider that there is a need to introduce new and amended paragraphs into the Code.

> Narrow Scope Amendments: IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*, Clarification of Acceptable Methods of Depreciation and Amortisation
>
> Q16 Do you agree with the approach to the adoption of the Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IFRS 11 *Joint Arrangements*, Accounting for Acquisitions of Interests in Joint Operations (ED5)

80. Amendments to IFRS 11 *Joint Arrangements* are relevant to the accounting for the acquisition of an interest in a joint operation that constitutes a business as defined in IFRS 3 *Business Combinations*. The acquirer of that interest is required to apply all of the principles on business combinations accounting in IFRS 3 and other IFRSs, with the exception of those principles that conflict with the guidance in IFRS 11 and disclose the information that is required in those IFRSs in relation to business combinations. The relevant changes proposed have been made to chapter nine, paragraph 9.1.2.52.

> Narrow Scope Amendments: IFRS 11 *Joint Arrangements*, Accounting for Acquisitions of Interests in Joint Operations
>
> Q17 Do you agree with the approach to the adoption of the Amendments to IFRS 11 *Joint Arrangements,* Accounting for Acquisitions of Interests in Joint Operations in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011), Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

81. The amendments to IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011), Sale or Contribution of Assets between an Investor and its Associate or Joint Venture issued in

September 2014 clarify the transactions when a parent loses control of a subsidiary that does not constitute the definition of a business in IFRS 3, on sale or contribution of a subsidiary to an entities' joint venture or an associate.

82. The gain or loss resulting from such transactions would be recognised in the parent's profit or loss (Surplus or Deficit on the Provision of Services) only to the extent of the unrelated investors' interest in the joint venture or associate that was counterparty to that transaction. If the parent retains an investment in a subsidiary which is now an associate or joint venture that is accounted for using the equity method, the parent recognises the part of the gain or loss resulting from the remeasurement at fair value of the investment retained in that former subsidiary in its profit or loss only to the extent of the unrelated investors' interests in the new associate or joint venture.

83. The amendments also include consequential amendments to gains and losses on "upstream" or "downstream" transaction in IAS 28. Interested parties will note that the amendments in IAS 28 are not paragraphs currently included in the Code and therefore where these provisions apply the Code would anticipate that preparers refer directly to IAS 28. Appropriate (minor) amendment to reflect the changes would also need to be made to paragraph 9.1.2.44 of the Code for the amendments to IFRS 10. CIPFA/LASAAC considers that these provisions would apply to local authorities, but that they are not frequently occurring transactions or events.

84. CIPFA/LASAAC would also note that in January 2015 the IASB announced that unintended consequences had arisen which they intended to correct. EFRAG highlighted that "the IASB decided to include these additional changes within the forthcoming Exposure Draft on *Elimination of gains or losses arising from transactions between an entity and its associate or joint venture* and postpone the effective date of the amendments to IFRS 10 and IAS 28 (published in September 2014) to align the effective dates of the different amendments." The Exposure Draft is anticipated to be issued in quarter 2 of 2015. EFRAG also indicated that the endorsement process would be postponed until the second set of amendments is complete. Therefore it seems unlikely that this amendment will be adopted by the EU in time for the implementation in the 2016/17 Code. However, CIPFA/LASAAC has included the amendments in this consultation for completeness.

Narrow Scope Amendments: IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011), Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

Q18 Do you agree with the approach to the adoption of the Amendments to IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011) - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture in the Code? If not, why not? What alternatives do you suggest?

Narrow Scope Amendments: IAS 27 *Separate Financial Statements* (2011), Equity Method in Separate Financial Statements

85. The IASB issued amendments to IAS 27 *Separate Financial Statements*, the Equity Method in Separate Financial Statements in August 2014 to permit the

equity method as one of the options to account for an entity's investment in subsidiaries, joint ventures and associates in the entity's separate financial statements. CIPFA/LASAAC has considered the amendments to this standard and is of the view that it would not be useful to the users of the local authority financial statements to include this amendment in the Code.

86. Its rationale for this is that the IASB did not introduce this amendment for technical accounting reasons but to reinstate the option because the laws of some countries require listed companies to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements.

87. This option had been removed from IAS 27 in 2003. Some of the reasons given by the IASB for making this change then were:

(i) The focus in separate statements is on the performance of the assets as investments. Cost and fair value can provide relevant information for this; and

(ii) To the extent that the equity method provides information about the profit and loss of a subsidiary or an associate, that information would be available in the consolidated financial statements[6].

