Valuing Heritage Assets

Final Report of a Research Project

Examining the case for the Valuation of Heritage Assets

Prepared by Kingston University on behalf of RICS and HM Treasury

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- granting interviews to members of the Research Team and in some cases providing site visits;
- participating in workshops to pursue emerging ideas and in some cases; and
- in responding to a consultation draft.

We have not listed all these in order to ensure that their confidentiality is maintained. To all of them we express our collective gratitude.

Whilst this report raises more issues than it can solve, we hope that it provides further stimulus to what is undoubtedly a vital question for our time, which is, how can we best assure the long-term future and good stewardship of our natural, built and created heritage? Without addressing such issues, we may be considered to be falling short of our duty to future generations.

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Executive summary

1. This report summarises the results of the research carried out by Kingston University on behalf of the Royal Institution of Chartered Surveyors (RICS) and HM Treasury. This unique funding partnership reflects the importance of heritage assets from both a valuation perspective and also a public sector financial reporting perspective. The report seeks to explore issues surrounding the valuation of assets within the balance sheets of both public and private sector organisations. It does not consider the valuation of assets for other purposes, except insofar as these might relate to asset valuations.

2. The report provides a background to the treatment of heritage assets within standard accounting practice and proposals to review and alter their treatment, as set out in the Accounting Standards Boards (ASB) Financial Reporting Exposure Drafts (FRED) 40 and 42. It concurs with ASB that the current system of accounting for heritage is inconsistent and may be unhelpful to those who rely on such accounts.

3. The work which is reported here was carried out primarily during 2007 but publication was delayed in order to obtain wide consultation and to incorporate the revised proposals of ASB contained in FRED 42, published in 2008.

4. The definition and classification of heritage assets are reviewed and the conclusion drawn that there is a need to review definitions better to recognise that some forms of heritage assets are irreplaceable and could be deemed to be 'National Treasures' whilst other, though very much part of heritage, are held within a context whereby they are capable of substitution. It further concludes that there is a rationale for treating 'National Treasures' differently from other heritage assets within a valuation and accounting framework.

5. The benefits and challenges of recognising heritage assets within the balance sheet are considered and, whilst recognising that the challenges are very real, concludes that where sufficient information is available to enable a reliable valuation the benefits could be sufficient to outweigh the challenges.

6. Heritage assets fall into sub-categories: real estate, including natural topography and historic landscapes and portable property. The range of possible valuation methods that can be applied to each sub-category is considered. It is concluded that for many heritage assets which do not fall to be considered as National Treasures, it is practical to establish market Value using transactional evidence. Those that are deemed to be National Treasures are deemed to be inappropriate to value with reference to the market or to a cost basis.

7. Whilst arguing that many heritage assets are capable of being valued to Market Value using conventional techniques, the report concludes that many are not. For such assets, the use of a cost approach is also inappropriate. Accordingly, it puts forward for debate some possible alternative methodologies that could be considered appropriate to provide owners and their stakeholders with better information as to the worth of their assets.

Executive summary

8. A series of recommendations are made as set out below:

- The international community of accountants, valuers and other advisors seek a common definition of heritage assets.
- The valuation of heritage assets for balance sheets should be encouraged or required where a meaningful figure using conventional approaches can be produced. It is recognised that such a recommendation is unlikely to be fully accepted in the short-term but, despite the challenges such valuations would present, the benefits to all stakeholders could be very real.
- Where valuations of real estate are undertaken, they are discussed with the client and take account of full market evidence. The use of Depreciated Replacement Cost is not normally considered appropriate for heritage assets; instead valuers should use the full range of conventional market-based techniques, even where these may reveal a negative value.
- For valuations of portable property, a market value approach is recommended, taking due account of issues of 'lotting' and 'locational connectivity'.
- A new sub-classification of heritage assets, National Treasure, should be recognised within accounting processes as being of high worth but incapable of explicit valuation. Such assets, it is suggested, could be subject to disclosure but not valuation.
- In order to enable enhanced knowledge to support effective decision-making, further research should be conducted into the possible applicability of a range of non-market valuation techniques such as willingness to pay and cost benefit analysis, to support a deeper understanding of worth to the community.
- Where a non-recognition approach to heritage assets is adopted, it is recommended that consideration be given to undertaking shadow accounting in order better to enable the aims and objectives of owning and stewardship organisations to be met.

01 Background to the research project

UK Concerns

1.1 The issue of whether heritage assets should be recognised on the balance sheet is longstanding. It has been in existence since entities holding heritage assets were required to prepare accruals based accounts. In the UK, the Accounting Standards Board (ASB) issued Financial Reporting Standard (FRS) 15 Tangible Fixed Assets in February 1999. The objective of FRS 15 is to achieve consistency in the initial measurement, valuation, depreciation and disclosure of tangible fixed assets. The provisions of FRS 15 allow for properties to be entered in the books at cost, and where a policy of revaluation is adopted, at valuation, normally to market value. It this intends that those relying on the accounts are provided with as clear and accurate an account of an organisations' financial asset base as it possible to achieve. In paragraph 50 of the section on the development of the standard, it is clear that the ASB intended FRS 15 to apply to heritage assets. In practice, the public sector applied FRS 15 only *prospectively* – that is, additions to heritage collections were recognised on balance sheet from, in most cases, 1 April 2001, and measured at acquisition cost (or donated value). Typically this valuation is only entered when the cost information is available without 'significant additional cost'. The result is that only a fraction of assets are reflected in the balance sheet. For the bulk of assets, many of which have been in collections for many years, there is no record of valuation.

1.2 The ASB and many key heritage groups view this situation as anomalous and misleading. There is also a realisation that the application of different accounting treatments to similar assets can lead to internal inconsistencies in terms of management decisions including strategic direction of portfolio development; further the quality of disclosure of assets is uneven. The view taken now is that the situation requires resolution with a consistent approach being adopted so that assets are treated the same way regardless of the date of acquisition.

1.3 In the light of these concerns, the ASB published a discussion paper *Heritage assets: can accounting do better?* in January 2006. The changes put forward in the discussion paper suggested that heritage assets should be valued, not depending on when they were acquired by their owners, but on whether or not it is possible to produce figures that are 'useful and relevant'. This intention presents challenges to both the owning community and their advisors.

International Concerns

1.4 The debate regarding the nature of heritage assets and their recognition (or otherwise) on the balance sheet is not restricted to the UK. International Public Sector Accounting Standard (IPSAS) 17 *Property, Plant and Equipment* (based on International Accounting Standard (IAS) 16 *Property, Plant and Equipment*) was issued in December 2001. IPSAS 17.7 does not require an entity to recognise heritage assets that would otherwise meet the definition of property, plant and equipment. The International Public Sector Accounting Standards Board (IPSASB) is actively considering the matter of heritage assets, and in 2006 consulted in the light of the ASB's initiative. Subsequently, in March 2007, IPSASB decided to carry out further analysis before determining whether to produce a new standard for heritage assets or make amendments to IPSAS 17. In reaching this decision, the Board identified a need to look more closely at the issues of definition of heritage assets, recognition and valuation approaches. In their view the matter of cost-benefit is 'pervasive to these areas' (http://www.ifac.org). This work stream is due to recommence at some stage during 2009.

