

A REVIEW OF THE CAPITAL ACCOUNTING SYSTEM APPLYING TO BODIES REPORTING UNDER THE LOCAL AUTHORITY SORP

PROJECT BRIEFS

APRIL 2002



A REVIEW OF THE CAPITAL ACCOUNTING SYSTEM APPLYING TO BODIES REPORTING UNDER THE LOCAL AUTHORITY SORP – PRINCIPAL PROJECT BRIEF

1. INTRODUCTION

1.1 The current capital accounting system was introduced in April 1994 following extensive development work and piloting. The introduction of capital accounting represented the final step in the migration to a full accruals basis of accounting and financial reporting for bodies reporting under the Local Government SORP.

1.2 One of the key projects on the work programme of the CIPFA/LASAAC Joint Committee for 2002 is a review of the capital accounting system. There are three main drivers:

- scepticism amongst accounts preparers about the rationale for and effectiveness of the new scheme
- the Whole of Government Accounts project and the related but separate Wales Whole of Government Accounts project
- the impact of the Prudential Code on Capital Finance.

Scepticism amongst accounts preparers

1.3 Scepticism about the merits of capital accounting has been prevalent since the inception of the system, although it appears to have become more intense recently. The main reason for this dissatisfaction is that, for statutory reasons related to existing control frameworks, many of the entries to the service segmented section of the consolidated revenue account have to be reversed and have no impact on annual financing requirements. This embeds a view that capital accounting involves “funny money”, making it difficult to provide coherent explanations to non-financial managers and incentivise positive behaviour.

Whole of Government Accounts

1.4 The SORP review identified the accounting policy for the measurement of infrastructure assets as the main difference between the SORP and the RAM with an impact on the carrying values of tangible fixed assets and the level of capital charges. The RAM requires infrastructure assets along with other operational tangible fixed assets to be carried at current value (which normally means depreciated replacement cost). In the SORP infrastructure assets, unlike other operational assets other than community assets, are measured at historical cost, net of depreciation.

Prudential Code on Capital Finance

- 1.5 The Prudential Code has as one of its objectives a move to a flexible capital control system in which reliance on UK GAAP is a significant component. Particularly significant, from a capital accounting perspective, is the role that depreciation might play in a new system.

2. SCOPE

2.1 It is proposed that the scope of the review will cover:

- an analysis of the appropriateness of the existing accounting mechanisms and requirements and a brief assessment of the extent to which capital accounting has improved asset management together with an evaluation of the barriers to more effective use of an accruals based system.
- an evaluation of the current approach to the recognition and measurement of infrastructure assets focusing on the advantages and disadvantages of moving from depreciated historical cost to current value as the measurement basis. This will include an analysis of resource implications and an analysis of renewals accounting as the basis of depreciation.
- an evaluation of the current approach to the recognition and measurement of community assets and donated assets from the perspectives of UK GAAP and the recently issued IPSAS 17, *Property, Plant and Equipment* and comparison of the current approach with that in the RAM for heritage assets.
- an evaluation of the links between capital accounting and the prudential framework.
- an analysis of the process for determining the notional interest rates for the financing element of the annual capital charge, the appropriateness of the current rates for both assets measured at current value and those measured at historical cost.
- an analysis of the case for bringing liabilities within the scope of capital charges.
- an evaluation of the advantages and disadvantages of replacing the existing consolidated revenue account with statements based on Schedule 1 – *Summary of Resource Outturn* and Schedule 2 – *Operating Cost Statement*- from the RAM. This will involve a consideration of the impact of current ASB proposals for a single performance statement on such a development and the advantages and disadvantages of including budget information in a Schedule 1 type statement. Whilst this component of the project relates primarily to the format of statements rather than capital accounting per se the rationale for introduction of Schedule 1 is strongly linked to capital accounting, because it is in this area that the SORP departs most from UK GAAP
- a clarification of the definition and revenue treatment of non-operational and community assets.

