

## Rother District Council

**Report to:** Audit and Standards

**Date:** 22 March 2021

**Title:** Accounting Policies 2020/21

**Report of:** Antony Baden – Finance Manager

**Purpose of Report:** To present the accounting policies and critical judgements that will be used in the preparation of 2020/21 Statement of Accounts

### Officer

**Recommendation(s):** It be **RESOLVED**: That the Council's proposed accounting policies to be adopted in completing the 2020/21 Statement of Accounts be approved and the critical judgements noted

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## Introduction

1. This report presents the accounting policies that will be used in the preparation of 2020/21 Statement of Accounts and summarises any changes from 2019/20 introduced as a result of amendments to the Code of Practice on Local Authority Accounting 2020/21 (the Code) or as part of the Council's annual review process. The report also explains the requirement to include notes on the critical judgements used in the production of the Statement of Accounts which have been presented alongside the accounting policies in line with best practice.

## Accounting Policies

2. The Council's accounting policies are the specific principles, conventions, rules and practices that are applied in the production and presentation of the annual Statement of Accounts. These policies have to be disclosed as a note to the annual accounts. A copy of the policies can be found at Appendix A.
3. The Code of Practice on Local Authority Accounting for 2020/21 has been reviewed and it introduces no significant changes, compared to the previous year, that need to be implemented. However, the Council, as part of its annual review of policies, has taken the opportunity to make some minor changes to improve the wording and presentation of the policies. In addition, the section on interests in companies has been updated to reflect that the Council has an interest in Alliance Homes (Rother) Ltd.
4. In applying the accounting policies set out in Appendix A the Council will need to make certain judgements about complex transactions or those involving uncertainty about future events. The external auditors (Grant Thornton) are kept informed of any such matters.
5. It is recommended that the proposed accounting policies, to be used to prepare the Council's 2020/21 Statement of Accounts, are approved by the Audit and Standards Committee before the financial statements are prepared.

## Critical Judgements

6. In line with International Financial Reporting Standards (IFRS) and the Code the Council is required to disclose those judgements that management have made in the process of applying the Council's accounting policies that have the most significant effect on the amounts recognised in the financial statements. Appendix B sets out those critical judgements that management have made.

## Consultation

7. Consultation has taken place with the Council's External Auditors, Grant Thornton UK LLP.

## Conclusion

8. Committee is asked to review and approve the Council's proposed accounting policies, to be adopted in completing the 2020/21 Statement of Accounts and to note the critical judgements.

Other Implications	Applies?	Other Implications	Applies?
Human Rights	No	Equalities and Diversity	No
Crime and Disorder	No	Consultation	No
Environmental	No	Access to Information	No
Sustainability	No	Exempt from publication	No
Risk Management	No		

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Appendices:	Appendix A – Accounting Policies Appendix B – Critical Judgements
Relevant Previous Minutes:	None
Background Papers: Reference Documents:	None

## Accounting Policies

### ACCOUNTING POLICIES

#### 1. General Principles

The Statement of Accounts summarises the Council's transactions for the 2020/21 financial year and its position at the year-end of 31 March 2021. The Council is required to prepare an annual Statement of Accounts by the Accounts and Audit Regulations 2015 which those Regulations require to be prepared in accordance with proper accounting practices. These practices primarily comprise the Code of Practice on Local Authority Accounting in the United Kingdom 2020/21, supported by International Financial Reporting Standards (IFRS). The accounting convention adopted in the Statement of Accounts is principally historical cost, modified by the revaluation of certain categories of non-current assets and financial instruments.

#### 2. Accruals of Income and Expenditure

Activity is accounted for in the year that it takes place, not simply when cash payments are made or received. In particular:

- Revenue from contracts with service recipients whether for services or the provision of goods, is recognised when (or as) the goods are transferred to the service recipient in accordance with the performance obligations in the contract. However, for low individual value annual transactions (e.g. annual payment for beach hut licences) this is recognised on a cash basis.
- Supplies are recorded as expenditure when they are consumed - where there is a gap between the date supplies are received and their consumption they are carried as inventories on the Balance Sheet.
- Expenses in relation to services received (including services provided by employees) are recorded as expenditure when the services are received rather than when payments are made.
- Interest receivable on investments is accounted for as income on the basis of the effective interest rate for the relevant financial instrument rather than the cash flows fixed or determined by the contract.
- Where revenue and expenditure have been recognised but cash has not been received or paid, a debtor or creditor for the relevant amount is recorded in the Balance Sheet. Where debts may not be settled, the balance of debtors is written down and a charge made to revenue for the income that might not be collected.
- Accruals are made for amounts exceeding £100.