1.5 In Australia and New Zealand, recognition of heritage assets in financial reports has been required since the mid-1990s, the rationale being a perceived need within public sector organisations to secure more explicit management performance measures and hence increased accountability. The introduction of a valuation of heritage assets within the balance sheet in New Zealand and Australia has raised some issues that are relevant to consider before similar provisions are implemented in the UK.

Background to the research project

The Research Project

1.6 After the ASB published its discussion paper *Heritage assets: can accounting do better?*, RICS and HM Treasury decided, in summer 2006, that there was a need to develop valuation guidance for valuers. This view was reinforced by the publication of the ASB's Financial Reporting Exposure Draft (FRED 40) in December 2006, setting out their proposals in the light of comments received about the discussion paper. The proposals in FRED 40 differed from those in the discussion paper: a new accounting standard on heritage assets would require entities, wherever practical, to report heritage assets at valuation in their annual accounts. The FRED was quite clear that entities should determine practicality at the level of the 'collection' in the case of museum and gallery assets, not the overall holding. Where it is not practicable to obtain a valuation, heritage assets should not be reported in the balance sheet, although enhanced disclosure is required.

1.7 RICS and HM Treasury funded Kingston University to carry out a research project *Valuing our Heritage.* The Research Team, drawn from RICS, HM Treasury and Kingston University, conducted a literature review in early 2007. This was followed by a series of stakeholder interviews and case study site visits across a range of entities – both those owning and managing diverse portfolios ranging from museum artefacts to historic properties and landscapes and other bodies concerned with the sector and directly with the ASB.

1.8 The International Valuation Standards Committee (IVSC) consulted on the valuation of historic property in 2006 and provided draft guidance in relation to the valuation approaches that could be adopted. To date this has not been implemented and it is recognised within the draft that the application would be to historic property only, not the full range of heritage assets.

1.9 A workshop was held in Spring 2007 with some twenty organisations to discuss emerging themes arising from the interviews and literature and in August 2007 a discussion document *Valuing our Heritage* was published (RICS and Kingston University) and widely circulated. Following that consultation, summary findings, conclusions and recommendations were published in January 2008. This paper consolidates the two documents and builds in consideration of the Accounting Standards Board FRED 42.

It considers:

- the definition and classification of heritage assets;
- the benefits and challenges of recognition;
- challenges for the preparers; and
- valuation methodologies

Events since the research project was undertaken

1.10 The ASB has decided that the responses to both its Discussion Paper and FRED 40 are such that it feels unable to continue with its proposals. It has, instead, decided to continue with the existing FRS 15 approach, but with the requirement for additional disclosures, as originally set out in the Discussion Paper. FRED 42 was issued on 11 June 2008 for comment by 10 October 2008. The Research Team responded to this consultation, but as at the date of finalising this report, there has been no change in the standard to incorporate the proposals in FRED 42.

1.11 The Research team has updated its previous papers (*Valuing our Heritage: a discussion document and A Draft Summary Report on the Valuation of Heritage Assets*) to refer to the requirements of FRED 42. Even if financial statements will go no further than at present in recognising heritage assets acquired since FRS 15 was issued, valuations of heritage assets will be needed for other purposes – insurance valuations for items on loan, sales values where items might be sold, and the value of donated assets. There is a question, too, not considered further in this paper, as to whether the acquisition cost or donated value of a heritage asset remains valid for any length of time.

1.12 RICS has reconsidered the position of portable property within their Valuation Standards, which provide mandatory guidance to valuers on the process and basis of value to be adopted when undertaking valuations for most purposes. At the commencement of this work, all such assets fell outside the scope of the standards but some chattels, though not heritage assets and antiques were brought within the scope from 2008. At the time of writing a decision has been taken to include all such assets within the scope, though this has not been implemented.

02 The definition and classification of heritage assets

Introduction

2.1 A literature review revealed that there is no single, agreed definition of a heritage asset, although a number of organisations have formally defined the concept. Definitions tend to highlight that objects, items and sites that are deemed to qualify as heritage have unique cultural, historic, artistic, environmental or scientific attributes and that they are being held for the public benefit, typically in the context of preservation (for future generations) and education. Not all jurisdictions where recognition of heritage assets in financial reporting is required have a formal definition. Perhaps one of the simplest definitions is that of the Peruvian National Institute for Culture which defines cultural heritage as the tangible and intangible assets that our ancestors have left to us over the centuries.

2.2 The Discussion Paper produced by the International Valuation Standards Committee (IVSC) rehearses a useful set of definitions but for the purposes of the Research team's consultation, the definition provided in FRED 40 (p.10) provided the starting point for discussion:

"An asset with historic, scientific, technological, geophysical or environmental qualities that is held and maintained principally for its contribution to knowledge and culture".

2.3 The ASB's discussion document and the Preface to FRED 40 made it clear that the scope of the term heritage asset includes three specific sub-sectors, namely:

- collections of objects held by museums and galleries;
- historic properties including archaeological sites; and
- landscapes, coastlines and natural geophysical features.

This definition differs from that of the draft IVSC definition which is more widely drawn and only requires that the asset has some cultural, environmental or historical significance.

2.4 In defining a heritage asset for accounting purposes, the ASB proposed a secondary test to that in the IVSC document, namely that the asset should be held to contribute to a principal objective of promoting knowledge and culture. Thus any asset which is held for other purposes, for example to provide office space, is not regarded as a heritage asset for the purposes of financial reporting, but as an operational asset and valued accordingly under FRS 15.

2.5 Whilst the word 'asset' is commonly used in accounting terms, in practical terms many such 'assets' are in reality revenue liabilities in that the costs of upkeep far outstrip any potential for income generation. It is therefore accepted within definitional terms that heritage assets include items which impose an overall cost liability on their owner. The potentially negative nature of the valuation is not a matter related to whether or not the property is an asset, although the inability for it to be other than a revenue liability may affect the decision as to the methodology of valuation to be adopted. The issue of valuation methodologies and the quantum of value is discussed in Chapter 6.

Real Estate Heritage Assets

2.6 Real estate heritage assets include historic buildings and monuments as well as landscape or geophysical or man-made physical features. In deciding whether such assets are heritage it is suggested that there are three considerations to be assessed. These are:

- whether the purpose of holding is primarily for contribution to knowledge, education or culture;
- definition of the unit; and
- whether the use and nature of the asset can appropriately be considered to constitute heritage.

2.7 It is important that the valuer, in consultation with the owner (or custodian), take a realistic approach to determining both what constitutes 'heritage' and what constitutes an asset. At no time is it considered appropriate, for example, to value individual components of a building separately. The holding should be taken holistically to fulfil any reasonable expectation of providing useful and transparent advice to the readers of the accounts.

The purpose of holding the real estate

2.8 Many properties of historic or cultural significance are used operationally (for example, a listed building used as an office). Under both ASB and RICS guidance, such properties are classified as operational and should be valued accordingly under FRS 15. Normally this will result in a valuation being undertaken to Existing Use Value as defined in the RICS Valuation Standards, 2008. The issue that is currently under consideration is whether the purpose for which the asset is held is *primarily* that of knowledge, education or culture or not. In many cases, (a University building, for example), the property may have an overarching educational use but the primary use would be regarded as operational for the purposes of the balance sheet. In other words, the educational activity taking place could equally well be conducted in a building of a non-historic nature. If this is the case, FRS 15 should be adopted and the property valued as an operational asset to Existing Use Value found by use of the Comparative Method, making reference to transactional evidence of similar assets or a Depreciated Replacement Cost method using current RICS guidance (Valuation Information Paper 10).

