

Meeting: International Public Sector Accounting
Standards Board

Meeting Location: Luxembourg, Luxembourg

Meeting Date: June 27–30, 2017

Agenda Item 11

For:
☐ Approval
☒ Discussion
☐ Information

Public Sector Measurement

Project summary	Project will: revise IPSAS requirements for measurement and measurement-related disclosure; provide guidance on measurement; and, address the treatment of transaction costs, including borrowing costs, for measurement.	
	Topic	Agenda Item
Project management	1. Instructions—Up to June 2017 meeting	11.1.1
	2. Decisions—Up to June 2017 meeting	11.1.2
	3. Project roadmap	11.1.3
Decisions required at this meeting	1. Project issues and subcomponents: Confirm	11.2.1
	2. Detailed project timetable: Confirm	11.2.2
	3. Transaction costs: Next steps	11.2.3
	4. Borrowing costs: Next steps	11.2.4
Supporting items	Analysis of responses to questionnaire	11.3.1
	Detailed project timetable	11.3.2
	Background information on transaction costs	11.3.3
	Excerpt: ED 35, <i>Borrowing Costs</i> , Basis for Conclusions	11.3.4

IPSASB Instructions—March 2017 meeting and earlier

Meeting	Instructions	Actions
March 2017	1. Revise project brief and create project page 2. Develop a questionnaire for IPSASB/Technical Adviser/Observers' input on the project's scope; 3. Identify project work streams 4 Provide education session on the IASB's post implementation review of IFRS 13 in September 5. Log information on how other IPSASB projects relate to the Public Sector Measurement project	1-3 Done 4 For September 5 In progress
September 2015 to December 2016	Project awaits start. First discussion in March 2017	Done
June 2015	Revise project brief for IPSASB revisions.	Done

IPSASB Decisions—March 2017 meeting and earlier

Meeting	Decisions
March 2017	Approved revisions to the project brief
September 2015 to December 2016	No decisions as project awaits start. First discussion will be in March 2017.
June 2015	Approved the “Public Sector Measurement” project brief

PUBLIC SECTOR MEASUREMENT PROJECT ROADMAP

Meeting	Objective: IPSASB to consider:
March 2017	<ol style="list-style-type: none"> 1. Introduction to the project 2. Project objectives and timetable 3. Revised project brief
June 2017	<ol style="list-style-type: none"> 1. Preliminary analysis of IPSAS measurement requirements, including treatment of transaction costs
September 2017	<ol style="list-style-type: none"> 1. Preliminary analysis of measurement-related disclosure 2. Decisions on project next steps
<i>Indicative</i>	<i>Indicative</i>
December 2017	<ol style="list-style-type: none"> 1. Discuss ED, <i>Transaction Costs</i> 2. Discuss CP for measurement
March 2018	<ol style="list-style-type: none"> 1. Approve ED, <i>Transaction Costs</i> 2. Review draft chapters for CP, <i>Public Sector Measurement</i>
June 2018	Review draft chapters for CP, <i>Public Sector Measurement</i>
Sept 2018	Approve CP, <i>Public Sector Measurement</i>
Dec 2018	Review of responses to ED, <i>Transaction Costs</i>
March 2019	Issue IPSAS amendment, <i>Transaction Costs</i>
June 2019	Review of Responses to CP, <i>Public Sector Measurement</i>
Sept 2019	Review draft ED, <i>Public Sector Measurement</i>
Dec 2019	Approve ED, <i>Public Sector Measurement</i>
March 2020	Consultation Period
June 2020	
Sept 2020	Review of responses to ED
Dec 2020	Review draft pronouncement (and/or revisions to existing IPSASs)
March 2021	Issue pronouncement (and/or revisions to existing IPSASs)

Agenda Item

11.2.1

1. Issues to Address in Public Sector Measurement Project

Questions

Do you agree with the Public Sector Measurement Task Force's recommendations that:

- (a) No new issues or subcomponents should be added to the project;
- (b) The project should not aim to address Issue 4, *Reduction of differences between IFRS measurement and IPSAS measurement*, and
- (c) Issue 5, *Reduction of unnecessary differences between IPSAS and GFS reporting guidelines*, should remain an important focus?

Detail

1. In May, IPSASB members and technical advisors responded to a questionnaire on project priorities. (An analysis of responses is provided as Agenda Item 11.3.1.) The Task Force reviewed responses and discussed whether:
 - (a) Any new project issues or subcomponents should be added; and,
 - (b) Any existing issues or subcomponents should be removed.
2. The Task Force's resulting recommendations are provided above as points (a)-(c).

Further information

3. The Task Force decided that the project brief already encompasses proposed new items. Those items have been noted as sub-items within the relevant work streams.
4. The Task Force found that the majority of issues received full support. Issues 4 and 5 were exceptions (see below). Issue 6, *Implementation Guidance*, was viewed as a high priority by the largest number of respondents (seven), with Issue 3, *Clarification of fair value in IPSAS*, viewed as a high priority by five respondents. Issue 1, *Consistency between IPSAS and the Conceptual Framework*, received good support; four respondents identified it as a high priority and none questioned its importance.
5. Respondents had conflicting views on whether Issues 4 and 5 should be project drivers:
 - (a) Issue 4, *Reduction of differences between IFRS and IPSAS measurement*: Four respondents disagreed or expressed concern (R1, R4, R12 and R14), while three viewed this issue as a priority (R8, R11 and R15).
 - (b) Issue 5, *Reduction of unnecessary differences between IPSAS and GFS reporting guidelines*: Four respondents disagreed or expressed concern (R2, R4, R13 and R14), while three viewed this issue as a priority (R3, R8 and R12).
6. The Task Force agreed that Issue 4, *Reduction of differences between IFRS and IPSAS measurement* should not be a primary focus for this project. However, the Task Force's view is that Issue 5, *Reduction of unnecessary differences between IPSAS and GFS reporting guidelines* is a public sector specific concern, noting that the emphasis should be on removing any *unnecessary* differences, and should therefore be retained.

Agenda Item 11.2.1

Decision required

The IPSASB is asked to confirm the Task Force's recommendations on issues and subcomponents for this project.

2. Timetable for Public Sector Measurement Project**Question**

Do you agree with the project timetable (Agenda Item 11.3.2)?

Detail

1. The timetable reflects the different work streams identified in the project brief. No new work streams have been identified, as noted in Item 11.2.1.
2. The Task Force reviewed an earlier draft timetable and directed that the first discussion of transaction costs should occur in June 2017. Apart from that change, the Task Force agreed with the timetable.
3. The timetable has the following underlying assumptions:
 - (a) Transaction costs will be the first subcomponent to be addressed.
 - (b) If the IPSASB decides to revise IPSAS 5, *Borrowing Costs*, then this will go straight to an exposure draft (ED), rather than involve a consultation paper (CP).
 - (c) A CP will be required for IPSASB views on measurement bases in IPSASs.
 - (d) The CP on measurement bases will comprehensively address IPSAS measurement, covering all IPSASs (other than those on financial instruments) and measurement of both assets and liabilities.
 - (e) Measurement-related disclosure and implementation guidance will be considered later in the project, after the IPSASB's positions on measurement bases are clear.
4. These assumptions reflect the following ideas:
 - (a) For measurement bases it is difficult (and undesirable) to separate out particular subcomponents for consultation because:
 - (i) Individual IPSASs may cover both assets and liabilities; and
 - (ii) This project is expected to take a comprehensive, overall approach to IPSAS measurement, rather than a piecemeal approach.
 - (b) Changes to IPSAS measurement warrant a CP stage, as the IPSASB decided during development of the project brief.
 - (c) Decisions on measurement-related disclosures and implementation guidance are conditional on the IPSASB's approach to measurement bases.

Decision required

The IPSASB is asked to confirm the project timetable.

3. Transaction Costs

Questions

1. Do the two issues in paragraph 5 below cover all the reasons why transaction costs are important for IPSAS measurement? (If not, what further concerns should this project address?)
2. Does the IPSASB agree that Task Force recommendations on treatment of transaction costs should occur later, as part of the IPSASB's review of measurement bases in IPSAS?

Detail

What are transaction costs?

1. Transaction costs are costs directly attributable to the purchase (or sale) of an asset or liability, but distinct from the asset's or liability's purchase (or sale) price. Examples of transaction costs include professional fees for legal services, transfer taxes and handling costs. IPSAS defines transaction costs for financial instruments in IPSAS 29, *Financial Instruments: Recognition and Measurement*¹. That definition revised to be more general is:

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of an asset or liability. An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the asset or liability. Examples of transaction costs include: professional fees for legal services and transfer taxes².
2. Borrowing costs, which arise from financing rather than a transaction, are discussed as Issue 4.
3. Economists and investors view transaction costs as expenses that do not add value³. They result from market imperfections and are sometimes called "frictional costs". A market improves if transaction costs reduce⁴. Financial reporting standards may require that transaction costs be capitalized when initially measuring the cost of an asset, which implies that they add value. Such costs may also be subtracted to determine the exit value of an asset.
4. Agenda item 11.3.3 has more detail on transaction costs and covers IFRS 13, *Fair Value Measurement*, which does not include transaction costs in fair value (exit value).

Why are transaction costs important for measurement in IPSAS?

5. Measurement in IPSAS should be clear about:
 - (a) Whether transaction costs impact on the monetary value assigned to an asset or liability at initial and subsequent measurement; and
 - (b) Those costs that are included in transaction costs.

¹ Paragraph 10, IPSAS 29, states that: Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability... An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial instrument.

² This description is consistent with the IFRS 13, *Fair Value Measurement*, definition and references in the project brief and Conceptual Framework. See Agenda Item 11.3.3 for further information.

³ Economics definition: "The cost associated with exchange of goods or services and incurred in overcoming market imperfections. Transaction costs cover a wide range: communication charges, legal fees, informational cost of finding the price, quality, and durability, etc., and may also include transportation costs."
<http://www.businessdictionary.com/definition/transaction-cost.html>

⁴ See <http://www.investopedia.com/terms/t/transactioncosts.asp>

Agenda Item 11.2.3

Conceptual Framework and Transaction Costs

6. The Conceptual Framework:
 - (a) Explains that transaction costs are one of two differences that distinguish entry prices from exit prices⁵;
 - (b) Classifies measurement bases as either⁶:
 - (i) Entry values or exit values; and
 - (ii) Entity specific or non-entity specific. (Financial reporting literature appears to accept that transaction costs are entity-specific costs.)
7. Therefore the treatment of transaction costs depends on the appropriate measurement basis. If a measurement basis is an entry value and entity-specific then transaction costs are likely to be included. Conversely, if a measurement basis is either an exit value or non-entity-specific then transaction costs are not included.

Is IPSAS clear about treatment of transaction costs?

8. IPSAS measurement often includes transaction costs. For example, *IPSAS 17, Property, Plant and Equipment*, and *IPSAS 31, Intangible Assets*, both include transaction costs in an asset's initial cost. *IPSAS 27, Agriculture*, measures biological assets at "fair value less costs to sell", on initial recognition and each reporting date [paragraph 16].
9. However, the IPSAS treatment of transaction costs can be unclear:
 - (a) *Accounting treatment unclear*. For example, when fair value is used to measure an asset acquired through a non-exchange transaction, IPSAS does not state whether fair value includes an estimate of transaction costs. When a replacement cost is used for measurement, it is unclear whether an estimate of transaction costs should be used to calculate the replacement cost.
 - (b) *Transaction costs unclear*. Transaction costs are not always identified in IPSAS measurement requirements. The term "transaction costs" is used in some IPSASs, but not in others. The only IPSAS definition of transaction costs relates to financial instruments. There is no general definition.

Recommendation: Consider transaction costs in the review of IPSAS measurement bases.

10. Given the connection between appropriate measurement bases and transaction costs, it is recommended that more in-depth consideration of transaction costs occur as part of the Task Force's review of IPSAS measurement bases, when the Task Force will consider the alignment of IPSAS measurement with the Conceptual Framework's approach to measurement, and:
 - (a) Map current IPSAS measurement bases to those in the Conceptual Framework; and
 - (b) Reach views on when IPSASs currently use either an entry or exit value.

Decision required

The IPSASB is asked to agree that further consideration of transaction costs should be included as part of the Task Force's review of IPSAS measurement bases.

⁵ Paragraph 7.8 of the Conceptual Framework.

⁶ See Table 1 after paragraph 7.6 of the Conceptual Framework.

4 Borrowing Costs and Public Sector Measurement

Questions

1. What next steps should the Public Sector Measurement Project take with respect to IPSAS 5, *Borrowing Costs*?
2. If the next step is development of an Exposure Draft (ED), what accounting treatment for borrowing costs does the IPSASB support? (See options A-D in paragraph 6 below.)