#### 3. Accounting for Council Tax and Non-Domestic Rates

The Council collects income from payers of Council Tax and Non-Domestic Ratepayers, but only part of the income relates to this Council, the balance being collected on behalf of other major precepting authorities, including the Government (for business rates). The amounts of debtors, adjustments for doubtful debts, overpayment creditors and receipts in advance that relate to the precepting authorities are shown as a single net debtor or creditor in the balance sheet. The element of the Collection Fund due to or from preceptors is held as part of the Short -Term Creditors or Debtors balance. Annual changes in the amounts held for preceptors are shown as part of financing activities in the Cash Flow Statement.

The amounts legally credited to the General Fund are those estimated before the start of the financial year, including distributions of estimated surplus, or contributions towards estimated deficits. In accounting terms, however, the Council's share of the

collectable debit (including adjustments to allowances for doubtful debts and appeals) are credited to the Comprehensive Income and Expenditure Statement (CI&ES). The difference between the cumulative amounts for statutory and accounting purposes forms the Collection Fund Adjustment Account (an unusable reserve) and the annual adjustment forms part of the accounting and financing adjustments.

#### **4. Cash and Cash Equivalents**

Cash is represented by cash in hand and deposits with financial institutions repayable without penalty on notice of not more than 24 hours. Cash equivalents are investments that mature in no more than ninety days from the date of acquisition and that are readily convertible to known amounts of cash with insignificant risk of change in value. In the Cash Flow Statement, cash and cash equivalents are shown net of bank overdrafts that are repayable on demand and form an integral part of the Council's cash management.

#### **5. Prior Period Adjustments, Changes in Accounting Policies and Estimates and Errors**

Prior period adjustments may arise as a result of a change in accounting policies or to correct a material error. Changes in accounting estimates are accounted for prospectively, i.e. in the current and future years affected by the change and do not give rise to a prior period adjustment. Changes in accounting policies are only made when required by proper accounting practices or the change provides more reliable or relevant information about the effect of transactions, other events and conditions on the Council's financial position or financial performance. Where a change is made, it is applied retrospectively (unless stated otherwise) by adjusting opening balances and comparative amounts for the prior period as if the new policy had always been applied. Material errors discovered in prior period figures are corrected retrospectively by amending opening balances and comparative amounts for the prior period.

#### **6. Charges to Revenue for Non-Current Assets**

Services, support services and trading accounts are debited with the following amounts to record the cost of holding non-current assets during the year:

- depreciation attributable to the assets used by the relevant service
- revaluation and impairment losses on assets used by the service where there are no accumulated gains in the Revaluation Reserve against which the losses can be written off
- amortisation of intangible assets attributable to the service.

The Council is not required to raise council tax to cover depreciation, revaluation and impairment losses or amortisations. However, it is required to make an annual provision from revenue to contribute towards the reduction in its overall borrowing requirement. This provision, known as Minimum Revenue Provision (MRP), is equal to an amount calculated on a prudent basis determined by the Council in accordance with statutory guidance. Depreciation, revaluation and impairment losses and amortisations are therefore replaced by the contribution in the General Fund Balance, by way of an adjusting transaction with the Capital Adjustment Account in the Movement in Reserves Statement for the difference between the two.

#### **7. Employee Benefits**

##### **Benefits Payable during Employment**

Short-term employee benefits are those due to be settled within 12 months of the year-end. They include such benefits as wages and salaries, paid annual leave and paid sick leave, bonuses and non-monetary benefits (e.g. cars) for current employees and

are recognised as an expense for services in the year in which employees render service to the Council. An accrual is made for the cost of holiday entitlements (or any form of leave, e.g. time off in lieu) earned by employees but not taken before the year-end which employees can carry forward into the next financial year. The accrual is made at the wage and salary rates applicable in the following accounting year, being the period in which the employee takes the benefit. The accrual is charged to Surplus or Deficit on the Provision of Services, but then reversed out through the Movement in Reserves Statement so that these benefits are charged to the General Fund in the financial year in which payment is made.

### **Termination Benefits**

Termination benefits are amounts payable as a result of a decision by the Council to terminate an officer's employment before the normal retirement date or an officer's decision to accept voluntary redundancy and are charged on an accruals basis to the relevant service cost line in the CI&ES when the Council is demonstrably committed to the termination of the employment of an officer or group of officers or making an offer to encourage voluntary redundancy. Where termination benefits involve the enhancement of pensions, statutory provisions require the General Fund balance to be charged with the amount payable by the Council to the pension fund or pensioner in the year, not the amount calculated according to the relevant accounting standards. In the Movement in Reserves Statement, appropriations are required to and from the Pensions Reserve to remove the notional debits and credits for pension enhancement termination benefits and replace them with debits for the cash paid to the pension fund and pensioners and any such amounts payable but unpaid at the year-end.

### **Post-Employment Benefits**

The majority of the Council's employees are members of the Local Government Pensions Scheme, administered by East Sussex County Council. The Scheme provides defined benefits to members (retirement lump sums and pensions), earned as employees worked for the Council.