Definition of the real estate unit

2.9 It is vital to establish the extent of the unit to be considered for valuation. In order to do this, it may be appropriate to consider the definition of the valuation unit as developed in the UK within the context of revenue taxation (rating) valuation practice. Under rating practice, the valuation of assets is established with reference to the ‘hereditament’, which is a parcel of land (and buildings) identified on the basis of a series of considerations established by law. In the case of Gilbert (VO) v. S Hickinsbottom & Sons Ltd [1956] the following principle was established:

“Where two or more properties are within the same curtilage or contiguous to one another, and are in the same occupation, they are as a general rule to be treated for rating purposes as if they formed parts of a single hereditament.…”

In most cases the identification of the hereditament will simply be a case of identifying the occupier and the extent of that occupation in relation to a geographical and ‘purpose’ test.

2.10 The decision in the case also set out the following considerations as being relevant in determining the extent and definition of the hereditament:

- whether or not the premises are in more than one rating area;
- whether two or more parts of the premises are capable of being separately let. If not, then the premises must be entered as a single hereditament;
- whether the premises form a single geographical unit;
- whether, though forming a single geographical unit, the premises by the structure and layout consist of two or more separate parts; and
- whether the occupier finds it necessary or convenient to use the premises as a whole for one purpose or whether he uses different parts of the premises for different purposes.

2.11 When historic properties are under consideration, in addition to the general rules as set out above, the following should be considered as separate from the heritage asset and valued operationally:

- offices and administrative facilities (such as training centres) where the use is not primarily concerned with the historic property itself (e.g. Head offices or regional offices of the National Trust or English Heritage or the leisure and museum departments of local authorities);
- catering and retail facilities outside the pay boundary of the historic property where it is likely that a significant proportion of customers will not visit the historic property (e.g. National Trust shops and restaurants in towns and villages);
- property used for the provision of short stay accommodation or self contained lets; and
- property used mainly for commercial purposes unconnected with the heritage of the property (such as conference lets).

2.12 In terms of scoping real estate heritage assets, be they historic properties or landscapes or other physical features, it is considered that the tests used for rating have applicability to valuations for capital accounts. The valuer should therefore consider the actual use and the physical unit test to establish the unit to be valued. It follows from this that what is considered to be an asset when determining the valuation test of practicability, should not be a component within a building or a single building within a group of buildings all within the same curtilage. In summary it is suggested that a commonsense and factual approach to the constitution of an asset should be adopted and the notion of a 'red line' around a building or holding could be adopted.

What is real estate heritage?

2.13 The third test in determining whether the property is appropriately considered to fall within the categorization of heritage is whether the cultural, historic, scientific, technological, geophysical or environmental qualities are sufficient to justify the term heritage. There are many old and interesting properties and attractive landscapes or geophysical features; however, to classify all of them as heritage would be inappropriate.

2.14 A set of criteria, known as The Waverley criteria, although originally developed in relation to artefacts, may, with adaptation, have some relevance to determining what constitutes heritage in the case of real estate. The rules are set out below:

- Is it (the object) so closely connected with our history and national life that its departure would be a misfortune?
- Is it of outstanding aesthetic importance?
- Is it of outstanding significance for the study of some particular branch of art, learning or history?

2.15 Adaptation of these criteria to real estate would suggest that, to qualify as a heritage asset, the real estate should:

- have a close connection to history and national life, such that its importance is recognised by protection measures such as listing;
- be generally conserved or preserved with the intention of enabling future generations to benefit from it and that, except in the case of total destruction, every effort would be made following accidental damage to carry out restoration works; and
- be of outstanding aesthetic significance.

Where the asset does not meet these tests, it is suggested that the asset, although possibly of historic interest, is not a heritage asset for the purposes of accounting valuation.

Portable Property

2.16 Personal or portable property encompasses an extremely broad range of objects and, whilst many may be old and interesting, not all will be heritage assets within the proposed definition. FRED 40 required that the decision whether or not to recognise a heritage asset in the case of personal property, as opposed to real estate, should be undertaken at the level of the individual collection, not the individual asset or the entire set of collections. This proposal presented two main issues to be resolved:

- how far must an asset or collection of assets be unique in order to be regarded as 'heritage'?
- what constitutes a 'collection'?

Although these proposals have now been overtaken by the ASB's decision not to issue an accounting standard with new recognition requirements, the Research Team believes that the situation may well be re-visited over time and that, despite the current decision, it is still worth considering these two questions.

The Test of Uniqueness

2.17 The existing Waverley criteria (see paragraph 2.14) provide an important point of reference. These criteria were established in 1952 to assess works of art and objects of cultural interest for their significance, in instances where an application to export from the UK has been made. If the object is deemed by the Export Reviewing Committee to satisfy the Waverley criteria, then the application for export is deferred (for an agreed period) in order to provide the opportunity for a UK institution or individual, frequently a museum, to submit an offer to purchase at the agreed price. If no offer to purchase is forthcoming, the deferral period may be extended but cannot be maintained indefinitely.

2.18 This definition may be regarded as a guide, rather than an absolute. Property not meeting the criteria can be regarded as an asset that should be accounted for as non-heritage and hence recognised in the balance sheet as any other asset and be subject to normal policies regarding revaluation and depreciation.

What constitutes a Collection?

2.19 The issue of what constitutes a collection requires explanation. In practical terms, the basis for distinguishing collections is not always clear and even the boundaries between sub-categories of heritage assets may be floating. Some institutions choose to define their holdings as a 'collection' in recognition of the current or former owner – for example, the Wallace Collection and the Gilbert Collection in London and the Burrell Collection in Glasgow. Many museums will hold multiple 'collections' generally designated by subject matter (for example, 19th Century furniture), region (for example, Asian Art) or age (for example, 20th Century) under the umbrella of the institution.

2.20 Whilst the valuation of an individual collection within an institution may be possible and provide certain relevant data, the usefulness of such valuation data in isolation is questionable unless it forms part of a phased valuation of all collections or appropriate supporting disclosures referencing the remaining collections are also included within the accounts.

2.21 Some fixtures and fittings within a building could be regarded as capable of separation from the building and hence being valued separately; others may form an integral part of the building and be valued as one with the structure. In making decisions in relation to assets in which the fixtures have a close relationship with the building (for example where a building has been designed and built to house a single collection), it might be more appropriate to consider the whole as a single entity, rather than as a building and collection. In arriving at this view, discussions should take place with the owner and cognisance made of the nature and purpose of the holding.

Conclusion

2.22 In considering the definition of heritage assets, the Research Team concluded that many assets, both portable and real estate, could legitimately be regarded as heritage on the basis that they meet the tests of:

- the purpose for which they are held; and
- their actual or (in the case of unexploited assets such as reserve or unshown collections) their potential contribution to knowledge and culture.

