



HOUSING SORP 2014: INVITATION TO COMMENT ON REVISED IMPAIRMENT GUIDANCE

ICAEW welcomes the opportunity to comment on the exposure draft *Housing SORP 2014 Impairment section* published by the National Housing Federation on 10 April 2014, a copy of which is available from this [link](#).

This response reflects consultation with the Social Housing subcommittee of the ICAEW Business Law Committee and with the Financial Reporting Faculty. The Business Law Committee includes representatives from public practice and the business community and is responsible for ICAEW policy on business law issues and related submissions to legislators, regulators and other external bodies. The Financial Reporting Faculty is recognised internationally as a leading authority on financial reporting and, through its Financial Reporting Committee, is responsible for formulating ICAEW policy on financial reporting issues and makes submissions to standard setters and other external bodies on behalf of ICAEW. The Faculty provides an extensive range of services to its members including providing practical assistance with common financial reporting problems.

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MAJOR POINTS

1. In our response dated 14 February 2014 to the Invitation to comment on the draft SORP, we stated our view that it is essential that the SORP both confirms that 27.20A is applicable to social housing assets and that the SORP gives guidance on the application of 27.20A to the measurement of recoverable amount whilst assessing potential impairment of social housing assets. We therefore welcome this proposed revised guidance.
2. We have answered the questions in the consultation document as set out below; however, we have two general comments which are very important in relation to impairment guidance.
3. The first comment is that our responses to the guidance set out below assume that the general principles behind 'cross subsidy accounting' as described in the current SORP (2010) paragraph 164 are essential for a true and fair view. Consequently, if this paragraph were removed in the revised SORP, in our view none of the proposed treatments outlined below would be appropriate. Our response is, therefore, conditional on the retention of the cross subsidy accounting principles, which in our view are consistent with the requirements of paragraph 23.20 of FRS102. In the event that the cross subsidy accounting principles are not reflected in the revised SORP, we strongly recommend that a further consultation takes place so that the issue can be properly evaluated.
4. The second comment is that the proposals on impairment do not specifically address the question of impairment where grant funded property is carried at valuation and consequently the performance model has been applied. If the proposal is that grant will be taken to income but at the same time no impairment is recognised on an asset which the grant has funded, then, in line with the cross subsidy accounting principles, we do not think this would be consistent with a true and fair view if the asset constructed had a value lower than cost. In that situation, recording a gain through income whilst recording a downward revaluation through reserves would be perverse.

RESPONSES TO SPECIFIC QUESTIONS

Q3: Do you agree with the SORP Working Party's conclusion that the assessment of whether a property is held for its service potential should be consistent with the principles set out in the earlier section of the SORP for classifying a housing property as property, plant and equipment or investment property based on its intended use?

5. Yes.
6. It needs to be made clear that the principle of holding properties for their social benefit should apply to non-housing property assets where these are integral to the social housing service being provided, for example shops selected by the social housing provider (RP) to preserve neighbourhood amenities. Garages might also be classified as held for social benefit rather than for investment or other purpose, if the intended use is to assist residents of social housing property with their enjoyment of the property. Non-housing property that should not be treated as for social benefit includes office space used by the registered provider, even though it may benefit or reduce the cost of the social benefit provided by the registered provider of social housing (RP). Property such as student accommodation may be held either for its social benefit or as an investment, depending on the objective of the registered provider. We therefore recommend an additional sentence to the introductory paragraphs of section 14 to clarify that if a property is not held for social benefit, then the service potential provisions may not be applied in any measurement of impairment. In some cases, the asset would have been classified as an investment property, but not always (for example where it is office space used by the RP itself).

Q4: If the SORP permits social landlords to use VIU-SP as an alternative estimation technique in determining value in use when performing an impairment assessment, do you consider that the resulting financial statements would provide sufficient, relevant and reliable information to the users of those financial statements, provided appropriate additional disclosures were made setting out the extent to which it has been applied?

