[Date]

GOVERNMENT FINANCIAL REPORTING MANUAL (FReM) EXPOSURE DRAFT NO:

(13)02

EXPOSURE DRAFT OF PROPOSED

AMENDMENTS TO THE FReM

Application of IFRS 13 *Fair Value Measurement* for the public sector

Comments to be received by [Date]

HM TREASURY

GOVERNMENT FINANCIAL REPORTING TEAM
HM TREASURY

This exposure draft of proposed amendments to the Government Financial Reporting Manual is published by HM Treasury for comment only. The proposals may be modified in the light of comments received in this consultation process before being presented to the Financial Reporting Advisory Board for its approval. Final proposals approved by the Financial Reporting Advisory Board will be published as amendments to the FReM from the proposed effective date.

Comments on this exposure draft should be submitted in writing so as to be received by **[Date].** Respondents are asked to send their comments electronically to FReM.consultation@hmtreasury.gsi.gov.uk

All responses will be published on the gov.uk website unless the respondent requests confidentiality.

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PROPOSED AMENDMENTS TO THE GOVERNMENT FINANCIAL REPORTING MANUAL (FReM)

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Proposed amendments to the FReM

Introduction

The Government Financial Reporting team, HM Treasury, has published this exposure draft of proposed amendments to the Government Financial Reporting Manual (FReM) as part of its ongoing work in ensuring that the Manual reflects the latest developments in government financial reporting.

There have been two previous exposure drafts on the application of IFRS 13 for the public sector (exposure drafts (13)01 and (12)03). Each of these consultations has informed the development of financial reporting policy and HM Treasury's final proposals as set out in this exposure draft.

Structure of exposure draft

The exposure draft includes a section for each FReM chapter for which an amendment is proposed. Each section includes:

(a) An explanation of why the amendment is proposed;

(b) When necessary any specific additional questions unique to that proposed amendment;

(c) The paragraphs of the FReM chapter that are affected by the proposed amendment;

(d) The proposed effective date of each proposed amendment.

Invitation to comment

HM Treasury invites comments on the proposed amendments. It would particularly welcome responses to the questions set out below. Comments are most helpful if they:

(a) Respond to the question as stated;

(b) Indicate the specific paragraph or paragraphs to which they relate;

(c) Contain a clear rationale; and

(d) Describe any alternative HM Treasury should consider.

HM Treasury will consider all comments received in writing by [date]. In considering the comments, HM Treasury will base its conclusions on the merits of the arguments for and against each alternative, not on the number of responses supporting each alternative.

Executive Summary

1. This exposure draft seeks views on the proposed amendments to the FReM arising from the application of IFRS 13 *Fair Value Measurement* (IFRS 13). The effective date for the proposed FReM amendments is 1 April 2015.

2. IFRS 13 sets out the measurement and disclosure requirements for reporting entities, where an asset or liability is measured at fair value on the Statement of Financial Position.

3. The principles of IFRS 13 affect all reporting entities covered by the FReM. The FReM currently provides guidance on the valuation techniques that might be used to calculate fair value. IFRS 13 will redefine references to fair value in all IFRS's (save the scope exceptions as detailed in IFRS 13 paragraphs 5 to 8) and HM Treasury proposes that IFRS 13 is adopted in full.

4. This exposure draft considers the implications of introducing IFRS 13 specifically for the accounting for non-financial assets. IFRS 13 raises significant conceptual issues regarding the measurement of public sector assets. The fundamental issue is that IFRS 13 defines fair value as the 'exit price' for an asset or liability. The standard then establishes principles for calculating an exit price, and the associated disclosure framework. The principle of exit price is based on the concept that assets are held to generate future inflows of economic benefit.

5. Public sector entities hold most classes of assets to deliver public services, rather than to realise future cash flows. This exposure draft explores how IFRS 13 may be applied in the public sector context by distinguishing between those assets which are held for their service potential (i.e. operational assets) and those that are held for financial return or are surplus. HM Treasury proposes that only assets in this second group are valued at fair value in accordance with IFRS 13, and then only if the entity holding those assets is not restricted from accessing the market.

6. This exposure draft seeks your views on the conclusions reached, and on the proposed amendments to the FReM arising from these conclusions.

General Questions

Question 1

Do you agree with the proposed amendments to the accounting for non-financial assets in the FReM to reflect the principles of IFRS 13? If so, why? If not, why not, and what alternatives do you propose?

Question 2

Do you agree with the proposed adaptation of IAS 16 for the public sector? If so, why? If not, why not, and what alternatives do you propose? Please provide supporting details (e.g. class, current use) of non-financial property assets that may fall within the scope of the adaptation.