The Local Government Scheme is accounted for as a defined benefits scheme:

- The liabilities of the East Sussex pension fund attributable to the Council are included in the Balance Sheet on an actuarial basis using the projected unit method - i.e. an assessment of the future payments that will be made in relation to retirement benefits earned to date by employees, based on assumptions about mortality rates, employee turnover rates, etc. and projections of projected earnings for current employees.
- Liabilities are discounted to their value at current prices, using a discount rate of x.x% (TBC at the appropriate time) based on the indicative rate of return on high quality corporate bond chosen by the Fund's Actuary.
- The assets of the East Sussex pension fund attributable to the Council are included in the Balance Sheet at their fair value:
  - quoted securities - current bid price
  - unquoted securities - professional estimate
  - unitised securities - current bid price
  - property - market value
- The change in the net pension liability is analysed into the following components:
  - current service cost - the increase in liabilities as a result of years of service earned this year - allocated in the CI&ES to the services for which the employees worked
  - past service cost - the increase in liabilities arising from current year decisions whose effect relates to years of service earned in earlier years

- debited to the Surplus or Deficit on the Provision of Services in the CI&ES as part of the cost of the Resources service
- net interest on the defined benefit liability, i.e. net interest expense for the Council – the change during the period in the net defined benefit liability that arises from the passage of time charged to the financing and investment income line of the Comprehensive Income and Expenditure Statement – this is calculated by applying the discount rate used to measure the defined benefit obligation at the beginning of the period to the defined benefit liability at the beginning of the period – taking account of any changes in the net defined benefit liability during the period as a result of contribution and benefit payments.
- remeasurements comprising:
  - the return on plan assets, excluding amounts included in net interest on the net defined liability, charged to the Pension Reserve as Other Comprehensive Income and Expenditure
  - actuarial gains or losses - changes in the net pensions liability that arise because events have not coincided with assumptions made at the last actuarial valuation or because the actuaries have updated their assumptions - charged to the Pensions Reserve as Other Comprehensive Income and Expenditure.
- contributions paid to the East Sussex pension fund - cash paid as employer's contributions to the pension fund in settlement of liabilities; not accounted for as an expense.

In relation to retirement benefits, statutory provisions require the General Fund balance to be charged with the amount payable by the Council to the pension fund or directly to pensioners in the year, not the amount calculated according to the relevant accounting standards. In the Movement in Reserves Statement, this means that there are appropriations to and from the Pensions Reserve to remove the notional debits and credits for retirement benefits and replace them with debits for the cash paid to the pension fund and pensioners and any such amounts payable but unpaid at the year-end. The negative balance that arises on the Pensions Reserve thereby measures the beneficial impact to the General Fund of being required to account for retirement benefits on the basis of cash flows rather than as benefits are earned by employees.

### **Discretionary Benefits**

The Council also has restricted powers to make discretionary awards of retirement benefits in the event of early retirements. Any liabilities estimated to arise as a result of an award to any member of staff are accrued in the year of the decision to make the award and accounted for using the same policies as are applied to the Local Government Pension Scheme.

### **8. Events after the Reporting Period**

Events after the Balance Sheet date are those events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the Statement of Accounts is authorised for issue. Two types of events can be identified:

- those that provide evidence of conditions that existed at the end of the reporting period - the Statement of Accounts is adjusted to reflect such events.
- those that are indicative of conditions that arose after the reporting period - the Statement of Accounts is not adjusted to reflect such events, but where a category of events would have a material effect, disclosure is made in the notes of the nature of the events and their estimated financial effect.

Events taking place after the date of authorisation for issue are not reflected in the Statement of Accounts.

## **9. Fair Values**

The Council measures some of its non-financial assets (surplus assets and investment properties), and any available for sale financial asset, at fair value at each reporting date. The Council also discloses fair values for financial assets and liabilities categorised as loans and receivables. Fair value is the price that would be received to sell an asset or transfer a liability in an orderly transaction at the year end. The fair value measurement assumes that the transaction takes place either in the principal market for the asset or liability, or, in the absence of a principal market, in the most advantageous market.

The Council measures the asset or liability using the assumptions that market participants would use when pricing the asset or liability, assuming that they act in their economic best interest.

When measuring the fair value the Council takes into account the market participants' ability to generate economic benefits by using the asset or liability in its highest or best use, or by selling it to another party that would use the asset or liability for its highest and best use.

The Council uses valuation techniques that are appropriate in the circumstances and for which sufficient data is available, maximising the use of observable inputs and minimising the use of unobservable inputs.

Inputs to the valuation techniques for assets and liabilities that are measured or disclosed in the financial statements are categorised within the fair value hierarchy, as follows:

- Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Council can access at the year end.
- Level 2 Inputs, other than quoted prices within Level 1, that are observable for the asset or liability, either directly or indirectly.
- Level 3 Unobservable inputs for the asset or liability.