2.23 The Research Team concluded, however, that many of these assets are not unique and, in the event of their destruction, appropriate alternative items could be acquired to fulfil the same purpose. For example, a collection of roman coins may not be unique, a stately home may be sufficiently similar to some other properties that value comparisons can be made, and an archaeological barrow may be but one of many. This is not to say that such assets are not heritage: under the criteria above; they would be. However, they are capable of sufficient element of substitution in economic terms that they are not worthy of the concept of 'pricelessness'.

2.24 However, there are some heritage assets for which the issue of uniqueness is important and for which Waverley provides some applicability. Such assets, the Research Team conclude, may lack any comparability to other assets, and consider that these could be regarded as a specific sub-class of heritage assets: National Treasures. Such assets could be taken to include assets such as Stonehenge, the major Palaces and major pre-eminent and unique Works of Art considered to be of particular individual importance. Such assets, it is argued are so characterised by uniqueness that the concept or replaceability or economic substitution is meaningless.

2.25 Assets falling within this proposed 'National Treasure' categorisation would in effect be regarded as a special category within heritage – not the only assets that fall within the definition. The distinctiveness of National Treasure assets lies in their uniqueness and hence lack of comparability and the uncertain and unpredictable nature of any market for them. The Research Team suggests that the decision as to whether any heritage asset merits National Treasure Status should be one for the owning entity upon advice from experts in the field and subject to auditor approval. The intention should be that once assets were so designated such designation would not generally be reversed; i.e. it would be a once and for all decision and would be restricted only to such items as would be anticipated would not in the future be gifted away, loaned, leased, licensed or sold.

2.26 It is acknowledged that currently, accounting standards bodies world-wide have not considered such a categorisation; the intention is only to increase the level of disclosure on the books of heritage assets. Nonetheless, the Research Team consider that the current definitions of heritage are simply too broad and that a sub-characterisation as set out above would aid clarity to the readers of accounts and a greater knowledge of the true underlying financial position of the organisation's asset base.

03 The benefits and challenges of recognition

Introduction

3.1 Many heritage assets, both portable and real estate, lie in public ownership; others are held by charitable concerns or are held privately. Many are traded; others, however, often those with the most cultural and societal importance, are seldom, if ever, traded and indeed may be held inalienably in order to protect them and ensure that they remain available for the enjoyment and cultural, educational or spiritual well being of the nation. It is therefore of great importance that heritage assets are appropriately recognised and managed. The key word is 'appropriately' as applied both to recognition and to management.

3.2 It is generally recognised that not all heritage assets are capable of valuation. Some by the uniqueness (the National Treasure properties as suggested in Chapter 2 above) are simply incapable of meaningful monetary evaluation using conventional approaches. The key questions for consideration are:

- which heritage assets are capable of being valued?
- what benefit will accrue to the owner and interested third parties by carrying out a valuation?

3.3 The challenges that have been recorded surround the following issues:

- the definition of what is a 'heritage' asset;
- a lack of acknowledgement by standard setters that conventional valuation processes may not be applicable to heritage assets;
- the impact of constraints on ownership of some heritage assets; and
- practical concerns on implementation.

3.4 These questions must be answered in order that the assets may appropriately be identified within the accounting regime of the responsible body or organisation. In particular the research probed the issue of the usefulness of valuing heritage assets and in so doing evaluated both the benefits of valuations being produced and the challenges that these raise for those charged with the preparation of valuations.

The benefits of recognition

3.5 It is generally recognised that not all heritage assets are capable of valuation. However, where meaningful figures can be produced with the use of existing recognised methodologies, it has been argued that a recognition approach can have positive benefits. IPSASB takes the view that the issue of cost-benefit is important in determining whether a recognition approach should be adopted and such a concern is implicit within the ASB discussion documents, although the ASB proposals do not state an explicit rationale for the proposals.

The Water-Lily Pond, Claude-Oscar MONET. Bought, 1927.
Credit: © The National Gallery, London.

03 The benefits and challenges of recognition

3.6 An analysis of the responses on FRED 40, the literature reviews (see Appendix A for a bibliography of main sources), and a series of stakeholder interviews (including a stakeholder workshop), revealed that there may be a strong case for recognition of heritage assets on the balance sheet. The reasons for this view are set out below:

- There is an inconsistency in the current approach, in which it is simply the date of the acquisition that determines whether or not an asset is recognised in the accounts. An approach which places the recognition not on the time of acquisition but on practicality and usefulness to the end user must be preferred.
- It is only if an asset is recognised on balance sheet at valuation, or information disclosed in the information accompanying the accounts, that an organisation's stakeholders (both internal and external) can gain an overview of performance. Recognition and valuation can therefore assist in performance management, providing that valuations are credible and that a revaluation approach is adopted.
- The process of preparing to recognise heritage assets on the balance sheet requires a comprehensive audit to be undertaken of what such assets are. It, therefore, leads to the development of a more comprehensive and transparent set of ownership or stewardship records and a more complete inventory of tangible assets.
- The possession of better ownership (or stewardship) records, especially where accompanied by up-to-date and meaningful valuations, provides a framework for more active asset management and useful information for potential donors, who will be presented with a more transparent view of the existing asset base of the recipient organisation.
- Improved data records and more active asset management can lead to easier and quicker identification of conservation and restoration needs and provide better information for the preparation of insurance policies when loans of assets are in contemplation.
- Valuations may reveal negative capital values in some cases; that is. the process of valuation could lead to the reporting of some assets as liabilities. This transparency could be useful when assessing a case for grant aid and other financial support including the case for donor contributions.
- Initial consultation indicated that the ability to de-accession, where possible, might provide a valuable incentive to undertake an audit of assets.

3.7 The issue of benefits to the owners (or custodians) are seen to lie primarily within the management arena and vary depending on the ability to pro-actively manage portfolios. One of the research findings was that some stakeholders saw a short-term benefit from the audit process in that it would lead to improved management systems. But this would only benefit owners (or custodians) where they have the ability to manage proactively their portfolios of heritage assets. The benefit may also be greatest at the point of first valuation. Stakeholders were far less likely to see longer-term benefits.

3.8 The research process has revealed that, within the short-term, it is the process of audit itself that is acknowledged by some stakeholders as leading to the possibility of improved management systems, with the greatest benefit arising at the point of first valuation.

3.9 Most respondents to the research document consultation recognised that, in principle, management benefits could flow from the introduction of valuations. Some went so far as to opine that recognition could lead to a more active and robust arts market as it could be linked to better identification of assets which are surplus and could be realised, although this view was not universally held. To some respondents the matter of an actual valuation was of less importance than the presence in the accounts of an inventory of assets accompanied by a narrative. In summary, good management was linked by many to the availability of relevant and accurate data and this prevailing view could be summed up as one respondent said *"good data is always useful."*

Recognition challenges

3.10 The view that the usefulness of valuations might be limited has to be put in the context of the challenges to recognition. These primarily related not to the principle of recognition but to measurement: the cost and practicability of producing valuations and their meaningfulness. Some respondents expressed the view that the introduction of recognition could result in very heavy workloads in arriving at valuations, the cost of which would outweigh the benefits – because they did not see any particular benefits associated with valuation that could not be achieved by other means. The sheer volume of artefacts held by some respondents was cited as a significant contributory factor to cost. Some respondents also pointed to the unique nature of many heritage assets which renders reliable valuations difficult, if not impossible, and the volatility of the arts market generally, which could render any valuation becoming quickly outdated.