Detail

1. The project brief states that this project will address the capitalizing or expensing of borrowing costs. IPSAS 5, *Borrowing Costs*, defines borrowing costs as follows:

Borrowing costs are interest and other expenses incurred by an entity in connection with the borrowing of funds. [Paragraph 5]
2. IPSAS 5 requires entities to expense all borrowing costs, with the exception of costs for a “qualifying asset” during the period between acquisition/construction and active use. A qualifying asset is one that takes a substantial period of time to get ready for use or sale. IPSAS 5 gives entities the option of capitalizing borrowing costs in these circumstances.
3. Borrowing costs are similar to transaction costs in that they are attributable to acquisition of an asset, but are not part of an asset’s purchase price. They are entity-specific costs. Using the IFRS terminology, they are not a “characteristic” of the asset but depend on an entity’s financing choices. Capitalization of borrowing costs will have the effect of similar assets being measured at different initial amounts, when one entity finances asset acquisition through direct borrowing while another does not; for example, where funds are appropriated through the budget process and any borrowing for capital financing is carried centrally with no direct link between the amounts borrowed and the asset acquired or constructed.

Previous IPSASB Project 2007–2009

4. The IPSASB discussed borrowing costs between 2007 and 2009. The IPSASB decided that:
 - (a) There are public sector specific reasons to diverge from IFRS in this case. (Agenda paper 11.3.4 provides a full description of those reasons⁷.)
 - (b) In most cases the expensing of borrowing costs is the most appropriate accounting policy. Capitalization of borrowing costs should be restricted to cases where there is a direct link between the debt instrument and the qualifying asset.
 - (c) The borrowing cost issue should be deferred until the Conceptual Framework is completed.
5. That earlier project considered the four options in Table 1, on the following page.

⁷ The explanation is taken from the Basis for Conclusions in ED 35, *Borrowing Costs*.

Agenda Item 11.2.4

Table 1: Treatment of Borrowing Costs: Options

Borrowing costs—acquisition, construction or production of qualifying asset:	IPSAS 5 (A)	IAS 23 (B)	ED 35 (C)	GFS⁸ (D)
Directly attributable ► and specifically incurred ⁹	Expense or capitalize	Must capitalize ¹⁰	Expense or capitalize ¹¹	Expense
Directly attributable ► but not specifically incurred	Expense or capitalize	Must capitalize	Expense	Expense
Borrowing costs—other	Expense	Expense	Expense	Expense

6. In terms of an amendment to IPSAS 5, *Borrowing Costs*, the four options are:
- A. *No revision to IPSAS 5*, which requires all borrowing costs to be expensed, except for those directly attributable to acquisition, construction or production of a qualifying asset, where there is an option to capitalize borrowing costs.
 - B. *IAS 23 convergence*: An amendment to require capitalization for borrowing costs that are directly attributable to acquisition, construction or production of a qualifying asset.
 - C. *ED 35's approach*: An amendment to require that the capitalization option only applies to those borrowing costs that are *both* directly attributable to, *and specifically incurred for*, acquisition, construction or production of a qualifying asset.
 - D. *GFS alignment*: An amendment to remove the capitalization option so that all borrowing costs are capitalized, with no exceptions.

GFS reporting guidelines—Expense Borrowing Costs

7. Since 2009 the IPSASB has approved a policy to reduce differences between IPSAS and GFS reporting guidelines¹². All borrowing costs are expensed under GFS reporting guidelines¹³.

Decisions required

The IPSASB is asked to decide on:

1. Whether the Public Sector Measurement Project should draft an ED to amend IPSAS 5, *Borrowing Costs* for IPSASB consideration in September, 2017; and
2. What (if any) amendment to IPSAS 5, *Borrowing Costs*, does the IPSASB support?

⁸ The IPSASB's March 2017 IPSASs–GFS tracking table (agenda item 1.8) states that the GFS-aligned treatment (available under IPSAS 5) is to “choose the “expense borrowing costs” option and list components of borrowing costs separately”.

⁹ ED 35 uses the phrase “specifically incurred for” instead of “directly attributable to”.

¹⁰ IAS 23 Borrowing Costs requires that borrowing costs directly attributable to the acquisition, construction or production of a 'qualifying asset' (one that necessarily takes a substantial period of time to get ready for its intended use or sale) are included in the cost of the asset.

¹¹ ED 35 notes that the capitalization option is available for cash-generating & non-cash-generating qualifying assets.

¹² *Process for Considering GFS Reporting Guidelines during Development of IPSASs*

¹³ Refer March IPSASB meeting's agenda item 1.8, Tracking Table—IPSASs and GFS Reporting Guidelines: Comparison of Recognition and Measurement Requirements. See issue 1B1 on page 8.

AGENDA ITEM 11.3.1: ANALYSIS OF RESPONSES TO QUESTIONNAIRE**List of Respondents**

Response #	Respondent Name	Country	Further Comment
01	Rod Monette and Leona Melamed	Canada	IPSASB Member, Technical Advisor (TA)
02	Mike Blake	Australia	IPSASB Member,
03	Jakob Prammer	Austria	IPSASB TA
04	Bernhard Schatz	Austria	IPSASB Member
05	Juan Zhang	China	IPSASB Member
06	Sebastian Heintges with Institut der Wirtschaftsprüfer Working group on Public Sector Accounting	Germany	IPSASB Member, Institute
07	Marc Weymuth and Claudia Beier	Switzerland	IPSASB Member and TA
08	Chris Nyong	Nigeria	IPSASB Member
09	Takeo Fukiya (with Kenji Izawa review)	Japan	IPSASB TA
10	Aracelly Mendez	Panama	IPSASB Member
11	Angela Ryan and Anthony Heffernan	New Zealand	IPSASB Member and TA
12	Ian Carruthers	United Kingdom	IPSASB Chair
13	Accounting Standards Board of South Africa	South Africa	Standard setter
14	Conseil de normalisation des comptes publics (CNOCP)	France	Standard setter
15	Australian Accounting Standards Board (AASB)—Staff	Australia	Standard setter

Question 1

Thinking about Appendix A and experiences in your jurisdiction and/or region,

(a) Are there any other issues that you consider should be covered by this project? **Yes / No**

(b) Have you identified any additional sub-components that the project should cover? **Yes / No**

Please provide brief details of why you think issues and/or additional sub-components should be included in the project (for example: public interest considerations, usefulness for accountability and decision-making purposes).

Summary of Responses

	RESPONDENTS (R #)	TOTAL
(a) Yes—other issues	01, 02, 04, 05, 10, 11, 12, 14	8
No other issues	07, 08, 09, 13, 15	5
No comment	03, 06	2
(b) Yes— additional sub-components	02, 07, 09, 11, 12	5
No additional sub-components	01, 04, 05, 08, 10, 13, 14, 15	8
No comment	03, 06	2
TOTAL RESPONDENTS		15

R#	C #	Question 1—Comments
01	Y	<p>(a) <i>Other issues</i>: Consider the extent to which market values should be used in IPSAS in relation to public interest considerations. In particular, the use of current market rates of interest as discount rates for long-term liabilities such as pensions, and use of market values for financial instruments such as reserve assets.</p> <p><i>Reasons why</i>: More specific analysis is needed to determine what best meets public sector accountability and public interest considerations.</p>
02	Y	<p>(a) <i>Other issues</i>: Firstly, I need to point out that Australia adopts IASB standards for both the private and public sectors – we adopt a transaction neutral approach - in this case IFRS 13 Fair value measurement, unchanged. Adoption in Australia of this standard in the public sector (in particular local government) has proven difficult mainly in relation to disclosures and some short-term relief has been provided although, in my jurisdiction</p>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 1—Comments
		<p>(Tasmania), all public sector entities have fully complied as this applies to assets. The issues which arose included:</p> <ul style="list-style-type: none"> - Mixed group arrangements – for-profit public sector entities, of which there are a number the most significant of which (in value terms) are in the electricity and water/sewerage sectors. These entities generally fair value their assets on an earnings basis which may give rise to complications when preparing whole of government consolidated accounts. - Establishing residual values mainly in the roads sector. Some constituents argued that for a road or for components of a road, the residual value should be high, in some cases higher than 50%, mainly because maintenance and other functions keep roads/road components in good condition/extending lives meaning that the annual depreciation charge will be low. In my view, Australia's suite of standards suggest that residual values should only ever be an insignificant amount and the concern could be addressed by sensible lives allocated to roads/road components. - Application of the fair value hierarchy – deciding between level 1 inputs through to level 3 inputs and then, having done so, complying with the relevant disclosure requirements. <p>Regarding the liabilities side of the balance sheet, the main issue of which I am aware is determining discount rates for valuing long-lived liabilities like superannuation/pension liabilities. Currently the Australian Standard – Employee benefits, requires use of a government bond rate at a point in time unless a deep market for securities exists – which is not the case for the public sector. Use of a point in time bond rate (normally being the balance date) can, and generally does, give rise to significant fluctuation in the liability with implications for the Income Statement. Jurisdictions in Australia have, to an extent, solved this with much disclosure including the cash based obligations of the liability and when these will be met over future years.</p> <p>(b) Additional subcomponents: As above. I support breaking down long-lived infrastructure assets into relevant components, roads being an example, with asset lives, values and depreciation periods established for each component. Reasons why: As outlined above.</p>
03	NC	[No comment]
04	Y	<p>(a) <i>Other issues:</i> I agree that the most misunderstanding in the use of certain measurement methods in the public sector are with the fair value measurement, but from my experience sometimes this also is true for historic cost. We have a pretty fair section in the CF dealing with measurement basis and which questions could be answered by them or what the underlying management perspective comes along with the measurement method maybe it will be worth the effort to include this line of thought also in the PSMP, whether or not this will lead to any changes or additional guidance I am unable to foresee.</p> <p><i>Reasons why:</i> Sometimes I come across the perception that there is a “free choice” between measurement bases or they are purely chosen by data availability or traditional motives instead of generating the best information for accountability and decision making.</p>
05	Y	<p>(a) <i>Other issues:</i> I think it is necessary to consider the initial measurement and subsequent measurement separately but not sure whether this is covered in Issue 7. For example, transaction price and fair value at initial measurement. Not sure whether this is covered in “Issues” or in “Subcomponents”. In view of those items listed in A2, I think this matter should be grouped in A1.</p>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 1—Comments
06	NC	[No comment]
07	Y	<p>(b) Additional subcomponents:</p> <p>Issue 3: Clarification of fair value in IPSASs</p> <p>Guidance related to IFRS 13 (linkage to FI Project). In the actual TBG proposal on Financial Instruments there is Fair Value guidance based on IFRS 13 in relation to the measurement of some public sector specific financial instruments.</p> <p>Clarification of the meaning of “fair value” in IPSASs. The boundary between Market Value and Fair Value is to be clarified as well.</p> <p><i>Reasons why:</i> Measurement of some public sector specific financial instruments (e.g. unquoted equity instruments or concessionary loans at initial recognition) remains a critical issue and is currently based on IFRS 13.</p> <p>Currently there is some wording to the difference between Fair Value and Market Value only on the level of BC’s, in the Conceptual Framework BC 7.20 to 28.</p>
08	N	[No further comment]
09	Y	<p>(b) Additional subcomponents: This issue is relating to both IPSAS 17 and 33. Initial measurement for existing PPE that have been measured at nominal value under the previous accounting method.</p> <p>Reasons why: In our jurisdiction, local governments are now moving to accrual based accounting (other than IPSASs), and there is an issue that which measurement basis is appropriate on first adoption.</p>
10	Y	<p>(a) Other issues: It would be important to include as part of Issue 4 – to improve consistency between the financial statements in IPSAS and IFRS. A good starting point would be to unify the names of the financial statements.</p>
11	Y	<p>(a) Other issues</p> <p>Some of our points may already be envisaged to be included in issues noted in the current project brief.</p> <p>For context, most property, plant and equipment, including specialist assets in New Zealand, are measured at fair value, so many of the issues in practice relate to challenges in determining fair value in the public sector.</p> <p>1. Selecting the appropriate valuation method</p> <p>Many public sector assets are used for both service potential and to generate cash. Making judgments about whether to use a replacement costs approach (to reflect service potential) or using a commercial-based valuation (e.g. discounted cash flow) can be difficult.</p> <p>2. DRC</p> <p>Public sector entities in New Zealand frequently use depreciated replacement cost (DRC) to estimate the fair value of property, plant and equipment, including infrastructure assets because of their specialist nature and to reflect their service potential. DRC includes “optimization” for obsolescence and relevant surplus capacity.</p> <p>Preparers highlight the application of a DRC (including all its component assumptions) is challenging because of the lack of guidance in the</p>