Question 3

Do you agree with the proposed adaptation of IAS 38 for the public sector? If so, why? If not, why not, and what alternatives do you propose?

Question 4

The disclosure requirements of the standard are laid out in IFRS 13 paragraphs 91 to 99, and are discussed from paragraph 24 of this exposure draft. Do you have any points to make about the disclosure requirements from a public sector perspective and the implications for reporting entities?

Question 5

Application of IFRS 13 may result in new valuation profiles for certain classes of non-operational and surplus assets. Do you have any further points to make about the introduction of IFRS 13 and the implications for reporting entities?

Question 6

Do you agree with the proposed effective date for the proposed amendments? If so, why? If not, why not and what alternative do you propose?

Principles of IFRS 13 *Fair Value Measurement*

1. In May 2011 the IASB issued IFRS 13, setting out the principles for the calculation and disclosure of fair value in financial statements. The standard was adopted by the EU in December 2012 with an effective date of 1 January 2013. The Government's financial reporting policy is to apply IFRS that have been adopted by the EU.

2. Some IFRSs require or permit entities to measure or disclose the fair value of assets, liabilities or their own equity instruments. As IFRSs have been developed over many years, the requirements for measuring fair value and for disclosing information about fair value measurements have been dispersed and "did not articulate a clear measurement or disclosure objective" (IFRS 13, paragraph IN5).

3. IFRS 13 paragraph 9 now defines fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

4. This definition equates fair value with an exit price and is defined from a market perspective, which requires consideration of a range of new factors (e.g. "highest and best use" of an asset by market participants, as per IFRS 13 paragraph 27). In a general sense, IFRS 13 promotes a value that reflects a theoretical market price as much as possible and will attempt to simulate this amount where a ready price is not available.

5. IFRS 13 paragraph 16 states that "a fair value measurement assumes that the transaction to sell the asset or transfer the liability takes place either:

- in the principal market for the asset or liability; or
- in the absence of the principal market, in the most advantageous market for the asset or liability."

6. Further to this, the reference to an orderly transaction requires a valuer to suppose that the transaction is not forced (i.e. there is no element of financial distress affecting the sale or transfer). For an orderly transaction to occur under the standard IFRS 13 paragraph 19 provides that "the entity must have access to the principal (or most advantageous) market at the measurement date". It should be noted that the standard disregards an entity's intent to sell an asset or transfer a liability as a factor at the measurement date.

7. Conceptually, IFRS's are written primarily for profit-making organisations. Consequently the principles consider the information requirements of investors on future economic benefits, which are intended to represent the future cash flows associated with assets and liabilities. In establishing a theoretical price for the item, the seller would take into account the fact that a buyer would pay according to the economic benefits expected to be gained in the use of the asset – that is, the asset would be valued as if it were employed in its "highest and best use", even if that is not its current use and even when an asset/liability is held for purposes other than the pursuit or economic goals (i.e. as the public sector holds many assets/liabilities in the course of providing public services).

8. Highest and best use contributes to the maximisation of the value of an asset based on the different physically possible, legal permissible and financially feasible uses that market participants could employ to generate economic benefits from the item undergoing valuation. Financially feasible supports the assumption that a market participant would factor conversion costs into a price when highest and best use is not existing use or supported by the asset's current configuration.

9. The standard also requires an entity to include appropriate disclosures supporting fair value calculations – in particular where fair value has been calculated using valuation techniques that are not derived from market information on exit prices (for example where such information is not available).

Applicability of IFRS 13 for Public Sector Reporting Entities

Principles

10. HM Treasury published Exposure Draft 13(01) on IFRS 13 in July 2013 which proposed that IFRS 13 should be adapted such that it did not apply to assets which were subject to restrictions on geographic location. After considering the responses to the exposure draft, the Treasury put forward a recommendation to the Financial Reporting Advisory Board (FRAB) that IFRS 13 should be adopted in full with no adaption, but with enhanced guidance in the FReM to explain the restrictions that are likely to apply in the public sector.

11. The rationale behind this proposal was that IFRS 13 is capable of being used to produce valuations for all public sector assets. Many public sector assets have statutory restrictions on them, so the entity owning the asset is not free to sell it without permission from an external party. In many such cases this will mean the restriction stops the organisation from having access to the open market and IFRS 13 would require this to be reflected in the valuation. This will result in a valuation based on an asset's existing use.

12. Similarly, market values are unlikely to be able to capture the characteristics of specialised assets. In this case, IFRS 13 requires an entity to disregard any market value that does not capture the nature of the asset and to instead employ either an income method or depreciated replacement cost to arrive at an appropriate valuation.

13. In practice then, under this option true 'exit values' reflecting the highest and best use would only have been used for a minority of public sector assets which are not specialised and are not subject to statutory restrictions on their use or disposal.

