Materiality thresholds

Adoption of a materiality threshold for the Police and Crime Commissioner for Lincolnshire.

Financial statements should present a true and fair view. An item that is not material will not be relevant, cannot influence a user's decisions and need not be reported in the financial statements.

Hence, ignoring immaterial items can save time and allows users of the accounts to focus on the main issues. However, materiality is subjective and requires professional judgement. It is inappropriate to set a fixed monetary value without reference to the context of a transaction. Factors which may make even small values material include:

- related party transactions;
- a transaction which changes a surplus to a deficit, or vice versa;
- non compliance with laws or regulations;
- deterioration in relationships with key stakeholders.

The guidance notes to the Code expect practitioners to presume that the Code should be followed until it can be established that a less rigorous approach does not lead users to misread the financial statements. There will be examples where no simplification is acceptable, some of which are listed above. However, in many cases a more straightforward approach will be considered the most pragmatic method. In such cases, the authority should have a default assessment of materiality for its financial statements.

It is proposed that the PCC adopts 0.1% of gross revenue expenditure as its own prudent materiality level, i.e., £100k. This will be used to inform internal considerations about the application of policies and accounting standards where doing so will not misrepresent the authority's position. Note that, as per the Code, it is the collective impact of a group of transactions which should be borne in mind rather than using this level to ignore transactions below £100k.

Table 1: proposed materiality thresholds for 2012/13 accounts

Policy Area	Suggested de minimis	Rationale and Consequences
All areas where there is no risk of a misreading of the overall financial position	£100k	Based on 0.1% of gross revenue expenditure. The default position is that transactions below this materiality level will still be accounted for under the Code. Only when non financial factors or other policies are thought to be irrelevant will consideration be given to ignoring the requirements of the Code.
Fixed assets	Nil	The PCC will continue to have freedom to capitalise any assets lasting more than one year.
De minimis level for identifying components in asset register	£500k	Only components which have a material impact on depreciation should be recognised. This will only happen when components of significant value have a shorter life than the main building asset. More detail is given in the componentisation policy.
De minimis level for de-recognising assets when superseded by subsequent expenditure	£25k	Double counting could lead to an overstatement of assets in the balance sheet. More detail is given in the componentisation policy.
Recognition of finance leases	75% in NPV test	No reason to make this a higher figure as the accounting standards are moving towards recording of all leases as finance leases.
Inventories	£5k	Avoid counting high volume small value stocks such as stationery. Main stock balances are diesel, vehicle parts and stores balances.
Group accounts	£1m turnover of the group	The Audit Commission have a range of factors to inform our materiality level, but it is generally around 1% of our gross turnover. For us, this is around £1m and so this seems a suitable level to review our group boundary. This will not stop us reporting jointly controlled assets in our accounts for arrangements such as EMSOU.