## **10. Financial Instruments**

### **Financial Liabilities**

Financial liabilities are recognised on the Balance Sheet when the Council becomes a party to the contractual provisions of a financial instrument and initially measured at fair value and carried at their amortised cost. Annual charges to the Financing and Investment Income and Expenditure line in the CI&ES for interest payable are based on the carrying amount of the liability, multiplied by the effective rate of interest for the instrument. The effective interest rate is the rate that exactly discounts estimated future cash payments over the life of the instrument to the amount at which it was originally recognised.

This means that the amount presented in the Balance Sheet is the outstanding principal repayable (plus accrued interest) and interest charged to the CI&ES is the amount payable for the year according to the loan agreement.

Liabilities include trade payables. It has been assessed that the carrying amount in the Balance Sheet is a proxy for the fair value of those liabilities.

## Financial Assets

Financial assets are classified based on a classification and measurement approach that reflects the business model for holding the financial assets and their cash flow characteristics. There are three main classes of financial assets measured at:

- Amortised cost
- Fair value through profit or loss (FVPL)
- Fair value through other comprehensive income (FVOCI)

The business model of the Council is to hold investments to collect contractual cash flows. Financial assets are therefore classified at amortised cost, except for those whose contractual payments are not solely payment of principal and interest (i.e. where the cash flows do not take the form of a basic debt instrument).

### *Financial Assets Measured at Amortised Cost*

Financial assets measured at amortised cost are recognised on the Balance Sheet when the Council becomes a party to the contractual provisions of a financial instrument and are initially measured at fair value. They are then measured at their amortised cost. Annual credits to the Financing and Investment Income and Expenditure line in the CI&ES for interest receivable are based on the carrying amount of the asset multiplied by the effective rate of interest for the instrument. For most of the loans that the Council has made, this means that the amount presented in the Balance Sheet is the outstanding principal receivable (plus accrued interest) and interest credited to the CI&ES is the amount receivable for the year in the loan agreement.

However, the Council has from time to time made a number of loans to voluntary organisations at less than market rates (soft loans). When soft loans are made, a loss is recorded in the CI&ES (debited to the appropriate service) for the present value of the interest that will be foregone over the life of the instrument, resulting in a lower amortised cost than the outstanding principal.

Interest is credited to the Financing and Investment Income and Expenditure line in the CI&ES at a marginally higher effective rate of interest than the rate receivable from the voluntary organisations, with the difference serving to increase the amortised cost of the loan in the Balance Sheet. Statutory provisions require that the impact of soft loans on the General Fund Balance is the interest receivable for the financial year – the reconciliation of amounts debited and credited to the CI&ES to the net gain required against the General Fund Balance is managed by a transfer to or from the Financial Instruments Adjustment Account in the Movement in Reserves Statement. Any gains and losses that arise on the de-recognition of an asset are credited/debited to the Financing and Investment Income and Expenditure line in the CI&ES.

### *Expected Credit Loss Model*

The Council recognises expected credit losses on all of its financial assets held at amortised cost, either on a 12-month or lifetime basis. The expected credit loss model also applies to lease receivables and contract assets. Lifetime losses are recognised for trade receivables (debtors) held by the Council.

Impairment losses are calculated to reflect the expectation that the future cash flows might not take place because the borrower could default on their obligations. Credit risk plays a crucial part in assessing losses. Where risk has increased substantially since an instrument was initially recognised, losses are assessed on a lifetime basis. Where risk has not increased substantially or remains low, losses are assessed on the basis of 12-month expected losses.

The Council has a substantial amount of investments and employs treasury management advisers in addition to full time professional staff. However, reasonable and verifiable information to support the measurement of lifetime losses on individual instruments is not available without undue cost or effort. Losses are mainly assessed for the portfolio on a collective basis.

Financial Assets are amalgamated into the following groups to assess risk and associated loss allowances whilst making use of a simplified approach contained in regulations.

Group 1 – Commercial investments in line with treasury management policy including counterparties that have external credit ratings of A or better. Loss allowances will be assessed on a group basis using the simplified approach of collective assessment.

Group 2 – Loans to related parties. Loss allowances for these loans are assessed on an individual basis and / or an individual borrower basis.

Group 3 – Other loans to local businesses, in support of the Council vision and objectives. Loss allowances for these loans are assessed on an individual basis and / or an individual borrower basis.

#### *Financial Assets Measured at Fair Value through Profit or Loss*

Financial assets that are measured at FVPL are recognised on the balance sheet when the Council becomes a party to the contractual provisions of a financial instrument and are initially measured and carried at fair value. Fair value gains and losses are recognised as they arrive in the Surplus or Deficit on the Provision of Services.