14. Following further discussions at the FRAB, HM Treasury has revised its proposal on the application of IFRS 13.

15. The key issue identified by some FRAB members following the previous exposure draft was that if the public sector is applying IFRS 13, then it is also necessary to subscribe to the principle of exit values which IFRS 13 is based on. However, exit values are not appropriate for most public sector assets, because they are specifically held for their service potential.

16. IFRS 13 could be used to produce valuations for assets held for their service potential, but, if fair value is not appropriate, then the FRAB suggested that the way forward could be to adapt other standards, in particular IAS 16, so that fair value is only used when it is appropriate. HM Treasury has therefore sought to identify those situations where fair values are appropriate and to restrict the use of IFRS 13 to those circumstances.

17. The application of the standard has therefore been considered with regard to the following effects on asset valuation methodologies:

- Cases where fair value based on exit value is not appropriate and valuation methodologies should be prescribed in other standards without reference to IFRS 13; and

- Cases where fair value based on exit value is appropriate and where IFRS 13 should therefore be applied in full.

Proposals

18. This exposure draft proposes that assets are first classified based on whether they are held for their service potential or not. Assets which are held for their service potential are then assessed as being in use or surplus.

19. All assets which are not held for their service potential will be valued in accordance with IFRS 5 or IAS 40 depending on whether the asset is or is not being held for sale. References to fair value within IFRS 5 and IAS 40 will not be adapted and IFRS 13 will be applied in full. The existing FReM interpretation which withdraws the option of the cost model within IAS 40 will continue.

20. Assets which are held for the service potential will be assessed as being either in use or surplus. Assets which are held for their service potential and are in use will be valued in accordance with the existing adaptations of IAS 16 to produce a current value of their service potential. For non-specialised assets such as office blocks this will be market value in existing use. For specialised assets, this will be depreciated replacement cost on a modern equivalent asset basis.

21. The valuation of assets which are held for their service potential and are surplus will depend on whether there are restrictions on the asset's use or disposal. Certain types of surplus operational assets will need to clear extensive procedural hurdles prior to any possible sale. These restrictions are more extensive than office accommodation requiring planning permission for development as residential properties – they often require lengthy public consultations, fulfilment of regulatory obligations and possible Secretary of State approval. The time required to complete this process often spans financial years. As such, these restrictions on sale constitute lack of access to many markets for the entity at the measurement date. If there are restrictions which would prevent the entity from accessing the market, then the asset will be valued at current value in line with the existing adaptations to IAS 16. If the entity could access the market then the asset will be held at fair value under IFRS 13.

22. The Treasury has considered practical difficulties to this approach. For example, assets may move between valuation categories when they are temporarily surplus. Where an asset has a history of moving between operational and non-operational use, or has only recently been made non-operational and the future status is uncertain, then a strong argument for maintaining current value would exist.

23. Another consideration is multi-use buildings. There will be multi-use buildings which are partly used for their service potential (either to deliver front or back office services) and partly held for financial return. Where this is the case, the guidance on multi-purpose properties in IAS 40 is relevant. If part of a building is not being used for operational reasons, there are no restrictions, and that part of the building can be separately sold or leased, then if material it should be recognised as an investment property under IAS 40 and held at fair value under IFRS 13. This will not require any amendments to existing standards.

Disclosure

24. As per IFRS 13 paragraph 93(i) "if the highest and best use of a non-financial asset differs from its current use, an entity shall disclose that fact and why the non-financial asset is being used in a manner that differs from its highest and best use." This disclosure may be utilised by commercial decision makers when an entity may not be utilising an asset to its highest economic benefit (possibly for competition reasons, i.e. withholding intellectual property until the most beneficial market entry point may yield long term benefits, but the asset is not generating cash flows until a future point in time and this would impact its valuation).

25. HM Treasury's view is that the disclosures required by IFRS 13 should be included if, and only if, an asset is being held at fair value under IFRS 13. The disclosure requirements would not apply to assets being held at current value under the adaptations to IAS 16.

IAS 16 adaptations and interpretations

26. The 2013-14 FReM includes the following adaptation to IAS 16:

- For 'in use' non-specialised property assets fair value should be interpreted as market value for existing use

and the following relevant interpretations:

- All tangible non-current assets shall be carried at fair value at the reporting date - that is, the option give in IAS 16 to measure at cost has been withdrawn, as has the option to value only certain classes of assets

- The 'value in use' of a non-cash-generating asset is the present value of the asset's remaining service potential, which can be assumed to be at least equal to the cost of replacing that service potential.

