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The Scottish Government

Local Government Finance Circular No. 7/2011
By email

To: Local Authority Directors of Finance

Copy to: Audit Scotland
COSLA

Our ref: B4576550
30 March 2011

Dear Director of Finance,

ACCOUNTING FOR INVESTMENT PROPERTIES

A number of authorities have queried whether investment properties continue to be included within the capital control regime and whether gains and losses arising on the annual revaluation are a charge to the General Fund.

This circular clarifies the statutory accounting requirements for investment properties.

This circular is also available through the Local Government section of the Scottish Government website at:
http://www.scotland.gov.uk/Topics/Government/local-government/17999/LAacc/LAaccguid

If you have any questions, please do not hesitate to contact me.

Yours faithfully,

Hazel Black

Hazel Black
Head of Local Authority Accounting
Local Government Division

ACCOUNTING FOR INVESTMENT PROPERTIES

Scottish Government

Contents

Part 1 of this document gives informal advice only and is not part of the guidance itself, which is contained in Part 2.

PART 1 – BACKGROUND AND COMMENTARY

Background

1. Section 12 of the Local Government in Scotland Act 2003 places a duty on a local authority to observe proper accounting practices. Section 99 of the Local Government (Scotland) Act 1973 (as amended) places a duty on auditors, in auditing the accounts of the local authority, to satisfy themselves that proper accounting practices have been observed in the preparation of those accounts.

2. Section 12 of the Local Government in Scotland Act 2003 identifies that proper accounting practices may be:

a) those that the local authority is required to observe by virtue of any enactment
b) those which have been specified in guidance issued for the purposes of section 12 of the 2003 Act and section 99 of the 1973 Act by the Scottish Ministers
c) those which, whether by reference to any generally recognised, published code or otherwise, are regarded as proper accounting practices to be observed in the preparation and publication of accounts of local authorities.

In the event of any conflict between the three the legislation ranks them in order from a to c, with a taking precedence over b and c, and b taking precedence over c.

3. The Code of Practice on Local Authority Accounting in the United Kingdom (the Code) is recognised as setting out proper accounting practices for local authorities. From 1 April 2010, the Code adopts International Financial Reporting Standards (IFRS), including IAS 40 (Investment Property). The Code provides guidance on accounting for investment property, adapted for the public sector, which reflects IPSAS 16 *Investment Property* when defining investment property for the public sector.

Investment property

4. IPSAS 16 *Investment Property* includes a public sector interpretation of the definition of investment property. Under this definition, an investment property is one that is used solely to earn rentals or for capital appreciation or both. Property that is used to facilitate the delivery of services or for the production of goods and services

as well as to earn rentals or for capital appreciation does not meet the definition of an investment property under IPSAS 16, and is accounted for as property, plant and equipment. The Code adopts this definition of investment property.

5. *The Local Government Investments (Scotland) Regulations 2010* (2010 No.122), which apply from 1 April 2010 include investment properties as an investment. As a general principle local authorities may not borrow to invest.

Non current assets – accounting and policy

6. The Code sets out proper accounting practice for the recognition, measurement, depreciation and derecognition of property plant or equipment. The Code sets out the charges which are to be 'recognised in Surplus or Deficit on the Provision of Services for the period..' through the Comprehensive Income and Expenditure Statement. In the absence of any statutory accounting requirements these would be charges to the General Fund.

7. The Code sets out proper accounting practice for the recognition, measurement, transfer and disposal of investment property. The Code sets out the charges which are to be 'recognised in Surplus or Deficit on the Provision of Services for the period..' through the Comprehensive Income and Expenditure Statement. In the absence of any statutory accounting requirements these would be charges to the General Fund.

8. Statute and statutory guidance restrict the use of capital receipts and the charges that may be made to the General Fund. Depreciation, gains and losses on revaluation or derecognition where charged to Surplus or deficit on the provision of services are not proper charges to the General Fund. Statutory charges for the repayment of debt are proper charges to the General Fund. When an asset is sold or disposed the receipt from the disposal (capital receipt) may only be used for the redemption of debt or for capital expenditure.

Investment property - policy

9. With the passing of the investment regulations in 2010, and the identification that investment properties are held for investment rather than for the provision of services, it was necessary to review whether investment properties should continue to be covered by the policy for non-current assets set out above.

10. The Capital Finance Working Group (paper CFWG paper 36) considered the matter at its meeting 25 August 2010. The group concluded that it may be appropriate for gains and losses arising from the annual valuation of investment property to be a charge to the General Fund (credit or debit). However, as IFRS was only just being introduced it was likely that it will take a couple of years for there to be consistency of reporting and accounting across authorities for investment properties. As such it was considered appropriate that statutory intervention should continue in the meantime.

11. A more detailed policy review is planned for investment property during 2011-12 which will be taken forward through the Capital Finance Working Group.

This will consider the extent to which the acquisition or construction of investment property is properly part of the statutory capital regime.

12. This statutory guidance sets out the statutory accounting arrangements for investment property which will apply until the more detailed policy review is completed.

Scottish Government
Local Government Division
30 March 2011

[PART 2]

ACCOUNTING FOR INVESTMENT PROPERTIES

Issued by Scottish Ministers under section 12(2)(b) of the Local Government in Scotland Act 2003

DEFINITIONS

1. ***Local Authority*** means a council constituted under section 2 of the Local Government etc. (Scotland) Act 1994. It includes a fire and rescue authority or a fire and rescue board as defined by the Fire (Scotland) Act 2005, regional transport partnerships and other bodies as set out in section 106 of the Local Government (Scotland) Act 1973.

2. ***Financial year*** is a year which commences 1 April and ends 31 March.

3. ***Proper accounting practices*** are as defined in section 12 of the Local Government in Scotland Act 2003.

APPLICATION

4. This statutory guidance applies from the financial year commencing 1 April 2010.

ACCOUNTING FOR INVESTMENT PROPERTIES

5. Local authorities shall account for investment property in accordance with proper accounting practices before applying these statutory accounting requirements.

6. A gain or loss arising from a change in the fair value of investment property is not a proper charge to the General Fund. Such amounts shall be transferred from the General Fund to the Capital Adjustment Account and reported in the Movement in Reserves Statement.

7. The gain or loss arising on derecognition of an investment property is not a proper charge to the General Fund. The disposal proceeds (net of any disposal costs) are to be treated as a capital receipt. The carrying amount of the investment property shall be charged to the Capital Adjustment Account. These entries will be reflected in the Movement in Reserves Statement.

8. Any impairment of an investment property shall not be a charge to the General Fund. Compensation from third parties for investment properties that becomes impaired, lost or is given up is not income to the General Fund. Such amounts shall be transferred from the General Fund to the Capital Adjustment Account and reported in the Movement in Reserves Statement.

9. Loans Fund advances made to finance Investment property shall be repaid by way of a charge to the General Fund (the Statutory Repayment of Debt). The repayment period (fixed period) is as determined by statute (see in particular paragraphs 17 and 31 of Schedule 3 of the Local Government (Scotland) Act 1973). Finance Circular 29/1975 sets out the fixed periods. This Circular is available from the Scottish Government website at:
http://www.scotland.gov.uk/Topics/Government/local-government/17999/FinCirc29-75

10. Investment properties financed by a finance lease shall be repaid by way of a charge to the General Fund (the Statutory Repayment of Debt). Finance Circular 4/2010 sets out the statutory accounting requirements. This Circular is available from the Scottish Government website at:
http://www.scotland.gov.uk/Topics/Government/local-government/17999/FinCirc4-2010

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