The fair value measurements of the financial assets are based on the following techniques:

- Instruments with quoted market prices – the market price
- Other instruments with fixed and determinable payments – discounted cash flow analysis

The inputs to the measurement techniques are categorised in accordance with the following three levels:

- Level 1 inputs – quoted prices (unadjusted) in active markets for identical assets that the authority can access at the measurement date.
- Level 2 inputs – inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly.
- Level 3 inputs – unobservable inputs for the asset.

Any gains or losses that arise on the derecognition of the asset are credited or debited to the Financing and Investment Income and Expenditure line in the CI&ES.

#### *Financial Assets Measured at Fair Value through Other Comprehensive Income*

Financial assets that are measured at FVOCI are recognised on the balance sheet when the Council becomes a party to the contractual provisions of a financial instrument and are initially measured and carried at fair value. Fair value gains and losses are charged to the Other Comprehensive Income and Expenditure and are held in the Financial Instrument Revaluation Reserve.

Movements in amortised cost are charged to the Surplus or Deficit on the Provision of Services

Cumulative gains/losses on fair value are transferred to the Surplus or Deficit on the Provision of Services on derecognition.

## **11. Government Grants and Contributions**

Whether paid on account, by instalments or in arrears, government grants and third-party contributions and donations are recognised as due to the Council when there is reasonable assurance that:

- the Council will comply with the conditions attached to the payments, and
- the grants or contributions will be received.

Amounts recognised as due to the Council are not credited to the CI&ES until conditions attached to the grant or contribution have been satisfied. Conditions are stipulations that specify that the future economic benefits or service potential embodied in the asset acquired using the grant or contribution are required to be consumed by the recipient as specified, or future economic benefits or service potential must be returned to the transferor.

Monies advanced as grants and contributions for which conditions have not been satisfied are carried in the Balance Sheet as liabilities. When conditions are satisfied, the grant or contribution is credited to the relevant service line (attributable revenue grants and contributions) or Taxation and Non-Specific Grant Income (non-ringfenced revenue grants and all capital grants) in the CI&ES.

Where capital grants are credited to the CI&ES, they are reversed out of the General Fund Balance in the Movement in Reserves Statement. Where the grant has yet to be used to finance capital expenditure, it is posted to the Capital Grants Unapplied Reserve. Amounts in the Capital Grants Unapplied Reserve are transferred to the Capital Adjustment Account once they have been applied to fund capital expenditure. The Council has elected to charge a Community Infrastructure Levy (CIL) on new builds with appropriate planning consent. The income from the levy will be used to fund various projects described as “infrastructure” in a broader sense than used for Council property in Note 1.16 below. The infrastructure investment is determined by a panel and it is not necessarily this Council that will undertake the works. Part of the CIL income is retained to offset the cost of administration and is accounted for as income for the Strategy and Planning service. Some is also payable to parishes: this is treated as an agency service and is excluded from the CI&ES. The rest is intended for use to finance capital and is treated as capital contributions. As it is received without conditions it is recognised immediately as capital grants and contributions income and is then transferred to the Capital Grants Unapplied Reserve.

The income from CIL is accounted for on an accruals basis and recognised immediately in the CI&ES at the commencement date of the chargeable development. Surcharges and interest received in accordance with the CIL regulations will be accounted for as if they were CIL receipts.

## **12. Investment Property**

Investment properties are those that are used solely to earn rentals and/or for capital appreciation. The definition is not met if the property is used in any way to facilitate the delivery of services or production of goods or is held for sale.

Investment properties are measured initially at cost and subsequently at fair value, being the price that would be received to sell such an asset in an orderly transaction between market participants at the measurement date. As a non-financial asset, investment properties are measured at highest and best use.

Properties are not depreciated but are revalued annually according to market conditions at the year-end. Gains and losses on revaluation are posted to the

Financing and Investment Income and Expenditure line in the CI&ES. The same treatment is applied to gains and losses on disposal.

Rentals received in relation to investment properties are credited to the Financing and Investment Income line and result in a gain for the General Fund Balance. However, revaluation and disposal gains and losses are not permitted by statutory arrangements to have an impact on the General Fund Balance. The gains and losses are therefore reversed out of the General Fund Balance in the Movement in Reserves Statement and posted to the Capital Adjustment Account and (for any sale proceeds greater than £10,000) the Capital Receipts Reserve.

### **13. Intangible Assets**

Expenditure on non-monetary assets that do not have physical substance but are controlled by the Council as a result of past events (e.g. software licences) is capitalised when it is expected that future economic benefits or service potential will flow from the intangible asset to the Council.