3. RESPONSIBILITIES

3.1 Overall co-ordination of the project lies with John Stanford, Assistant Director.

Component	Lead responsibility
1. Assessment of current system	Angela Scott and CIPFA Scotland
2. Evaluation of current approach to recognition and measurement of infrastructure assets	John Stanford
3. Evaluation of links between capital accounting and prudential framework	Maureen Wellen
4. Notional interest rates	Kieran Rix
5. Liabilities and capital charges	Kieran Rix
6. Local Government Equivalent of Schedule 1 and Schedule 2	John Stanford
7. Non-operational and community assets	John Stanford

3.2 Project components or parts of components may be contracted out depending on resources. The named secretariat officer will retain overall management of work contracted out.

4. TIMESCALES

4.1 Integrated report by end of September, for consultation, with a draft available by mid-July. It is likely that changes to the SORP resulting from the project will take effect from 1 April 2004, although more minor amendments involving modifications or clarifications to definitions may be actioned in the 2003 SORP.

5. DETAILED BRIEFS

5.1 Detailed briefs shall be prepared setting out the reasons for the inclusion of the component in the review, the objectives of the component, the approach to be adopted, responsibilities and timescale.

5.2 The component project briefs are attached to this paper.

A REVIEW OF THE CAPITAL ACCOUNTING SYSTEM APPLYING TO BODIES REPORTING UNDER THE LOCAL AUTHORITY SORP

COMPONENT PROJECT BRIEFS

APRIL 2002



COMPONENT 1 ASSESSMENT OF CURRENT SYSTEM

1. INTRODUCTION

- 1.1 The current capital accounting system was introduced in April 1994 in the UK. In Scotland, the arrangements were introduced on a phased basis. The introduction represented the final step in the migration to a full accruals basis of accounting and financial reporting.
- 1.2 One of the key projects on the work programme of the CIPFA/LASAAC Joint Committee for 2002 is a review of the capital accounting system.

2 JUSTIFICATION FOR PROJECT COMPONENT

- 2.1 The following project is a core component of the overall wider review of capital accounting.
- 2.2 The principal reasons for inclusion in the wider review are:
 - Evidence of practitioner views that current accounting treatments are unnecessarily complex.
 - Concern by practitioners that many of the revenue aspects of the current framework do not impact on the annual financing requirements of local authorities and that the framework is difficult to explain to non-financial managers.
 - Uncertainty about the extent to which the wider asset management benefits of capital accounting have been realised.

3 OBJECTIVE

- 3.1 An analysis of the appropriateness of the existing accounting mechanisms and requirements.
- 3.2 A brief assessment of the extent to which capital accounting has improved asset management.
- 3.3 An evaluation of the barriers to more effective use of an accruals based system.
- 3.4 To highlight ways in which capital accounting can lead to improvements in asset management.

4. APPROACH

- 4.1 The capital accounting approaches in other public sector bodies will be reviewed.

- 4.2 Consultation will be held with targeted groups of CIPFA practitioners from both Scotland, England, Wales & NI to identify specific problem areas, identify solutions and to highlight ways in which capital accounting has promoted better asset management.
- 4.3 Consultation will be held with targeted groups of local authority asset management professionals in Scotland, England, Wales & NI to identify specific problem areas and to identify solutions.
- 4.4 An evaluation of the findings and proposals will be undertaken and presented to the CIPFA review team for assessment against the background of existing and future regulatory accounting statements.

5. RESPONSIBILITIES

- 5.1 To be undertaken by Don Peebles in liaison with the managers responsible for related components in the review, reporting via Angela Scott to John Stanford for overall co-ordination of the capital accounting review.

6. TIMESCALE

- 6.1 Draft report to be available by July 2002 for incorporation in the overall report by September 2002.

