Appendix 1

Narrative Summary of Annual Statement of Accounts and Annual Governance Statement 2015-16

1. Introduction

1.1 As part of the formal process of closing the County Council's 2015-16 accounts, Members are required to consider and approve the Annual Governance Statement attached as Appendix 2, and to approve the Statement of Accounts ("the accounts"), attached as Appendix 3, by 30 September. This process of approval is included within the Committee's terms of reference.

1.2 It is also considered good practice to publish a short Summary of the Statement of Accounts (Appendix 4) alongside the full accounts.

1.3 The Council's external auditor, Ernst & Young, has examined the accounts. Their examination is now substantially complete and there is a separate report from them on this agenda.

1.4 This report summarises the contents of the Annual Governance Statement, and of the accounts, and highlights any significant issues arising from the audit or as a result of officer review during the audit period.

2. Background

2.1 The Local Government England and Wales Accounts and Audit Regulations 2015 issued by the Secretary of State set out the requirements for the preparation and publication of final accounts. These regulations include the requirement for the formal approval, by a full Committee, of the Council's Statement of Accounts.

2.2 The Executive Director of Finance is satisfied that the Statement of Accounts has been prepared in accordance with both the current Code of Practice on Local Authority Accounting in Great Britain ("the Code") and the Service Reporting Code of Practice for Local Authorities ("SeRCOP") supported by International Financial Reporting Standards ("IFRS") and other statutory guidance. The Statement of Accounts is required to present a true and fair view of the County Council's financial position at 31 March 2016 and also the income and expenditure for the financial year.

2.3 The Council continues to prepare the 2015-16 Statement of Accounts under International Financial Reporting Standards. There is one additional accounting policy added since 2015-16. The new policy "Fair Value Measurement is at note 1.10 and is a result of a requirement to implement IFRS 13 — Fair Value Measurement in

2015-16. This policy explains how assets which are measured at "fair value" in the accounts are valued.

2.4 There are inherent uncertainties associated with the measurement of fair values where quoted prices on an active market do not exist, and this is now explained in note 4.

2.5 The Executive Director of Finance reported the final revenue and capital expenditure positions for 2015-16 and the provisions and reserves held at 31 March 2016 to Policy and Resources Committee on 31 May 2016. The net revenue expenditure reported in May is reconciled to the Comprehensive Income and Expenditure statement in note 23 to the accounts.

2.6 The net underspend of £0.052m reported to Policy and Resources Committee on 31 May 2016 has been transferred to General Balances. Details of movements on this balance are shown in paragraph 5.8.

2.7 A public inspection period of 30 working days commencing 30 June was publicised on the Norfolk County Council web site in accordance with the relevant regulations. No enquiries from the public were received during that period.

2.8 In accordance with good practice, the draft 2015-16 Statement of Accounts has been publicly available on the Council's web site since 30 June.

2.9 Ernst & Young have performed a detailed examination of the accounts through July and August, and will present their Audit Results Report to this meeting. They will only be able to formally conclude the audit, and issue their report and certificate once they have received a copy of the Statement of Accounts as approved by this Committee.

2.10 Any further audit amendments to these accounts between the date of this report and the meeting will be notified to members of the Audit Committee at the meeting.

2.11 The Accounts and Audit Regulations require that the 2015-16 Statement of Accounts must be published by 30 September.

3. Annual Governance Statement

3.1 Regulations require that:
- the Council must conduct a review at least once a year of the effectiveness of its system of internal control, including internal audit;
- findings of this review should be considered by the Council;
- the Council must approve an Annual Governance Statement; and
- the Annual Governance Statement must accompany the Statement of Accounts.

3.2 For Norfolk County Council the Audit Committee undertakes these duties on behalf of the Council.

3.3 The Executive Director of Finance reviews the effectiveness of the system of internal control throughout the year and reports annually to the Audit Committee. The Executive Director of Finance reported to the Audit Committee on 16 June 2016 that in his opinion the effectiveness of risk management and internal control for 2015-16 is 'Acceptable' and therefore considered 'sound'.