R#	C #	Question 1—Comments
		<p>standards. Also, any small amount of guidance that does exist in the standards is not always consistent between standards.</p> <p>Should the “economic value” of assets that produce public goods or services that do not generate revenue be used in assumptions about replacing assets and replacement cost?</p> <p>3. Unit of account</p> <p>Lack of guidance and inconsistencies between standards regarding the unit of account when determining the appropriate measurement basis for different transactions. Differences arise between applying different measurement bases on a unit of account basis for initial recognition, subsequent re-measurement, impairment and reclassification of assets and liabilities.</p> <p>4. Valuation Profession</p> <p>It's desirable that standards and guidance align with the valuation standards used by the international valuation profession and actuaries where appropriate. If accounting requirements and valuing/actuarial standards are not aligned where appropriate this can lead to frustration and a lack of credibility with the valuation process for financial reporting. It also adds to the direct cost of the valuation process.</p> <p>5. Measurement changes and reporting performance</p> <p>Changes in measurements of assets and liabilities can be material and volatile. Some valuation movements are presented through net assets/equity and some through surplus/deficit. There appears to be inconsistency in the treatment of similar valuation movements across standards and lack of conceptual basis for whether a valuation change should be recorded in net assets/equity or surplus/deficit.</p> <p>Communicating the impact of large valuation movements in surplus/deficit can be challenging. This may lead to preparers using alternative measures of performance to help tell their performance story. The impact of large and volatile movements in measuring assets and liabilities through surplus/deficit may lead to some countries choosing not to adopt certain IPSASs.</p> <p>Is there merit in distinguishing movements in a valuation for which the entity is accountable and reflects entity performance (e.g. forgiveness of debt, concessions granted) and movements which reflect market or environment changes?</p> <p>6. Cost-benefit of current value measurement approaches</p> <p>Some preparers (particularly medium-to-small public sector entities in New Zealand applying IPSAS based standards) argue that difficulties and costs exceed the benefits when determining fair value of certain assets and liabilities. Preparers want more flexibility to apply a cost approach when they consider the cost of measuring the fair value outweighs the benefits.</p> <p>7. Management intention</p> <p>Preparers feel the basis for choosing an appropriate measurement approach, should include consideration of the intention for holding the asset or liability. Also there is lack of IPSASB guidance for how a PPE asset should be measured when it is no longer expected to be used as originally intended, because it is now expected to be recovered through a sale.</p> <p>8. Consideration of IFRS 13 Fair Value guidance</p> <p>With the lack of public sector guidance on fair value preparers often use the framework and guidance in IFRS 13 as authoritative support. However,</p>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 1—Comments
		<p>IFRS 13 has not been written with the public sector in mind. We would like to see IFRS 13 principles and guidance being tested for application in the public sector.</p> <p>9. Mixed group concerns</p> <p>To avoid mixed group issues, the reasoning for any difference in the concept of fair value/market value (and the measurement requirements) between the public sector and for-profit sector would need to be clearly explained.</p> <p>10. Useful Life Assumptions</p> <p>Should useful life assumptions be sensitive to maintenance assumptions? If assets are not regularly maintained, it generally means that assets will depreciate faster than well maintained assets. How should this be measured and communicated? Similarly, how should deferred maintenance be measured and communicated to users?</p> <p>11. When is a value too unreliable for financial reporting?</p> <p>Sometimes a valuation will involve a wide range of possible outcomes and a probability estimate (which may really reflect a “best guess” based on a lot of uncertain factors). At what point should a very uncertain estimate of an asset or liability not be recognized. Is it always better to have some sort of measure recognized (no matter how uncertain) rather than have none at all?</p> <p>(b) Additional subcomponents:</p> <p>We have included a list of specific measurement practice issues for your consideration in Appendix 2¹⁴. Some of the items in the appendix illustrate the issues noted above.</p> <p>Reasons why: included under each issue noted in (a) and (b)</p>
12	Y	<p>(a) Other issues:</p> <ul style="list-style-type: none"> - Links to IVSC guidance - Hierarchy on how to apply IVSC guidance in particular situations e.g. Listed building used as an office inside another heritage building not used for operational purposes <p>(b) Additional subcomponents:</p> <ul style="list-style-type: none"> -Issue needs to start with mapping existing GFS guidance, and examining what the practical and/or theoretical differences are. <p>Reasons why:</p> <p>Practical links to valuation guidance, so that accountants can understand what they're getting from valuers and valuers understand what the accountants want from them and why.</p>

¹⁴ Respondent 11's appendices (1 and 2) are included after the end of this table.

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 1—Comments
13	N	<p>(a) Other issues: <i>We agree with the issues identified in Appendix A and have not identified any additional issues that should be considered.</i></p> <p><u>Issue 1</u></p> <p><i>Since the issue of the Conceptual Framework by the IPSASB, the general feedback from our stakeholders indicates that they are unsure how the current inconsistencies that exist between the Conceptual Framework and the IPSASs will be addressed. In particular:</i></p> <ul style="list-style-type: none"> <i>There is uncertainty about how the measurement requirements in the Conceptual Framework affect the existing IPSASs. For example, the Conceptual Framework omits fair value as a measurement basis but refers to market value, while substantially all the IPSASs include fair value in the measurement requirements. Value in use and the replacement cost are measurement bases in the Conceptual Framework but they are currently only used in calculating the recoverable (service) amount in the impairment standards.</i> <i>The IPSASB has not clearly communicated how the new recognition requirements will be addressed in the measurement project, especially when entities consider measurement uncertainties when recognizing elements of the financial statements.</i> <p><i>In addition, our stakeholders are concerned about how the new thinking and concepts in the Conceptual Framework should be applied as there is no guidance that assists in clarifying how the measurement bases, and the circumstances under which such bases, should be applied.</i></p> <p><u>Issue</u></p> <p>(b) Additional subcomponents: <i>No comment can be provided as we are unsure how the subcomponents in A2 relate to the issues identified in A1.</i></p> <p>Reasons why:</p> <p><i>While it is clear that the Conceptual Framework is applicable in cases where there is no guidance for the accounting treatment of certain transactions, for as long as the inconsistencies addressed above remain, there is a risk that entities that apply the Conceptual Framework will present accounting policies that conflict with, or are different to, the requirements in the current IPSASs.</i></p>
14	Y	<p>(a) Other issues: <i>We would put forward an issue that clearly states that some specific areas in the public sector might need significant adaptations of the measurement bases set out in the Conceptual Framework.</i></p> <p>(b) Additional subcomponents: <i>N/A at this stage</i></p> <p><i>Reasons why:</i> We strongly advocate that it is critical to the project to identify the specific needs of the public sector in terms of measurement as compared to the private sector. It follows that usual measurement bases should be tailored to fit those specificities. Such an issue stands halfway between an adaptation of concepts and implementation guidance.</p> <p><i>In our jurisdiction, some specific assets are measured at a token or a non-revisable fixed value:</i></p> <ul style="list-style-type: none"> <i>Some heritage assets are measured using symbolic values for the sake of completeness of inventory and to facilitate the identification and the recognition of related capitalised subsequent expenditure;</i> <i>Some very specific assets of the Ministry of Defence are considered to not deteriorate and are neither depreciated nor impaired. Such items are not intended to be replaced; they have no equivalent in the private sector and would require extensive conversion work to be suitable for everyday use, if ever it made sense or were feasible to do so.</i> <p><i>Those assets have specific features in that they cannot easily be sold and they cannot be reliably measured.</i></p>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 1—Comments
15	N	<p>(a) Other issues: N/a</p> <p>(b) <i>Additional subcomponents:</i> We wanted to highlight that these are the areas in which Australian entities have identified challenges with or that the AASB is exploring further (these topics are likely to be addressed by already identified subcomponents):</p> <ul style="list-style-type: none"> • what is obsolescence and how does it affect measurement • identifying entity-specific restrictions vs. market restrictions • providing meaningful disclosure about assumptions/judgments/estimates used in the measurement of assets • (recognition and) measurement of licences by a grantor when potential revenue stream created • appropriate discount rates for long-term liabilities <p><i>Reasons why:</i> As noted, the areas mentioned are likely within scope of the already identified subcomponents.</p>

Question 2

Are there any issues and/or sub-components listed in Appendix A that you think should not be covered by this project? **Yes / No**

If so, please provide your reasons:

Summary of Responses

	RESPONDENTS (R #)	TOTAL
Yes	04, 10, 12, 13, 14	5
No	02, 05, 07, 08, 09, 11, 15	7
Other comment	01	1
No comment	03, 06	2
TOTAL RESPONDENTS		15

R#	C #	Question 2— Comments
01	OC	<i>Issue 4:</i> Proceed with caution for Issue 4, reduction of differences between IPSAS and IFRS measurement. <i>Reasons why:</i> Following the rules of the road should have resulted in consistent guidance with IFRS unless public sector specific considerations warranted a different measurement basis.
02	No	No
03	NC	[No comment]
04	Y	<i>Issues and/or subcomponents that should <u>not</u> be covered:</i> I am not sure about Issue 4 and 5. Currently we do this on a standard level, what kind of benefit or line of work would be dealt with in the PSMP? <i>Reasons why:</i> Limit double efforts.
05	N	[No further comment]
06	NC	[No comment]
07	N	No issues or subcomponents not to be covered.

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 2— Comments
08	N	[No further comment]
09	N	[No further comment]
10	Y	<p><i>Issues and/or subcomponents that should not be covered:</i> Financial instruments: Address the relationship between Financial Instruments measurement and measurement terminology used in other IPSASs.</p> <p><i>Reasons why:</i> In the Republic of Panama, this subcomponent has low impact because very few public institutions are allowed to use financial instruments (e.g. Ministry of the Economy and Finances and a couple of public companies). If there is a seminar about financial instruments, most of the accountants in the public sector will not take advantage of the new knowledge because they don't deal with financial instruments in their day-to-day work. Therefore, it would be better to focus on issues and sub-components that will be useful for the majority of accountants in the public sector.</p>
11	N	<p><i>Issues and/or subcomponents that should <u>not</u> be covered:</i> At this stage we do not suggest any be removed.</p> <p><i>Reasons why:</i> It's not clear what is meant by the description of some of the issues in Appendix A. It's possible with some initial work to understand them a bit more, some could be removed from the project or addressed in the infrastructure project.</p>
12	Y	Issue 4. <i>Reasons why:</i> Don't think it does differ. Also potentially conflicts with whole purpose of the project! Issue 1 must take priority.
13	OC	Issues and/or subcomponents that should <u>not</u> be covered: <i>We do not believe that the elimination of differences between IPSAS and the GFS is a priority. Reasons why: As noted above.</i>
14	Y	<p><i>Issues and/or subcomponents that should <u>not</u> be covered:</i></p> <p>While it would be useful to understand the differences between IPSAS measurement and GFS measurement (see issue 5 of appendix A1) we would still question the need to reduce those differences.</p> <p>Reducing differences between IPSAS and IFRS measurement bases (see issue 4 of appendix A1) should not be an objective in itself, especially if it is used to address difficult areas in public sector measurement (see issue 6 of appendix A1) for the reasons explained below.</p> <p><i>Reasons why:</i></p> <p>Issue 5: This is because IPSASs and GFS do not address the same objectives and the same need for information. GFS are set towards the goal to analyse and evaluate fiscal policy, through the use of macroeconomic data, whereas accounting principles are set to reflect operations an entity (a group of entities) is(are) accountable for with a view to help the decision-making process of that entity (group of entities).</p> <p>Articulation of issues 4 and 6 of appendix A1: pointing out difficult areas in the public sector measurement might mean that the measurement bases retained in the Conceptual Framework are not fully relevant and that they should be adapted. Reducing differences with IFRS measurement in those areas might prove inefficient. Those specific areas should be carefully identified and delineated and any adaptation should come with a clear articulation with the measurement bases that are set out in the Conceptual Framework. In a nutshell, reducing differences with IFRS measurement should only relate to non-specific public sector items.</p>
15	N	N/A (Not applicable)

Question 3

Thinking about guidance on measurement bases and/or application of measurement requirements:

- Where are the gaps on measurement guidance which, in your view need to be addressed?
- What type of additional guidance would be helpful?

Please provide any examples of measurement guidance, developed in your jurisdiction to address public sector measurement issues, that you consider would be useful references for this project.