COMPONENT 2 EVALUATION OF CURRENT APPROACH TO RECOGNITION AND MEASUREMENT OF INFRASTRUCTURE ASSETS

1 JUSTIFICATION FOR PROJECT COMPONENT

- 1.1 This project is a component of the wider review of capital accounting commissioned to examine the future workings of the capital accounting system.
- 1.2 Under the current system of accounting for fixed assets by bodies covered by the local authority accounting SORP, most fixed assets are required to be regularly revalued according to their current valuation – specifically at the lower of net current replacement cost or net realisable value (in existing use for operational assets). However, infrastructure and community assets are required to be included in the balance sheet at historical cost net of depreciation.
- 1.3 The following are examples of infrastructure assets:
- roads
 - sea defences
 - bridges
 - permanent ways
 - street furniture.
- 1.4 It is understood that the main reasons why, when the current system of accounting for fixed assets for local authorities was introduced in 1994/95, it was decided to value infrastructure assets on an historical basis are:
- (i) the cost and practicality of measuring infrastructure assets at current value
 - (ii) a concern that current valuation of infrastructure assets would result in balance sheets so heavily weighted towards roads that local authorities would appear to be, broadly speaking, highway authorities.
- 1.5 The reasons for undertaking a review now are:
- (i) the desire for consistency in valuation bases for the whole of government accounts programme
 - (ii) the government's modernising agenda for local government finance offers the opportunity for a re-examination of the relationship between accounting for fixed assets in local government and generally accepted accounting practice (see the specification for an evaluation of the links between capital accounting and the prudential framework)

- (iii) developments in asset management planning for infrastructure assets in the intervening period.

2 OBJECTIVES

To evaluate the current approach to the recognition and measurement of infrastructure assets, focusing on the advantages and disadvantages of moving from depreciated historical cost to current value as the measurement base.

3 SUGGESTED APPROACH

3.1 This project is divided into two phases

3.2 Phase I(A): Central Government context

- (i) list all the different types of fixed assets that are included within the definition of infrastructure assets within central government accounts
- (ii) for each type of fixed asset identified, record how the fixed asset is being recognised and measured within central government accounts, including identifying any detailed guidance on this that has been published, and identifying any use of renewals accounting
- (iii) revisit the reasons why central government adopted the policies in (ii), including the anticipated policy and operational benefits.

3.3 Phase I(B): Local Government context

- (i) list all the different types of fixed assets that are included within the definition of infrastructure within the accounts of organisations covered by the local authority accounting SORP. The list in the introduction is not necessarily exhaustive
- (ii) for each type of fixed asset identified:
 - undertake joint working with the RICS to establish what, if any, requirements there currently are on the Valuer for the valuation of such assets
 - undertake joint working with the RICS to establish an outline of what work would be necessary to produce requirements for valuers for the valuation of such assets, that would meet the valuation requirements for local authority assets that are measured at current value
 - investigate and comment on the potential for using renewals accounting (as defined in FRS 15) for that type of fixed asset
 - undertake joint working with DTLR and local government to establish the range of approaches to asset management planning already in use within local government and, by comparison with the Highways Agency, the developments that would be required in order to move to a renewals accounting approach.

3.4 Phase I(C): Other UK experience

Meet with OFWAT, the SRA and relevant regulated companies to understand their experience of the use of renewals accounting and evaluate the operational and management information benefits.

3.5 Phase I(D): Commentary

On the basis of the findings from phases I(A) to I(C) comment on the advantages and disadvantages of moving from a depreciated historical cost to current value for local authority infrastructure assets, including an analysis of the resource implications eg:

- cost of valuations
- benefits of additional management information
- resource implications if depreciation and impairment are required to hit the bottom line of local authority accounts in the future

3.6.1 Phase II: Stakeholder consultation and pilots

- (i) discuss with key stakeholders such as Treasurers' societies, Audit Commission, Audit Scotland and Treasury and assess the likely reaction to proposals for change
- (ii) undertake pilot studies with local authorities.

4 RESPONSIBILITIES

- 4.1 HM Treasury to be invited to undertake Phase I(A), in consultation with the DTLR, NAW and Scottish Executive, and to input to other phases of work as appropriate. The work to be undertaken in liaison with the managers responsible for related components of the review, reporting to John Stanford for overall co-ordination of the capital accounting review.