27. This exposure draft proposes that the existing adaptations and interpretations be altered to refer to current value, rather than fair value, where IFRS 13 is not being

applied, and that IAS 16 is further adapted to specify those circumstances when current values and fair values should be used.

IAS 38 interpretation

28. The existing interpretation to IAS 38 in the FReM removes the cost option given in IAS 38 and requires entities to use a revaluation model for each class of intangible asset. Where an active (homogeneous) market exists, the FReM specifies that intangible assets should be carried at fair value at the reporting period date. Where no active market exists, entities should revalue the asset, using indices or some suitable model, to the lower of depreciated replacement cost and value in use where the asset is income generating. Where there is no value in use, the asset should be valued using depreciated replacement cost.

29. This exposure draft proposes that IAS 38 is adapted such that intangible assets that are held for sale are valued at fair value using IFRS 13 and that all other intangible assets are held at current value on the basis that exit values are not applicable.

FReM chapters addressed

The following table shows the topics addressed by these proposed amendments.

FReM Chapter	**Subject of amendments**
Chapter 6, Applicability of accounting standards	To include IFRS 13 in the list of EU-adopted standards that are applied without adaptation and to amend adaptations and interpretations to IAS 16 and IAS 38.
Chapter 7, Further guidance on accounting for assets and liabilities	To reflect revised adaptations and interpretations to IAS 16 and IAS 38.

Proposed amendments to the Government Financial Reporting Manual

Introduction

An amendment to each of the following chapters is proposed:

- Chapter 6, *Applicability of accounting standards*
- Chapter 7, *Further guidance on accounting for assets and liabilities*

Why the amendments are proposed

The amendments proposed in this exposure draft seek to amend the FReM to incorporate the financial reporting principles contained in IFRS 13 where it is appropriate for them to be applied. HM Treasury considers that where an asset is held primarily for its service potential as an operational asset, that its valuation should reflect its service potential and not fair value as determined by exit value. For non-specialised assets such as office blocks this will be market value in existing use. For specialised assets, this will be depreciated replacement cost on a modern equivalent asset basis. Assets which are not held for their service potential, or are surplus and not subject to restrictions on use or disposal, should be valued in accordance with IFRS 13.

Effective date of amendments

The effective date for the proposed amendments is 1 April 2015.

Proposed amendments

FReM amendments are proposed to reflect IFRS 13 being adopted for the first time and to reflect revised adaptations and interpretations to IAS 16 and IAS 38.

6 Applicability of accounting standards

6.1 EU adopted IFRS

6.1.1 A list of EU adopted IFRS is shown in Table 6.1, together with a record of whether they have been adapted or interpreted for the public sector context in this Manual. All standards apply to all reportable activities and reporting entities applying this Manual to the extent that each standard is relevant to those activities and in the light of any statutory requirements or other pronouncements that might from time to time be made by the relevant authorities. Where adaptations or interpretations are different for ALBs this is identified below.

Table 6.1

International Standard	Applies without adaptation	Applies as interpreted for public sector	Applies as adapted for public sector	Different adaptations or interpretation for ALBs
IFRS 13 Fair Value Measurement	●			
~~IFRS 13 Fair Value Measurement~~	~~IFRS 13 applies prospectively to entities covered by this Manual from 1 April 2015. Early adoption is not permitted.~~			
IAS 16 Property, plant and equipment		●	●	
IAS 38 Intangible Assets		●		

6.2 Interpretations and adaptations for the public sector context

6.1.2 Table 6.2 provides details of those adaptations and interpretations for the public sector context. Where an adaptation or interpretation to a standard results in an inconsistency with a related Interpretation issued by the IFRS Interpretations Committee (IFRIC) or Standards Interpretations Committee (SIC), that Interpretation is similarly adapted or interpreted. In all other case, IFRIC and SIC Interpretations will apply in full.

6.1.3 Chapter 10 of this Manual provides additional guidance on adaptations and interpretations for the Whole of Government Accounts.

Table 6.2

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations	
Interpretations	~~(1)~~ In order to qualify as 'discontinued operations', the activities must cease completely: that is, responsibilities transferred from one part of the public sector to another (such as machinery of government changes) are not discontinued operations. ~~(2) The 'value in use' of a non-cash-generating asset is the present value of the asset's remaining service potential, which can be assumed to be at least equal to the cost of replacing that service potential.~~
IAS 16 Property, Plant and Equipment	
Adaptations	IAS 16 is adapted to specify the following valuation bases for property, plant and equipment: - Assets which are held for their service potential (i.e. operational assets) and are in use should be measured at current value. For non-specialised assets current value should be interpreted as market value for existing use. In the RICS Red