3.11 For museums, the issue of the ability or otherwise for de-accessioning is very real and some respondents expressed the view that the inability to dispose of assets provides a reason for non-valuation. However, this does not counter the argument of improved stewardship. Some respondents argued that inalienability would render a valuation impossible or meaningless as the resultant figure could not be realised in the marketplace. This is a matter that has been considered by ASB, and the current position is that inalienability is not a bar to valuation; it is simply a factor that has to be disclosed alongside any valuation.

3.12 However, if the concept of National Treasure (see 2.24 and 2.25) were adopted, the Research Team believes that these challenges would be minimised. The uniqueness of National Treasures are such that the Research Team proposes that they should not be recognised on balance sheet, since there would be no relevant information on which to base a valuation. Where, however, heritage assets are not National Treasures, sufficient information should be available to inform a valuation, albeit that the initial data collection exercise could be time and cost heavy. Subsequent valuation, if undertaken in accordance with normal FRS 15 rules, should however be less burdensome.

04 The challenges for preparers

4.1 The implementation of any accounting standard for heritage assets is likely to present challenges for the owner or custodian. Some of these challenges are acknowledged by the ASB; others have been revealed by the responses to their consultation and by the Research Team's initial research interviews and subsequent consultation. The challenges are summarised in the following paragraphs. Primarily they relate to cost, logistics and complexity.

4.2 For many organisations the issue of cost is very real. Cost constraints are most likely to arise where incomplete records are held, where the assets are difficult to categorise, and where there is little in-house expertise. The issue of cost has also been highlighted by IPSASB. The proposal by the ASB that valuations can be undertaken by internal valuers is helpful in logistical terms. There may be a practicality issue as well as a cost issue in some cases.

4.3 The issue of practicality may relate to methodology or to logistics, for example where the portfolio of assets to be valued comprises very many assets or where the expertise required, either internally or externally, may be insufficient. Where practicality relates to logistics caused by large numbers of assets, a representative sampling approach could be usefully be considered. Such an approach could help overcome the cost issue in some cases as it would be spread over a number of accounting periods.

4.4 The valuation of many heritage assets is likely to give rise to considerable complexity. The valuer and the client should discuss the practical issues and any underlying assumptions that may be required to provide a meaningful valuation. Complexity is likely to arise where assets are not owned but held in stewardship arrangements and where there is the need to resolve matters such as the possibility of de-accessing (museums and galleries) or complex leasing arrangements (stewarded lands) and public access or public rights issues. Complexity does not, in itself, imply that valuations cannot be undertaken; indeed valuers of many commercial properties deal with complexity of funding and leasing arrangements as a standard part of their work. However, they need to be recognised and discussed before decisions regarding valuation and methodology are undertaken.

4.5 In many cases, what can be defined as a single heritage asset may be clear. It might be a small collection, a single property or monument held in a single ownership, or a single piece of land of special value. However, it is frequently not that simple. A museum may contain a number of items which could be argued to be a single collection or a group of collections; similarly, a property may comprise a range of buildings. Many museums have substantial holdings which are not on public display and are held in temporary or permanent storage. The principal and reserve collections will often contain loan items. Many institutions often hold duplicate or multiple versions of the same object. Where this arises it will be vital to arrive at what is scoped to be within the definition of a single asset.

4.6 Many heritage properties, sites and objects are held inalienably, preventing disposal or sale. This has led to the argument that, without the ability to dispose of a heritage asset, there can be no commercial value attached to it and the inclusion of a notional value for accounting purposes may be considered irrelevant. In some jurisdictions, the ability to purchase and de-accession objects provides a valuable feature in the curatorial and financial management of a collection.

4.7 The valuation of large numbers of individual items, often of individual modest financial value, will generate significant cost and time implications. One leading heritage body has estimated that a valuation of the contents of properties within its custody would cost between £3 million and £4 million. Another has suggested that undertaking a sample valuation exercise of portable heritage would take 2.4 years of staff time. Conversely, the valuation of large numbers of similar objects within the same or proximate location will typically generate certain economies of scale found within valuation practice more widely.

The challenges for preparers

4.8 It has been argued that to place a theoretical value on a property, site or object that cannot be sold would be misleading within the context of accounting standards. Even if an asset can be defined and the complexities of title etc, resolved, in many cases it will present a challenge to establish a methodology that is robust, consistent and capable of producing reliable and meaningful valuations. Preliminary research into valuation methodologies adopted for the treatment of certain heritage assets in other jurisdictions has indicated that this would conflict with current best practice in the UK. The matters in relation to valuation methodology must be discussed with the client and an appropriate approach adopted. Guidance in relation to each of the major categories of assets is considered under valuation below.

4.9 In summary, the challenges for preparers are real. The introduction of a 'norm' of initial valuation and regular re-valuations, even if conducted on a sample basis, would for many large organisations, prove both difficult in practical terms and expensive. These challenges however are very variable. For many heritage assets, market evidence of value does exist and once established the process of revaluation would be less onerous. Moving forward, in a climate in which measurement and metrics are becoming increasingly part of asset and organisational management practices, there is increasing expertise on meeting the challenges that heritage assets present.

05 Valuation methodologies

5.1 Before discussing the valuation basis to be adopted for each of the three main categories of heritage assets, it is useful to refer to the general issues that have been recognised within the IVSC Exposure Draft as presenting valuation challenges. The draft recognises that:

- the economic benefit in cultural, educational and historic terms is unlikely to be fully reflected in a financial value based purely on market price;
- legal and/or statutory obligations may impose prohibitions or severe restrictions on disposal by sale;
- heritage assets are often irreplaceable and their economic benefit may increase over time even if their physical condition deteriorates; and
- it may be difficult to estimate their useful lives, which in some cases could be hundreds of years.

This list of characteristics is important, as it highlights that, for many heritage assets, market value may not be a fair reflection of the worth of the asset to the nation or, by implication, to the owner or custodian.

The Valuation Approach

5.2 The characteristics of the three broad sub-sectors of heritage asset dictate that the valuation approach for each may differ significantly. Some degree of specific expertise is required in relation to markets, legal ownership arrangements, and valuation methodology. Even under the new proposal that heritage assets should be recognised in financial statements under FRS 15, the ASB continues to recognise that carrying out a valuation has implications for both cost and expertise and these issues have been explored in Chapters 3 and 4 of this report. In the Discussion Paper, and in FRED 40, the ASB allowed the use of internal expertise if that were the most appropriate approach. However, although the Discussion Paper and FRED 40 gave no set requirements for the frequency of valuations, FRS 15 requires assets carried at value to be re-valued at least every five years. The valuation methodology should be determined by discussion between the client and the valuer.

5.3 Whilst there are and have been for many years, RICS standards which provide, through a series of Information Papers and Guidance Notes, advice on the valuation of real property for inclusion in financial statements, guidance for members on how to value personal property for this purpose is new. From 2008, some personal property is covered by the Valuation Standards but the decision to cover antiques and heritage assets within the scope of the standards was taken after completion of the empirical phases of this work. The recent decision to include them within the Standards adds further relevance to the findings and recommendations of this project. The following sections consider the approaches that may be applicable to heritage assets, and the degree to which the resultant value could be said to be reliable, relevant and current.