3.4 The Accounts and Audit Regulations require the preparation of an Annual Governance Statement, signed by the Leader and the Managing Director. Guidance for the preparation, review and reporting of the Annual Governance Statement has been issued by CIPFA /SoLACE and has been used in its preparation.

3.5 The draft Annual Governance Statement ("AGS") has been published along with the draft Statement of Accounts on the Council's website. The final AGS will be published alongside the audited Statement of Accounts.

3.6 The AGS confirms that, during the 2015-16 financial year, and up to the date the accounts are published, overall Corporate Governance arrangements and internal controls in the Council were in place and effective in terms of business as well as financial risk. It also confirms that areas where controls need to be developed or improved are known about and are being actioned.

3.7 An Annual Governance Statement is attached as Appendix 2. Two updates have been made to the draft published in July, at pages 32 and 37. These changes are clearly highlighted in the Appendix.

4. Changes to the Presentation of the Accounts

4.1 Each year the Code of Practice on Local Authority Accounting is revised and updated to ensure accounts produced by local authorities comply, where relevant, with the latest accounting standards.

4.2 The one significant changes to the format or content of the accounts relate to the new requirements under IFRS 13 — Fair Value Measurement. The Investment properties note (note 14) now contains additional tables and information relating to valuations and valuation techniques. Prior to the revision of this note, a review of assets classed as investment properties was undertaken by the Council’s valuers, resulting in just the Airport Industrial Estate and certain agricultural land with development potential remaining under that classification. Other properties previously classified as investment properties are now classed within operational assets.

4.3 The Joint Arrangements note (note 26) has been expanded to include details of the Better Care Fund arrangements with Clinical Commissioning Groups in Norfolk.

4.4 The Amounts reported for Resource Allocation Decisions note has been updated to reflect changes to the Council’s management structure (note 23).

4.5 A small number of notes to the accounts have been enhanced, including a note concerning the impact of the EU referendum (note 6).

4.6 From 2015-16, the Council’s joint committees (Norfolk Museums, and Records) are no longer required to produce separate statements of accounts. As a result of this, the joint committees note is no longer required in the Council’s statement of accounts.

5. Statement of Accounts – Content

5.1 The accounts are set out in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16. Apart from the changes relating to IFRS13 noted above, there have been no significant changes to generally recognised accounting practices affecting the Council since 2014-15.

5.2 The Statement of Accounts includes the Movement in Reserves Statement (“MIRS”), the Comprehensive Income and Expenditure Statement (“CIES”), a Balance Sheet and Cash Flow Statement. In addition there is a summary of the Fire fighters’ pension scheme, the Norfolk Pension Fund Accounts, and Norfolk County Council’s Group Accounts which incorporate the financial results, where material, of companies controlled by the Council including the Norse Group and Independence Matters CIC.

<u>Explanatory Foreword</u>

5.3 The purpose of the foreword is to offer interested parties an easily understandable guide to the most significant matters in the accounts.

Statement of Responsibilities

5.4 This statement sets out the respective responsibilities of the Council and the Executive Director of Finance in relation to the production of the final accounts.

Independent Auditors' Report

5.5 This report will set out the External Auditor's opinion in respect of the Statement of Accounts. Based on an assumption that the Audit Committee will agree to approve the Statement of Accounts, the Council expects to receive unqualified audit opinions in respect of the Council's accounts and the pension fund accounts.

Movement in Reserves Statement

5.6 This statement shows the movement during the year of all the Council/Group's useable and unusable reserves and shows the aggregate change in its net worth.

5.7 As well as any surplus or deficit on the provision of services, the statement includes gains and losses relating to the revaluation of fixed assets and re-measurement of the net liability to cover the cost of retirement benefits.