	Book, this is defined as 'market value on the assumption that property is sold as part of the continuing enterprise in occupation'. For specialised assets current value should be interpreted as the present value of the asset's remaining service potential, which can be assumed to be at least equal to the cost of replacing that service potential. - Assets which are surplus should be valued at current value as above if there are restrictions on the entity or the asset which would prevent access to the market at the reporting date. If the entity could access the market then the surplus asset should be valued at fair value using IFRS 13. - Assets which are not held for their service potential should be valued in accordance with IFRS 5 or IAS 40 depending on whether the asset is actively held for sale. T For 'in use' non-specialised property assets fair value should be interpreted as market value for existing use. In the RICS Red Book, this is defined as 'market value on the assumption that property is sold as part of the continuing enterprise in occupation'.
Interpretations	(1) All tangible non-current assets shall be carried at either current value or fair value at the reporting date - that is, the option give in IAS 16 to measure at cost has been withdrawn, as has the option to value only certain classes of assets (2) It is not necessary to disclose the historical cost carrying amounts (where available) (3) The 'value in use' of a non-cash-generating asset is the present value of the asset's remaining service potential, which can be assumed to be at least equal to the cost of replacing that service potential. **Chapter 5 provides additional guidance on asset valuations and additional interpretations for applying IAS 16 to heritage assets. Further application guidance on accounting for property, plant and equipment, including heritage assets, networked assets and PPP arrangements, including PFI is included in chapter 7.**
IAS 38 Intangible Assets	
Interpretations Adaptations	Following the initial recognition of an intangible asset, for subsequent measurement IAS 38 permits the use of either the cost or revaluation model for each class of intangible asset. Where an active (homogeneous) market exists, intangible assets other than those that are held for sale should be carried at fair current value at the reporting period date – that is, the cost option given in IAS 38 has been withdrawn and the current value should be based on the market value in existing use. Where no active market exists, entities should revalue the asset, using indices or some suitable model, to the lower of depreciated replacement cost and value in use where the asset is income generating. Where there is no value in use, the asset should be valued using depreciated replacement cost. These measures are a proxy for fair value. **Chapter 7 provides application guidance for Carbon Reduction Commitment (CRC) Energy Efficiency Scheme**
IAS 40 Investment Properties	
Interpretations	All investment property should be accounted for under the fair value model - that is, the option given in IAS 40 to adopt the cost model has been withdrawn. IAS 40 applies in full to all reporting entities covered by this Manual that hold (or are constructing or developing) properties only for the purpose of earning rentals or for capital appreciation or both. If earning rentals were an outcome of a regeneration policy, for example, the properties concerned would be accounted for under IAS 16 and not IAS 40.

7 Further guidance on accounting for assets and liabilitiesProperty, plant and equipment (PPE)

Valuations (excluding networked assets, donated assets and heritage assets)

7.1.1 In considering how best to apply the valuation requirements of IAS 16 so as to ensure that the Statement of Financial Position gives a true and fair view of the value of the

assets at the reporting date, entities should consider the following guidance on property and non-property assets.

~~Property~~

7.1.2 Entities should value their ~~property~~ PPE using the most appropriate valuation ~~methodology~~process. Such ~~methods~~ processes might include:

- a quinquennial valuation supplemented by annual indexation and no interim professional valuation;
- annual valuations; or
- a rolling programme of valuations ~~of properties (whether specialised or non-specialised)~~.

7.1.3 It is for valuers, using the Royal Institution of Chartered Surveyors; (RICS) 'Red Book' (RICS Appraisal and Valuation Standards), and following discussions with the entity, to determine the most appropriate methodology for obtaining either a current value or a fair value.

7.1.4 Assets which are held for their service potential (i.e. operational assets used to deliver either front line services or back office functions) should be measured at their current value. For non-specialised assets current value should be interpreted as market value in existing use and is defined in the RICS Red Book as the 'market value on the assumption that property is sold as part of the continuing enterprise in occupation'. For specialised assets current value should be interpreted as the present value of the asset's remaining service potential, which can be assumed to be at least equal to the cost of replacing that service potential.

7.1.5 Assets which are surplus should be valued at current value as per paragraph 7.1.4 if there are restrictions on the entity or the asset which would prevent access to the market at the reporting date. If the entity could access the market then the surplus asset should be valued at fair value using IFRS 13.

7.1.6 Assets which are not held for their service potential should be valued in accordance with IFRS 5 or IAS 40 depending on whether the asset is actively held for sale.

~~7.1.3~~7.1.7 Where a valuer, following discussion with the entity, determined that depreciated replacement cost (DRC) is the most appropriate measure of current value, entities and their valuers should have regard to the guidance contained in the most recent RICS Red Book.