Definitions of Value and Worth

5.4 Where real estate assets are to be valued for balance sheet purposes, the basis of valuation depends on whether the asset is owner-occupied or held for investment purposes. Where they are held for investment they are valued on the basis of Market Value. This is defined as:

The estimated amount for which a property should exchange on the date of valuation, between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion (RICS 2008, PS3)

However, many heritage assets will be owner-occupied and if so, under current RICS standards, they will be valued on the basis of Existing Use Value (EUV). This is defined as:

'The estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction, after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion, assuming that the buyer is granted vacant possession of all parts of the property required by the business and disregarding potential alternative uses and any other characteristics of the property that would cause its Market Value to differ from that needed to replace the remaining service potential at least cost.'
(RICS, 2008, UKPS1.3)

5.5 The UK currently differs in its approach to balance sheet valuation from most other countries who have adopted only the market value basis. The Market Value, as defined, allows the valuer to include any prospect of additional value that could be realised through redevelopment, provided that such added value is recognisable in the market place and is not simply speculative. However, where heritage assets are under consideration, the question of redevelopment is unlikely to arise due to legal protection measures and for this reason the EUV and the Market Value are likely to be the same. The concept of EUV does however, allow for the possibility that a purchaser could undertake works not requiring a change of use which could provide a more economically advantageous position to the owner. Such additional realisable value does come within the concept of EUV.

5.6 Before considering the practical considerations involved in valuation, the distinction between value and worth must be considered. Under the existing accounting regime, assets which are recognised on the balance sheet are normally entered at value. However, it is recognised that this may or may not equate to the worth of the asset to the owner or custodian. Value, wherever possible, will be estimated using market evidence from comparable transactions either in relation to rents and capitalisation rates, to direct capital transactions or to the capitalisation of maintainable profits. Worth, on the other hand, may be calculated using a cash flow approach or it may take into account non-monetary values. Such estimates of worth may be critical to the owner or custodian in making management decisions and it is specifically recognised as being subjective as it is normally prepared for an individual owner to enable them to strategically manage their assets. Under existing accounting principles, worth is not the measure placed in the accounts: value is. Increasingly, however, worth is being used as a management tool.

Applying Valuation Methods to Real Estate Heritage Assets

5.7 Conventional methodology applicable to real estate heritage assets comprises the following market driven approaches:

- use of comparable sales or sale and rental evidence appropriately analysed (the comparables method and the investment method);
- capitalisation of net profit (or loss) derived from establishing and analysing the fair maintainable trade (the profits or accounts approach); or
- discounted cash flow based on predictions of income and expenditure over a given projected time span. This last approach is more commonly adopted where a worth calculation is sought.

5.8 Where *either* there is evidence of market transactions on which the valuer can rely, *or* the property is producing (or could produce under pro-active management) a significant cash flow, then a competent valuer with appropriate expertise, as defined in the Valuation Standards, should be capable of establishing a market value in existing use.

5.9 It is widely recognised, however, that establishing the value of such assets can raise specific challenges, which may or may not mean that a defensible valuation cannot be prepared. The following issues should be considered and evaluated by the valuer before advising a client on whether or not the property can/should be recognised. The list offered below is not to be regarded as comprehensive, but advisory:

- a lack of comparable evidence renders use of conventional techniques inappropriate or impossible in many instances. This may not be a large issue for some historic buildings, but landscapes, coastlines and geophysical features are very seldom brought to market except as part of a much larger transaction;
- transactional evidence may be limited in amount and applicability. This does not necessarily render a valuation impossible, but it may require the valuer to point out to the client that some uncertainly surrounds the valuation. Guidance on this is provided to valuers by the RICS (Guidance Note 5).
- the question of legal title may need to be resolved as many assets are held inalienably;
- the asset may have a cash flow that will enable a trading approach to valuation to be adopted. However, even if it is trading, it may produce a negative cash flow in that the operational costs of running the property may well outweigh the income. This is particularly the case with historic buildings (rather than landscapes), where upkeep is expensive due to the need to match historic materials and building techniques. Such issues do not preclude valuation but may result in a zero or negative capital sum being reported;
- many assets are not capable of producing any significant or, indeed, any cash flow and require, at a very minimum, security arrangements and, in some cases, significant costs of upkeep, maintenance and periodic restoration. Again such assets may in reality have a negative capital value; and
- any value that can be calculated may fail the test of a ‘good’ valuation in that it cannot be defended by robust methodology.

Inalienability

5.10 One of the issues relates to inalienability or other title issues – for example, many such assets are held in stewardship or guardianship arrangements where custody and managerial cost and responsibility reside separately from legal title. Discussion with the client will be required to establish whether the matter of title is such that it precludes the ability to undertake a valuation. In many instances, an assumption can be inserted within the valuation to recognise that the asset cannot be sold. In this respect heritage assets present a similar set of issues to those which affect many conventional assets.

Heterogeneity

5.11 The issue of heterogeneity is a critical one. Not only does the unique nature of many heritage assets mean that comparables are not available, there is a view held by many that there are some assets which are considered ‘priceless’. By this, it is meant, not that they cannot be priced, but that the price that would be achievable may not be a true reflection of their unique contribution to overall cultural wealth. In short, such a market value may fail to recognise worth as opposed to value. Where the asset is deemed to have high ‘worth’, but does not yield a market value using any conventional methodology (other than a depreciated replacement cost approach, which is clearly inappropriate), it might be decided that it is not practical to value the asset on the balance sheet. Where this is the case, it is proposed that the valuer identifies the property and reports that it does not have a recognisable value for inclusion on the balance sheet. This situation is most likely to arise in relation to assets which could be considered to fall under the head of National Treasure.

Cash flow

5.12 Many heritage assets, however pro-actively managed, may be incapable of providing a cash flow which would yield a capital asset. For example, a remote ancient barrow or earthworks may not be capable of exploitation as a tourist attraction, but will incur expenses in terms of maintaining safe public access. Similarly, an historic property may have high maintenance costs which far outweigh the economic income. In such cases the valuer has two choices:

- report that the asset cannot be valued in any meaningful way; or
- present a negative valuation to reflect the liability.

5.13 Many of the properties that fall into the revenue liability category are in receipt of subsidies and grants towards their maintenance. Where this is the case, the loss *before* subsidy could be capitalised to provide a negative capital value which could be useful information to inform the owner seeking to gain financial support for the building. Such an approach would only be appropriate where the property, if placed on the market for sale subject to the EUV constraints, would not be likely to attract a buyer at any figure other than a nominal amount[1]. Where this is the case, the valuer should consider whether it is appropriate to place a nominal value on the asset or to report a negative figure.

5.14 Alternatively, there may be cases where an asset which incurs considerable and non-recoverable ongoing costs of management and maintenance will have a value in exchange which far outstrips any figure which is rational in cash flow analysis terms. For example, a property which has a decaying fabric may attract buyers drawn to its aesthetic and historic interest features and who are in a financial position such that their decision-making is not dictated by consideration of costs. Where this is the case and it can be established that there would be a ready market for the asset in its existing use, such a value should be established and reported.

5.15 Finally, the valuer, before making a recommendation as to the practicality of preparing a valuation, should consider the relevance and usefulness of the figure that would be produced. In the case of many historic properties, the benefits argument may prevail, but it is recognised that, for many natural geophysical features, it is likely that a valuation would be either not practical or would be meaningless to the client.