Summary of Responses

	RESPONDENTS (R #)	TOTAL
(a) Gaps on measurement guidance to address	01, 02, 04, 05, 07, 09, 10, 11, 12, 13, 15	11
(b) Type of helpful additional guidance	01, 02, 03, 04, 07, 09, 10, 11, 12, 13, 15	11
Examples of guidance provided	02, 11, 13	3
No comment	06, 08, 14	3
TOTAL RESPONDENTS		15

R#	C #	Question 3— Comments
01	R	<p><i>Gaps on guidance:</i> Selection of discount rates is an issue currently being addressed at the Government of Canada.</p> <p><i>Type of helpful additional guidance:</i> Guidance on selection of discount rates to reflect the specific measurement objective/basis. For example, how does use of a current rate of interest reflect the “cost of fulfillment” measurement basis for liabilities?</p>
02	R	<p><i>(a) Gaps on measurement guidance:</i></p> <p>The most useful guidance I have come across is that issued by the State of New South Wales - https://www.treasury.nsw.gov.au/sites/default/files/pdf/TPP14-01_Accounting_Policy_-_Valuation_of_Physical_Non-Current_Assets_at_Fair_Value.pdf</p> <p>In addition - all of these have been included in the draft briefing paper on infrastructure I prepared and forwarded to John and Jo early in April 2017)</p> <ul style="list-style-type: none"> • Conseil de Normalisation des Comptes Publics (CNOCP), Standard 6, <i>Tangible Assets</i> • Chartered Institute of Public Finance and Accountancy (CIPFA): <i>Code of Practice on Transport Infrastructure Assets (and also Guidance</i>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 3— Comments
		<p><i>Notes)</i></p> <ul style="list-style-type: none"> • CIPFA Local Authority Technical Bulletin 100, <i>Project Plan for Implementation of the Measurement Requirements for Transport Infrastructure Assets by 2016/17</i> • South African Accounting Standards Board (SAASB), <i>Accounting for Infrastructure Assets - Facts and Fiction</i> • SAASB, <i>Summary of Results of the Post-implementation Review of Selected Standards of GRAP</i> • CPA Canada, <i>Accounting for Infrastructure Assets</i> • CPA Australia, <i>Guide to Valuation and Depreciation under the International Accounting Standards for the Public Sector</i> • Queensland Treasury, <i>Non-Current Asset Policies for the Queensland Public Sector</i> • International Valuation Standards Council, Exposure Draft, <i>Valuations of Specialised Public sector Assets</i> • International Monetary Fund, <i>Government Finance Statistics Manual 2014</i> • In Australia the AASB deliberated on impairment related matters resulting in its development of “Simplified impairment requirements bring cost savings to Australian NFPs+ - refer http://www.aasb.gov.au/News/Simplified-impairment-requirements-bring-cost-savings-to-Australian-NFPs?newsID=213529. This may be relevant to IPSASB considerations <p>(b) <i>Type of helpful additional guidance:</i> Guidance issued by a State jurisdiction for use in that State but more generally available to others. Refer above.</p>
03	R	<p>(b) <i>Type of helpful additional guidance:</i></p> <p>e.g. a decision tree or a catalogue with questions, on how to choose the most appropriate measurement base for certain transactions with respect to your entity/entities;</p> <p>definitions and very thorough and consistent use of the terms: cost / expense / value / price;</p> <p>guidance on how to deal with left-out areas that are deliberately not measured correctly or at all, eg. military assets</p>
04	R	<p>(a) <i>Gaps on measurement guidance:</i> Determination of reliable information. A receipt from a purchase is an easy to get and very easy to verify information for the historic cost. Nearly all other measurement basis require judgment or the use of volatile information (where you will have to explain the differences). Arguing the use of this “more volatile information” would need to be done in regard to the benefits for decision making and accountability.</p> <p>Many institutions have established a purchase department and respective rules and regulations therefore it is easy to use this information for measurement. How would these organizational requirements look like if you go for fair value or replacement cost?</p> <p>What about the frequency of re-measurement? Are there experiences on the cost involved etc.</p> <p>(b) <i>Type of helpful additional guidance:</i> Model processes and flow charts (not within the mandate of a standard setter but maybe as supplement information); Databases and information sources to be used</p>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 3— Comments
05	R	<i>(a) Gaps on measurement guidance:</i> I noted one practical difficulty regarding investment in unquoted shares, the fair value of which is difficult to be obtained. In my view, the guidance in IFRS 9 cannot help, especially for investment in public sector entities.
06	NC	[No comment]
07	R	<p><i>(a) Gaps on measurement guidance:</i> Linkage to Fair Value (see above)</p> <p>There is a potential conflict between Issues 4 and 5. Although IFRS and GFS have similarities (such as using market values for a wide range of assets) there are also differences. In these cases, a decision on what to prioritize might be necessary. Generally, differences between IPSAS and GFS increase the costs in the public sector.</p> <p><i>(b) Type of helpful additional guidance:</i> See above [Staff: Response to Q1 includes suggested guidance.]</p>
08	NC	<p>(a) MY JURISDICTION IS YET TO COMMENCE ACCRUAL ACCOUNTING IN ITS FULLNEWS. WE AWAIT THE BOARD'S GUIDANCE.</p> <p>(b) No.</p>
09	R	<p>3 (a) Considering the CFW, fair value is one of the important gaps.</p> <p>3 (b) Potentially, IFRS 13 equivalent standard or guidance on fair value will be useful.</p>
10	R	<p><i>(a) Gaps on measurement guidance:</i> It is difficult to answer this question because one needs to be an expert in guidance on measurement bases and measurement requirements to identify the gaps. However, in IPSAS there are some measurement requirements that seem to be impossible to put into practice. For instance, the measurement of Non-Financial Assets, one would think that one needs to obtain the fair value of absolutely all the non-financial assets within the same classification in order to replace the historic cost.</p> <p><i>(b) Type of helpful additional guidance:</i> In the Republic of Panama, we are in our first steps towards the implementation of IPSAS. We have not yet developed guidelines on public sector measurement issues, but we are looking forward to use the guidelines developed by IPSAS in this project as reference.</p>
11	R	<p><i>(a) Gaps on measurement guidance:</i></p> <ol style="list-style-type: none"> 1. Guidance on current value measurement approaches and value in use, including DRC, to be consistently applied across different standards (e.g. PPE, impairment) 2. Guidance on what measurement basis to use. For example, whether to apply a replacement costs basis (to reflect service potential) or a commercial discounted cash flow (to reflect economic benefits) for assets that have mixed objectives 3. Guidance for impairment of network assets, where only a portion of the network is damaged (likely to be covered in the infrastructure guidance) 4. Guidance on determining discount rates (including risk adjustments for assets), consistently applied across all standards (where relevant) especially when cash flows extend beyond the observable market yields available

R#	C #	Question 3— Comments
		<p>(b) <i>Type of helpful additional guidance:</i></p> <ul style="list-style-type: none"> • Additional guidance/implementation support on measuring the value-in-use of cash and non-cash generating assets for impairment testing purposes, especially determining an appropriate discount rate. • Implementation guidance on how to apply the different measurement approaches to transactions with both exchange and non-exchange characteristics. • Some prepares have highlighted IPSAS 27 Agriculture causing significant implementation issues when applying its fair value measurement requirements – additional guidance/implementation support may be useful <p><i>Examples of guidance? Yes</i>—attached</p> <ul style="list-style-type: none"> • The NZASB have added some integral application guidance to PBE IPSAS 17 on the estimation of fair value using the depreciated replacement cost method (refer Appendix 1 attached plus it's available on the XRB website: https://xrb.govt.nz/accounting-standards/public-sector/pbe-ipsas-17/) • The New Zealand Treasury has published <i>Valuation Guidance for Property, Plant and Equipment, Including Specialised Items in the Health and Education Sectors</i> This can be downloaded at: http://www.treasury.govt.nz/publications/guidance/reporting/accounting/property • NAMS has published asset valuation and depreciation guidelines for the valuation of assets using DRC. This is not publicly available and can only be purchased at: http://www.nams.org.nz/pages/75/asset-valuation-and-depreciation-guidelines.htm • The New Zealand Treasury has published a discount rates and CPI assumptions methodology. In practice, this is used by certain public sector entities when applying PBE IFRS 4, PBE IPSAS 19, PBE IPSAS 25, and PBE IPSAS 29. (The methodology is towards bottom of the web page). http://www.treasury.govt.nz/publications/guidance/reporting/accounting/discountrates • The New Zealand Treasury has published <i>Valuation Guidance for Cultural and Heritage Assets</i> in 2002. This can be downloaded here: http://www.treasury.govt.nz/publications/guidance/reporting/accounting/cultural
12	R	<p>(a) <i>Gaps on measurement guidance:</i> Links to IVSC guidance and clarity over GFS requirements and how these differ from IPSAS in theory and in practice.</p> <p>(b) <i>Type of helpful additional guidance:</i> (i) Cross references / links to IVSC guidance.</p> <p>(ii) 'How to' application guide – ie flow-chart of how to navigate difficult issues (see response to 1(a)) Also how to meet GFS requirements.</p>
13	R	<p>(a) <i>Gaps on measurement guidance:</i> Our stakeholders identified the following gaps on measurement where guidance could be developed:</p> <p><u>IPSAS 33 on First Time Adoption of IPSAS</u></p> <p><i>IPSAS 33 requires a public sector entity to measure assets and liabilities at fair value if there is no reliable information on cost when adopting IPSAS for the first time. However, IPSAS 33 does not provide guidance on which measurement bases can be used to measure assets and liabilities if information on fair value and cost is not available when adopting IPSAS 33 for the first time.</i></p> <p><i>The ASB has issued Directive 7 on The Application of Deemed Cost which provides application guidance for determining deemed cost in accordance</i></p>

R#	C #	Question 3— Comments
		<p>with the Standards of Generally Recognised Accounting Practice (GRAP). We suggest that the IPSASB considers similar guidance for IPSAS 33. Our guidance (paragraphs .6 to .11 of Directive 7) provides the following:</p> <ul style="list-style-type: none"> • When an entity initially recognises or acquires an asset using the Standards of GRAP, it measures such assets using either cost or fair value (acquisition cost). Where the acquisition cost of an asset is not available on the adoption of the Standards of GRAP or on the transfer date or the merger date (initial acquisition), acquisition cost is measured using a surrogate value (deemed cost) at the date an entity adopts the Standards of GRAP or on the transfer date or the merger date (measurement date). Deemed cost is determined as the fair value of an asset at the measurement date. • We have defined “deemed cost” to be a surrogate value for the cost or fair value of an asset at its initial acquisition, and is determined by reference to the fair value of the asset at the date of adopting the Standards of GRAP or on the transfer date or the merger date (measurement date). • If fair value cannot be determined, the Directive allows entities to estimate the fair value based on the depreciated replacement cost of the assets, in the case of investment property, property, plant and equipment and intangible assets, and replacement cost for heritage assets. <p>Link to guidance: http://www.asb.co.za/LinkClick.aspx?fileticket=x-BGR02xVtw%3d&portalid=0</p> <p><u>IPSAS 27 on Agriculture (relates to issue 6)</u></p> <p>IPSAS 27 requires entities to measure biological assets at fair value, or where fair value is not reliably determinable, at cost. There are also practical issues regarding the measurement of bearer plants based on the new amendment made to IPSAS 27 and IPSAS 17. In particular, there is no practical guidance in situations where fair value or cost cannot be reliably measured. With the amendment to the accounting treatment for bearer plants, it is difficult to track and measure the cost inputs incurred in a plantation, and the fair value could also be difficult to determine, particularly where the plantation has not yet matured.</p> <p><u>IPSAS 17 on Property, Plant and Equipment (relates to issue 6)</u></p> <p>IPSAS 17 does not provide guidance on the recognition and measurement of heritage assets and only requires disclosure of such items citing that measurement is not easy to determine. The ASB has developed such guidance. Whilst, we are aware that the IPSASB has recently issued a Consultation Paper on the topic, guidance on the measurement of heritage would be vital to enhance the reliability and relevance of financial reporting on heritage. Link to guidance: http://www.asb.co.za/LinkClick.aspx?fileticket=I9SjFbwykGU%3d&portalid=0</p> <p><u>Non-cash-generating assets (relates to issue 6)</u></p> <p>Public sector assets are often non-cash-generating and are used to generate service potential. Additional guidance on the measurement of non-cash-generating assets may be useful, particularly if it results in more objective, non-entity specific values.</p> <p><u>Infrastructure assets (relates to issue 6)</u></p> <p>IPSAS 17 does not provide guidance on the recognition and measurement of infrastructure assets, other than stating that infrastructure assets meet the definition of property, plant and equipment and should be accounted for as such.</p> <p>In our jurisdiction, the measurement of infrastructure assets where historical cost is not available remains a challenge. Preparers find it difficult to</p>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 3— Comments
		<p>determine whether such assets should be valued based on the different parts comprising the asset (pipes, cement, etc.), based on sections of the assets (e.g. per kilometre of road), etc.</p> <p>We take note of the IPSASB's planned project on infrastructure assets. However, we believe that guidance on the measurement of infrastructure assets may be useful, both in terms of initial measurement where historical cost is not available, and for subsequent measurement where a measurement basis other than historical cost is used.</p> <p><u>Provisions for rehabilitation of landfill sites (relates to issue 6)</u></p> <p>In our jurisdiction, preparers experience difficulties in accounting for landfill sites and the related obligations. Issues identified include:</p> <ul style="list-style-type: none"> • Asset recognition <ul style="list-style-type: none"> ○ Difficulties in distinguishing the components of cost on initial recognition including the distinction between land and the landfill, and the cost of permits and other regulatory fees ○ Treatment of the useful life and change in use of landfill sites after closure • Liability recognition <ul style="list-style-type: none"> ○ Determination of the cost of rehabilitation, including the treatment of compliance costs arising from changes in legislation, which discount rate to use, how to treat monitoring and post-closure monitoring expenses, whether the cost of rehabilitation relates to the whole site or just the part that has been utilised. ○ Treatment of changes in cost and other estimates, including changes in the discount rate, changes in costs after the closure of the landfill site, changes in legislation as a result of new regulations affecting items in the landfill site such as tyres, changes in expected post closure monitoring expenditure. • Treatment of changes in the provision – as a change in estimate or as an error. • Recognition and measurement of ongoing expenditure after closure of the site, such as monitoring and site inspections, etc. • Application of the principles by analogy to other assets such as quarries. <p>Guidance, to address these difficulties would be useful. The ASB has included a project on its work program to develop such guidance in 2017, and will be willing to share any developments from this project with the IPSASB.</p> <p><u>Inability to reliably measure assets (relates to issue 6)</u></p> <p>A number of IPSASs allow certain assets not to be recognised if the asset cannot be reliably measured. Guidance on how to think about and apply this consideration of not being able to make a reliable estimate of the asset's value will be useful in existing IPSASs. It would also be useful to consider guidance on how to deal with assets and liabilities that are not recognized where they cannot be measured in a manner that achieves the qualitative characteristics in accordance with the new recognition criteria in the Conceptual Framework.</p> <p><u>Determining fair value (relates to issue 3)</u></p> <p>Generally, we note that there is a lack of understanding of how fair value should be calculated in the public sector. There is a need for guidance to be</p>