88. CIPFA/LASAAC considers that these reasons are appropriate for not including the equity method option in the Code and therefore proposes interpreting IAS 27 to remove this option[7]. It also considers that this issue is more important for local authority financial statements, where the single entity financial statements have a higher priority over the group statements, particularly the importance of the information for ensuring the accuracy of the General Fund Balance and the impact on Prudential Borrowing requirements. This is also similar to the rationale that the Board used in the introduction of IFRS when the original IFRS-based Code and subsequent editions required that authorities produced group accounts when they had material interests in joint ventures and associates.

89. The IASB is undertaking a research project into the equity method which will involve a fundamental assessment of the equity method in terms of its usefulness to investors and difficulties to preparers[8]. CIPFA/LASAAC will review the position on the inclusion of equity accounting in the single entity financial statements following the IASB's review.

Augmentation of the Code's Provisions on Concepts -The IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (ED6)

90. The IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (IPSASB Conceptual Framework) was issued in October 2014. The publication of the Conceptual Framework provides the IPSASB with the concepts that will underpin the development of International Public Sector Accounting Standards and other guidance issued by IPSASB. CIPFA/LASAAC has considered Chapter's Chapters Two, *Objectives and Users of General Purpose Financial Reporting* and Three, *Qualitative Characteristics* of the IPSASB Conceptual Framework against the provisions in Section 2.1 of the Code to

[6] See IPSAS 34, Separate Financial Statements, IPSASB January 2015.
[7] This interpretation will be confirmed in paragraph 9.1.1.3 of the Code.
[8] See Equity Method of Accounting Project pages on the website of the IFRS Foundation and the IASB.

consider whether this would assist in exemplification of the concepts for public sector circumstances.

91. CIPFA/LASAAC has not considered the remaining chapters of the Conceptual Framework as the IASB Conceptual Framework[9] is also subject to review and an Exposure Draft on the Conceptual Framework was issued in May 2015, CIPFA/LASAAC considers that it will not be helpful to accounts preparers to issue two sets of amendments to Section 2.1 in a relatively short period of time.

92. CIPFA/LASAAC will review the remaining chapters of the IPSASB Conceptual Framework with the IASB Conceptual Framework when the new IASB Conceptual Framework is issued.

93. Following the deliberations of the Working Group on improving the presentation of local authority financial statements (Working Group) CIPFA/LASAAC proposes adding further commentary on the users of the financial statements as this is an area which is subject to much debate for local government. CIPFA/LASAAC has therefore used the approach in the IPSASB Conceptual Framework to identify the prime users of local authority financial statements ie service recipients and resource providers who do not possess the authority to require local authorities to disclose the information they need for accountability and decision-making purposes.

94. Whilst reviewing this section of the Code and again in the light of the experiences of the Working Group, CIPFA/LASAAC also decided to reorder the objectives of the financial statements in an order better suited to those users of the financial statements ie to provide information about the authority’s financial performance, financial position and cash flows that is useful to a wide range of users for assessing the stewardship of the authority’s management and for making economic decisions.

95. Again this is similar to the approach in the IPSASB Conceptual Framework which uses the terminology “useful for accountability and decision-making purposes”. This reordering, however, retains the objectives of the financial statements from the IASB Conceptual Framework ie to provide financial information about the reporting authority that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources as CIPFA/LASAAC considers this remains relevant in accordance with its decisions to include this originally in the 2012/13 Code.

96. The IPSASB Conceptual Framework uses the same characteristics of useful financial information as the Code (these characteristics were drawn from the IASB Conceptual Framework as amended in September 2010) and therefore there has not been a need to make any substantial amendment to the characteristics in the Code. However, CIPFA/LASAAC considers that it is useful to add further context on the complexity of useful financial information as this is has been a particular issue in the improving the presentation of the local authority financial statements review. This addition clarifies that the information should not be excluded because it is complex and all efforts should be undertaken to represent economic and other phenomena included in the financial statements in a manner that is understandable to a wide range of users.

[9] IASB Conceptual Framework for Financial Reporting issued by the IASB in September 2010 (IASB Conceptual Framework).

Augmentation of the Code's Provisions on Concepts - The IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*

Q19 Do you agree with the approach to the amendments to section 2.1 of the Code based on the IPSAB Conceptual Framework? If not, why not? What alternatives do you suggest?

