

REPORT

CL 08c 09-08

Committee	CIPFA/LASAAC LOCAL AUTHORITY SORP BOARD
Venue	Robert Street, London
Date	12 September 2008
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Subject	Impairment Section of Draft IFRS-Based Code

1. INTRODUCTION

- 1.1. At its meeting held on 15 April 2008, CIPFA/LASAAC agreed the format and structure of the IFRS-based Code of Practice.
- 1.2. This report considers the impairment section of the draft IFRS-based Code of Practice on Local Authority Accounting, and CIPFA/LASAAC is asked to approve the section or suggest amendments.

2. SUMMARY OF COMPLIANCE WITH STANDARDS / IMPACT

IFRS Compliance / Adaptations	One interpretation in respect of 'value in use' for assets not held for the purpose of generating cash flows (detailed in paragraph 3.4)
IPSASB Compliance / Adaptations	Full compliance, no adaptations
i-FReM Compliance / Adaptations	Reference to ' <i>downward revaluations result in an impairment only where an asset is revalued below its historical cost carrying amount</i> ' is not applicable to local government (detailed in paragraph 3.5)
Changes to SORP	Yes (detailed in paragraphs 3.2 and 3.3)
Impact on Taxation	No impact on taxation; impairments and reversal of impairments charged to Statement of Comprehensive Income are transferred to the Capital Adjustment Account and reported in the Statement of Changes in Equity

3. DRAFT CODE

- 3.1. The accounting requirements for impairments are detailed in *IAS 36 Impairment of Assets*. *IPSAS 21 Impairment of Non-Cash Generating Assets* and *IPSAS 26 Impairment of Cash-Generating Assets* are based on *IAS 36* and introduce no additional requirements, although they provide additional guidance on issues that might arise in the public sector. Assets falling under the definition of Cash-Generating Assets (i.e. assets held for the primary objectives of generating a commercial return) may not be common within local authorities. Where authorities deem they have assets under this definition they should refer to *IAS 36* and *IPSAS 26* in relation to impairment.
- 3.2. Many of the requirements are similar to those previously included in the SORP, following *FRS 11 Impairment of fixed assets and goodwill*. Changes to the requirements are summarised below:
- Unlike the SORP, the *IAS 36* does not include a specific requirement to undertake an impairment assessment of assets when either; (a) no depreciation charge is made on the grounds that it would be immaterial (either because of the length of the estimated remaining useful life or because the estimated residual value of the fixed asset is not materially different from the carrying amount of the asset), or (b) the estimated remaining useful life of the fixed asset exceeds 50 years.
 - *IAS 36* does not exempt non-depreciable land from impairment reviews.
 - All impairment losses on re-valued assets are to be recognised in the Revaluation Reserve up to the amount in the Revaluation Reserve for each respective asset, and thereafter within the Statement of Comprehensive Income. In contrast the SORP requires an impairment loss due to the clear consumption of economic benefits on a re-valued asset to be recognised in the Statement of Comprehensive Income.
 - The events or circumstances that indicate that a previous impairment can be reversed are the same for both intangible and tangible assets under *IAS 36*. In contrast *FRS 11* sets out the events or circumstances separately for intangible and tangible fixed assets.
- 3.3. A point that is worthy of comment is the events or circumstances that indicate that a previous impairment can be reversed. *IAS 36* states that the indications of the potential decrease of an impairment loss will mainly mirror (but are not limited to) the indications of a potential impairment loss. *FRS 11* sets out in detail the events or circumstances separately for intangible and tangible fixed assets; these events or circumstances do not always 'mirror' the indications of a potential impairment loss (for example, reversal of an impairment of an intangible asset is more restrictive under *FRS 11*). This may result in the reversal of a previous impairment changed to the Statement of Comprehensive Income becoming more common under the IFRS than under UK GAAP. Reversal of impairment is not common in local authorities, and emphasising this point within the Code is not considered necessary.
- 3.4. The draft Code identifies one area where the requirements of *IAS 36* should be varied. This is in relation to the definition of 'value in use' for assets that are not held for the purpose of generating cash flows. The interpretation for the public context assumes that 'value in use' is to equal the cost of replacing the service potential provided by the asset, unless there has been a reduction in service potential. This interpretation follows *IPSAS 21* and is consistent with the i-FReM.

- 3.5. The i-FReM states under the heading of revaluations; *'Downward revaluations result in an impairment only where an asset is revalued below its historical cost carrying amount. In these cases, the accounting treatment is as for any other impairment'*. The draft Code does not follow this accounting practice, with any downward valuation (as opposed to an impairment loss) below historical cost being categorised as a revaluation loss in line with BVACOP. There will be explicit reference to this accounting treatment within the property, plant and equipment section of the draft Code. Downward revaluations below the historical cost carrying amount will be reflected in the Statement of Comprehensive Income.
- 3.6. The draft section of the Code covering impairment is included as Appendix A.
- 3.7. The draft section of the Code covering the transition arrangements for impairment is included as Appendix B (the text in bold will form part of the associated Guidance Notes). It should be noted that there are no adjustments required to authorities' opening balance sheet in relation to impairments. The restatement of comparative figures for 2009/10 may require impairments due to the consumption of economic benefits and any associated reversal that were recognised in the Income and Expenditure Account on a previously re-valued asset to be recognised in the Revaluation Reserve.
4. RECOMMENDATION

CIPFA/LASAAC is asked to approve the impairment section of the IFRS-based Code of Practice on Local Authority Accounting, or comment on areas where further analysis or changes are requested.