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 3— Comments
		<p><i>developed to assist in the calculation of fair value for various assets and liabilities in the public sector.</i></p> <p><i>In addition, our stakeholders observed that the nature of public sector assets and liabilities is often such that an active market for the determination of fair value / market value does not exist. Additional guidance on how fair value / market value should be determined in an inactive market may be useful, particularly if it results in more objective, non-entity specific values.</i></p> <p><i>We believe it is vital for the IPSASB to clarify how Issue 3 (clarification of fair value) of this project will be addressed seeing that fair value is omitted in the Conceptual Framework. If fair value has limited relevance in the public sector environment, does this mean market value will replace fair value in the measurement requirements in the IPSASs?</i></p> <p><u>Replacement cost</u></p> <p><i>Our stakeholders noted that there is a general lack of understanding of the concepts of “replacement cost” and “optimized replacement cost” when measuring assets. As these valuation methods are used in measuring infrastructure and similar assets, and these valuations are most often prepared by engineers at entities, it may be to engage with engineers to understand the meaning of the concepts from an engineering perspective, and the linkages with financial reporting.</i></p> <p><u>Engagement with valuation professionals</u></p> <p><i>We believe it would be useful for the IPSASB to engage with the International Valuation Standards Council on this project.</i></p> <p><i>(b) Type of helpful additional guidance: See links to examples of guidance in the responses above.</i></p>
14	NC	[No comment]
15	R	<p><i>(a) Gaps on measurement guidance: Our comments are based on Australian public sector entities’ experience in applying AASB 13, which incorporates IFRS 13 Fair Value Measurement.</i></p> <ul style="list-style-type: none"> • The application of fair value to a non-financial asset where there is no market for the asset. • Determination of “highest and best use” for assets whose future economic benefits are not regarded to be primarily dependent on the asset’s ability to generate net cash inflows • Appropriateness of inputs in valuation models and understanding whether inputs are observable or unobservable. • Allocation of ‘fair value’ amongst individual assets where ‘fair value’ has historically been assessed on a group basis. • whether measurement should reflect the nature of the asset in its current use or its heritage value • identification of entity-specific versus asset-specific restrictions <p><i>(b) Type of helpful additional guidance: Relationship between measurement model, depreciation, and impairment</i></p>

Question 4

Thinking about the issues and sub-components in Appendix A, which do you think should be higher priorities?

Please explain why they should be addressed earlier than others.

Summary of Responses

	RESPONDENTS (R #)	TOTAL
<i>Higher priority issues identified</i>	01, 02, 03, 05, 08, 09, 10, 11, 12, 13, 14, 15	12
<i>Higher priority subcomponents identified</i>	01, 02, 04, 05, 06, 07, 10, 11, 14	9
Other comments		0
TOTAL RESPONDENTS		15

R#	C #	Question 4— Comments
01	R	<p><i>Higher priority issues and subcomponents:</i> Issues 3 & 6, Sub-component 5</p> <p><i>Reasons why:</i> Issue 3: Clarification of the meaning of fair value: necessary given conceptual framework references to market value but standards level references to fair value. As noted above, there may be public sector specific reasons why market/fair value may not be appropriate. Also, consider whether there should be a requirement for use of market value when an item cannot be sold or there is no deep market. Consider developing an IPSAS equivalent of IFRS 13.</p> <p>Issue 6: More detailed implementation guidance – although discount rates are being addressed in an IFRS research project, specific IPSAS guidance would be helpful to preparers.</p> <p>Sub-component 5 – Guidance related to measurement: In particular, how to measure assets for which economic benefits arise in the form of service potential rather than cash flows, e.g. heritage assets.</p>
02	R	<p><i>Higher priority issues and subcomponents:</i> I might drop issue A1 issue 5 to be last – I think all other issues listed need to be addressed in the first instance. <i>Reasons why:</i> Let's deal with all issues and then have regard to GFS.</p>
03	R	<p><i>Higher priority issues and subcomponents:</i></p> <p>Issue1. Improve consistency between measurement requirements and guidance in IPSASs and the Conceptual Framework's approach to measurement bases, including the measurement bases identified therein.</p>

R#	C #	Question 4— Comments
		<p>Why? Because consistency of measurement concepts across all IPSASs is reducing complexity to users and increasing trust</p> <p>Issue2. Enhance consistency of measurement requirements in IPSAS (e.g. reduce the extent of different meanings for the same measurement term and/or terms not clearly defined, allowing different interpretations).</p> <p>Why? Because consistency of measurement concepts across all IPSASs is reducing complexity to users and increasing trust</p> <p>Issue5. Reduction of unnecessary differences between IPSAS measurement and GFS measurement.</p> <p>Why? In Austria ESA is very important when it comes to financial policy objectives (eg. Maastricht indicators, debt ceilings). From my point of view it is not so important to reduce the differences between IPSAS and GFS measurement – although I think ‘unnecessary differences’ should always be eliminated completely – but to explain the differences and give guidance on how to change IPSAS financial statements to derive GFS financial statements.</p> <p>Issue6. Provide more detailed implementation guidance to address difficult areas in public sector measurement.</p> <p>Why? Guidance will be crucial in trying to enable accountants to choose appropriate measurement bases for initial and subsequent measurement.</p>
04	R	<p><i>Higher priority issues and subcomponents:</i> I don't have a strong opinion on that. I think there is a certain benefit of doing assets or mixed-assets/liabilities first because from my perception this is kind of underrated in many (European) countries. Liabilities are usually quite well known, even if they are not cherished.</p>
05	R	<p><i>Higher priority issues and subcomponents:</i> Issue 6. Provide more detailed implementation guidance to address difficult areas in public sector measurement. Subcomponent 5. Guidance related to measurement</p> <p><i>Reasons why:</i> This is the most difficult area in practice. Especially for countries which are now transferring to accrual accounting, it's crucial how to use consistently different measurement bases in practice for recognizing non-monetary assets (such as infrastructures) in the financial statements.</p>
06	R	<p>Feedback from Institut der Wirtschaftsprüfer's constituents through its working group on public sector accounting, which indicates a few areas which we are informed are often challenging in practice, and which could be prioritized in a measurement project, as follows:</p> <p><u>High priority:</u> Infrastructure assets –for both initial and subsequent measurement</p> <p><u>Medium priority:</u></p> <ul style="list-style-type: none"> -Assets no longer in use –, including decommissioned, partly used and underutilized assets (e.g., school too large for the current pupil base) -Other items such as valuation of local government holdings in private companies where a fluctuation in value appears less than short-term (i.e. impairment trigger -Emissions trading (e.g., valuation of CO2 emissions rights)) -Subsidies (including impacts for recognition and measurement resulting from the timing issue already under discussion at the IPSASB).

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 4— Comments
07	R	<p><i>Higher priority issues and subcomponents:</i></p> <p>Issue 3: Fair Value guidance should be a high priority</p> <p>Issue 8 should be of lower priority.</p> <p><i>Reasons why:</i> Fair Value guidance in relation to the measurement of some public sector specific financial instruments (e.g. unquoted equity instruments) remains a critical issue that should be solved ahead of the issuing of the new FI-Standards based on IFRS 9.</p> <p>The requirements for disclosure should in the first instance derive from the concept of materiality and the economic nature of transactions and to a smaller extent from very specific and possibly too narrowly defined disclosure requirements (substance of the transaction vs. disclosure checklist).</p>
08	R	<p><i>Higher priority issues and subcomponents:</i> ISSUES 3, 4 & 5</p> <p><i>Reasons why:</i> TO ENHANCE EASY IMPLEMENTATION</p>
09	R	<p><i>Higher priority issues and subcomponents:</i> IPSAS 17</p> <p><i>Reasons why:</i> The importance of amount of PPE.</p>
10	R	<p><i>Higher priority issues and subcomponents:</i></p> <p>Issue 2. Enhance consistency of measurement requirements in IPSAS (e.g. reduce the extent of different meanings for the same measurement term and/or terms not clearly defined, allowing different interpretations).</p> <p>Issue 6. Provide more detailed implementation guidance to address difficult areas in public sector measurement.</p> <p>Issue 7. Improve IPSAS treatment of transaction costs, including the capitalizing or expensing of borrowing costs.</p> <p>Subcomponents: (1) Assets, (2) Transaction costs, and (3) Disclosures.</p> <p><i>Reasons why:</i></p> <p>Issue 2 is very important because enhancing consistency would avoid unnecessary confusion and misunderstandings in implementing the norm.</p> <p>Issue 6 has high priority because in the case of measurement of non-financial assets the norm is very strict and it might be impossible to implement. The norm does not offer an intermediate solution for the transition, it states that to switch from historic costs to fair value, it is necessary to measure <u>all</u> the assets within the same classification with their fair value.</p> <p>Issue 7 is relevant because it is difficult to include the borrowing costs as costs of projects. In most of cases, the amortization of loans culminates several years after the completion of the project.</p>
11	R	<p><i>Higher priority issues and subcomponents:</i> The following projects are identified as requiring a higher priority:</p> <ul style="list-style-type: none"> • Issues 3—Clarification and meaning of “fair value” in IPSASs • Issue 6—Provide more detailed implementation guidance to address difficult areas in public sector measurement. • Issue 7 - Improve IPSAS treatment of transaction costs, including the capitalizing or expensing of borrowing costs

11.3.1 Analysis of Responses to Public Sector Measurement Project Survey
IPSASB Meeting (June 2017)

R#	C #	Question 4— Comments
		<ul style="list-style-type: none"> • Issue 4—Reduction of differences between IPSAS measurement and IFRS measurement <p><i>Reasons why:</i> Preparers want more guidance on the difficult areas in public sector measurement, especially around measuring fair value to ensure consistency in valuations, particularly when instructing valuation professionals and explaining values to users. This is particularly important in the New Zealand public sector where many assets are measured on current values.</p>
12	R	<p><i>Higher priority issues and subcomponents:</i> Priority 1: Issues 1, 5, 7; Priority 2: Issues 2&3; Priority 3: Issue 6 guidance for Heritage, Infrastructure assets and military assets; Priority 4: Issue 8.</p> <p><i>Reasons why:</i> Priority 1 are the fundamental / conceptual issues that need to be sorted before moving onto Priority 2 issues which apply the guidance developed under Priority 1 to the existing standards suite. Priority 3 are the new areas we need to develop measurement guidance for. Priority 4 – disclosure requirements do need review, but I see this as the last thing to sort out as no real burning platform.</p>
13	R	<p><i>Higher priority issues and subcomponents:</i> As explained in Question 1 above, we strongly believe that Issue 1 and Issue 2 should be prioritized first to address the inconsistencies in the IPSASs and Conceptual Framework and provide guidance on how entities should apply the new measurement concepts. <i>Reasons why:</i> As noted in above.</p>
14	R	<p><i>Higher priority issues and subcomponents:</i> As mentioned in our response to question 1, we would strongly advocate that identifying the specificities of the public sector in terms of measurement as compared to measurement in the private sector should be top priority.</p> <p>We also believe that improving the accounting treatment of transaction costs is of lesser importance.</p>
15	R	<p><i>Higher priority issues and subcomponents:</i> Preference for Issue 4 to be addressed as a higher priority</p> <p><i>Reasons why:</i> Australian accounting standards apply to both private and public sector entities. AASBs are based on IFRS with limited modification for application by public sector entities, so it would be useful to understand the rationale for IPSASB divergence (as this will inform the AASB as to whether further modification is necessary to AASBs for application by public sector entities)</p>

Response #11

Appendix 1 Application Guidance for the Estimation of Fair Value Using Depreciated Replacement Cost in IPSAS 17, *Property, Plant and Equipment*

PROPERTY, PLANT, AND EQUIPMENT

Application Guidance

This Appendix is an integral part of PBE IPSAS 17.