Telling the Story, Consultation on Improving the Presentation of Local Authority Financial Statements (ED1)

97. CIPFA/LASAAC is continuing to consider opportunities to improve the presentation of local authority financial statements improve the presentation of local authority financial statements focusing particularly on the presentation of the Comprehensive Income and Expenditure Statement and the Movement in Reserves Statement and how they reflect local authority performance. A separate consultation *Telling the Story, Consultation on Improving the Presentation of Local Authority Financial Statements* is available on www.cipfa.org/tellingthestory2016.

The Local Audit and Accountability Act 2014 and the Accounts and Audit Regulations 2015 (English Authorities) (EDs7 and 1)

98. The 2015/16 Code does not take into account the Local Audit and Accountability Act 2014 and the Accounts and Audit Regulations 2015 as the latter was not issued in time for inclusion in the 2015/16 Code. This will not make a difference to the application of these statutory provisions whilst the Code is not consistent with the Regulations as both Section 21 of the Local Government Act 2003 and the Code confirm that statutory provisions take precedence over the Code.

99. The new Act and the Regulations will mean changes to the relevant references throughout the 2016/17 Code for English Authorities. These include:

- Changes to the references relating to the application of the 2016/17 Code (and by statutory override to the 2015/16 Code).
- Changes to the references to the authorised for issue date in section 3.8 of the Code.
- Consequential changes to the audit fee disclosure and other elements of the disclosures in Section 3.4 of the Code.
- The introduction of requirement to provide a narrative statement.

Changes to the references relating to the application of the 2016/17 Code (and by statutory override to the 2015/16 Code)

100. The combination of the Local Audit and Accountability Act 2014 (which defines relevant authorities to which the Act applies) and the Accounts and Audit Regulations 2015 sets out the framework under which relevant authorities apply the Code. The latter sets out that there are category 1 and category 2 authorities which apply the Code under the relevant proper practices.

101. Proper practices are defined under Section 21 of the LGA 2003 and specifically under the Capital Finance and Accounting Regulations in England to include the

Code. Largely this will mean very little change for most of the bodies applying the Code; however, it may mean that some of the smaller local authorities have the option to follow a framework for smaller relevant authorities. Chapter 1 of the Code also refers to in Section 141 of the Anti-social Behaviour Crime and Policing Act 2014 which confirms that the relevant sections of the Local Government Act 2003 including proper practices in relation to accounts apply to Chief Constables as they apply to a local authority.

The Introduction of the Requirement to Provide a Narrative Statement

102. Regulation 8 of the Accounts and Audit Regulations 2015 requires English local authorities to provide a narrative statement with the statement of accounts. CIPFA/LASAAC has kept the issue of the production of a narrative report or a management commentary under review since 2012/13 Code. It decided at that juncture to postpone the publication of the recommendations on the narrative report until the legislative position across jurisdictions is clear and in the interim encouraged local authorities to provide a management commentary or strategic report following the approach in the government's financial reporting manual.

103. The four administrations have recently published new sets of accounts and audit regulations and therefore the legislative position is currently clear on narrative reporting. However, CIPFA has initiated its integrated reporting public sector network with a Secretariat provided by both CIPFA and the International Integrated Reporting Council. This network is expected to run over two years, covering two financial reporting cycles from 2014/15 onwards. CIPFA/LASAAC is of the view that narrative reporting for local government should be informed by the work of this network and therefore is concerned not to initiate more detailed proposals until it can take into account the output of this network.

104. CIPFA/LASAAC considers that a full interpretation of the requirements of section 3.1 can provide an effective narrative report and therefore considers that it will not make any substantial changes to the overall provisions at this juncture. It would reiterate its comments in the Code and would encourage local authorities to follow the requirements of the FReM for a strategic report and would encourage local authorities to provide a clear and effective explanation of the authority's financial position, financial performance and cash flow and an easily understandable guide to the most significant matters reported in the accounts.

105. However, as a part of the narrative statement regulation 8(2) of the English Regulations requires that the narrative statement "must include comment by the authority on its financial performance and economy, efficiency and effectiveness in its use of resources over the financial year". In order to ensure this new statutory requirement is supported by appropriate guidance on proper practices CIPFA/LASAAC has provided guidance based on business performance elements of the Financial Reporting Council's Guidance on the Strategic Report issued in June 2014. This has been interpreted for local government circumstances.

106. The section on the Narrative Report also includes comment on the new guidance on the management commentary issued by the Scottish Government in Scottish Government Circular 6/2015.