5.8 The 31 March 2016 the General Fund Balance stood at £19.252m:

	£m
Actual General Balances at 31 March 2015	**19.000**
Use of funds for one-off purposes: Increase in General Balances (as approved in 2015-18 budget)	0.200
Net underspend 2015-16	0.052
General Balances at 31 March 2016	**19.252**

Comprehensive Income and Expenditure Statement

5.9 The Comprehensive Income and Expenditure Statement shows the resources generated and consumed by the Council, including income and expenditure associated with each major service heading.

5.10 Balance Sheet

The Balance Sheet statement sets out the financial position of the Council at 31 March 2016 The statement shows the balances and reserves at the Council's disposal, its long-term borrowing, and the fixed assets and net current assets employed. The principal movements on the balance sheet are described below.

5.11 The net book value of Property Plant and Equipment (note 12) is broadly unchanged since 2015-16. Reductions due to schools converting to academy status, and a reduction in assets classed as being under construction (including County Hall) have been off-set by the cost of infrastructure assets added to the valuation. There have been no additions or disposals of material Heritage Assets (note 13) during the year.

5.12 The value of investment properties (note 14), which are those held to generate an income such as the Council's share of the Airport Industrial Estate, has decreased by £9.5m as a number of properties such as the Scottow Enterprise Park have been re-assessed as operational properties for accounting purposes.

5.13 Long term investments, which include residual amounts due from Icelandic banks, and long term debtors, are broadly unchanged since 2014-15. Short term investments have decreased by £11m due mainly to an increase in short term loans and receivables held under the Council's Treasury Management strategy. This movement is offset by a decrease of £13m in Cash and Cash Equivalents (note 17) which represents a reduction in the amount of surplus cash invested in short term money markets.

5.14 The levels of both long term and short term debtors combined (note 16) remain broadly in line with 2014-15. Amounts due from central government have decreased under short term debtors, but long term debtors have increased by £9m consistent with a new capital loan of £10m made to the Norse Group during the year. As with other transactions between group members, this loan is not included in the group accounts.

5.15 Amounts classed as Asset Held for Sale (note 18) were slightly lower than 2015-16. During the year an additional £1.3m of the Council's property met the detailed accounting conditions to be classed as an Asset Held for Sale. £1.5m of these properties were sold leaving a balance of £1.1m awaiting sale at 31 March 2016.

5.16 Total long-term liabilities shown on the face of the balance sheet decreased from £1,686m to £1,463m due mainly to a decrease in the Council's Pension Liabilities (Local Government Pension Scheme and Fire-Fighters Pension Scheme) with the reported deficit reducing from £1,087m to £871m (note 39, total obligations less scheme assets), effectively reversing the previous year's movement.

The IAS19 reporting standard requires the Fund Actuary to set the Discount Rate (the rate used to value liabilities) by reference to market bond yields. All things being equal, as the discount rate rises, the value attributable to liabilities will decrease. Therefore the balance sheet position for the typical employer is likely to have improved over 2015-16 as a result of an increase in the net discount rate over this period.

Period ended	31 March 2016 % p.a.	31 March 2015 % p.a.
Pension increase rate	2.2%	2.4%
Salary increase rate	3.2%	3.3%
Discount rate	3.5%	3.2%

The impact of this on the CIES is a £190m re-measurement of the net defined benefit liability. The reduction in scheme net liabilities is shown in note 38 (Defined Benefit Pension Schemes). The impact on the Council's "other long term liabilities" and reserves can be seen in the Balance sheet and MIRS respectively.

The IAS19 report used for statutory accounting purposes is prepared using a different set of assumptions to the Funding calculation used in the Triennial Valuation to determine employer contribution rates and to which a stabilisation mechanism is applied to smooth volatility in the discount rate over the funding period. The deficit on the local government scheme will be made good by increased contributions over the remaining working life of employees, as assessed by the scheme actuary.

5.17 Cash Flow Statement
The cash flow statement summarises the inflows and outflows of cash arising from transactions with third parties for both revenue and capital purposes. The statement shows any increases or decreases in cash and cash equivalents as discussed in paragraph 5.13 above.

