Leicester City Council

WARDS AFFECTED:
ALL WARDS (CORPORATE ISSUE)

AUDIT & RISK COMMITTEE 21st March 2018

Financial and Accounting Developments Update

Report of the Director of Finance

1. **Purpose of Report**

1.1. To provide the Committee with an update on key changes currently affecting the Council, and which may have an impact on the work of this committee.

2. **Summary**

2.1. The report will include an update to the committee on the following areas:

- Personal Service Companies/ IR35
- Markets in Financial Instruments Directive (MiFID)
- Base Rate Rises
- Faster Closedown
- Minimum Revenue Provision

3. **Recommendations**

The Committee is recommended to:

3.1. Receive the report and note its contents;
3.2. Make any recommendations or comments it sees fit, either to the Executive or Director of Finance

4. **Personal Service Companies**

4.1. New tax rules have applied to the engagement of temporary staff since 6 April 2017 (IR35). In particular this concerns workers engaged via their own limited company, so-called 'personal service companies'. Such companies are seen as promoting unfair tax avoidance, and some employers have facilitated the use of such companies (the Council has not). When a staff member is to all intents and purposes an employee, the rules require employers to deduct and pay to HMRC the same amount of income tax as if the staff member was an actual employee. Corporate procedures have been put in place to ensure the Council is not inadvertently caught out.

4.2. The Council has engaged a trusted employment agency for the provision of temporary staff. This company is responsible for accounting for tax to HMRC, and these arrangements cater for the majority of temporary staff appointments. In a minority of cases this will not meet business needs (for example a specialist appointment) and in such cases an assessment is made to determine whether the IR35 tax rules apply and, if so, to make the necessary deductions.

5. MiFID

5.1. MiFID II (the Markets in Financial Instruments Directive) is legislation for the regulation of investment services within Europe. MiFID replaces earlier legislation. It reflects both changes that have taken place in financial services and markets since the earlier legislation and concerns raised as a consequence of the financial crisis of 2008. Taken as a whole, the changes will substantially affect the providers of a very wide range of financial services and investment products.

5.2. The impact on the Council, however, will be limited. The main administrative impact has been that it has needed to obtain a registration number and to opt to be treated as a professional investor (as opposed to a retail investor). If the Council did not do this it could not invest in certain investment products, most noticeably money market funds (which are low risk investments, essentially “unit trusts” investing in a diversified pool of investments of high credit worthiness such as deposits with banks). To be treated as professional investor the Council must employ staff with relevant knowledge and experience, and the new rules may penalise smaller authorities.

6. Base Rate Rises

6.1. The Monetary Policy Committee (MPC) of the Bank of England increased Bank Base Rate in November 2017 to 0.5%. The bank has previously suggested that further increases would be gradual and limited. The bank has subsequently raised expectations that rate rises would be both sooner and to a higher level because of inflationary pressures. Our treasury advisors, Arlingclose, see base rates rising twice in 2018, then once more in the first half of 2019 and ending 2018/19 at a rate of 1.0%. This outlook is a marked change from that seen in January at which time our advisors saw interest rates remaining at 0.5% for an extended period (a view that reflected the stance of the MPC).

6.2. The main financial impact of changes to base rates is on the interest earned on investments, and the budget assumes that investment returns will average 0.4%. The impact of any change will not be immediate as significant parts of the Council’s investments are at fixed rates for periods of up to one year or more. If the most recent Arlingclose forecast is correct, then base rates might average 0.75% in 2018/19 and interest earned might be around £500,000 higher when we come to prepare the budget for 2019/20. However, forecasts of future interest rates are of course just forecasts, and may easily fail to materialise.

6.3. The changed outlook will feature in future treasury strategies.

7. Faster Closedown

7.1. The Council has a statutory requirement to produce a statement of accounts on an annual basis, the purpose being to show the financial position of the Council at 31st March. In previous years the Council has been required to publish a draft set of accounts by the 30th June and an audited set for the 30th September. For this financial year the date has been bought forward, with the draft accounts being required to be published for the 31st May and an audited set of accounts to be approved by the 31st July 2018.

7.2. This is going to be a challenge to the Council. To assist the Finance team in achieving this we have done the following in preparation:

- Early engagement with third parties including valuers & external auditors
- Better use of financial systems
- Review of materiality thresholds
- Use of estimates
- Review of the notes in the accounts

7.3. Even with the changes above it will still be difficult to achieve the early statutory deadline without the support of the whole organisation, the Senior Management Team and the Audit & Risk Committee.

7.4 For the committee, it means a draft set of accounts will be circulated at the end of May, to enable committee members to review them; with a final set being sent out shortly before the July meeting. The July meeting will then be when the accounts are signed off by the committee.

8. Minimum Revenue Provision

8.1 The Council is required to set aside money each year for the repayment of debt which has been raised to pay for capital expenditure in the past. This is known as minimum revenue provision (MRP)

8.2 The Government used to support borrowing through Revenue Support Grant, but no longer does so, choosing instead to give one off grants for new capital expenditure. Consequently, most of the debt we are repaying is historic. MRP is still significant, however (amounting to £14m in 2017/18).

8.3 The Government issues statutory guidance on how MRP should be calculated, and the policies councils can adopt. This guidance has recently been revised, in large part over concerns that some councils were retrospectively changing their policies and (in effect) borrowing money to avoid cuts.

8.4 The Council changed its policy in 2015/16, but this was not made retrospective. The impact of Government changes will not be significant, but the budget for 2019/20 will need to be more explicit about certain aspects of our policy, particularly where more money has been set aside than our policies required (in practice, recent Council budgets continued to set aside money to repay debt at the amount required prior to the policy change, in order to ensure that we don’t slow down debt repayment until Government cuts force us to do so).

9. Financial Implications

9.1. There are no direct financial implications arising from this report.

10. Legal Implications

10.1 There are no direct legal implications arising to this report.

11. Other Implications

OTHER IMPLICATIONS	YES/NO	PARAGRAPH REFERRED
Equal Opportunities	No	
Policy	No	
Sustainable and Environmental	No	
Crime and Disorder	No	
Human Rights / People on low incomes	No	
Corporate Parenting	No	
Health Inequalities Impact	No	

12. Consultations

Not applicable

13. Author

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