7. Yes.

Q5: Would the use of a purely cash flow based estimate (ie value in use) in determining the recoverable amount of social housing properties provide more relevant and reliable information for users?

8. No.

Q6: Do you agree that depreciated replacement cost provides an appropriate measurement basis for assets held for their service potential?

9. Yes.

10. We consider that DRC should be the method used to assess VIU-SP in order to achieve consistency across the sector. Paragraph 14.28 allows the use of alternative models but we recommend that it be made clearer that circumstances where DRC does not provide the best basis for a true and fair view are likely to be rare. In such circumstances, the departure from SORP should be justified and the basis of measurement explained in the notes to the accounts.

Q7: If not, what alternative measures would be more appropriate?

11. Not applicable.

Q8: Is there sufficient guidance in paragraphs 14.25 and 14.26 to explain the calculation of depreciated replacement cost?

12. No.

13. We consider that the proposed guidance may not work well in practice. There are three possible bases for calculating DRC:

- 1) construction of a new property with the same service potential as the original asset**
- 2) purchase of an equivalent property from another registered provider**
- 3) purchase of an equivalent property on the open market, possibly with part of the cost being met (reduced) by social housing grant.**

14. However, we do not consider that DRC should include the second of the three unless there was a reasonably likely prospect that the RP would be in a position to purchase equivalent units from other RPs of a similar nature. This would therefore require there to be an active market at the year end, rather than just a theoretical option of purchasing a property that was not actually being offered for sale. We also note that DRC based on estimated construction costs (1) and equivalent market price (3) can be appraised objectively, whereas there is no objective basis for testing the cost put on the purchase of an equivalent property from another RP in the absence of an active market (2)

15. We do not agree that the cost of replacing the land should be included in the DRC calculation under the first basis above, because the RP already owns the land. In this situation, DRC should be estimated using the existing carrying value of the land on which the new property is being theoretically constructed combined with the cost of constructing the property. The only circumstances in which current land costs would have to be taken into account when assessing DRC from the perspective of construction of a new property on an existing site would be where money needed to be spent on the land itself, for example if it were contaminated or subject to some other defect.

16. DRC should be the cost of constructing or acquiring an asset to provide the same level of service potential. Thus, if a property had some features that were of benefit to the tenant (eg, energy efficiency measures) then it would be appropriate to capture this in assessing DRC. On the other hand, DRC should not be inflated by unnecessary costs. Where technological advances mean that the specification for a property can be met at a lower cost than that of the original, this should be reflected in the assessment of DRC.

17. Paragraph 14.27 states that the depreciation in the context of DRC is 'not the same as the depreciation charged.' This paragraph should make more explicit that depreciation in the context of DRC applies the same principles as depreciation used for financial reporting purposes, but should not be assumed to be the same amount given that the costs may be different. In other respects, it is the same.

Q9: If not, would the inclusion of worked examples be of assistance in applying this guidance?

18. Yes. The practical points raised in answer to Question 8 show the need for examples with numbers to articulate the underlying principles.

Q10: Are the disclosure requirements of paragraph 14.42 sufficient? If not, what further disclosures are required?

19. Yes.

Q11: Should a social landlord be required to disclose the value in use of a cash generating unit if it chooses to use the VIU-SP estimation technique in performing an impairment assessment?

20. No.

21. Further disclosures should not be necessary if the accounts provide sufficient, clear information about the measurement method and assumptions used.

Q12: Is the redrafted impairment section sufficiently clear that an impairment assessment is only required where there is an indicator of impairment?

22. Yes.

23. However, we have the following comments on the detail of paragraph 14.5:

- In 14.5(b), we recommend that the words 'rent that can be charged' should be changed to 'net income that is expected to be collected less relevant expenditure';
- In 14.5(e) we recommend that the SORP defines what is meant by the words 'where there is a plan'. We note that the example refers to 'probable'.
- Further guidance should be provided on what is meant by 'material' in its various contexts. This might be illustrated by some specific examples indicating how the RP is meant to judge whether an event is material.