5 TIMESCALE

- 5.1 Draft report for Phase I(A) to be available by July 2002 for incorporation in the overall report by September 2002.
- 5.2 Phases I(B), I(C) and I(D) to be undertaken in 2003 due to resource constraints.
- 5.3 Detailed requirements for Phase II to be reviewed following the outcome of Phase I.

COMPONENT 3

EVALUATION OF LINKS BETWEEN CAPITAL ACCOUNTING AND THE PRUDENTIAL FRAMEWORK

1 JUSTIFICATION OF PROJECT COMPONENT

- 1.1 This project is a component of the wider review of capital accounting commissioned to examine the future workings of the capital accounting system.
- 1.2 As part of the modernising agenda for the public services, the government is undertaking a review of local authority finance. An important element of this is the introduction of a new prudential framework for local authority capital finance.
- 1.3 In England, the recent white paper *Strong Local Leadership – Quality Public Services* states:

“We will abolish the existing system of credit approvals. It will be replaced by a local prudential regime under which individual authorities will be responsible for deciding how much they can afford to borrow, in accordance with the Code which CIPFA is developing.”
- 1.4 A similar announcement is expected shortly in Wales. In Scotland, consideration is being given as to whether to adopt the prudential framework.
- 1.5 The introduction of the prudential framework, together with the introduction of resource accounting and budgeting in central government, provides an opportunity for a re-evaluation of the relationship between local authority accounting for fixed assets and generally accepted accounting practice (GAAP).
- 1.6 The SORP review conducted by CIPFA/LASAAC in 2001 identified differences between local authority accounting for fixed assets and GAAP that were caused by the current statutory regime for local authorities. Specifically, these relate to the treatment of depreciation, impairment and the income from the disposal of fixed assets.
- 1.7 Whilst the introduction of the prudential framework might eliminate many of these adjustments it seems likely that DTLR and devolved administrations will wish to retain the ring fencing of capital receipts and a statutory over-ride allowing them to define certain expenditure as capital for control purposes. Therefore, as a separate component of the reviews on the capital accounting system, there is a project on the benefits and disbenefits of introducing a local government equivalent of schedule 1 and schedule 2.
- 1.8 However, the white paper for England *Strong Local Leadership – Quality Public Services* states, in relation to the form of government support for local authority capital investment, that some responses to the earlier green paper

highlighted the desirability of moving towards a system that would better reflect true depreciation costs. The white paper further states that the government shares this objective, although there would be issues of affordability to be addressed in such a move. The government proposes to consider the matter further, in consultation with local government “given the breadth of the issues, ... and their links to issues such as the development of better asset management systems and the forthcoming introduction of Whole of Government Accounts.”

- 1.9 CIPFA has already commissioned, through the work of the Prudential Code Steering Group, a review of the potential that depreciation could play in the new prudential framework. It is proposed that this review is completed and fed in to the review of capital accounting as well as to the reviews of local authority finance being undertaken by the DTLR and devolved administrations.

2 OBJECTIVES

- (i) explain the contribution that an accounting solution could make to a system for capital investment by local authorities, matching finance to the rate of consumption of resources equitably over the life of assets
- (ii) summarise the impact that a pure (GAAP) current value depreciation accounting system, with no restrictions on the application of resources to either capital or revenue purposes
- (iii) given the comments in paragraph 1.7 above, also investigate
 - a ‘reserves’ option that would allow any resources generated by depreciation to be reserved on the balance sheet and applied to new capital investment and/or to finance unfinanced capital expenditure
 - a ‘cash’ option that would allow any cash surpluses generated by depreciation to be identified and applied to new capital investment and/or to finance unfinanced capital expenditure.

3 SUGGESTED APPROACH

- 3.1 Project already initiated by Maureen Wellen with Stephen Sheen as consultant, reporting to the Prudential Code Steering Group (PCSG). Output from that project to be fed into the capital accounting review.