107. The section in the Code (3.1) on the Narrative Report also includes CIPFA/LASAAC's proposals under the *Telling the Story, Consultation on Improving the Presentation of Local Authority Financial Statements review* (paragraph 97 above refers) to introduce a mandatory Funding Analysis, this will assist authorities with the demonstration of financial performance. CIPFA/LASAAC is

seeking interested parties views on whether there are any other areas of Narrative Reporting that they consider should be mandated by the Code.

Changes to the Disclosures in Section 3.4 of the Code

108. The new audit framework has meant that the fees payable under the Audit Commission Act 1998 are not specified in the Local Audit and Accountability Act and therefore the relevant references have been removed (see paragraph 3.4.4.1 7[10]).

109. The 2016/17 Code has been updated to clarify that the remuneration disclosures should follow the requirements of the relevant regulations in England and Wales as there are slight differences between the two regulations in the definition of remuneration and pensions contributions. Any disclosures will need to be produced in accordance with the relevant requirements.

Changes to the references to the authorised for issue date in section 3.8 of the Code

110. The new Accounts and Audit Regulations 2015 no longer include the explicit date for authorisation by the Responsible Financial Officer prior to audit. The date, however, needs to be prior to the notification the mandatory period for the exercise of electors rights for 2016/17, this is prior to 1 July. CIPFA/LASAAC has taken the opportunity to simplify its corresponding provisions for authorised for issue date.

Application in the 2015/16 Financial Year

111. As noted above the Accounts and Audit Regulations will apply to local authorities in the 2015/16 financial year. Most of the changes will not need separate specification as they are largely matters of fact. However, the principles set out in the Code for the part of the Regulations that "must include comment by the authority on its financial performance and economy, efficiency and effectiveness in its use of resources over the financial year" will be confirmed by in guidance issued by CIPFA following the consultation.

The Local Audit and Accountability Act 2014 and the Accounts and Audit Regulations 2015 (English Authorities)

Q20	Do you agree with the proposed amendments to Chapter 1 of the Code for the application of the Code to the relevant authorities covered by the Accounts and Audit Regulations 2015? If not, why not? What alternatives do you suggest?
Q21	Do you agree with the approach to the proposed amendments to Section 3.1 of the Code for the narrative statement for local authorities in England? If not, why not? What alternatives do you suggest?
Q22	Do you consider that there are any other areas of Narrative Reporting which ought to be stipulated in the Code? Please provide reasons for your response.

[10] This paragraph has also been updated to reflect the current position for Welsh Local Authorities.

Q23	Do you agree with the proposed amendments to Section 3.4 of the Code as a result of the application of the Accounts and Audit Regulations 2015 to the provisions of Code for English local authorities? If not, why not? What alternatives do you suggest?
Q24	Do you agree with the proposed amendments to Section 3.4 of the Code as a result of the application of the Accounts and Audit Regulations 2015 to the provisions of the Code for English local authorities? If not, why not? What alternatives do you suggest?

The Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015 (ED7)

112. The 2015/16 Code does not take into account The Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015 as the regulations were not issued in time for inclusion. This will not make a difference to the application of these statutory provisions whilst the Code is not consistent with the Regulations as both Section 2(4) of the Local Government Finance Act 2011 and the Code confirm that statutory provisions take precedence over the Code.

113. The new Regulations will mean changes to the relevant references throughout the 2016/17 Code. These include:

- Changes to the references relating to the application of the 2016/17 Code (and by statutory override to the 2015/16 Code). Chapter one of the Code has been updated for the relevant references to the new Regulations.
- The introduction of the requirement to include a remuneration report with the statement of accounts. Section 3.4 has been updated to include appropriate reference to this requirement (see inserted paragraph 3.4.5.2).
- Changes to the references to the authorised for issue date in section 3.8 of the Code. These changes have followed the same approach as for the Accounts and Audit Regulations 2015.

The Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015	
Q25	Do you agree with the proposed amendments to the Code for the Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015? If not, why not? What alternatives do you suggest?

Minor Amendments (ED8)

114. The Scottish Government has issued new Statutory Guidance on Accounting for Equal Pay and Severance in Scottish Government Finance Circular 4/2015. The relevant amendments have been made to paragraphs 8.2.3.1 to 8.2.3.4.

