

Mr A O'Connor
Accounting Standards Board
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Dear Mr O'Connor

Financial Reporting Exposure Draft 40 'Accounting for heritage assets'

Our firm welcomes this opportunity to comment on the above exposure draft and are pleased that the Accounting Standards Board is seeking to address inconsistencies in the financial reporting of heritage assets. We also appreciate that difficulties that arise in forming an acceptable accounting standard for such assets.

However, although FRED 40 might bring improvements, (albeit that some inconsistency will remain in the financial reporting of heritage assets), there is a risk that the costs of implementing the proposed standard might outweigh the benefits that would be derived.

Our response to the specific questions raised in the invitation to comment is included in the attached appendix along with our observations and concerns raised.

Yours faithfully

BDO Stoy Hayward LLP

APPENDIX**RESPONSE TO THE INVITATION TO COMMENT ON FRED 40**

1 Do you agree that rather than the current arrangements, under which entities generally capitalise only recently acquired heritage assets at cost, the requirement should be that an entity should, where practicable, adopt a valuation approach for its heritage assets?

This [draft] FRS requires a valuation approach where practicable but, where this is not practicable, prescribes a non-recognition approach. Do you agree this proposal will lead to an improvement in the quality of the financial reporting of heritage assets?

We agree that the current practice which has evolved in accounting for heritage assets (as highlighted in paragraph 1 of Appendix 1 to the FRED) does not provide a very satisfactory basis for accounting for such assets. A greater level of consistency and comparability between entities in reported amounts and disclosures would be helpful.

A valuation approach, where practicable, would therefore remove certain of the inconsistencies that have developed and represent an improvement in financial reporting.

We disagree with the proposed approach of non recognition where a valuation approach is not practicable. Instead, we consider that entities which are unable to value their heritage assets should continue to account for their heritage assets at cost.

2 This [draft] FRS proposes the assessment of practicability should be applied to individual collections rather than for the entity's total holding of heritage assets (see paragraphs 22 and 23 of Appendix I). Do you agree?

We agree. While the approach outlined in the Discussion Paper, of determining practicability at entity rather than collection level, would result in a consistent approach at entity level, the proposals set out in the FRED are preferable. Assessing practicability at entity level might lead to collections that would otherwise be capable of being recorded at fair value not being recognised, due to it being impracticable to value only one out of a number of collections held.

3 If the approach is to be determined at the level of an individual collection, it is necessary to define the term 'collection'. Do you consider the definition proposed in paragraph 4 of the [draft] FRS is appropriate? If not, what alternative would you propose and why?

The proposed definition in paragraph 4 begins with a 'group of artefacts, exhibits or other items'. We suggest that it might refer instead to 'a group of heritage assets' to link the definition of a collection to that of individual assets.

We note that the definition of a collection includes the manner in which a group of heritage assets is managed (with a distinction being made between those which are managed separately and those which are managed together). However, it is not entirely clear whether the term 'managed' refers specifically to the location of heritage assets and how they are arranged for public inspection, or whether the definition is intended to include the manner in which the entity itself is structured for the purpose of managing its heritage assets. It would be helpful if this was clarified; this would also assist in determining whether and when a single heritage asset might be considered to be managed separately.

4 The [draft] FRS proposes the approach should be determined for individual collections following an assessment of whether it is practicable to obtain valuations that provide useful and relevant information. This assessment will include consideration of the relevance of valuations as well as their reliability and the costs and benefits of obtaining them.

Do you support this approach or would you prefer that the approach emphasises that valuation is required only where the valuation is reliable? If you believe that a reliability approach, or some other approach, should be adopted, what guidance would you see as being necessary to assess the reliability of valuations?

We consider that all valuations undertaken need to provide information that is both reliable and relevant to the assets being valued. While the criteria 'useful and relevant' imply an additional requirement for reliability (otherwise it is difficult to see how it could properly be regarded as useful and relevant), we consider that reliability of measurement should be an explicit requirement.

5 Do you consider that the proposals will cause auditors significant difficulties when assessing an entity's approach, particularly in terms of applying the assessment of practicability at the level of an individual collection? Where a valuation approach is adopted, do you think auditors will face further difficulties in evaluating the valuations being reported?

We do not consider that the proposals will necessarily cause auditors significant difficulties although we do have some concerns which are outlined below. However, where a valuations approach is not adopted due to impracticability, the current disclosures proposed might lead some preparers to include brief and uninformative disclosures. We suggest that the disclosure requirements are enhanced, such that sufficient information is included that will enable a reader of the financial statements fully to understand the reason(s) for the impracticability.

We note that paragraph 14 of the FRED does not include any prescribed minimum period between valuations, instead noting that valuations must be carried out with sufficient frequency to ensure that they meet the objective described in paragraph 8 which requires the entity to supplement valuations to assist in an assessment of the value of the collection at the balance sheet date. This might cause auditors certain difficulties, as paragraphs 8 and 14 imply a requirement to assess the fair value of collections at each balance sheet date and whether the fair value has changed significantly from the date of the last valuation. In the absence of an up to date valuation at the balance sheet date it may be difficult for the auditor to make a reasonable assessment as to the adequacy of a valuation done for a previous financial year without significant additional work or specialist involvement.

Whilst FRED 40 exempts entities from adopting FRS 11 it may also be difficult for auditors to identify whether impairments or diminutions in value of heritage assets have occurred between valuation dates.