4 RESPONSIBILITIES

- 4.1 Maureen Wellen to report on output from the project to the managers responsible for related components of the capital accounting review, reporting to John Stanford for overall co-ordination of the capital accounting review. This is additional to the reports to PCSG and input to consultations by DTLR and devolved administrations as appropriate.

5. TIMESCALE

- 5.1 Draft report to be available by July 2002 for incorporation in the overall report by September 2002.

COMPONENT 4

NOTIONAL INTEREST RATES FOR COST OF CAPITAL CHARGES

1. JUSTIFICATION FOR PROJECT COMPONENT

- 1.1 This project is a component of the wider review of capital accounting commissioned to examine the future workings of the capital accounting system.
- 1.2 The reasons for including this component in the wider review are:
- (i) a widespread perception that the interest rates set by CIPFA/LASAAC overstate local authorities' cost of capital;
 - (ii) concerns expressed by some commentators that the process for setting interest rates is not transparent and accountable
 - (iii) the desirability for harmonisation of accounting policies between the SORP and the Resource Accounting Manual (RAM) to support the Whole of Government Accounts (WGA) project;

2. OBJECTIVE

- 2.1 Considering the conclusions of the project component reviewing the basis for calculating the cost of capital charge, to determine a relevant and robust method for establishing interest rates to be used in calculating the cost of capital charge in the light of practice elsewhere (in particular the Resource Accounting Manual).

3. APPROACH

- 3.1 Review the background and basis for setting interest rates in the SORP and the RAM.
- 3.2 Investigate practice in other parts of the public sector.
- 3.3 Review with CIPFA/LASAAC their current process and suggested amendments to it.
- 3.4 Investigate the views of key stakeholders to the current system and potential solutions.

4. RESPONSIBILITIES

- 4.1 To be undertaken by Kieran Rix in liaison with the managers responsible for related components of the review, reporting to John Stanford for overall co-ordination of the capital accounting review.

5. TIMESCALE

- 5.1 Draft report to be available by July 2002 for incorporation in the overall report by September 2002.

COMPONENT 5

A REVIEW OF THE ELEMENTS INCLUDED WITHIN THE SCOPE OF CAPITAL CHARGES

1. JUSTIFICATION FOR PROJECT COMPONENT
 - 1.1 This project is a component of the wider review of capital accounting commissioned to examine the future workings of the capital accounting system.
 - 1.2 The Resource Accounting Manual (RAM) includes provision (paragraph 7.4.1) for the Operating Cost Statement to be credited with a “capital charge” for current assets and liabilities, representing the extent to which the assets of the entity have been financed by liabilities thus reducing the need for, and cost of, taxpayers’ equity.
 - 1.3 The reasons for including this component in the wider review are:
 - (i) Convergence between the SORP and RAM is necessary to facilitate the Whole of Government Accounts (WGA) project
 - (ii) Equality of treatment between different parts of the public sector is desirable both in itself and to enhance comparability.
2. OBJECTIVE
 - 2.1 To determine an appropriate basis for calculating the cost of capital charge in the light of practice elsewhere (in particular the Resource Accounting Manual).
3. SUGGESTED APPROACH
 - 3.1 Review basis and reasoning for the calculation of the cost of capital charges in the SORP and the RAM.
 - 3.2 Investigate practice in other parts of the public and private sectors.
 - 3.3 Consult key stakeholders for views and suggestions.
4. RESPONSIBILITIES
 - 4.1 To be undertaken by Kieran Rix in liaison with the managers responsible for related components of the review, reporting to John Stanford for overall co-ordination of the capital accounting review.
5. TIMESCALE
 - 5.1 Draft report to be available by July 2002 for incorporation in the overall report by September 2002.