~~7.1.4~~7.1.8 Where DRC is used as the valuation methodology:

- entities should normally value a modern equivalent asset in line with the Red Book. Any plans to value a reproduction of the existing asset instead should be discussed with the relevant authority (through sponsoring bodies where appropriate) to determine whether such an approach is appropriate to the entity's circumstances.
- entities should use the 'instant build' approach;
- the choice of an alternative site will normally hinge on the policy in respect of the locational requirements of the service that is being provided.

~~7.1.5~~7.1.9 The cost of enhancements to existing assets (such as building of a new wing within an existing prison or adding a lane to a motorway) should be capitalised during the construction phase as an asset under construction. At the first valuation after the asset is brought into use, any write down of cost should be treated as an impairment and charged to the Statement of Comprehensive Net Expenditure.

~~7.1.6~~7.1.10 Entities should:

- disclose in the accounting policies note the fact that assets are carried at ~~fair~~ current value or fair value. Entities should also provide information about the

approach to valuing their estates, including a statement (where applicable) that alternative sites have been used in DRC valuations;

- disclose in the notes on tangible non-current assets: the date of the last valuations of those property assets that are subject to revaluation, and the names and qualifications of the valuer; and
- discuss in the Management Commentary, where they hold extensive estates: their estate management strategy; the indicative alternative use values provided by the valuer as part of the routine valuation work, and what those alternative use values mean in terms of their estate management policy.

7.1.77.1.11 As part of the Property, Plant and Equipment note entities are required, in the year the asset is acquired, to separately disclose the current value or fair value of those assets funded by government grant, donation or lottery funding. Where the funder provides cash, rather than the physical assets, any difference between the cash provided and the fair value of the assets acquired should also be disclosed.

Non-property (excluding networked assets, donated assets and heritage assets)

7.1.87.1.12 Entities may elect to adopt a depreciated historical cost basis as a proxy for current value or fair value for assets that have short useful lives or low values (or both). For depreciated historical cost to be considered as a proxy for current value or fair value, the useful life must be a realistic reflection of the life of the asset and the depreciation method used must provide a realistic reflection of the consumption of that asset class. If depreciated historical cost is used as a proxy for current value or fair value then this fact should be disclosed, including the classes of assets where it has been used (where appropriate), the reasons why, and information about any significant estimation techniques (where applicable).

7.1.9 Assets that are not covered by the above paragraph should be carried at fair value. Entities should value such assets using the most appropriate valuation methodology available (for example, appropriate indices).

7.1.10 Entities should disclose the following in the notes to their accounts in relation to the valuation of non-property assets:

- in the accounting policies note: the fact that assets are carried at fair value; that depreciated historical cost is used as a proxy for fair value for named classes of assets (where appropriate) and the reasons why; information about any significant estimation techniques (where applicable); and
- in the notes on tangible non-current assets: the dates of the last valuations of any non-property assets that are subject to revaluation and the names and qualifications of the valuer.

Networked assets

7.1.117.1.13 Networked assets comprise assets that form part of an integrated network servicing a significant geographical area. These assets usually display some or all of the following characteristics:

- they are part of a system or network;
- they are specialised in nature and do not have alternative uses;
- they are immovable; and
- they may be subject to restrictions on disposal.

Examples of networked assets include road networks, sewer systems, water and power supply systems and communications networks.

The road network

7.1.127.1.14 Land, Structures and Communications will be accounted for following the guidance in IAS 16.

~~7.1.13~~7.1.15 The road surface asset managed by each of the highways authorities in England, Scotland, Wales and Northern Ireland will be recognised as a single asset by each such authority following the additional guidance in this manual.

~~7.1.14~~7.1.16 The road surface asset will be held at depreciated replacement cost based on service potential.

~~7.1.15~~7.1.17 Subsequent expenditure on the road surface will be capitalised where it enhances or replaces the service potential. Spending that does not replace or enhance service potential will be expensed.

~~7.1.16~~7.1.18 The annual depreciation charge for the road surface will be the value of the service potential replaced through the maintenance programme plus, or minus, any adjustment resulting from the annual condition survey. The value of maintenance work undertaken will be used as an indication of the value of the replaced part. Where the condition survey show that deterioration in the road surface exceeds the service potential replaced by the maintenance programme the additional deterioration will be taken to the Statement of Comprehensive Net Expenditure as part of the depreciation charge. Where the condition survey shows that deterioration in the road surface is less than the service potential replaced by the maintenance programme the depreciation charge will be reduced by the excess maintenance.

~~7.1.17~~7.1.19 The road surface will be subject to annual valuations as measured by suitable indices. Upward movements in value will be taken to the revaluation reserve and included in comprehensive net expenditure. Downward movements in value will be set against any credit balance held in the revaluation reserve until this credit is exhausted and thereafter to net operating cost.