Valuing Portable Property

5.16 The issues surrounding the valuation of portable property are different from those relating to real estate heritage property, but equally complex. However, the full range of valuation methods is not applicable – with only a comparable evidence approach being considered suitable. Initial consultation with key stakeholders has indicated that there are significant concerns in relation to the valuation of portable property. Principal issues raised include, *inter alia*:

- the volume of objects encountered within a typical museum or gallery and the logistics and associated costs of undertaking a valuation exercise;
- the accuracy and reliability of a valuation placed upon objects for which there is often a limited market and the assertion that a materially accurate valuation for many objects within this category is not possible;
- a limited number of qualified professionals with sufficient knowledge to value certain specialist categories of objects will make valuation and auditability difficult;
- the market value of many types of asset will not be an appropriate measure of their perceived cultural or educational worth, which cannot be measured in financial terms; and
- the ability to obtain robust reliable market evidence from transactions of comparable items may be limited. However recent growth in the number of data banks of such information is reducing this as a concern.

5.17 In additional to the more conventional categories of object, other, less tangible assets such as contemporary art, including installation art and film/video art, might also fall under the definition in FRED 40 and therefore be eligible for consideration.

5.18 Restrictions on the trade and movement of certain categories of item (for example, certain natural history specimens) may limit their marketability and therefore influence valuation decisions.

5.19 A review of all assets within the collection may present certain logistical difficulties. A significant proportion of the collection(s) held by many institutions is not on public display and is often held at a separate geographical location. Many institutions will hold items on permanent or temporary loan and these may be of significant financial or cultural value. It will be necessary to differentiate these for accounting purposes from the remainder of the collection and to adjust any valuation accordingly. Museums and galleries will also usually have an on-going programme of conservation/restoration and this will entail the removal of objects from the principal location to external studios and workshops, often for a period of months.

5.20 Case law relating to this area has acknowledged that, by definition, the valuation of this type of property is, on occasion, highly subjective and that the opinions of experts may vary considerably in terms of attribution and authenticity, as well as value.

[1] *Such as approach has been adopted for rating (Hoare (VO) and Spratling (VO) v The National Trust [1998], RA 391*

Valuation methodologies

5.21 The provenance of an item will often significantly enhance value due to association with a particular former owner(s). It is necessary to recognise that, in certain circumstances, items of portable property may also suffer a reduction in market value due to an unknown, disputed, or questionable provenance. This may result in significant differences in value between items of apparently identical description. In light of the commonly encountered vagaries encountered when valuing assets within this category, it is difficult to identify an acceptable degree of tolerance within valuations.

5.22 The market for works of art and certain other types of portable heritage is subject to a number of variable market influences and may be subject to change over a relatively short period of time. There is currently no formally defined recommended period between valuations but a period of 3 to 5 years is generally accepted as a reasonable timescale for most purposes. Therefore, if undertaking a valuation of portable property, comparable sales evidence must be recent or its reliability will be questionable.

5.23 In recognising the narrow, and often limited, market for certain categories and types of object, it is generally accepted that the financial value of a ‘collection’ is unlikely to exceed the combined value of the individual elements. The dynamic of the market in portable property is such that collectors and dealers will generally only wish to buy individual examples to add to an already extant collection and are not generally seeking to purchase complete collections. In other cases, however, the value may be enhanced by the unusual ability to acquire a complete collection, rather than an individual item. Whilst these issues present challenges to the valuer, they are ones with which competent valuers frequently engage when assessing valuation either for sale, or for taxation purposes. They are, therefore, not outside the scope of a competent and experienced valuer.

5.24 The cultural benefits in resisting the dispersal of an acknowledged collection via sale on the open market are often highlighted through the media. This will frequently coincide with fundraising efforts amongst heritage bodies, charities, institutions and private individuals in an attempt to raise funds in order to secure the purchase and future preservation of a property and collection as a single entity. A high profile example of this could be observed in the sale of Dumfries House, Scotland in 2007 where a Palladian mansion and its internationally renowned collection of antique furniture and works of art, many originally commissioned for the house, were to be dispersed on the open market[2]. Following a three-year fundraising campaign, a number of heritage bodies and private/commercial donors eventually secured the house and contents shortly before its sale, thereby preventing disposal by the owner on the open market. The valuation point of note here is that the value of the portable property had a direct relationship both to the real estate asset and that the value of the whole collection could be deemed to have been in excess of the individual lots.

5.25 The Dumfries House example therefore raises two important valuation considerations:

- Locational connectivity; and
- Lotting.

Locational connectivity

5.26 It will be a matter of valuer judgement and experience as to the added value that may arise by the connection of a portable asset to a particular location. For example, the very fact that an item of art is placed within its original setting may add value which, if moved, would be lost. In such cases it is the co-location of the portable and the realty which can create additional value.

[2] *Race to save Dumfries House. Sale of historic mansion and Chippendale furniture is slated for July. The Art Newspaper, No. 180, May 2007, p.9*

Lotting

5.27 The issue of 'lot size' is also of vital importance. Should the valuation be undertaken at the level of the individual asset or the collection and what constitutes a 'collection? In arriving at a suggested 'lot size' for a group of objects defined as a collection, it is likely that the values of the individual objects will vary considerably, and may include items of very modest financial value. In view of the concern expressed generally regarding the issues of practicality and cost, it is recommended that consideration be given to the introduction of *de minimis* limits or value thresholds. The application of any future recommendations should not necessarily be rejected as impractical solely on the basis of the currently perceived scale of the project in respect of individual institutions.

5.28 As stated above, all portable property is to be included within the scope of the Valuation Standards and the 'Market Value' basis of valuation has been identified as generally the most appropriate basis of valuation for assets falling within this sector. A lack of evidence of active commercial markets for certain categories of object has raised concern over how such a market value would be

- established; and
- audited by a third party.

5.29 The issues surrounding the selection of an appropriate valuation methodology valuation for portable property are often compounded by a lack of valuation formula available to the valuer, thereby placing a greater emphasis on the comparables approach. This has, in turn, led to comment that, in view of the limited market for certain categories and type of object, arriving at a reliable valuation that may be tested by audit will be at least problematic and, in many cases, impossible.

Conclusion

5.30 The Research Team concluded that, unless and until new methodologies are developed to allow for cost-effective meaningful valuations using a non-market approach, the more appropriate solution is to fall back on the test of practicability. The Research Team recommends that heritage assets should be sub-divided between those that are National Treasures, as defined in this paper, and those that are not. Further, it is recommended that only those heritage assets that are not National Treasures should be regarded as capable of accurate and meaningful valuations. Where a non-recognition route is adopted, full disclosures in line with FRED 42 should be given.

5.31 For non-National Treasures, heritage assets should be recognised at market value. The Research team recognises that, where holdings are significant in number, it may not be feasible to introduce full recognition and valuation within a short time-frame and recommends that a sampling technique or phased approach could be adopted.

06 Alternative valuation approaches

6.1 Heritage assets present unique challenges to valuers. Many heritage assets have seldom been valued in the past and valuation methodologies for accounts purposes might not have been developed. For this reason, the Research team suggested possible alternative methods to comparable evidence analysis. These included techniques such as:

- Contingent valuation and Willingness to Pay (WTP)
- Cost-Benefit Analyses
- Hedonic Pricing Techniques (i.e. attributes analysis).

