

AUDIT COMMITTEE

28 March 2018

Statement of Accounts - Group Boundary Review

Report of Alison Elsdon Director of Finance

Cabinet Member: Councillor Nicholas Oliver – Portfolio Holder for Corporate Services and Cabinet Secretary

Purpose of Report

The purpose of this report is to provide members of the Audit Committee with details of the boundary review which has been undertaken to determine whether or not Arch and Active Northumberland's financial statements should be consolidated with the Council's Statement of Accounts for the financial year ended 31 March 2018 and future years.

Recommendations

It is recommended that the members of the Audit Committee:

1. note the contents of the report;
2. agree that Arch's financial statements should be consolidated with the Council's Statement of Accounts for the financial year ended 31 March 2018 and future years;
3. agree that Active Northumberland's financial statements should not be consolidated with the Council's Statement of Accounts for the financial year ended 31 March 2018 and future years.

Link to the Corporate Plan

This report is consistent with the priorities in the Corporate Plan 2018 to 2021 "A Council that works for everyone".

Key Issues

The Council has undertaken an assessment (Boundary Review) in advance of producing its 2017-18 Statement of Accounts to ascertain if there are any relationships which fall under the definition of the Code and should therefore be consolidated into the group position. The outcome of the review is detailed within the report.

Background

The Code of Practice on Local Authority Accounting in the United Kingdom 2014/15 “the Code” is the first to adopt the group accounting principles. Paragraph 9.1.1.6 of the Code sets out a requirement to prepare group accounts where the authority has interests in subsidiaries, associates and/or joint ventures, subject to consideration of materiality. The implications of this requirement are set out in the table below:

	Subsidiaries	Associates	Joint Ventures
Definition	<p>Entities where the authority is exposed to (or has rights to) variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.</p> <p>The nature of the involvement and the returns is not restricted in the Code. Control might normally be established where an authority owns a majority of shares in a company that pays dividends. However, all relationships need to be considered where there might be variable returns for an authority and it has power that might be exercised to increase the returns or minimise reductions(in returns).</p> <p>If two or more entities have rights that give a unilateral ability to direct different activities that affect returns, control is attributed to the entity that can direct the activities that most significantly affect returns.</p>	<p>Entities for which the authority is an investor that has significant influence.</p> <p>Significant influence is the power to participate in the financial and operating policy decisions of the investee (stopping short of control or joint control). It is presumed that holding more than 20% of the voting power of an investee (either directly or indirectly) brings significant influence, but this presumption can be rebutted. It is possible for significant influence to be exerted where an investor has less than 20% of the voting power or where another party has majority ownership.</p> <p>An authority can have an associate relationship with an entity that is a joint venture under the control of other investors.</p>	<p>Arrangements under which two or more parties have contractually agreed to share control, such that decisions about activities that significantly affect returns require the unanimous consent of the parties sharing control, and joint venturers have rights to the net assets of the arrangement.</p>

ARCH

1. Arch is a wholly owned subsidiary of the Council. Therefore, under “the code”, Arch must continue to be consolidated into the group structure as a subsidiary. The group results are presented in the Council’s annual financial statements along with the Council’s own single entity statements.
2. In line with “the Code” Arch is consolidated with the Council on a full line by line basis. Inter company transactions are removed on consolidation and the accounting policies of Arch are aligned with those of the Council. Only those areas that are considered to be material, i.e. where the group position is materially different from the single entity, will be shown within the Council’s Statement of Accounts from 2017-18 onwards.

ACTIVE NORTHUMBERLAND

3. The Code does not make any specific comments on the consolidation of charitable organisations in local authority financial statements; therefore, local authorities are required to follow the requirements of IFRS 10 in the Code; and, where material, consolidate any charitable trust where an authority meets the three criteria for control identified in the table above.
4. The following factors should be considered when determining whether Active Northumberland should be consolidated with the Council’s accounts:

The purpose and design of the charitable trust

5. Active Northumberland’s Memorandum and Articles of Association were amended in November 2017 to change the membership of the charity to both organisation members and individual members. Previously members consisted of a suitably qualified senior representative from the following 5 organisations:
 - Northumberland County Council
 - Northumberland National Park Authority
 - Northumbrian Water Limited
 - Arch
 - Northumbria Healthcare NHS Trust
6. The change made to the Memorandum and Articles of Association allowed for the Charity to appoint up to five individual members, in addition to the five organisation members. Active Northumberland is currently recruiting to appoint the additional 5 individual members, one of which was appointed in March 2018.

7. It should be considered whether the Council has voting rights on the Board of Trustees and if the Council is able to exercise the majority of voting power over the Trust. With the 5 organisation members the Council has 40% voting power with the representatives from Northumberland County Council and Arch. However when all 10 Members are appointed this will reduce the voting power of the authority to 20%. It should be noted that despite Arch being wholly owned by the Council, the Council does not actually have any influence over the Arch vote.
8. The Council is not involved with the recruitment of Active Northumberland Board members. The Memorandum and Articles of Association allow the Active Northumberland Board the ability to appoint and remove Board members.
9. Board members are required to adhere to the Code of Conduct and submit declarations of interest. In instances where the NCC and Arch members have an interest they leave the meeting while any discussion takes place or decision is made by the remaining members. This can be evidenced in the Board minutes.