Internally generated assets are capitalised where it is demonstrable that the project is technically feasible and is intended to be completed (with adequate resources being available) and that the Council will be able to generate future economic benefits or deliver service potential by being able to use the asset. Costs relating to the development of computer software for internal use are capitalised where it can be measured reliably as attributable to the asset and is restricted to that incurred in the development phase. When the software is available for its intended use, these costs are amortised in equal annual amounts over the estimated useful life of the software. Amounts capitalised include the total cost of any external products or services and labour costs directly attributable to development. Management judgement is involved in determining the appropriate internal costs to capitalise and the amounts involved. The useful life is determined by management at the time the software is acquired and brought into use and is regularly reviewed for appropriateness. For computer software licences, the useful life represents management's view of the expected period over which the Council will receive benefits from the software.

Intangible assets are measured initially at cost. The depreciable amount of an intangible asset is written down over its useful life, to the appropriate line in the CI&ES. No intangible assets are recorded with indefinite lives. An asset is tested for impairment whenever there is an indication that the asset might be impaired, and any losses are posted to the appropriate line in the Income and Expenditure Statement. The calculated amounts for amortisation and impairment are charged to the Cost of Services in the CI&ES, but they are not proper charges against the General Fund. A transfer is therefore made from the Capital Adjustment Account to the General Fund to reverse the impact.

### **14. Leases**

Leases are classified as finance leases where the terms of the lease transfer substantially all the risks and rewards incidental to ownership of the property, plant or equipment from the lessor to the lessee. All other leases are classified as operating leases.

Where a lease covers both land and buildings, the land and buildings elements are considered separately for classification.

Arrangements that do not have the legal status of a lease but convey a right to use an asset in return for payment are accounted for under this policy where fulfilment of the arrangement is dependent on the use of specific assets.

All of the Council's leases have been determined to constitute operating leases.

### **The Council as Lessee**

Rentals paid under operating leases are charged to the CI&ES as an expense of the services benefitting from use of the leased property, plant or equipment. Charges are made on a straight-line basis over the life of the lease, even if this does not match the pattern of payments (e.g. there is a rent-free period at the commencement of the lease).

### **The Council as Lessor**

Where the Council grants an operating lease over a property or an item of plant or equipment, the asset is retained in the Balance Sheet. Rental income is credited to the appropriate line in the CI&ES. Credits are made on a straight-line basis over the life of the lease, even if this does not match the pattern of payments (e.g. there is a premium paid at the commencement of the lease). Initial direct costs incurred in negotiating and arranging the lease are added to the carrying amount of the relevant asset and charged as an expense over the lease term on the same basis as rental income.

## **15. Overheads and Support Services**

The cost of overheads and support services are charged to service segments in accordance with the Council's arrangements for accountability and financial performance.

## **16. Property, Plant and Equipment**

Assets that have physical substance and are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and that are expected to be used during more than one financial year are classified as Property, Plant and Equipment.

### **Recognition**

Expenditure on the acquisition, creation or enhancement of Property, Plant and Equipment is capitalised on an accruals basis, provided that it is probable that the future economic benefits or service potential associated with the item will flow to the Council and the cost of the item can be measured reliably. Expenditure that maintains but does not add to an asset's potential to deliver future economic benefits or service potential (i.e. repairs and maintenance) is charged as an expense when it is incurred.

### **Measurement**

Assets are initially measured at cost, comprising:

- the purchase price
- any costs attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management
- the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

The cost of assets acquired other than by purchase is deemed to be its current value, unless the acquisition does not have commercial substance (i.e. it will not lead to a variation in the cash flows of the Council). In the latter case, where an asset is acquired via an exchange, the cost of the acquisition is the carrying amount of the asset given up by the Council.

Assets are then carried in the Balance Sheet using the following measurement bases:

- Vehicles, plant, etc. and infrastructure - depreciated historical cost.

- Community assets and assets under construction - historic cost.
- Land and buildings - current value, determined as the amount that would be paid for the asset in its existing use (existing use value - EUV). Where there is no market-based evidence of current value because of the specialist nature of an asset, depreciated replacement cost is used as an estimate of current value.
- Surplus Properties – fair value, as described in accounting policy 1.9 above, equating to market value for their highest and best use from a market participant's perspective.

Assets included in the Balance Sheet at current value are subject to a full valuation once every five years but are subject to a desktop review at the end of each year to ensure that their carrying amount is not materially different from their current value, or fair value at the year-end. Increases in valuations are matched by credits to the Revaluation Reserve to recognise unrealised gains. Exceptionally, gains might be credited to the CI&ES where they arise from the reversal of a loss previously charged to a service. Where decreases in value are identified, they are accounted for by:

- where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against that balance (up to the amount of the accumulated gains)
- where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the CI&ES.

The Revaluation Reserve contains revaluation gains recognised since 1 April 2007 only, the date of its formal implementation. Gains arising before that date have been consolidated into the Capital Adjustment Account.

The values of Land and Buildings assets individually worth less than £10,000 are recorded, but not included in the balance sheet values.

### **Impairment**

Assets are assessed at each year-end as to whether there is any indication that the value of an asset may be impaired. Where indications exist and any possible differences are estimated to be material, the recoverable amount of the asset is estimated and, where this is less than the carrying amount of the asset, an impairment loss is recognised for the shortfall.

