



Local Government Finance Circular No. 5/2013  
Directors of Finance of Scottish Local Authorities



Our ref: A6189205

19 June 2013

Dear Director of Finance,

## INSURANCE RECEIPTS – NON STATUTORY GUIDANCE 2012-13

### Background

- Reflecting on the capital control framework in place for local government the Capital Finance Working Group (CFWG) was requested by the Local Authority (Scotland) Accounts Advisory Committee (LASAAC) to consider whether an insurance receipt should be treated as a capital receipt.
- The CFWG considered the following information:

#### **Capital receipts - definition**

- .1 In Scotland there is no legislative definition of a capital receipt.
- .2 In England, Section 9(1) of the Local Government Act 2003 provides a basic definition of a capital receipt:  
“...a sum received by the authority in respect of the disposal by it of an interest in a capital asset.” A capital asset is defined by section 9(2) as “An asset is a capital asset...if, at the time of the disposal, expenditure on the acquisition of the asset would be capital expenditure.”
- .3 CIPFA’s publication, a “*Practitioners’ Guide to Capital Finance in Local Government*” (2008) identifies that this definition is based on a mirror principle. If an



authority enters into a transaction where it will receive income for a disposal, it has to imagine that it is the other party to the transaction. If the acquisition of the interest would meet the statutory definition of capital expenditure it is a capital receipt.

.4 The CIPFA Guidance, in considering the legislation, notes that the definition is a precise one and no matter how big the sum received, it will not be a capital receipt unless it satisfies the terms of section 9. The guidance uses insurance as an example, and advises that insurance proceeds would only be a capital receipt if the settlement related specifically to the insurer purchasing the damaged asset from the authority.

.5 Applying this approach, an insurer may be considered to have purchased a vehicle but it is not so likely that an insurer would be considered to have purchase a damaged or destroyed building. It is probably more likely that the insurer is considered to have compensated the authority rather than have purchased the asset. The conclusion is that, applying this approach, the insurance receipt is not considered to be a capital receipt.

### ***Statutory accounting adjustments***

.6 Losses arising from impairments, or from the de-recognition of an asset, is not a charge to the General Fund. If the insurance receipt is a revenue receipt, a question arises as to whether the impairment, or loss arising, which is the subject of compensation income, should continue to be the subject of a statutory adjustment.

- The CFWG considered that the intended use of the insurance receipt was more important than its classification as a capital receipt or revenue compensation payment. The CFWG agreed that a local authority should act prudently in the use and application of an insurance receipt.

### **Prudent use of an insurance receipt**

- Where a non-current asset is damaged or destroyed and the local authority replaces or rebuilds the non-current asset it is considered prudent that the insurance receipt is used to fund any capital expenditure. Prudence in this regard extends beyond the strict application of an exact replacement or rebuild of an asset, and encompasses any capital expenditure to restore or continue service provision the subject of the insurance claim.
- Where a non-current asset is damaged or destroyed and the local authority does not replace or rebuild the non-current asset, it is for the local authority to determine what is prudent. In making such a determination a local authority is expected to consider whether there is any outstanding borrowing on the non-current asset and the long term capital investment plans of the local authority. The materiality of the insurance receipt should also be taken into account. If a local authority maintains a statutory Insurance Fund a prudent application of the receipt may be a transfer to the Insurance Fund.

## Proper accounting practice

- Proper accounting practice shall be applied to insurance receipts.
- Insurance receipts may not be carried directly to the statutory Insurance Fund. Any application of an insurance receipt must be in accordance with proper practices by way of a transfer from the General Fund.

I trust this guidance is helpful.

Yours faithfully

*Hazel Black*

### **Hazel Black**

Head of Local Authority Accounting  
Local Government Division