FRAB (120) 02
3 April 2014

Appendix A

Summary of previous options considered

October 2013 – No additional adaptations to IAS 16, apply IFRS 13 to all assets

1. This option was presented at the October 2013 FRAB meeting. It sought to use the IFRS 13 definition of fair value as being the 'exit price' for an asset or liability and to use the principles within IFRS 13 for calculating an exit price for all assets.

2. 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.

3. 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.

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

5. Some Board members raised significant concerns about this method of applying IFRS 13. This was on the basis that if IFRS 13 is being used to fair value assets then it is necessary to subscribe to exit values as the measurement objective which is a significant departure from previous public sector accounting practice.

6. The Treasury, which put forward this proposal at the October 2013 meeting, agrees with these members' concerns and as noted at the December 2013 meeting no longer recommends this option. Aside from the fact that many public sector assets cannot be disposed of because of statutory restrictions or, realistically, won't be disposed of because they are being used to deliver services to a local area, the overriding measurement objective for public sector assets has been to value service potential and not exit value. To attempt to determine a valuation which will provide the best incentives for good asset management by amending IFRS 13 is not appropriate.

7. The Treasury and CIPFA, therefore agree that the application of IFRS 13 should be restricted to cases where fair value is appropriate and have not developed this option further.

December 2013 – Adapt IAS 16, apply IFRS 13 to assets which are not used to deliver services directly to the public

8. This option was proposed at the December 2013 FRAB meeting. Under this model, assets that are used to deliver services directly to the public are judged as being held for their service potential and would be measured at current valuation (either existing use value or depreciated replacement cost) in accordance with existing interpretations of IAS 16.

9. Public sector assets that are not used to provide services directly to the public, and which are not subject to any service or other constraints that would limit the ability of the reporting entity to sell them, would be measured at fair value in accordance with IFRS 13.

10. The overall result would be that entities would only apply IFRS 13 valuations to assets when these assets are not being used to provide services directly to the public and the entity is able to act without any service or other constraint as if it were a commercial organisation.

11. The deemed advantage of this approach was that it would provide financial information aligned with the purpose of holding the asset; users would receive information about the service potential of assets that were being held to directly deliver services to the public and the fair value of assets that were not used for the directly delivery of services and were not subject to restrictions or constraints on disposal. As depreciation charges would also typically be higher for assets that could be disposed of, as a result of their being held at highest and best use valuations, this would give a budgetary incentive to make best use of those assets. It was thought that this would be specifically useful for general administrative buildings.

12. As a number of Board members identified, the difficulty with this approach is that it is dependent on there being a clear distinction between assets that are used to provide services directly to the public and those that aren't. Conceptually, it is very difficult to define where the boundary should be. For example, how should entities treat assets which are used to support services being delivered digitally? There would also be significant practical difficulties, for example as a result of sites and individual assets being used for multiple purposes.

13. HM Treasury and CIPFA have considered these practical difficulties in more detail since the December meeting and have two particular concerns. The first is the level of subjective judgement that would be needed to designate assets as delivering services to the public or not. Although service delivery could be defined in guidance, this is unlikely to be able to capture all scenarios and it could be exploited by using an asset to deliver a token amount of services. The second concern is how understandable and comparable the resulting information would be, particularly if different valuation methodologies are used for different components of an asset which are not in fact separable. Therefore we consider that this option would result in financial information that was difficult to audit and difficult for a user to understand and consequently we do not recommend it.