6.2 These techniques, which all seek to provide an acknowledgement of the overall cultural as well as economic value of an asset, could be regarded as more appropriate measures to ensure good management decision-making than any simple estimate of value in exchange for inalienable property. The Research Team acknowledges that valuations under these alternative techniques are often costly to produce and that some criticisms have been directed at their usefulness. Nevertheless, they have been widely used in a number of real estate contexts (see for example Mundy and McLean, 1998) and may provide a basis for investigation and development of new applications of the techniques. As such they could be regarded as offering potential for the assessment of value for assets deemed to have worth but not capable of conventional valuation.

6.3 Additionally, the Research Team suggested the possibility of other approaches including:

- net present value analysis, of future known and estimated liabilities, discounted at an appropriate rate of return, in accordance with known valuation methodology;
- gap funding based on the capitalisation of Grant in Aid (GIA) which is taken as a surrogate for public sector value (or worth); and/or
- non-depreciated rebuilding cost., such as is conventionally applied for insurance purposes with the addition of land value in existing use.

The responses highlighted that, whilst they might be worthy of further exploration, they did not offer appropriate solutions within the short term. Instead, the issue of valuation revolves more on what assets can be appropriately valued using established methodologies, notably market value with reference to comparable transactions, or in the case of some real estate assets, potential profitability. Whilst "worth to the owner" using an environmental valuation approach received some support for real estate assets, this was perceived as too costly in most cases. For portable property such an approach is not considered to be applicable.

The Case for Shadow Accounting

6.4 The Research team recognises that not all assets can be valued in ways that produce meaningful and useful valuations. One of the main roles of the valuer will be to liaise with the client and provide advice as to the practicality of preparing valuations for the balance sheet, but the decision whether or not a recognition route is to be adopted must rest with the owner or custodian. In making such a choice, it is recommended that the positive benefits of producing valuations, such as the management information such valuations may provide, are weighed against any issues of cost and logistics.

6.5 In the event that a non-recognition route is adopted, it is recommended that consideration is given to whether the aims and goals of the organisation would be enhanced by considering the issue of value within the wider accounting process, rather than on the balance sheet itself.

6.6 This can be done by, for example, running shadow accounts which present not just the economic (or market) value but also present the social and environmental balance sheets as well. In this connection the work of the Accounting for Sustainability Project (www.accountingforsustainability.org.uk) is relevant as it is investigating ways in which organisations can present a more balanced assessment to their stakeholders of the full costs and contribution of their assets and activities. Further the work of the IFAC is now advocating use of a sustainability framework (www.ifac.org/PIAB). Whilst adoption of such 'triple bottom line'[3] accounting is still in its infancy, it is suggested that the adoption of such an approach could enable the owners of heritage assets to present a more comprehensive and transparent overview of their contribution to the wider economy and hence provide a framework within which enhanced decision-making can take place.

[3] *The term 'Triple Bottom line is now widely used as a means of introducing the concept of sustainability and aims to assess performance against economic, social and environmental considerations.*

07 Conclusions and recommendations

Conclusions

7.1 It is concluded that the valuation of heritage assets present unique challenges, but ones that, in many instances, are possible to overcome to the potential benefit of both their owning or stewarding organisations. Importantly, the production of valuations, where they can be undertaken, would provide those who read and rely on the accounts of those organisations with more accurate, timely and transparent information. Having evaluated the benefits and challenges, the overall conclusion is that, for many heritage assets, valuations are both possible and desirable. There are, however, important exceptions to this conclusion, as set out below.

7.2 A consideration of the definitional issues surrounding heritage assets led the Research Team to conclude that current definitions are often unhelpful and may be in conflict one with another. It is recommended that consideration be given to the establishment of a universally acceptable definition

7.3 Almost all parties consulted during the conduct of this research recognise that the situation as it currently exists in relation to accounting for heritage assets in the balance sheet is no longer fully appropriate. The current solution proffered by the ASB in FRED 42 is to move towards greater disclosure of assets within the balance sheet, rather than a requirement to value. The Research Team regard such a proposal as an important step forward as it will provide owners with greater amounts of information and enhanced transparency. The suggested requirement for reporters to specifically state the reasons for non-disclosure is also helpful and will require many preparers to undertake some auditing of assets. As concluded in Chapter 3 of this report, such auditing is likely to produce benefits to owners and account users alike. Lastly the proposed requirement to provide a summary of transactions is seen as a step along the way towards a more rational and appropriate approach to accounting values for heritage.

7.4 In conducting the research, the test of a meaningful valuation was applied at all times. There is no point in valuing assets where the resultant figure, does not provide useful and meaningful results. However, such assets constitute the minority position, where valuation to Existing Use Value (in the case of real estate) or Market Value (for portable property) can be determined using conventional techniques, it is recommended that such a course should be adopted.

7.5 In preparing valuations, the Research Team identified that some heritage assets, to which market principles can be applied, may present complexity and challenge to the valuer. They are of a type which is commonly or occasionally transacted or valued for the purposes of insurance or probate. Others however have such national or international significance and such quality of lack of substitution that they are realistically incapable of monetary valuation. Accordingly, the Research Team recommend that such assets be identified by owners with the assistance of expert advice and categorised as National Treasures. For such assets, it is concluded, recognition rather than valuation is the appropriate process.

7.6 Although welcoming the steps that are being taken by ASB, the Research Team conclude that there are compelling reasons why the valuation of heritage assets should continue to be a live issue for consideration and debate. These reasons relate to the perceived benefits that a more comprehensive approach to regular valuation would yield, including greater transparency and the ability to inform strategic asset management. Valuations which revealed negative market values could also form a useful platform for the consideration of the need for grants and subsidies where it is recognised that worth to the nation (as opposed to value in the market place) exists. It is concluded that consideration could and should be given to establishing alterative methods of establishing worth in order to provide such a rationale.

Recommendations

7.7 In summary, it is recommended that:

- The international community of accountants, valuers and other advisors seek a common definition of heritage assets.
- The valuation of heritage assets for balance sheets should be encouraged or required where a meaningful figure using conventional approaches can be produced. It is recognised that such a recommendation is unlikely to be fully accepted in the short-term but, despite the challenges such valuations would present, the benefits to all stakeholders could be very real.
- Where valuations of real estate are undertaken they are discussed with the client and take account of full market evidence. The use of Depreciated Replacement Cost is not normally considered appropriate for heritage assets; instead valuers should use the full range of conventional market-based techniques, even where these may reveal a negative value.
- For valuations of portable property, a market value approach is recommended, taking due account of issues of ‘lotting’ and ‘locational connectivity’.
- A new sub-classification of heritage assets, National Treasure, should be recognised within accounting processes as being of high worth but incapable of explicit valuation. Such assets, it is suggested, could be subject to disclosure but not valuation.
- In order to enable enhanced knowledge to support effective decision-making, further research should be conducted into the possible applicability of a range of non-market valuation techniques such as willingness to pay and cost benefit analysis, to support a deeper understanding of worth to the community.
- Where a non-recognition approach to heritage assets is adopted, it is recommended that consideration be given to undertaking shadow accounting in order better to enable the aims and objectives of owning and stewardship organisations to be met.

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