~~7.1.18~~7.1.20 The road surface will be subject to an annual impairment review. Impairments will be recognised as required by IAS 36 Impairment of Assets as applied by the manual (see section 7.3).

Other Infrastructure

~~7.1.19~~7.1.21 Where Bodies hold other networked assets the road surface accounting methodology detailed above may be used where it is appropriate to do so. However approval to use the road surface methodology should first be obtained from the relevant authority.

Donated assets

~~7.1.20~~7.1.22 Assets donated by third parties (see also paragraph 7.1.16 on asset ransfers), either by gift of the asset or by way of funds to acquire assets (including national lottery-funded assets), and which meet the criterion in paragraph 7.1.13, should be capitalised at current value or fair value on receipt, depending on whether the assets will be held for their service potential and as set out in paragraphs 7.1.4 to 7.1.6. The funding element should be recognised as income as required by IAS 20 as interpreted in this Manual.

~~7.1.21~~7.1.23 To qualify for treatment as a donated asset there should be no consideration given in return.

~~7.1.22~~7.1.24 Donated assets do not include:

a) assets financed by grant-in-aid;

b) the subsequent capitalised expenditure on a donated asset which is capitalised;

c) assets constructed or contributed to by a developer to benefit the developer's business;

d) assets accepted in lieu of tax.

These types of asset should be accounted for in accordance with IAS 16 in the same way as other assets of that general type.

~~7.1.23~~7.1.25 Donated assets should be revalued, depreciated and subject to impairment review in the same way as other non-current assets.

~~7.1.24~~7.1.26 Details of any restrictions or conditions imposed by the donor on the use of the donated asset should be disclosed in a note to the financial statements.

Asset transfers

~~7.1.25~~7.1.27 Entities (other than trading funds) may give or receive assets to/from another public sector body (including public sector bodies not covered by the requirements of this Manual) for no consideration. Assets acquired in this way will normally be recognized in accordance with IAS 20 as interpreted in this Manual. Entities should consult the relevant authority (through sponsoring bodies where appropriate) before entering into such a transaction.

Heritage assets

Definition

~~7.1.26~~7.1.28 A heritage asset is a tangible asset with historical, artistic, scientific, technological, geophysical or environmental qualities that is held and maintained principally for its contribution to knowledge and culture. Heritage assets are those assets that are intended to be preserved in trust for future generations because of their cultural, environmental or historical associations. They are held by the reporting entity in pursuit of its overall objectives in relation to the maintenance of the heritage. Non-operational assets are those that are held primarily for this purpose. Operational heritage assets are those that, in addition to being held for their characteristics as part of the nation's heritage, are also used by the reporting entity for other activities or to provide other services (the most common example being buildings).

~~7.1.27~~7.1.29 The reporting entity holding the asset should attest annually to the ongoing heritage credentials of its heritage assets. Heritage assets include historical buildings, archaeological sites, military and scientific equipment of historical importance, museum and gallery collections and works of art.

~~7.1.28~~7.1.30 In principle, heritage assets should be accounted for in the same way as any other asset under IAS 16. There are, however, certain characteristics associated with heritage assets that give rise to the need for interpretation of IAS 16:

a) Their value to government and the public in cultural, environmental, educational and historical terms is unlikely to be fully reflected in a financial value derived from a market mechanism or price.

b) Established custom and, in many cases, primary statute and trustee obligations impose prohibitions or severe restrictions on disposal by sale.

c) They are often irreplaceable and their value may increase over time even if their physical condition deteriorates.

d) They may require significant maintenance expenditure so that they can continue to be enjoyed by future generations.

e) Their life might be measured in hundreds of years.

f) Antiques and other works of arts held by reporting entities outside the main collections should be classified as heritage assets only when they fulfil the above requirements. Otherwise, antiques and other works of art should be accounted for in the same way as other assets.

Recognition and measurement

~~7.1.29~~7.1.31 Operational heritage assets should be valued in the same way as other assets of that general type (buildings, for example).

~~7.1.30~~7.1.32 Non-operational heritage assets should be valued subject to the requirements set out in paragraphs 7.1.~~31~~ 33 to 7.1.~~34~~ 36 below.

~~7.1.31~~7.1.33 Where information is available on the cost or fair value of heritage assets:

(i) they should be presented in the Statement of Financial Position separately from other tangible assets;

(ii) the Statement of Financial Position or the notes to the accounts should identify separately those classes of heritage assets being reported at cost and those at fair value; and

(iii) changes in the valuation should be recognised in the Other Comprehensive Expenditure section of the Statement of Comprehensive Net Expenditure, except impairment losses that should be recognised in accordance with section 7.3 of this Manual.