COMPONENT 6

BENEFITS AND DISBENEFITS OF INTRODUCING A LOCAL GOVERNMENT EQUIVALENT OF SCHEDULE 1 AND SCHEDULE 2

1 JUSTIFICATION FOR PROJECT COMPONENT

- 1.1 This project is a component of the wider review of capital accounting commissioned to examine the future workings of the capital accounting system.
- 1.2 The introduction of a local government primary statement, based on Schedule 1, *Summary of Resource Outturn* in the central government RAM, has been suggested by key stakeholders, including the Audit Commission and Treasury. The purpose of Schedule 1 would be to link annual financing requirements to net operating expenditure, by recognising accruals adjustments required by control frameworks. Whilst introduction of such a statement is not directly linked to the capital accounting framework the majority of the adjustments which would be reflected in a Schedule 1 style Statement would be capital related.
- 1.3 Whilst the introduction of the Prudential Framework might eliminate many of these adjustments it seems likely that DTLR (and devolved administrations) will wish to retain the ring-fencing of capital receipts and a statutory over-ride allowing them to define certain expenditure as capital for control purposes. Therefore it is appropriate to include this analysis within the scope of this Review. Introduction of a Schedule 1 type statement would necessitate modifications to the existing format of the consolidated revenue account, possibly so that it resembles the Schedule 2, *Operating Cost Statement* in the RAM.
- 1.4 There is also a view from some stakeholders, most notably the Audit Commission in its recent Think piece, that the paucity of budgetary information in the financial statements, limits their usefulness for readers.

2 OBJECTIVES

- 2.1 To consider and make a recommendation for consideration by the CIPFA/LASAAC Joint Committee on the merits of introducing a primary financial statement based on Schedule 1, *Summary of Resource Outturn* in the RAM. The conclusion should consider how any changes comply with UK GAAP and the possible implications of the introduction to UK GAAP of a single performance statement as envisaged in FRED 22, *Reporting Financial Performance*. The changes should also be assessed from the perspectives of user understandability and practicality for accounts preparers.
- 2.2 To consider related changes to the format of the consolidated revenue account.
- 2.3 To consider whether a Schedule 1 type Statement should include budget information.

2.4 To produce illustrative examples for a local authority.

3 APPROACH

3.1 Review the current requirements in the SORP and the RAM.

3.2 Investigate practice in other parts of the public and not-for-profit sectors.

3.3 Discuss with key stakeholders such as Treasurers' societies, Audit Commission, Audit Scotland and Treasury and assess the likely reaction to proposals for change.

4 RESPONSIBILITIES

4.1 To be undertaken by Harry Wilkinson in liaison with the managers responsible for related components of the review, reporting to John Stanford for overall co-ordination of the capital accounting review.

5 TIMESCALE

5.1 Draft report to be available by July 2002 for incorporation in the overall report by September 2002.

COMPONENT 7

A REVIEW OF THE RECOGNITION, MEASUREMENT AND CHARGING OF NON-OPERATIONAL AND COMMUNITY ASSETS

1 JUSTIFICATION FOR PROJECT COMPONENT

- 1.1 This project is a component of the wider review of capital accounting commissioned to examine the future workings of the capital accounting system.
- 1.2 The SORP includes non-operational assets as one of the categories for recognition of fixed assets in the consolidated balance sheet. The Accounting Policies section of the SORP requires non-operational land and properties to be measured at the lower of net current replacement cost or net realisable value. In the case of investment property this will normally be open market value.
- 1.3 The SORP defines non-operational assets as “fixed assets held by a local authority but not directly occupied, used or consumed in the delivery of services. Examples of non-operational assets are investment properties and assets that are surplus to requirements, pending sale or redevelopment.”
- 1.4 Further guidance is given in the *Capital Accounting Guidance Notes*. This states that “non-operational assets are held by an organisation but not directly occupied, used or consumed in the delivery of services.” Examples of non-operational assets may include:
 - investment and commercial property, usually occupied by tenants from which an income is derived and which may be held for economic or social activities such as employment opportunities
 - vacant property or property temporarily occupied for another purpose but awaiting either development or disposal
 - land and buildings in the course of development but not yet completed and occupied for the proposed service
- 1.5 The Guidance states “the definition of operational assets implies that if an organisation has passed responsibility for control of the management of the property (and all associated running costs, outgoings and repairs) to a contractor or external service provider the property is no longer operational in the strict interpretation of the definition. However, where a public service body delivers a service through a third party by means of a management agreement, the third party occupies property owned by the body under a lease or licence and the body retains effective control of and responsibility for the property, the property may be regarded as operational.”
- 1.6 Questions have arisen with respect to the categorisation of assets. In particular, ostensibly quite similar assets may be owned by different authorities for different purposes, e.g. commercial units, which may be held either for investment purposes or for service (economic development)

