

# Crawley Borough Council

## Report to Audit Committee

20 March 2023

### IFRS 16: Explanation and Impact

Report of the Head of Corporate Finance – FIN/617

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#### **1. Purpose**

- 1.1 The purpose of this report is to explain the impact of IFRS 16 Leases on the Council.

#### **2. Recommendations**

- 2.1. That the Committee notes this report.

#### **3. Reasons for the Recommendations**

- 3.1. The Code of Practice on Local Authority Accounting mandates the adoption of IFRS 16 from 1 April 2024. This has been postponed a number of times: the latest followed an emergency consultation on deferring implementation until 1 April 2024 in an attempt to alleviate current delays to the publication of audited financial statements. The proposed deferral was approved but allowed early adoption from 1 April 2022 or 1 April 2023. The Council elected to adopt from 1 April 2022.

#### **4. Background**

- 4.1. The adoption of IFRS 16 will be a change in accounting policy for the 2022/23 financial statements. The previous accounting standard was IAS 17.
- 4.2. Traditionally there was a distinction between finance leases and operating leases. Finance leases were accounted for as acquisitions (with the asset on the balance sheet, together with a liability to pay for the asset acquired). In contrast, operating leases were treated as 'pay as you go' arrangements with rentals expensed in the year they are paid. IFRS 16 removes this distinction.

## 5. Planning for IFRS 16

- 5.1. Work on IFRS commenced before the start of the 2022/23 financial year as any impacts needed to be built into the Budget and Treasury Management Strategy. Identification of leases involved reviewing the financial records and through discussions with service departments. All leases had to be identified, even if they were for a peppercorn rent or hidden within a service contract.
- 5.2. Once identified, the leases were assessed against accounting policy criteria – short-term leases (lease terms of 12 months or less) were outside the scope, as were leases with underlying assets of low value (judged to be under £10,000).

## 6. Impact of IFRS 16

- 6.1. Two qualifying leases were identified with a combined annual rental value of £13,601. IFRS 16 would then bring these assets onto the balance sheet with a corresponding lease liability. In the Comprehensive Income and Expenditure Statement, the annual rental is replaced with depreciation (and statutory reversal), a minimum revenue provision (MRP) and an interest expense. The following table shows the changes to the 2022/23 accounts:

	Before IFRS 16 £	After IFRS 16 £
<u>Comprehensive Income and Expenditure Statement</u>		
Operating Leases in Net Cost of Services	13,601	-
Depreciation in Net Cost of Services		12,901
Statutory Reversal of Depreciation		(12,901)
MRP (within Financing and Investments I&E)		12,901
Interest (within Financing and Investments I&E)		700
<b>Total impact on General Fund Balance</b>	<b>13,601</b>	<b>13,601</b>
<u>Balance Sheet at 1 April 2022</u>		
Property, Plant and Equipment		44,336
Short Term Borrowing		(13,395)
Long Term Borrowing		(30,941)
<b>Total impact on Balance Sheet</b>	<b>0</b>	<b>0</b>

- 6.2. As these leases bring borrowing onto the Balance Sheet, the prudential and treasury management indicators in the Treasury Management Strategy for 2022/23 had to be adjusted. These included the Capital Financing Requirement (CFR), the MRP, the Authorised Limit and the Operational Limit for Debt.

## 7. Background Papers

- Code of Practice on Local Authority Accounting in the UK 2022/2023 (Chartered Institute of Public Finance and Accountancy)
- IFRS 16 Leases: An Early Guide for Local Authority Practitioners (Chartered Institute of Public Finance and Accountancy)
- [CIPFA Bulletin 10 – Closure of the 2021/22 Financial Statements](#)

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