5.18 Notes to the Core Financial Statements
The first note to the Accounts is the Statement of Accounting Policies which summarises the accounting rules and conventions that have been used in preparing the accounts.

5.19 The Code requires that some specific notes have to be included in the Statement of Accounts, e.g. disclosure of related party transactions. In addition, other notes may be added in order that a reader of the accounts has sufficient information to have a good understanding of the Council's activities.

5.20 The "movement in reserves statement – adjustments between accounting basis and funding basis under legislation" (note 7) reconciles the total comprehensive income and expenditure recognised in accordance with proper accounting practice, to the resources that are specified by statutory provisions as being available to the Council to meet future capital and revenue expenditure.

5.21 When the adjustments in note 7 have been applied to the Movement in Reserves Statement, the General Fund Balance of £19.252m is equal to the General Balances figure reported to 31 May 2016 Policy and Resources Committee.

Fire Fighters' Pension Fund

5.22 This statement summarises the pension arrangements for the fire fighters' pension scheme.

Group Accounts

5.23 As well as publishing its accounts as a single entity, Norfolk County Council must also publish group accounts which incorporate the financial results, where material, of companies and other entities controlled by the Council – primarily the Norse Group of companies and Independence Matters CIC.

5.24 The group accounts are shown as a separate section in the statement of accounts.

5.25 The group accounts comprise group movement in reserves, group comprehensive income and expenditure, the group balance sheet and a group cash flow statement. It also includes notes to the group accounts where these differ or include information in addition to the single entity accounts.

Pension Fund Accounts

The detailed Pension Fund Accounts which are incorporated into this Statement of Accounts were considered by the Pensions Committee on 6 September 2016. The Pension Committee agreed to recommend to the Audit Committee that the 2015-16 Annual Report and Accounts of the Norfolk Pension Fund accounts be approved, and also endorsed the associated letter of representation.

6. Accounting adjustments, corrections and changes since the June draft

Material adjustments since the June draft accounts

6.1 There have been two material adjustment to the accounts since the draft Statement of Accounts dated 29 June. One adjustment has affected presentation within note 12: Property, Plant and Equipment, and the second has had the effect of re-allocating expenditure between categories within the CIES. Neither the Balance Sheet nor the MIRS have been affected by these adjustments.

6.2 The first adjustment affected only note 12: Property, Plant and Equipment. In the draft statement of accounts, all additions were routed through the “assets under construction” line. After discussion with Ernst & Young, it was agreed that for projects started and completed within the financial year additions would be allocated directly to the relevant class of asset rather than indirectly through the re-classification and transfers line.

The totals for each asset class and for total PPE remain unchanged.

6.3 The second adjustment relates to sponsored academies. The Council was responsible for the construction of the new buildings used by these academies. These buildings have been transferred to the Academies on long leases, and consequently the costs written out of the accounts. In the draft statement of accounts, the transaction was treated as revenue expenditure funded from capital under statute (“REFCUS”), which is the usual treatment for capital work on third party assets. After discussion with Ernst & Young, it was agreed that because the lease agreements with the Academies were short rather than long term at the time of the build, the transfer would be treated as a loss on disposal. This has had the effect of re-allocating the £52.468m “loss” in the CIES from a cost directly attributed to Children’s Services, to other operating expenditure.

The overall (Surplus)/Deficit on Provision of Services in the CIES remains unchanged. Related transfers between lines have occurred in note 33: Capital Expenditure and Capital Financing, the Capital adjustment account, and the Cash Flow statement, but in all cases the totals remain unchanged.

Neither the Balance Sheet nor the MIRS have been affected by this adjustment.

Non material adjustments and error corrections

6.4 Prior to and during the audit, officers and Ernst & Young have identified a number of adjustments to correct non-material errors or to enhance disclosures within the financial statements and associated notes.

6.5 With the agreement of the auditors, adjustments and corrections have been made where appropriate, and a number of disclosures added or enhanced. In addition there have been a number of amendments to improve the clarity and quality of information in the accounts. These amendments include a note concerning the impact of the EU referendum (note 6) and expanded Better Care Fund disclosures (note 26).