24. We do not understand the purpose of including the reference to Section 18 of the draft revised SORP (*Intangible Assets other than Goodwill*).

Q13: If not, what further information is required?

25. Not applicable.

Q14: Does the section setting out the indicators of impairments provide sufficient guidance to social landlords to understand when there may be an indicator necessitating an impairment assessment?

26. No.

Q15: If not, what further guidance is considered necessary / useful?

- 27.** We recommend that paragraph 14.5 needs to make it clearer that the five 'most common' indicators identified do not constitute a comprehensive list. There may be circumstances in which none of the listed indicators exist, but the RP is aware of other factors that either individually or collectively indicate impairment. In all cases, where there is impairment, and it is material, it will need to be measured and the carrying value reduced.
- 28.** As an example, consider the situation where an RP has completed a complex scheme with various parts to it. If the RP was aware that both VIU and fair value less costs to sell were less than carrying value on an historic cost basis of the elements of the scheme it has retained, and at the same time it has recorded a gain either from disposals of assets or grant treated under the performance model, then this should be regarded as an indicator of impairment.

Q16: Do you agree with the guidance set out in this draft section of the SORP for determining cash generating units?

- 29.** Yes.
- 30.** However, the guidance needs to be more precise on the conditions attaching to the identification of cash inflows for the group as independent of other groups or assets. By 'precision', we mean that the principles for grouping assets should be clearly spelt out, not the criteria. The bus company illustrative example in the consultation paper is useful but it needs to be extended to show how, in the context of a housing association, the components of a CGU might change once an asset has moved from development into management. We therefore recommend that the SORP explain more clearly that when a development is completed the CGUs may change.

Q17: If not, why?

- 31.** Not applicable.

Q18: Is there sufficient guidance included within the SORP to enable social landlords to determine cash generating units within their individual business?

Q19: If not, what additional guidance is required?

- 32.** Both questions covered by comments at Q16 above.

Q20: Do you agree that value in use should be available to a social landlord as a method of measuring recoverable amount for the purposes of impairment?

- 33.** Yes.

Q21: If not, why?

- 34.** Not applicable.

Q22: Do the worked examples included in the impairment section provide sufficient guidance for social landlords to apply the principles set out in the SORP?

- 35.** Yes.

- 36.** However, as in our comments under Question 9 above, we recommend the use of examples with numbers to articulate the underlying principles.

- 37.** We also recommend that an alternative be found to the use of the term 'loss' in Example 1.

Q23: If not, what further examples would be of value in applying FRS 102 and the SORP when assessing impairment of social housing properties? Please provide brief details as to what examples would be of value.

38. Not applicable.

Q24: Is it sufficiently clear how accounting for government grant interacts with impairment?

39. No.

Q25: If not, why?

40. We recommend that example 3 be extended to show the effect of impairment on the related grant.

41. We also recommend an additional example to cover the interaction of grant and impairment in relation to property, plant and equipment (PPE). If PPE is carried at cost less depreciation, then the associated grant has to be carried using the accrual model, which means in effect at amortised cost also. When considering impairment, the carrying value is considered to be the PPE carrying value less the grant less amortisation. There was a request to show as an example how this worked.

OTHER COMMENTS

42. Apart from the major points above, we have some additional comments that do not address the specific questions asked in the consultation.

43. We consider that some more clarity on the disclosures relating to inclusion of impairment loss/reversal of impairment loss (paragraphs 14.33 and 14.36) in the Statement of Comprehensive Income, such as a separate line in a note, would be helpful.

44. We do not consider that paragraphs 14.35 and 14.37 to 14.39 add significantly to the utility of the SORP and on the basis that the SORP should focus on issues where there is a specific RP point to be made (and be silent on issues where there is not), we suggest that the paragraphs be deleted.