115. Additional minor clarification has been made to Appendix E to confirm for the avoidance of doubt that the recognition of schools non-current assets must meet the definition of an asset to be recognised on a local authority balance sheet. CIPFA/LASAAC is of the view that this change does not to change the provisions of the Code in any way but is a drafting improvement only.

Minor Amendments	
Q26	Do you agree with the proposed amendments to the Code to reflect the new Statutory Guidance on Equal Pay and Severance for Scottish Authorities? If not, why not? What alternatives do you suggest?

Further Guidance

116. CIPFA/LASAAC would be interested to hear respondents' views on whether there are any areas within the Code where additional guidance would be welcomed or improvements to the Code could be made.

Further Guidance	
Q27	Are there any areas within the Code where additional guidance or improvements to the Code would be helpful? Please support your answer by giving details of the difficulties being experienced.

Future Editions of the Code – Application of IFRS 9 *Financial Instruments* and IFRS 15 *Revenue Recognition for Contracts with Customers*

Introduction and Background

117. Interested Parties will be aware that the IASB has issued two standards IFRS 9 *Financial Instruments* and IFRS 15 *Revenue Recognition for Contracts with Customers*. These standards will apply in future editions of the Code and CIPFA/LASAAC with the other relevant authorities that prepare Manuals under the oversight of the Government's Financial Reporting Advisory Board are considering application of the standards for the public sector and for local authorities in the Code.

IFRS 15 Revenue Recognition for Contracts with Customers

118. IFRS 15 *Revenue from Contracts with Customers* was issued in May 2014. The Standard will replace IAS 18 *Revenue* and IAS 11 *Construction Contracts* and a number of related interpretations. Following a consultation by the IASB on deferral, the effective date of the standard is 1 January 2018.

119. IFRS 15 applies to all contracts with customers (except those within the scope of IAS 17 *Leases*, IFRS 9 *Financial Instruments*, the Group Accounts Standards[11] and IFRS 4 Insurance Contracts and non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers).

120. The core principle in IFRS 15 is that entities should recognise revenue to depict the transfer of promised goods or services to the customer in an amount that

[11] IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosure of Interest in Other Entities, IAS 27 Separate Financial Statements (2011) and IAS 28 Investments in Associates and Joint Ventures (2011).

reflects the consideration to which the company expects to be entitled in exchange for those goods or services.

121. The disclosure objective of IFRS 15 is for the users of the financial statements to better understand the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers. IFRS 15 requires an entity to disclose quantitative and/or qualitative information about:

- revenue recognised from contracts with customers, including the disaggregation of revenue into appropriate categories;
- contract balances, including the opening and closing balances of receivables, contract assets and contract liabilities;
- performance obligations, including when the entity typically satisfies its performance obligations and the amount of the transaction price that is allocated to the remaining performance obligations in a contract;
- significant judgements, and changes in judgements, made in applying the requirements; and
- assets recognised from the costs to obtain or fulfil a contract with a customer.

122. For many contracts for local authorities it is likely that the accounting for revenue will remain unchanged. For other contracts, including long-term service contracts, there may be changes to the timing and amount of revenue recognised, depending on how local authorities previously accounted for these contracts. Possible areas where practice may change include:

- sales with incidental obligations (eg equipment sales with maintenance agreements),
- transfers of goods and services where there is no observable evidence of the stand-alone price of each of the goods and services,
- licences of intellectual property,
- situations where there is uncertainty about whether revenue should be recognised at a point in time or over time (eg development of a service provided over time or a good transferred on completion),
- estimates where consideration is variable, and
- situations where customers pay in advance or arrears and financing of the contract needs to be considered.

Any changes may have budgetary implications. Where contacts include a variable consideration, this is measured at either expected value (ie probability-weighted amount) or the most likely amount, depending on which is the best predictor of the amount of consideration to which the entity is entitled).

123. CIPFA/LASAAC's early views do not consider that there are any particular issues that will require substantial interpretation or adaptation in the Code. However, it would seek local interested parties' views on this issue.

124. CIPFA/LASAAC would recommend that local authorities start to consider their contractual arrangements against the provisions of the new standard so that they can ensure their budgetary assumptions will be in line with any newly required accounting and financial reporting treatments.

> IFRS 15 *Revenue for Contracts with Customers*
>
> Q28 Do you agree with CIPFA/LASAAC's early views that there are no substantial issues that would require interpretation or adaptation in the Code for local authorities for the adoption of IFRS 15 *Revenue for Contracts with Customers*? If not, why not? Please give reasons for your response.