Introduction

- AG1. PBE Standards define fair value as the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. An entity that elects to measure a class of property, plant and equipment using the revaluation model, as permitted by paragraph 44 of this Standard, may need to estimate the fair value of certain assets. This Application Guidance provides guidance on the estimation of fair value using the depreciated replacement cost method¹ in the circumstances permitted by paragraph 48 of this Standard.
- AG2. For the purposes of this Standard, if depreciated replacement cost is used to estimate the fair value of property, plant and equipment:
- (a) The value of land shall reflect the fair value of the actual land held, in terms of both its size and location; and
 - (b) The value of improvements to property, plant and equipment shall be estimated as the current replacement cost of the asset less deductions for all relevant forms of obsolescence, including physical deterioration.
- AG3. Adjustments to assets, apart from land, are normally considered for the following types of obsolescence:
- (a) Physical obsolescence;
 - (b) Functional obsolescence; and
 - (c) External obsolescence.
- AG4. All types of obsolescence are measured by making comparisons between the subject asset and the asset of equal utility upon which the cost estimate is based.
- AG5. This guidance discusses three types of obsolescence and proposes that an entity shall identify a separate adjustment for each form of obsolescence. In practice PBEs may not always be able to separately identify adjustments for each form of obsolescence. In particular, it may be difficult for PBEs to distinguish between functional obsolescence and external obsolescence. In such cases the adjustments for obsolescence may need to be considered collectively.

Bases of Value

- AG6. The term depreciated replacement cost is often used to describe the application of the cost approach to property, plant and equipment. In the case of PBE IPSAS 17, depreciated replacement cost may be used to estimate the fair value of an asset. Application of depreciated replacement cost in estimating fair value for financial reporting purposes should, wherever possible, be based on the market prices of inputs.
- AG7. For example, the replacement cost, the level of utility required from the asset, the assessment and measurement of different types of obsolescence and depreciation profiles should, as far as is possible, be based on market observations of inputs such as material costs and labour costs.
- AG8. If the purpose of the valuation requires an entity-specific basis of value, e.g. investment value, the cost input will still be based on cost that would be incurred by the entity in replacing the asset, and therefore will normally be no different from the cost calculation for market value, unless the entity is in a situation where it could either procure a replacement asset at a lower cost, or would incur higher costs, because of factors specific to its situation. However, the entity's actual operating experience of the subject asset and intentions for future utilisation could result in a significant difference in the measurement of obsolescence.

Land

- AG9. In instances where land is underutilised, the fair value of the land shall be determined by reference to the highest and best use of such land. For example, in a case where specialised facilities are located in a prime

¹ Paragraphs AG11–AG17, AG19–AG20 and AG22 are largely based upon guidance from Technical Information Paper 2 *The Cost Approach for Tangible Assets*, published by the International Valuation Standards Council in 2012.

PROPERTY, PLANT, AND EQUIPMENT

central business district site but the operation would be able to be run from a smaller sized and/or less valuable alternative site offering the same service potential, the fair value of the land would be the market value of the entire central business district-located site.

AG10. The fair value of land would normally be determined from market-based evidence. However, in the rare instances where extensive works have been carried out in order to prepare land for use in the entity's operations, available market evidence will normally relate to land of the same size and in the same general vicinity but which is priced for uses that are sub-optimal relative to the use for which the works were carried out. In these rare instances the fair value of the land shall be determined by having regard to the replacement cost of the land. For example, a customs department or marine research entity may acquire a section of seabed, fill it in and build a seawall in order to produce flat land for use in the entity's operations. The reclaimed land is in the precise location where the entity requires land. Market evidence may exist for other land of the same size and in the same general vicinity as the reclaimed land, but that other land is not suitable for the use intended by the entity. Thus, the market evidence on the fair value of that other land is not relevant to the reclaimed land, and the best indicator of the fair value of the reclaimed land is the replacement cost of that land. A similar situation occurs when a local authority carries out extensive works constructing new roads.

Physical Obsolescence

AG11. Physical obsolescence is any loss of utility due to the physical deterioration of an asset or its components resulting from its age and normal usage that results in loss of value.

AG12. Some physical obsolescence can be corrected or ameliorated by maintenance and repair. Other forms of physical obsolescence cannot be corrected or ameliorated, i.e., the deterioration in condition cannot be remedied, either at all or cost effectively. The measurement of physical obsolescence that can be remedied is the cost to remedy it. Physical obsolescence that cannot be remedied can be measured by considering the asset's age, expected total and remaining life where the adjustment for physical obsolescence is equivalent to the proportion of the expected total life consumed.

AG13. The value of an asset will not be below its value for an alternative use, including for scrap, salvage or recycling, less the costs of clearance, decommissioning and any decontamination required.

Functional Obsolescence

AG14. Functional obsolescence is any loss of utility resulting from inefficiencies in the subject asset compared to its replacement that results in a loss of value. There are two forms of functional obsolescence:

- (a) Excess capital cost which can be caused by changes in design, materials of construction, technology or manufacturing/construction techniques resulting in the availability of modern equivalent assets with lower capital costs than the subject asset; and
- (b) Excess operating cost which can be caused by improvements in design or excess capacity resulting in the availability of modern equivalent assets with lower operating costs than the subject asset.

AG15. Functional obsolescence can arise due to either:

- (a) The design or specification of the asset no longer being the most appropriate for delivery of the service for which it was originally intended as it may be inadequate or over-engineered;
- (b) The technology used in the asset having been superseded; or
- (c) A combination of both of the above factors.

AG16. For inadequate items, functional obsolescence is measured by considering the cost of correcting the inadequacy compared with the value gained. For over-engineered or "super-adequate" items, functional obsolescence is measured by the excess capital cost compared with the modern equivalent asset.

External Obsolescence

AG17. External obsolescence is any loss of utility value caused by economic or locational factors external to the asset that results in a loss of value. It may be called economic obsolescence when the external factors relate to changes in supply or demand for the asset or for products or services produced by the asset. Changes in the way goods and services are delivered in a sector may give rise to external obsolescence. When considering demand for the asset or for the products or services produced from the asset, demand both by

PROPERTY, PLANT, AND EQUIPMENT

policy makers in seeking to further public policy objectives and demand evidenced by the recipients of the products or services produced by the asset should be taken into account.

- AG18. The external obsolescence adjustment is deducted after physical deterioration and functional obsolescence. External obsolescence should be measured at the lowest level possible.
- AG19. An example of external obsolescence is where the subject asset has excess capacity compared to the reasonably foreseeable demand. In such circumstances it may be possible to make the appropriate adjustment using the cost-to-capacity method.
- AG20. The cost-to-capacity method can be used to address both functional and external obsolescence depending on the cause of the lack of utility. The cost-to-capacity method can be used as a method to:
- (a) Estimate the replacement cost for an asset with one capacity where the replacement costs of an asset or assets with a different capacity are known; or
 - (b) Estimate the replacement cost for a modern equivalent asset with capacity that matches foreseeable demand where the subject asset has excess capacity (as a means of measuring the penalty for the lack of utility to be applied as part of an external obsolescence adjustment).
- AG21. No obsolescence adjustment is made in respect of surplus capacity that, while rarely or never used, is necessary for stand-by or for safety purposes.
- AG22. If the whole entity or operating unit is affected by adverse external factors, this will be evident in the drop in demand for the goods and services produced by the asset and therefore an overall measure of external obsolescence can be determined by reference to the performance of the entity or unit. The way in which performance is assessed will depend on whether the entity or unit holds cash-generating or non-cash-generating assets. In order to estimate the value of an individual asset the overall external obsolescence will have to be allocated to individual assets. Cash or cash equivalents do not suffer obsolescence and are not adjusted. Marketable assets are not adjusted below their market value determined using the market approach.
- AG23. In determining depreciated replacement cost, the extent of any obsolescence adjustment for surplus capacity depends on whether that surplus capacity has an alternative use to the current use of the asset. Where there is no alternative use, the value of the surplus capacity is zero. Where there is an alternative use, the value of the surplus capacity is the value of the highest and best alternative use of that capacity. To illustrate the distinction between surplus capacity not having an alternative use to the current use of the asset and that which does, consider the following example. Assume depreciated replacement cost is to be determined for a network of water pipes where the pipe diameter is greater than currently required or ever expected to be required (including that necessary for stand-by or for safety purposes). There is also a discrete segment of the piping network that is similarly not required for the current use of the asset but which can be closed off and used for other purposes, such as a liquid storage facility. In this case, an obsolescence adjustment would be made in respect of the surplus diameter of the piping. The surplus segment of the piping network would be valued at its highest and best alternative use.
- AG24. In determining depreciated replacement cost, an adjustment for obsolescence and relevant surplus capacity is applied only to the extent that it reflects the most probable use of the asset that is physically possible, appropriately justified, legally permissible and financially feasible.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, PBE IPSAS 17.

- BC1. The New Zealand Accounting Standards Board (NZASB) has modified IPSAS 17 *Property, Plant, and Equipment* for application by Tier 1 and Tier 2 public benefit entities. Where applicable, disclosure concessions have been identified for Tier 2 entities and the language generalised for use by public benefit entities. The NZASB considered that the requirements of IPSAS 17 are generally appropriate for application by public benefit entities.

Heritage Assets

- BC2. The NZASB considered the requirements of IPSAS 17 in relation to heritage assets in the New Zealand context. IPSAS 17 does not mandate the recognition of heritage assets. If an entity does recognise heritage assets, IPSAS 17 requires that the entity disclose certain information about those heritage assets. However, IPSAS 17 does not require that the entity apply the measurement requirements in IPSAS 17 to those heritage assets. An entity applying IPSAS 17 could therefore elect not to recognise heritage assets, or to recognise heritage assets but not to assign them an amount in the statement of financial position.
- BC3. The NZASB decided that the IPSAS 17 requirements were not appropriate in the New Zealand context. The NZASB noted that for many years NZ GAAP has required that entities recognise and measure heritage assets in the same way as other items of property, plant and equipment and that accordingly, many heritage assets have been recognised and measured. The NZASB did not identify any reasons why the requirements in relation to heritage assets should be less than that required in NZ IAS 16 *Property, Plant and Equipment*, or in the case of entities applying previous NZ GAAP, FRS-3 *Accounting for Property, Plant and Equipment*.
- BC4. The NZASB noted that there are instances where heritage assets are not able to be reliably measured and are therefore not recognised in the statement of financial position. The NZASB agreed that although non-recognition of heritage assets in such circumstances is appropriate, heritage assets should be recognised when they can be reliably measured.
- BC5. The NZASB therefore determined to modify IPSAS 17 for application in New Zealand by requiring application of the recognition and measurement requirements in that Standard to heritage assets when they can be reliably measured. The NZASB agreed to retain the discussion of heritage assets in IPSAS 17.