Paragraph 19 of FRED 40 proposes disclosures about the entity's policy for the acquisition, preservation, management and disposal of heritage assets, including the extent to which access to the assets is permitted. If these disclosures are not given in the financial statements, it is noted that these may instead be given in a separate document which sets out this information. If such a cross reference is made to a separate document then this will need to be audited in order to ensure that the disclosure requirements of the paragraph are met. In such cases, it would be helpful to specify that the disclosures would need to be in a separate and specifically identifiable part of that separate document.

6 The [draft] FRS requires that where an entity adopts a non-recognition approach for some or all of its collections, acquisitions and disposals of heritage assets should not be reported in the profit and loss account or equivalent statement. Do you agree?

As noted above, we disagree with the proposals for non-recognition of heritage assets where it is not practicable to obtain a valuation. Instead, such assets should be reported at cost.

The costs of acquisitions and the proceeds on disposal of heritage assets, whether reported at valuation or at cost, would still remain a part of the normal operating activities of an entity (as would expenditure on major restoration costs). We therefore consider that the acquisition and disposal of heritage assets carried at cost should be reported in a similar manner to those held at valuation.

7 The proposals require enhanced disclosures of heritage assets. Do you consider the nature and extent of the required disclosures are appropriate? Do you consider any of the disclosure requirements are unduly onerous?

Paragraph 21 (i) of the FRED requires the carrying amount of heritage assets analysed by principal collection. From the definitions in the FRED it is not entirely clear what 'principal collection' means in the context of the defined term 'collection'. It would be helpful if this was clarified.

The disclosure requirements set out in paragraph 22 are of key importance in terms of understanding the nature and the types of assets that are excluded from a valuations approach. However if there are significant limitations on the amount of information for valuation purposes, this could result in information disclosed in accordance with paragraph 22 being unreliable and potentially misleading. We suggest that the disclosure requirement is limited to information that has certain qualitative aspects, such as recent market transactions for assets that are similar to certain of the assets held in a particular collection.

Where this type of information is not available, paragraph 22 should be amended to require disclosure of the nature of collections which have not been included in the entity's financial statements (we note that disclosure of the reasons why a valuation is impracticable are already required by paragraph 20).

We consider that the disclosures required in Paragraph 23 are excessive and that they should be required for the current and preceding financial period only. A five year analysis may provide useful information but we believe that such an analysis should only be disclosed on a voluntary basis. Such a five year analysis of asset movements is currently not required by paragraph 100 of FRS 15 'Tangible fixed assets'.

Paragraph 24 of the FRED allows only voluntary disclosure for the sources of funding for acquisition of heritage assets, or expenditure on major restoration costs. However, this might conflict with FRS 8 'Related party transactions'. For example if a related party (in accordance with the definition under FRS 8) had lent the entity monies in order to acquire such assets then this would seem to be a required disclosure. We suggest that either a cross reference is made to FRS 8, or a specific exemption is given.

8 The definition of a heritage asset is set out in paragraph 4 of the [draft] FRS and the scope of the proposed new standard is set out in paragraph 5. The rationale for these is discussed in paragraphs 7 to 12 of Appendix 1. Do you agree with the proposed definition and scope?

We consider that additional guidance would be helpful to clarify the definition and scope of the draft FRS and to be more specific. In particular, we consider that the definition should refer to an entity's single objective being in relation to heritage assets, rather than it being 'a principal objective'.

As an example, certain commercial entities may have a wide range of objectives and activities, and may at the same time own a collection of heritage assets which are important to the entity's history and are available for the public to inspect at, for example a museum on the factory premises. Such a collection might be viewed as being an important marketing tool. This would imply that 'a' principal objective of that entity might be in relation to its heritage assets. Whilst paragraph 10 of the appendix does clarify the scope of FRED 40 in this regard, it is not quite clear and in some cases it may be difficult to judge with certainty whether heritage assets would need to be accounted for in accordance with this FRED.

We also note that paragraph 6 states that buildings that are a primarily used to provide office accommodation or teaching facilities should not be accounted for as heritage assets. However, certain buildings may provide a dual purpose, such as a Church or Cathedral of historical significance which may be open to the public as well as being used for the purposes of religious worship. Further guidance would be helpful in determining how to account for such buildings.

9 As explained in paragraphs 8 to 12 of the Preface, the Board believes the costs of implementing the proposals should not be disproportionate. Do you agree? It would be particularly helpful if any significant costs that would arise on implementation of the proposals (including any not identified above) could be identified and quantified.

We do not believe that paragraphs 8 to 12 within the preface fully address the effect of the FRED on both smaller (above the thresholds for FRSSE exemption) and larger entities that would fall under the scope of the FRED.

An entity which owns only a small collection of heritage assets may find that the initial cost of obtaining valuations may not be a significant amount. However these costs may cumulatively become significant over a period of time.

Although larger entities might have more financial resources which would be available to absorb the costs of the initial implementation and ongoing requirements of the FRED, this may be at the expense of not undertaking certain restoration projects or acquiring heritage assets in the future.

We are concerned that the cumulative costs of accounting under the proposed standard could affect an entity's objective of maintaining heritage assets and thus restrict them from increasing the size of their collections of heritage assets in the future. This would seem an undesirable result of an accounting standard that applies to what is often a not for profit sector.

There may also be significant additional costs in respect of audit services for those entities that are within the scope of the FRED due to the need for specialist input. Such costs would also need to be considered in arriving at the overall costs of implementing the proposals.

Finally, we have reservations about the extent to which management and staff time would be required in terms of evaluating collections, collating valuations and analysing this for the purposes of internal record keeping and the maintenance of accounting records.