IFRS 9 *Financial Instruments*

125. The IASB has developed IFRS 9 in phases. It was first issued in 2009 with a new classification and measurement model for financial assets, which was followed by additions in 2010 relating to requirements for financial liabilities and derecognition. In 2013, the Standard was amended to include the new hedge accounting model. It was finalised in July 2014 with the final version of the Standard, superseding all previous versions. The new standard has an effective date of 1 January 2018.

126. IFRS 9 is built on a single classification and measurement approach for financial assets that reflects the business model in which they are managed and their cash flow characteristics.

127. The final IFRS 9 replaces most of the guidance in IAS 39 and has reduced the number of classifications for financial instruments. IFRS 9 applies a single classification and measurement approach to all types of financial assets, thus eliminating the complex requirements for bifurcation of hybrid financial assets; the entire hybrid instrument is assessed for classification and embedded derivatives are no longer separated from financial asset hosts.

Financial Assets – Classification and Measurement

128. The final Standard includes a rationale for classification which is based on two criteria. The Standard moves away from IAS 39 *Financial Instruments: Recognition and Measurement* reliance on the terms of an instrument (and whether it is traded or not). The two criteria that are used to determine how financial assets should be classified and measured are:

(a) the entity's business model for managing the financial assets; and

(b) the contractual cash flow characteristics of the financial assets.

129. If financial assets:

- are held within a business model whose objective is to hold assets in order to collect contractual cash flows, and
- their terms give rise to specified cash flows that solely consist of payments of principal and interest.

They are measured at amortised cost using the effective interest method.

130. All other financial assets are measured at fair value whether their gains and losses are posted to profit or loss (Surplus or Deficit on the Provision of Services) or other comprehensive income (Other Comprehensive Income and Expenditure). Other comprehensive income treatment (ie as currently applied to available for sale assets) is only available for instruments that are:

- part of a hedging relationship
- equity instruments that an entity has elected for this treatment
- designated by the entity as fair value through profit and loss where the change in fair value is attributable to changes in credit risk.

(Accumulated gains and losses are only recognised in profit or loss when an asset is derecognised, impaired or reclassified.)

131. Gains and losses on financial assets measured at fair value that do not meet these criteria will be debited to profit and loss (Surplus or Deficit on the Provision of Services) as they arise.

Financial Liabilities

132. IFRS 9 carried forward unchanged almost all of the accounting requirements in IAS 39 for financial liabilities. No changes were introduced for the classification and measurement of financial liabilities. This is with the exception of the recognition of changes (i.e. the effect) in own credit risk. IFRS 9 removes the volatility in profit or loss that was caused by changes in the credit risk of liabilities elected to be measured at fair value. IFRS 9 requires changes in the fair value of an entity's own credit risk to be recognised in other comprehensive income (and expenditure for local authorities) rather than in profit or loss the (Surplus or Deficit on the Provision of Services).

Impairment

133. IFRS 9 contains a single forward-looking 'expected-loss' impairment model applied to all financial instruments subject to impairment accounting which will result in earlier and more timely recognition of expected credit losses. This is a different approach to the impairing of financial instruments compared with the IAS 39 'incurred loss' model, which delays the recognition of credit losses until there is evidence of a credit loss. This is likely to bring about a significant change in the subsequent measurement of financial assets. It is very possible that local authorities will under the new standard recognise impairment losses in substantially different patterns than under the Code's adoption of IAS 39.

Hedge Accounting

134. The new model represents a significant change to hedge accounting requirements. The model aligns the accounting treatment with risk management activities, enabling entities to better reflect these activities in their financial statements. There are also enhanced disclosures about risk management activity.

Application to Local Authority Financial Instruments

135. CIPFA/LASAAC is considering the impact of the new classification and measurement requirements of the introduction of IFRS 9 for local authority financial instruments but would welcome commentary from interested parties on

how they consider the standard (including the transition arrangements) might impact on financial instruments they hold or are aware of.

136. CIPFA/LASAAC is of the view that local authorities should monitor their contractual arrangements so that they can ensure their budgetary assumptions for the effected financial instruments will be in line with any new accounting treatments.

IFRS 9 *Financial Instruments*	
Q29	Do you consider that there will be any particular application issues for the adoption of IFRS 9 *Financial Instruments* with regard to the financial instruments held by local authorities? Please set out what you consider these issues will be and the potential impact on adoption of the standard by the Code.