Use of Independent Valuers

- BC6. The issue of whether accounting standards should require the use of independent valuers for determining the fair value of assets has been considered in New Zealand at length over a period of time.
- BC7. Prior to the adoption of NZ IFRSs, New Zealand generally accepted accounting practice permitted an item of property, plant and equipment to be revalued subsequent to initial recognition. Where an item was revalued, fair value was considered to be the most appropriate basis of valuation.
- BC8. During its deliberations on whether or not to include requirements regarding the use of independent valuers in the proposed NZ IAS 16 *Property, Plant and Equipment*, the Financial Reporting Standards Board (FRSB), the standard setting body at that time, noted that the requirements regarding asset valuations were not consistent throughout the suite of NZ IFRSs (for example, the fair value of intangible assets is measured by reference to an active market). On initial adoption in 2004, NZ IAS 16 included a requirement for property, plant and equipment carried at a revalued amount to be measured at fair value at the date of the revaluation, with valuations undertaken by an independent valuer or a suitably qualified employee (with their valuation being subject to review by an independent valuer).
- BC9. In April 2011 *Harmonisation Amendments* was approved for issue in New Zealand. This Standard eliminated many of the differences between the accounting standards in Australia and New Zealand for for-profit entities. As part of the harmonisation project, the requirement to use independent valuers for the revaluation of property, plant and equipment, and the related disclosure requirements, was removed from NZ IAS 16.
- BC10. In developing the exposure draft of the suite of PBE Standards, the NZASB proposed the inclusion of a requirement to use an independent valuer, together with related disclosure requirements, because these requirements have been part of New Zealand GAAP for an extensive period and the information provided

is considered to be useful. However, some constituents expressed the view that there was no PBE-specific reason for the PBE Standards to include more restrictive valuer requirements than IPSASs or NZ IFRSs.

BC11. The NZASB has, therefore, decided not to include in PBE IPSAS 17 a requirement, and the related disclosures, to use an independent valuer even though this proposal continues to be supported by some New Zealand constituents. The reasons for this decision include:

- (a) The proposed requirement to use independent valuers was limited to investment properties and property, plant and equipment and not extended to all classes of assets that are revalued;
- (b) It would be inconsistent with the requirements applicable to for-profit entities; and
- (c) There is now significant experience and expertise in measuring assets at fair value.

Depreciated Replacement Cost

BC12. In certain circumstances, IPSAS 17 permits the use of depreciated replacement cost as a means of estimating the fair value of an asset. Public benefit entities in New Zealand frequently use depreciated replacement cost to estimate the fair value of property, plant and equipment, including infrastructure assets. The NZASB noted that neither IPSAS 17 nor IPSAS 21 provide guidance on this topic at the level of detail previously provided in NZ IAS 16. The NZASB agreed that guidance on this topic was required in order to enhance the consistency of asset valuations in financial statements.

BC13. The NZASB noted that the International Valuation Standards Council had recently issued Technical Information Paper 2 *The Cost Approach for Tangible Assets (TIP 2)* which provides guidance on the application of the cost approach to valuation, including application of the depreciated replacement cost method. The NZASB noted the desirability of aligning, to the extent possible, the guidance in PBE IPSAS 17 with that issued by the international valuation profession. The NZASB agreed that, with the exception of the measurement of land, the guidance in Appendix A should be consistent with TIP 2.

BC14. The NZASB decided that, where land is under-utilised, the fair value of the land should be determined by reference to its highest and best use. The NZASB noted that this could result in different measures for some assets than under TIP 2, but considered that continuation of this existing requirement was appropriate in the New Zealand environment. The NZASB noted that TIP 2 acknowledges that there may be a higher value for an alternative use, but cautions that the cost approach may or may not provide an appropriate measure of market value in such cases.

Disclosure

BC15. The NZASB decided to remove the requirement to disclose the sum of all revaluation surpluses and revaluation deficits for individual items of property, plant and equipment within a class of assets on the grounds that the benefits to users of the financial statements were small and were likely to be outweighed by the costs of collecting and disseminating the information..

2015 Omnibus Amendments to PBE Standards

BC16. In the IASB's *Annual Improvements to IFRSs Cycle 2009-2011* the IASB amended IAS 16 *Property, Plant and Equipment* to clarify when servicing equipment is considered property, plant and equipment or inventory. The IPSASB made equivalent amendments to IPSAS 17 as there was no public sector specific reason for not adopting the amendments. The NZASB made these amendments as part of the *2015 Omnibus Amendments to PBE Standards*.

BC17. In the IASB's *Annual Improvements to IFRSs Cycle 2010-2012* the IASB amended IAS 16 to clarify the treatment of the carrying amount and accumulated depreciation when an item of property, plant and equipment is revalued. The IPSASB made equivalent amendments to IPSAS 17 as there was no public sector specific reason for not adopting the amendments. The NZASB made these amendments as part of the *2015 Omnibus Amendments to PBE Standards*.

BC18. In the IASB's *Clarification of Acceptable Methods of Depreciation and Amortisation* (Amendments to IAS 16 and IAS 38) the IASB amended IAS 16 and IAS 38 *Intangible Assets* to clarify the acceptable methods of depreciating assets and amortising intangible assets. The IPSASB made equivalent amendments to IPSAS 17 and IPSAS 31 as there was no public sector specific reason for not adopting the amendments. The NZASB made these amendments as part of the *2015 Omnibus Amendments to PBE Standards*.

PROPERTY, PLANT, AND EQUIPMENT

Implementation Guidance

This guidance accompanies, but is not part of, PBE IPSAS 17.

Frequency of Revaluation of Property, Plant and Equipment

- IG1. Paragraph 44 of PBE IPSAS 17 requires entities that adopt the revaluation model to measure assets at a revalued amount that does not differ significantly from that which would be determined using fair value at the reporting date. Paragraph 49 of PBE IPSAS 17 specifies that the frequency of revaluations depends upon the changes in the fair values of the items of property, plant and equipment being revalued. When the fair value of a revalued asset differs materially from its carrying amount, a further revaluation is necessary. The purpose of this guidance is to assist entities that adopt the revaluation model to determine whether carrying amounts differ materially from the fair value as at reporting date.
- IG2. An entity assesses at each reporting date whether there is any indication that a revalued asset's carrying amount may differ materially from that which would be determined if the asset were revalued at the reporting date. If any such indication exists, the entity determines the asset's fair value and revalues the asset to that amount.
- IG3. In assessing whether there is any indication that a revalued asset's carrying amount may differ materially from that which would be determined if the asset were revalued at the reporting date, an entity considers, as a minimum, the following indications:

External sources of information

- (a) Significant changes affecting the entity have taken place during the period, or will take place in the near future, in the technological, market, economic, or legal environment in which the entity operates or in the market to which the asset is dedicated;
- (b) Where a market exists for the assets of the entity, market values are different from their carrying amounts;
- (c) During the period, a price index relevant to the asset has undergone a material change;

Internal sources of information

- (d) Evidence is available of obsolescence or physical damage of an asset;
 - (e) Significant changes affecting the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. Adverse changes include the asset becoming idle, or plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite. Favourable changes include capital expenditure incurred during the period to improve or enhance an asset in excess of its standard of performance assessed immediately before the expenditure is made; and
 - (f) Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse or better than expected.
- IG4. The list in paragraph IG3 is not exhaustive. An entity may identify other indications that a revalued asset's carrying amount may differ materially from that which would be determined if the asset were revalued at the reporting date. The existence of these additional indicators would also indicate that the entity should revalue the asset to its current fair value as at the reporting date.

Response #11—Refer Question 1 (a) Additional Subcomponents

Appendix 2: Measurement Issues in Practice in New Zealand

Property, plant, and equipment valuations

- There can be challenges in determining the appropriate valuation method for some assets held or consolidated by a public benefit entity (PBE), such as whether the valuation approach should solely be depreciated replacement cost (DRC) or a commercial-based valuation. Examples include:
 - Rail infrastructure assets e.g. tracks, bridges, and tunnels.
 - Previous commercially used buildings that have been converted into tertiary education facilities.
 - Buildings within a tertiary campus that are leased on a commercial basis.
- The valuation approach that should be applied to rail and road corridor land, and other land with restrictions/designations on use e.g. Council reserve land, conservation estate (e.g. National Parks), lighthouse land. There has been diverse practices over the years on the approach to valuing some land and/or significant judgements are required in determining the valuation approach and adjustment.
- Limited accounting guidance on DRC valuations e.g.:
 - What costs should be included in the replacement cost valuation? There can also be issues where costs capitalised on initial recognition get lost or “leak out” in future DRC valuations because they have not been captured in the DRC valuation methodology used for subsequent measurement (for example traffic management costs when building a new road). Refer to page 72 of the 2016 Financial Statements of Government for New Zealand for discussion in context of the state highway valuation of “brown field” issues.
 - Dealing with obsolescence adjustments, such as for network overcapacity and inadequacies such as for earthquake prone buildings.
 - NAMS¹⁵ has published asset valuation and depreciation guidelines for the valuation of assets using DRC. This is not publicly available and can only be purchased at:
 - <http://www.nams.org.nz/pages/75/asset-valuation-and-depreciation-guidelines.htm>
 - The New Zealand Treasury has published valuation guidelines for health and tertiary property valuations. This can be download at:
<http://www.treasury.govt.nz/publications/guidance/reporting/accounting/property>

PDF document:
<http://www.treasury.govt.nz/publications/guidance/reporting/accounting/property/val-guidance-property.pdf>
- PBE IPSAS 17 para 53 needs to be clearer on what it means by a “short period” for when a rolling revaluation must be completed.
- If an entity capitalises borrowing costs, then there are issues on how that is factored into a DRC valuation as there is no accounting guidance. For example, what level of assumed borrowing

¹⁵ New Zealand Asset Management Support (NAMS) is a non-for-profit industry leader we provide benefits to the community by improving the future planning of our resources.

should be used for the replacement; and for network assets, how the period of construction is determined i.e. at the whole of network level or at a more granular level such as each component in the asset register.

Taxes

- There are challenges in forecasting income tax flows due to the period and timing of income tax returns not aligning to the government's balance date. This necessitates complex forecasts to accrue tax receivables at the balance date. It is acknowledged there is some guidance in IPSAS 23 but this still is a major challenge in practice.

Financial instruments

- Equity instrument investments held in non-commercial entities:
 - There is presently no accounting guidance in IPSAS 29 on how to measure the fair value of such investments in its scope, such as shares in a company that hold non-cash generating infrastructure assets or shared service type assets. The existing guidance is only suited to investments in commercial entities.
 - Similarly, there is no guidance on how to apply the impairment requirements of IPSAS 21 to non-commercial investments recorded in the separate financial statements, such as when these are investments in associates, jointly controlled entities, and subsidiaries. In particular, when is there an indicator of impairment, and how to apply the value in use requirements to shares when those requirements are based on the depreciated replacement cost (DRC) concept? The existing DRC guidance is largely focussed on impairment of property, plant and equipment and intangible assets.
- Concessionary loans, both provided and received:
 - Determining an appropriate discount rate for initial fair value of the loan can sometimes be difficult due to:
 - No directly comparable "market" to derive an interest rate due to the non-commercial nature of the arrangements and nature of counterparties.
 - The expected repayment of the loan could be forecast to occur several decades into the future so there are challenges in deriving long term discount rates beyond interest rate market data.
 - Forecasting future cash flows under the loans when there are many variables at play. For example, loans that have contingent repayment features.
- Need clarity on whether counterparty credit risk must be factored into the measurement of the fair value of all derivatives (i.e both asset and liability positions).

Service concession arrangements

- For an entity that expenses borrowing costs, it is unclear how to account for borrowing costs during the construction phase of a service concession asset when such costs are included in the purchase price of the asset (and payment is deferred to after construction) and an asset and financial liability are being progressively recognised during construction.
 - Para 15 says the assets and liability are initially measured at the same amount. Para AG30 says that the transaction price is considered to be fair value. These paras would support recognised at the purchase price that includes interest.

- Paras 21 and 22 states that finance charges are recognised as an expense. Para AG30 also states that transaction price is considered fair value unless indicated otherwise. A deferred payment beyond construction completion would indicate there is a financing arrangement. It would also seem unusual to not recognise interest expense on a financial liability during the construction phase. This would support the recognition of a borrowing expense during construction.

Long-dated employee benefits and provisions

- There are challenges in the determining discount rate and cost growth assumptions for defined benefit plans and environmental obligations that can go several decades beyond market data for interest rates and cost growth forecasts. There is no agreed approach to how such rates should be “extrapolated” beyond the market data.
 - The New Zealand Treasury has published a discount rates and CPI assumptions methodology. In practice, this is used by certain PBEs when applying PBE IFRS 4, PBE IPSAS 19, PBE IPSAS 25, and PBE IPSAS 29.
 - <http://www.treasury.govt.nz/publications/guidance/reporting/accounting/discount rates>
(methodology is towards bottom of the web page).