What the relevant activities of the charitable trust are and how decisions about those activities are made

10. During the financial year 2017-18 Active Northumberland has provided Leisure Services, Northumberland Sport and Sports Development. Some of the libraries and tourist information centres have been run by Active Northumberland and some have been run by the Council. From 1 April 2018 Active Northumberland will only be commissioned to provide Leisure Services, with all of the remaining services transferring back to the Council. Whilst the Council determines what activities it requires Active Northumberland to deliver on its behalf, e.g. leisure etc; the Council is not involved operationally with how those services are delivered and this is a matter for the Active Northumberland Board. This can be evidenced in a strictly confidential letter dated 27 February 2018 from the Council's Chief Executive to the Chair of Active Northumberland. The Council has recently communicated with the Active Northumberland Board to clearly set out their role.

Whether the rights of the authority give it the current ability to direct the relevant activities of the charitable trust

11. As described in point 10 operational decisions are taken by the Board and not the Council. This can be evidenced in the Board minutes.

Whether the authority is exposed, or has rights, to variable returns from its involvement with the charitable trust

12. No returns are made from Active Northumberland to the Council. All balances are retained by Active Northumberland, and it is their decision how those reserves are used. In the event that the charity dissolves then the Board will decide what it does with the funds.

13. During 2017-18 Active Northumberland has provided a library service, which is a statutory service for local authorities. Some of the libraries were run by the Council. From 1 April 2018 Active Northumberland will provide Leisure Services only; this is not a statutory function for Local Authorities.

Whether the authority has the ability to use its power over the charitable trust to affect the amount of the returns to the authority

14. No returns are made from Active Northumberland to the Council. The Council does not exercise control or power over the level of services that Active Northumberland provide. The Board determines the level of service provided.

Other factors

15. The budget for Active Northumberland is funded predominantly by service income; as well as a charitable donation from Arch; and, a management fee from the Council. The proportion of income which is service income in 2017-18 is 88% and the Arch donation and management fee makes up the remaining 12%. In 2018-19 the proportion of income which is service income is 84% and the Arch donation and management fee is 16%.
16. An independent strategic review of Active Northumberland commenced in May 2017 and was presented to Audit Committee on 6 December 2017 and County Council at its meeting on 21 February 2018. Following that, the Board has drafted an implementation plan in respect of the recommendations made in the strategic review. This will be monitored and reviewed by the Board. The Board has voluntarily agreed that this will be presented to the Council's Audit Committee as required as an assurance mechanism to ensure that the Council's Management Fee is used appropriately.
17. Going forward there will be a formally documented commissioner/provider contractual relationship between the Council and Active Northumberland for the provision of Leisure Services only.
18. A number of Service Level Agreements have been drafted for support services which are currently provided by the Council to Active Northumberland. It is intended that these will be agreed and be effective from 1 April 2018.
19. A facilities review has commenced during 2017-18, with Active Northumberland staff presenting reports to the Board in relation to Active Northumberland's portfolio. The reports advise the Board on issues such as annual visits; impact on staff; political, economic, social, legal, and financial implications; as well as the options available for each facility. The Board considers the facilities review on a monthly basis and is actively making decisions around the future facilities to be included in the portfolio. This can be demonstrated in the Board minutes.

20. Active Northumberland will develop a business plan which includes long term financial model. The 2018-19 budget was agreed by the Board at the meeting on 15 March 2018 and the Board has agreed to develop a 3 year financial plan.
21. There has always been a management agreement. However, it was not previously signed. Going forward it is intended to have a formally documented commissioner/provider contractual relationship between the Council and Active Northumberland.

Conclusion

22. It has been demonstrated that the Council does not have significant influence or control over Active Northumberland. This can be evidenced through the Code of Conduct, Memorandum and Articles of Association, declaration of interests and minutes of Board meetings. It is concluded that Active Northumberland falls outside of the scope of group accounts and should not be consolidated with Northumberland County Council's Statement of Accounts for the financial year ended 31 March 2018 and future years.

IMPLICATIONS ARISING OUT OF THE REPORT

Policy:	The CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2017/18. The CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 guidance notes for practitioners. The CIPFA accounting for collaboration in Local Government.
Finance and value for money:	This report has no financial implications for the Council.
Human Resources:	Not applicable
Property:	Not applicable
Equalities: (Impact Assessment attached) Yes No N/A	Not applicable
Risk Assessment:	Not applicable
Carbon Reduction:	Not applicable
Crime & Disorder:	Not applicable
Customer Considerations:	Not applicable
Consultation:	Active Northumberland Board
Wards:	All wards in Northumberland

BACKGROUND PAPERS

The CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2017/18.

The CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 guidance notes for practitioners.

The CIPFA accounting for collaboration in Local Government.

Report sign off:

Finance	Alan Mason
Monitoring Officer/Legal	Liam Henry
Human Resources	Not applicable
Procurement	Not applicable
IT	Not applicable
Chief Executive	Daljit Lally
Portfolio Holder	Nick Oliver

Report Authors: Suzanne Dent & Andy Stewart – Finance Manager
(01670) 625515:suzanne.dent@northumberland.gov.uk
(01670) 622161:andy.stewart@northumberland.gov.uk