purposes. The Guidance Notes state that a practical test is whether the authority is seeking to achieve a particular policy objective through the use of the asset by another organisation. They state that “assets owned by an authority but used by another organisation (not for providing the authority’s services) should be treated as non-operational for the owning body.”

- 1.7 Impressionistic evidence suggests that users do not find the current requirements and guidance straightforward to interpret and that there are probably diverse practices amongst accounts-preparers. In particular it appears that the non -occupational category may be used more widely than anticipated and that the dividing line between investment property and property primarily held for a service delivery purpose is narrow, especially in areas like economic development.
- 1.8 There are also issues related to capital charges. Currently the SORP requires that service revenue accounts should be charged with a capital charge and, where required, any related impairment loss (related to a consumption of economic benefits) for all fixed assets used in the provision of the service. Logically, charges cannot be made for assets which are not used in service provision. The Best Value Accounting Code of Practice reflects this in not requiring capital charges to be made to services for the purposes of determining “total cost.” It is thus clear that no capital charges should be made to services for non-operational assets. However, the question of whether capital charges for non-operational assets should be made elsewhere within the accounts of local authorities has not to date been addressed. Therefore, there is a tacit implication that non-operational assets should be outside the capital charging framework. In terms of depreciation and impairment it is questionable whether this treatment is appropriate for all non-operational assets.
- 1.9 Community assets are a separate category of assets, which share some of the characteristics of non-operational assets (i.e. they may not be held for operational purposes, but because of their value to the community). Community assets are defined by the SORP as:
- 1.10 The SORP requires that community assets are recognised on the balance sheet and measured at historical cost, net of depreciation where relevant. There are no specific requirements in the SORP related to the charges to revenue for community assets, although usual depreciation rules would apply to community assets with a finite life. There is also no specific requirement for capital charges made to services in respect of community assets.
- 1.11 The category of community assets is not recognised in UK-GAAP, being generally not relevant in the private sector. The Resource Accounting Manual (RAM) contains a category of heritage assets. The treatment of heritage assets depends on whether they are used for operational purposes. The RAM also contains specific rules for the recognition and measurement of donated assets (which may or may not be heritage assets).

2 OBJECTIVES

2.1 To consider the appropriateness of the current requirements and guidance relating to the recognition, measurement, depreciation and charging to revenue of non-operational and community assets, and make recommendations for change.

2.2 In so doing:

(i) to compare accounting treatments with those in central government.

(ii) to evaluate how current approaches are in accordance with UK GAAP.

(iii) to compare approaches with those in International Public Sector Accounting Standards.

3 SUGGESTED APPROACH

3.1 Review current requirements and guidance in the SORP and Capital Accounting Guidance Notes.

3.2 Ascertain extent to which current approaches are in accordance with guidance issued by RICS.

3.3 Consider extent to which current approaches meet the requirements of FRS 11, *Impairment* and FRS 15, *Tangible Fixed Assets*.

3.4 Compare current approaches with those in the RAM.

3.5 Compare current approaches with those in IPSAS 16, *Investment Property* and IPSAS 17, *Property Plant and Equipment*.

3.6 Discuss with key stakeholders.

4 RESPONSIBILITIES

4.1 To be undertaken by Harry Wilkinson in liaison with the managers responsible for related components of the review, reporting to John Stanford for overall co-ordination of the capital accounting review.

5. TIMESCALE

5.1 Draft report to be available by July 2002 for incorporation in the overall report by September 2002.