~~7.1.32~~7.1.34 The accounting convention in this manual is to recognise non-current assets at either current value or fair value but, where exceptionally, it is not practicable to obtain a fair value, the heritage assets may be reported at historical cost.

~~7.1.33~~7.1.35 Where assets have previously been capitalised or are recently purchased, information on their cost or fair value will be available. Where this information is not available, and cannot be obtained at a cost commensurate with the benefits to users of the financial statements, the assets will not be recognised in the Statement of Financial Position and the disclosure required by this manual should be made.

~~7.1.34~~7.1.36 Valuations may be made by any method that is appropriate and relevant. There is no requirement for valuations to be carried out or verified by external valuers, nor is there any prescribed minimum period between valuations. However, where heritage assets are reported at valuation, the carrying amount should be reviewed with sufficient frequency to ensure the valuations remain current.

Depreciation and impairment

~~7.1.35~~7.1.37 Depreciation is not required on heritage assets which have indefinite lives.

~~7.1.36~~7.1.38 The carrying amount of an asset should be reviewed where there is evidence of impairment, for example, where it has suffered physical deterioration or breakage or new doubts arise as to its authenticity. Any impairment recognised should be dealt with in accordance with the recognition and measurement requirements of IAS 36 - 'Impairment of Assets' in section 7.3.

Donations

~~7.1.37~~7.1.39 The receipt of donations of heritage assets should be recognised as income and taken through the Statement of Comprehensive Net Expenditure where there are no conditions specifically relating to the operating activities of the entity or recognised as deferred income in the Statement of Financial Position. Where exceptionally, it is not practicable to obtain a valuation for a donated heritage asset, the reasons why should be stated. Disclosures should also be provided on the nature and extent of significant donations.

Disclosures

~~7.1.38~~7.1.40 The disclosures required for heritage assets are set out below and apply to all heritage assets:

a) An entity's financial statements should contain an indication of the nature and scale of heritage assets held by the entity;

b) The financial statements should set out the entity's policy for the acquisition, preservation, management and disposal of heritage assets. This should include a description of the records maintained by the entity of its collection of heritage assets and information on the extent to which access to the assets is permitted. The information required by this paragraph may alternatively be provided in a document that is cross-referenced from the financial statements;

c) The accounting policies adopted for an entity's holding of heritage assets should be stated, including details of the measurement bases used;

d) For heritage assets that are not reported in the Statement of Financial Position, the reasons why should be explained and the notes to the financial statements should explain the significance and nature of those assets that are not reported in the Statement of Financial Position; and

e) The disclosures relating to assets that are not reported in the Statement of Financial Position should aim to ensure that, when read in the context of information about capitalised assets, the financial statements provide useful and relevant information about the entity's overall holding of heritage assets.

~~7.1.39~~7.1.41 Where heritage assets are reported in the Statement of Financial Position, the following should be disclosed:

(i) the carrying amount of heritage assets at the beginning of the financial period and at the Statement of Financial Position date, including an analysis between those classes or groups of heritage assets that are reported at cost and those that are reported at valuation; and

(ii) where assets are reported at valuation, sufficient information to assist in an understanding of the valuations being reported and their significance.

This should include:

a) the date of the valuation;

b) the methods used to produce the valuation;

c) whether the valuation was carried out by external valuers and, where this is the case, the valuer's name and professional qualification, if any; and

d) any significant limitations on the valuation.

~~7.1.40~~7.1.42 An example of a limitation to be disclosed under paragraph 7.1.~~39~~ 41 (ii) (d) would be where an asset has a particular provenance, the effect of which is not fully captured by valuation.

~~7.1.41~~7.1.43 Information that is available to the entity and is helpful in assessing the value of those heritage assets that are not reported in the entity's Statement of Financial Position should be disclosed.

~~7.1.42~~7.1.44 The financial statements should contain a summary of transactions relating to heritage assets disclosing, for the accounting period and each of the previous four accounting periods:

a) the cost of acquisitions of heritage assets;

b) the value of heritage assets acquired by donation;

c) the carrying amount of heritage assets disposed of in the period and the proceeds received; and

d) any impairment recognised in the period.

This summary should show separately transactions in assets that are reported in the Statement of Financial Position and those that are not.

~~7.1.43~~7.1.45 The disclosures required by paragraphs 7.1.~~38~~ 40 to 7.1.~~42~~ 44 may be presented in aggregate for groups or classes of heritage assets provided this aggregation does not obscure significant information. Separate disclosures should be provided for those assets reported at cost and those reported at valuation. Amounts in respect of assets that are not reported in the Statement of Financial Position should not be aggregated with amounts for assets that are recognised at cost or valuation.