

Appendix 1

CITY OF
WOLVERHAMPTON
COUNCIL

Accounting Estimates

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Introduction

- Financial statements which include comprehensive income and expenditure, balance sheet and cash flow statements, require proper use of accounting theories and techniques.
- **Accounting policies** and **accounting estimates** serve this purpose by ensuring that the accounting data used is valid (in terms of regulatory requirements and financial reporting accuracy).
- **Accounting policies** are standards, rules, and principles used by the Council to prepare its financial statements, e.g. the method the Council uses to value its inventories.
- **Accounting estimates** are required when such clear cut standards are not available, requiring the Council to make an informed judgement, e.g. the use of certain assumptions.

Common areas

- Valuation, depreciation and impairment of property, plant and equipment
- Defined benefit pension liability
- Provisions
- Expected credit loss provisions
- Accruals

Property, plant and equipment

Valuers in attendance to discuss:

- JLL
 - Council dwellings

- Bruton Knowles
 - Other land and buildings
 - Investment properties
 - Surplus assets

Defined benefit pension liability

Estimates:

- Asset returns
- Mortality assumption
- Financial assumptions
 - Inflation expectations
 - Salary increases
 - Discount rate

The Director of Pensions will attend the next Committee to discuss in detail

Provisions

- A best estimate of the amounts that the Council would rationally pay to settle the obligations at the balance sheet date or to transfer them to a third party.
- In reaching these best estimates, the Council take into account the risks and uncertainties that surround the underlying events.
- Examples:
 - Insurance
 - Termination benefits, e.g. voluntary redundancy
 - Outstanding NNDR appeals
 - Court cases

Expected credit loss provisions

- Examples:
 - Short-term loans
 - Financial guarantees
 - Allowances for receivables
- Factors considered:
 - Business failure scores from Creditsafe (showing probability of failure)
 - Repayment profile
 - Knowledge of the customer's finances: cash flow, profits, funding
 - Knowledge of wider economy and its impact on the customer

Accruals

- Expenses or income that are recognised when they are incurred but not yet paid/received, for example a February utility bill paid in March.
- Accrual accounting requires revenues and expenses to be recorded in the accounting period that they are incurred.
- Examples:
 - Utilities
 - Salaries
 - Goods and services
 - Other expenses, e.g. fees
 - Insurance expenses

Auditing standard ISA 540 – auditing accounting estimates and related disclosures

- Increasing focus from regulators and other stakeholders on estimates (especially those which are complex or require significant judgement)
- ISA 540 has been enhanced to place increasing demands on auditors to understand and assess an entity's internal controls over accounting estimates.

Forming the accounting estimate

We need to:

- Identify the methods, assumptions and source data used for each material accounting estimate and the need for any changes to these
- Understand the degree of estimation uncertainty related to each accounting estimate
- Address the estimation uncertainty when selecting the estimate

Internal controls over accounting estimates

We need to demonstrate:

- The nature and extent of oversight and governance
- How management identifies the need for and applies specialised skills
- How management identifies and addresses risks
- The information system and controls applied by management
- Control activities
- How management reviews the outcomes of previous estimates
- The role of those charged with governance.

Accounting Estimate Management Summary

The “**Accounting Estimate Management Summary**” in agenda item 8 sets out:

- how we meet this criteria and;
- continuing work we are undertaking to further enhance controls.

Questions

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