Notes to the financial statements continued

2 Principal accounting policies continued

2.12 Intangible assets

a) Goodwill

Goodwill arises on the acquisition of subsidiaries and other businesses, joint ventures and associates and represents the excess of the fair value of consideration over the fair value of the identifiable assets and liabilities acquired. Goodwill on acquisitions of subsidiaries and other businesses is included in non-current assets. Goodwill on acquisitions of joint ventures and associates is included in investments in joint ventures and associates.

Goodwill is reviewed annually for impairment and is carried at cost less accumulated impairment losses. Goodwill is included when determining the profit or loss on subsequent disposal of the business to which it relates.

Goodwill arising on acquisitions before the date of transition to IFRS (1 January 2004) has been retained at the previous UK GAAP amounts subject to being tested for impairment. Goodwill written off or discount arising on acquisition credited to reserves under UK GAAP prior to 1998 has not been reinstated and is not included in determining any subsequent profit or loss on disposal.

b) Other intangible assets

Other intangible assets are stated at cost less accumulated amortisation and impairment losses. Amortisation charges in respect of software and Infrastructure Investments intangibles are included in underlying items.

c) Research and development

Internally generated intangible assets developed by the Group are recognised only if all the following conditions are met:

– an asset is created that can be identified
– it is probable that the asset created will generate future economic benefits
– the development cost of the asset can be measured reliably.

Other research expenditure is written off in the period in which it is incurred.

2.13 Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairment losses. Cost includes expenditure associated with bringing the asset to its operating location and condition.

2.14 Investment properties IAS 40

The Group classifies land and buildings which it holds to generate capital appreciation and/or to earn rental income as investment property. The Group has chosen to state its investment properties at cost less accumulated depreciation and impairment losses. The Group depreciates its investment properties over 25 years. Land is not depreciated.

2.15 Leasing

Leases which transfer substantially all of the risks and rewards of ownership to the lessee are classified as finance leases. All other leases are classified as operating leases.

Assets held under finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, determined at the inception of the lease, and depreciation is provided accordingly. The liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant effective rate of interest on the remaining balance of the liability.

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

2.16 Impairment of assets

Assets that have an indefinite useful life (such as goodwill arising on acquisitions) are reviewed at least annually for impairment. Other intangible assets and property, plant and equipment are reviewed for impairment whenever there is any indication that the carrying amount of the asset may not be recoverable.

If the recoverable amount of an asset is less than its carrying amount, an impairment loss is recognised.

Recoverable amount is the higher of fair value less costs to sell and value in use. Value in use is assessed by discounting the estimated future cash flows that the asset is expected to generate. For this purpose assets, including goodwill, are grouped into cash-generating units representing the level at which they are monitored by the Board of Directors for internal management purposes. Goodwill impairment losses are not reversed in subsequent periods. Reversals of other impairment losses are recognised in income when they arise.

2.17 Investments

Investments are recognised and derecognised on the trade date where a purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at cost, including transaction costs.

Available-for-sale investments are measured at fair value. Gains and losses arising from changes in the fair value of available-for-sale investments are recognised in equity, until the investment is disposed or is determined to be impaired, at which time the cumulative gain or loss is included in the net profit or loss for the period. Held to maturity investments are measured at amortised cost.

2.18 Assets held for sale and discontinued operations

Non-current assets and groups of assets to be disposed of are classified as held for sale if their carrying amounts will be recovered through a sale transaction rather than through continuing use. Held for sale assets are measured at the lower of their carrying amount on classification as held for sale or fair value less costs to sell.

A component of the Group is presented as a discontinued operation if it has either been disposed of or is classified as held for sale and it is a separate major line of business or geographic operation or the proposed sale is part of a single co-ordinated plan to dispose of a single separate major line of business or geographical operation. When classified as a discontinued operation, income statement performance is reported in summary form outside continuing operations and comparative figures are restated.

2.19 Inventories

Inventories are valued at the lower of cost and net realisable value.

Cost includes an appropriate proportion of manufacturing overheads incurred in bringing inventories to their present location and condition and is determined using the first-in first-out method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

17 Investment properties

	Cost £m	Accumulated depreciation £m	Carrying amount £m
Cost or valuation			
At 1 January 2016	4	–	4
Additions	32	–	32
At 31 December 2016	36	–	36
Additions	**4**	**–**	**4**
Reclassified from inventories	**7**	**–**	**7**
Depreciation charge for the year	**–**	**(1)**	**(1)**
At 31 December 2017	**47**	**(1)**	**46**

Investment properties are held by the Group to generate rental income and capital appreciation. The Group has chosen to account for its investment property assets under the cost method. For one of its investment properties, the Group has secured non-recourse project specific financing amounting to £26m (2016: £18m), which is secured through a floating charge over the property. As a result, £1m of interest cost was capitalised on the asset in 2017 whilst the property was under construction.

Construction commenced on one property in 2016 and this was completed in 2017. Once the property was ready for use, the Group ceased capitalisation of interest cost and commenced depreciation on the property, on a straight-line basis over 25 years.

The remaining investment properties within the Group consist of one other fully constructed property and £4m of land. The fair value of the Group's investment properties at 31 December 2017 approximates the carrying value. The Group generated £1m (2016: £nil) of rental income from its investment properties.

IAS 23.10: borrowing costs are specific and attributable to the construction. Hence, they are capitalised for the duration of the construction.

The loan to finance the development is secured through a floating charge over the property: that means Balfour Beatty cannot realise the value of the investment property through sale.
1. Why is it useful for stakeholders to know that there is a charge over the property?
2. Does the charge affect the value of the property under IFRS 13 fair value? Give reasons to support your answers?
3. Explain the key financial reporting decisions that the management has made about investment property in producing the financial statements. (PREPARER'S PERSPECTIVE)
4. How would you assess the qualities of this note? Does it satisfy user needs? Would you say it is cluttered? (USERS PERSPECTIVE)
5. Comment on the choice of cost basis? What information in the note confirms that the management made the right choice?