Where impairment losses are identified, they are accounted for by:

- where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against that balance (up to the amount of the accumulated gains)
- where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the CI&ES.

Where an impairment loss is reversed subsequently, the reversal is credited to the relevant service line(s) in the CI&ES, up to the amount of the original loss, adjusted for depreciation that would have been charged if the loss had not been recognised.

### **Depreciation**

Depreciation is provided for on all Property, Plant and Equipment assets by the systematic allocation of their depreciable amounts over their useful lives. An exception is made for assets without a determinable finite useful life (i.e. freehold land and certain Community Assets) and assets that are not yet available for use (i.e. assets under construction).

Depreciation is calculated on the following bases:

- dwellings and other buildings - straight-line allocation over the useful life of the property as estimated by the Valuer. Useful life is between 10 and 50 years depending on the asset.
- vehicles, plant, furniture and equipment – straight line allocation over the useful life of the asset. Useful life is between 7 and 20 years.
- Infrastructure - straight-line allocation over 50 years.

No depreciation is charged in year of acquisition but is charged at a full year rate in the year of disposal.

Reclassified assets are depreciated from year of reclassification.

Revaluation gains are also depreciated, with an amount equal to the difference between current value depreciation charged on assets and the depreciation that would have been chargeable based on their historical cost being transferred each year from the Revaluation Reserve to the Capital Adjustment Account.

### **Componentisation of Property Assets**

Where an item of Property, Plant and Equipment asset has major components whose cost is significant in relation to the total cost of the item, the components are depreciated separately. Where the Council has revalued a property, or carried out major capitalised works, it has been necessary to identify the major components making up the property using the following major component analysis:

- Land
- Buildings
- External areas (such as car parks)
- Plant and equipment (such as lifts and heating systems)

The Council has also adopted a de minimis level of 10% of the building value or £50,000 to apply componentisation.

### **Disposals**

When an asset is disposed of or decommissioned, the carrying amount of the asset in the Balance Sheet is written off to the other Operating Expenditure line in the CI&ES as part of the gain or loss on disposal. Receipts from disposals (if any) are credited to the same line in the CI&ES also as part of the gain or loss on disposal (i.e. netted off against the carrying value of the asset at the time of disposal). Any revaluation gains accumulated for the asset in the Revaluation Reserve are transferred to the Capital Adjustment Account.

Amounts received for a disposal in excess of £10,000 are categorised as capital receipts and are credited to the Capital Receipts Reserve and can then only be used for new capital investment. Receipts are appropriated to the Reserve from the General Fund Balance in the Movement in Reserves Statement.

The written-off value of disposals is not a charge against council tax, as the cost of non-current assets is fully provided for under separate arrangements for capital financing. Amounts are appropriated to the Capital Adjustment Account from the General Fund Balance in the Movement in Reserves Statement.

## **17. Provisions, Contingent Liabilities and Contingent Assets**

### **Provisions**

Provisions are made where an event has taken place that gives the Council a legal or constructive obligation that probably requires settlement by a transfer of economic

benefits or service potential, and a reliable estimate can be made of the amount of the obligation. For instance, the Council may be involved in a court case that could eventually result in the making of a settlement or the payment of compensation.

Provisions are charged as an expense to the appropriate service line in the CI&ES in the year that the Council becomes aware of the obligation and are measured at the best estimate at the balance sheet date of the expenditure required to settle the obligation, taking into account relevant risks and uncertainties.

When payments are eventually made, they are charged to the provision carried in the Balance Sheet. Estimated settlements are reviewed at the end of each financial year - where it becomes less than probable that a transfer of economic benefits will now be required (or a lower settlement than anticipated is made), the provision is reversed and credited back to the relevant service.

Where some or all of the payment required to settle a provision is expected to be recovered from another party (e.g. from an insurance claim), this is only recognised as income for the relevant service if it is virtually certain that reimbursement will be received if the Council settles the obligation.

### **Contingent Liabilities**

A contingent liability arises where an event has taken place that gives the Council a possible obligation whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the Council. Contingent liabilities also arise in circumstances where a provision would otherwise be made but either it is not probable that an outflow of resources will be required, or the amount of the obligation cannot be measured reliably. Contingent liabilities are not recognised in the Balance Sheet but disclosed in a note to the accounts.

### **Contingent Assets**

A contingent asset arises where an event has taken place that gives the Council a possible asset whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the Council.

Contingent assets are not recognised in the Balance Sheet but disclosed in a note to the accounts where it is probable that there will be an inflow of economic benefits or service potential.

## **18. Reserves**

The Council maintains two groups of reserves, usable and unusable.