6.6 During the year it was necessary to reclassify capital grant income totalling £0.257m which was included in the Capital Grant Unapplied Account in the 2014-15 accounts. The draft accounts dated 29 June 2016 treated this adjustment as a re-classification of the opening balance. Since then, due to the non-material nature of the adjustment it has been accounted for in 2015-16. This has resulted in a small change to opening balances and total reported comprehensive income and expenditure since the June accounts. This adjustment had no impact on the revenue outturn position.

Unadjusted non-material item

6.7 There is one non-material item which has been identified by the external auditors, but which has not been adjusted. This item is the result of the way that the values of certain assets have been split into separate components for the purpose of calculating depreciation, and does not affect earmarked reserves or general balances.

The method applied has been consistent since “componentisation” was introduced in 2013-14, but has resulted in a cumulative under-statement of depreciation at 31 March 2016 of £1.210m.

While it would be possible to adjust the statement of accounts, the change affects a large number of underlying records. The resource required to update and reconcile these records for previous years would be considerable in relation to the non-material nature of the difference and the proportion of asset value represented.

A revised method of calculating depreciation on componentised assets has been agreed with the auditors, and will be implemented for 2016-17 and beyond.

Overall impact of adjustments since the June draft

6.8 There has been no impact on the net assets of the Council reported in the draft dated 29 June 2016, nor to the Council’s earmarked reserves or general balances.

6.9 Any material changes to the Pension Fund accounts since the draft accounts were approved for Audit by the Executive Director of Finance in June are reported to the Pension Committee.

7. Developments in local authority accounting

7.1 **Highways Network Asset (previously referred to as transport infrastructure assets)**

The latest HNA Code and associated guidance was issued at the end of August 2016, and will be used as a basis for including the Highways Network Asset in the Statement of Accounts. A previous Code was published in 2010 and revised in 2013.

The Code covers carriageways, footways and cycleways, highways structures, street lighting, traffic management systems and street furniture. The main accounting impact of the code is that these assets will be valued at depreciated replacement cost rather than the historic cost basis used under current guidance. Due to the long average asset lives in this area, there is likely to be a significant increase in accounting asset values.

Data and calculations performed in the Highways service will form the foundation of the figures that will appear in the accounts. Work has started with both internal and external auditors to evaluate the processes in place. Colleagues in the Highways service have been documenting systems and processes. When the recent technical guidance issued by CIPFA has been assessed by officers, the authority will be in a good position to extract the information required and create the systems required to generate the appropriate accounting entries.

The change comes into place for the 2016-17 accounts. At this time last year, it was envisaged that retrospective valuations as at 1 April 2015 would be required. However, this requirement has since been removed. The 2015-16 accounts contain a short note explaining the change, and an anticipated valuation of £13bn. This value is considerably higher than the cost-based £0.7bn currently carried in the accounts.

A previously reported estimate of £23bn for the anticipated valuation was based on provided rates for land values, which have since been significantly reduced by the central Highways Asset Management Financial Information Group (HAMFIG). Norfolk has not been unique in experiencing these variations, and believes that the higher figure was a one-off error.

7.2 **Faster closing**

The Accounts and Audit Regulations 2015 will significantly affect the speed at which local authority financial statements are produced, published and audited. From the 2017-18 financial year, draft accounts will have to be published by 31 May (currently 30 June) with the audit and final accounts deadline of 31 July (currently 30 September). This will clearly bring challenges, given the group accounting and pension fund accounts that are required at this council. In order to balance speed, accuracy and cost, the change is likely to affect accounting and external audit systems throughout the year as well as during the traditional financial close down period. Year-end close-down processes were brought forward in 2015-16 with a view to further streamlining and elements of a dry-run in 2016-17.

In order to achieve what will be an extremely tight timetable, the timing of Audit Committee meetings during 2018 and later years will be affected.