Usable reserves comprise the following:

- **Capital Receipts Reserve:** proceeds from the sales of non-current assets are initially credited to the CI&ES, but legally can only be used to finance capital expenditure, and so are transferred to the Capital Receipts Reserve and afterwards used for this specific purpose.
- **Capital Grants Unapplied:** the Council receives grants and contributions towards capital expenditure, and, where repayment conditions are not present or no longer apply, they are credited to the CI&ES and immediately transferred into the Capital Grants Unapplied Reserve until required to finance capital investment.
- **Earmarked Reserves:** the Council may set aside earmarked reserves to cover specific projects or contingencies. These are transferred from the General Fund, and amounts are withdrawn as required to finance such expenditure. The expenditure itself is charged to the appropriate line in the CI&ES. There are no

legal restrictions on the use of earmarked reserves, and unspent balances can be taken back to the General Fund in the same way.

- General Fund: this represents all other usable reserves, without legal restrictions on spending, which arise from annual surpluses or deficits.

Unusable Reserves consist of those which cannot be used to finance capital or revenue expenditure:

- Revaluation Reserve: this consists of accumulated gains on individual items of Property, Plant and Equipment. The Reserve contains only gains accumulated since 1 April 2007, the date that the Reserve was created. Accumulated gains before that date were consolidated into the balance on the Capital Adjustment Account. The balance is reduced when assets with accumulated gains are:
  - revalued downwards or impaired and the gains are lost
  - used in the provision of services and the gains are consumed through depreciation, or
  - disposed of and the gains are realised.
- Capital Adjustment Account: Receives credits when capital is financed from the General Fund or from the Capital Receipts and Capital Grants Unapplied reserves and receives debits to offset depreciation and other charges relating to capital which are not chargeable against the General Fund. The account contains revaluation gains accumulated on non-current assets before 1 April 2007, the date on which the Revaluation Reserve was created to hold such gains.
- Deferred Capital Receipts: in some cases (particularly former housing stock disposed of, where the purchaser financed the transaction through a mortgage from the Council) an asset is disposed of, but the income cannot be collected immediately. The Council maintains records for a long-term debtor, offset by a balance in the Deferred Capital Receipts Account. When the income is received the debtor is written down and a transfer is made between this account and the Capital Receipts Reserve.
- Pensions Reserve: The Pensions Reserve absorbs the timing differences arising from the different arrangements for accounting for post-employment benefits and for funding benefits in accordance with statutory provisions. The Council accounts for post-employment benefits in the CI&ES as the benefits are earned by employees accruing years of service, updating the liabilities recognised to reflect inflation, changing assumptions and investment returns on any resources set aside to meet the costs. However, statutory arrangements require benefits earned to be financed as the Council makes employer's contributions to pension funds or eventually pays any pensions for which it is directly responsible. The debit balance on the Pensions Reserve therefore shows a substantial shortfall in the benefits earned by past and current employees and the resources the Council has set aside to meet them. The statutory arrangements will ensure that funding will have been set aside by the time the benefits come to be paid.
- Collection Fund Adjustment Account: this represents the differences arising from the recognition of Council Tax income and Non-Domestic Rates in the CI&ES as they fall due from payers, compared with the statutory arrangements for paying across amounts from the Collection Fund to the General Fund.
- Accumulated Absences Reserve: this contains the difference between the statutory and accounting liability for the cost of accumulated absences: the cost is properly chargeable to the CI&ES, but not to the General Fund.
- Pooled Investment Fund Adjustment Account: this contains the unrealised gains or losses made by the Council arising from increases or decreases in the

value of its investments that have quoted market prices or otherwise do not have fixed or determinable payments.

### **19. Revenue Expenditure Funded from Capital under Statute**

Expenditure incurred during the year that may be capitalised under statutory provisions but that does not result in the creation of a non-current asset is charged as expenditure to the relevant service in the CI&ES in the year. Where the Council has determined to meet the cost of this expenditure from existing capital resources or by borrowing, a transfer in the Movement in Reserves Statement from the General Fund Balance to the Capital Adjustment Account then reverses out the amounts charged so that there is no impact on the level of council tax.

### **20. VAT**

VAT payable is included as an expense only to the extent that it is not recoverable from Her Majesty's Revenue and Customs. VAT receivable is excluded from income.

### **21. Interests in Companies and Other Entities**

The Council is 100% shareholder of Alliance Homes (Rother) Ltd. The company was incorporated in October 2020. Group accounts will be prepared where material.

In the Council's own single-entity accounts, its interest in companies and other entities are recorded as financial assets at cost, less any provision for losses.

**Critical Judgements****Alliance Homes (Rother) Ltd**

The Council is sole shareholder of Alliance Homes. Since the company's inception in October 2020 costs incurred by Alliance have been small in scale. The Council has determined that group accounts will not be prepared in 2020/21, in addition to its single entity accounts, since the interest is not material to the Council's overall financial position. It is anticipated that group accounts will be prepared for 2021/22.