Inventories

- IPSAS 12 requires inventories held for distribution to be subsequently measured at the lower of cost and current replacement cost. This approach is onerous to apply by entities with significant holdings of such inventories and it also not consistent with the general impairment requirement for other non-cash-generating physical assets that are only impaired and their carrying value reduced when their service potential has been adversely affected. New Zealand has therefore modified PBE IPSAS 12 to require inventories held for distribution to be measured at cost, adjusted for any loss of service potential.

AGENDA ITEM 11.3.2: DRAFT PROJECT TIMETABLE

► IPSASB meeting:	2017			2018			
IPSASB will:	June	Sept	Dec	March	June	Sept	Dec
Measurement bases (Part 1)							
Review questionnaire results	√						
Approve project timetable	√						
Review/approve liabilities approach		√	√				
Review/approve assets approach			√	√	√		
Review/approve mixed IPSASs approach				√	√	√	
Review/approve CP-A chapters					√	√	√ CP-A
Transaction/ borrowing costs:							
Approve approach	√						
Review draft ED, IPSAS 5		√					
Approve ED, IPSAS 5			√ ED				
Review responses to ED					√		
Review /approve revised IPSAS 5						√	√ IPSAS
Guidelines and disclosures (Part 2)	Development awaits IPSASB decisions on measurement bases						

11.3.2 Timetable for Public Sector Measurement Project
IPSASB Meeting (June 2017)

Project Plan (Continued-1)

► IPSASB meeting:	2019				2020			
IPSASB will:	March	June	Sept	Dec	March	June	Sept	Dec
Review responses to CP-A chapters			√	√				
Develop/approve ED-Measurement				√	√ ED-A			
Review responses to ED-Measurement								√
Guidelines and disclosures (Part 2)								
Guidelines & disclosures	Development awaits IPSASB decisions on measurement bases							√

Project Plan (Continued-2)

► IPSASB meeting:	2021				2022			
IPSASB will:	March	June	Sept	Dec	March	June	Sept	Dec
Review responses to ED-Measurement	√							
Develop/approve IPSAS revisions	√	√	√ IPSAS					
Guidelines and disclosures (Part 2)								
Develop/approve measurement guidelines	√	√						√
Measurement disclosures	√	√	√					
Review/approve CP-B			√	√ CP-B				
Review responses to CP-B							√	
Develop/approve EDs-RPG/IPSAS							√	√ ED-B

11.3.2 Timetable for Public Sector Measurement Project
IPSASB Meeting (June 2017)

Project Plan *(Continued-3)*

► IPSASB meeting:	2021				2022			
IPSASB will:	March	June	Sept	Dec	March	June	Sept	Dec
Guidelines and disclosures (Part 2)								
Review responses to EDs-RPG/IPSAS			√	√				
Develop IPSAS revisions (disclosure)				√	√			
Develop implementation guidance for IPSASs (or RPG)					√			
Approve IPSAS revisions (and/or RPG)						√ IPSAS		

AGENDA ITEM 11.3.3: BACKGROUND INFORMATION: TRANSACTION COSTS

Introduction

1. This agenda item provides the following information to support the IPSASB's discussion of agenda item 11.2.3:
 - (a) Treatment of transaction costs in IPSAS;
 - (b) Transaction costs in IFRS 13, *Fair Value Measurement*, and

Treatment of Transaction Costs in IPSAS

2. IPSAS includes a mixture of explicit reference to transaction costs (see, for example, IPSAS 16, *Investment Properties*) and references to costs that would usually be viewed as transaction costs. Excerpts from IPSASs are provided below to illustrate present practice. IPSASs will usually capitalize transaction costs for an entry value (see, for example, IPSASs 17 and 31), while transaction costs are subtracted to derive an exit value (see IPSAS 27, *Agriculture*.)

Consistency with Conceptual Framework and Improvements to Clarity of IPSAS

3. IPSAS measurement generally can be linked to entry or exit values. Classification in these terms would be a starting point to achieve consistency with Conceptual Framework's approach to measurement, where measurement bases have been classified in terms of entry/exit values. The IPSASB may also want to consider the more fundamental question of whether or not (and in what circumstances) transaction costs should be capitalized.
4. The clarity of IPSAS treatment of transaction costs can be improved as follows:
 - (a) Use one term for transaction costs, instead of different terms in different IPSASs;
 - (b) Group transaction costs together; and
 - (c) Explain whether or not estimated transaction costs should be included when an IPSAS measurement (e.g. use of deemed cost or replacement cost) involves acquisition cost estimates.

Excerpts from IPSAS—Transaction Costs

5. IPSAS 9, *Revenue from Exchange Transactions* refers to transaction costs in paragraph 26 and has an extensive discussion of transaction costs in its implementation guidance, from the perspective of seller's revenue.

26. During the early stages of a transaction, it is often the case that the outcome of the transaction cannot be estimated reliably. Nevertheless, it may be probable that the entity will recover the transaction costs incurred. Therefore, revenue is recognized only to the extent of costs incurred that are expected to be recoverable. As the outcome of the transaction cannot be estimated reliably, no surplus is recognized.

6. In IPSAS 12, *Inventories*, the costs of purchase, other than the purchase price, appear to be transaction costs:

Costs of Purchase

19. The costs of purchase of inventories comprise (a) the purchase price, (b) import duties and other taxes (other than those subsequently recoverable by the entity from the taxing authorities), and (c) transport, handling, and other costs directly attributable to the

acquisition of finished goods, materials, and supplies. Trade discounts, rebates, and other similar items are deducted in determining the costs of purchase.

7. IPSAS 16, *Investment Property*, includes transaction costs in initial measurement:
 26. Investment property shall be measured initially at its cost (transaction costs shall be included in this initial measurement).
 27. Where an investment property is acquired through a non-exchange transaction, its cost shall be measured at its fair value as at the date of acquisition.
 28. The cost of a purchased investment property comprises its purchase price and any directly attributable expenditure. Directly attributable expenditure includes, for example, professional fees for legal services, property transfer taxes, and other transaction costs.
8. IPSAS 17, *Property, Plant and Equipment*, does not refer to transaction costs. Some of the elements of cost for initial recognition are transaction costs. For example, paragraphs 30-31 identify initial delivery and handling costs, and professional fees as included in the asset's cost for initial measurement.
9. IPSAS 27, *Agriculture*, describes "costs to sell" a biological asset:
 14. The fair value of an asset is based on its present location and condition. As a result, for example, the fair value of cattle at a farm is the price for the cattle in the relevant market less the transport and other costs of getting the cattle either to that market or to the location where it will be distributed at no charge or for a nominal charge.
 16. A biological asset shall be measured on initial recognition and at each reporting date at its fair value less costs to sell, except for the case described in paragraph 34 where the fair value cannot be measured reliably.
10. IPSAS 31, *Intangible Assets*, takes a similar approach to that used in IPSAS 17. It does not break costs down into transaction costs and other costs, with elements of cost including examples of transaction costs.

Transaction Costs in IFRS 13, *Fair Value Measurement*

11. IFRS 13, *Fair Value Measurement*, refers to transaction costs to explain "fair value":

The price

24 Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions (ie an exit price) regardless of whether that price is directly observable or estimated using another valuation technique.

25 The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. Transaction costs shall be accounted for in accordance with other IFRSs. Transaction costs are not a characteristic of an asset or a liability; rather, they are specific to a transaction and will differ depending on how an entity enters into a transaction for the asset or liability.

26 Transaction costs do not include *transport costs*. If location is a characteristic of the asset (as might be the case, for example, for a commodity), the price in the principal (or most advantageous) market shall be adjusted for the costs, if any, that would be incurred to transport the asset from its current location to that market.

12. IFRS 13 defines transaction costs, as follows:

transaction costs

The costs to sell an asset or transfer a liability in the principal (or most advantageous) market for the asset or liability that are directly attributable to the disposal of the asset or the transfer of the liability and meet both of the following criteria:

- (a) They result directly from and are essential to that transaction.
- (b) They would not have been incurred by the entity had the decision to sell the asset or transfer the liability not been made (similar to costs to sell, as defined in IFRS 5).

13. IFRS 13's Basis for Conclusions refers to transaction costs as follows:

BC33 The IASB asked valuation experts to take part in a case study involving the valuation of the identifiable assets acquired and liabilities assumed in a sample business combination. The IASB learned that differences between an exit price and an exchange amount (which might be interpreted as an entry price in a business combination) were unlikely to arise, mainly because transaction costs are not a component of fair value in either definition. The IASB observed that although the definitions used different words, they articulated essentially the same concepts.

BC54 The boards also concluded that the determination of the most advantageous market (which is used in the absence of a principal market) for an asset or a liability takes into account both transaction costs and transport costs. However, regardless of whether an entity measures fair value on the basis of the price in the principal market or in the most advantageous market, the fair value measurement takes into account transport costs, but not transaction costs (see paragraphs BC60–BC62 for a discussion on transport and transaction costs). That is consistent with the proposal in the exposure draft.

The price

BC60 IFRS 13 states that the price used to measure fair value should not be reduced (for an asset) or increased (for a liability) by the costs an entity would incur when selling the asset or transferring the liability (i.e. transaction costs).

BC61 Some respondents stated that transaction costs are unavoidable when entering into a transaction for an asset or a liability. However, the IASB noted that the costs may differ depending on how a particular entity enters into a transaction. Therefore, the IASB concluded that transaction costs are not a characteristic of an asset or a liability, but a characteristic of the transaction. That decision is consistent with the requirements for measuring fair value already in IFRSs. An entity accounts for those costs in accordance with relevant IFRSs.

BC62 Transaction costs are different from transport costs, which are the costs that would be incurred to transport the asset from its current location to its principal (or most advantageous) market. Unlike transaction costs, which arise from a transaction and do not change the characteristics of the asset or liability, transport costs arise from an event (transport) that does change a characteristic of an asset (its location). IFRS 13 states that if location is a characteristic of an asset, the price in the principal (or most advantageous) market should be adjusted for the costs that would be incurred to transport the asset from its current location to that market. That is consistent with the fair value measurement guidance already in IFRSs. For example, IAS 41 required an entity to deduct transport costs when measuring the fair value of a biological asset or agricultural produce.

AGENDA ITEM 11.3.4: PUBLIC SECTOR SPECIFIC REASONS—BORROWING COSTS

1. When the IPSASB considered whether to update IPSAS 5, *Borrowing Costs*, for changes to IAS 23, *Borrowing Costs*, it concluded that there were significant differences between borrowing in the public sector and the private sector. This appendix provides an excerpt from ED35's *Basis for Conclusions*, which explains the basis for non-convergence with IFRS.

Excerpt from ED 35, *Borrowing Costs: Basis for Conclusions*

- BC5. ED 35 differs significantly from the key requirement of the revised IAS 23, which is to capitalize borrowing costs directly attributable to the acquisition, construction or production of qualifying assets. The IPSASB decided that it was inappropriate to require public sector entities to capitalize borrowing costs. ED 35 therefore retains the option of either capitalizing or immediately expensing borrowing costs, when those costs are specifically incurred in relation to financing the acquisition, construction or production of a qualifying asset. However, unlike the existing IPSAS 5 and the revised IAS 23, this proposed IPSAS does not permit or require borrowing costs to be capitalized in relation to other borrowings that are directly attributable to financing the acquisition, construction or production of a qualifying asset.
- BC6. When borrowing costs are not specifically incurred in relation to financing the acquisition, construction or production of a qualifying asset, ED 35 would require immediate expensing of those borrowing costs. This Basis for Conclusions explains the public sector specific reasons for these departures from the revised IAS 23. These are in relation to:
- Borrowing in the Public Sector;
 - Specifically Incurred Borrowing Costs and Directly Attributable Borrowing Costs;
 - Non-Cash-Generating Assets and the Revaluation Model in IPSAS; and
 - Convergence with Statistical Bases of Reporting.

Borrowing in the Public Sector

- BC7. Borrowing in the public sector is often centralized and borrowing requirements are determined for the economic entity as a whole. Borrowing may be for investing, financing or operating activities. The aggregate level of borrowing will be set in the context of political and economic factors, such as decisions on the appropriate levels of taxation. The funding allocated to specific programs and entities may be derived from a variety of sources, and consequently the resources transferred are often indistinguishable in character. A feature of fiscal management in the public sector is that governments sometimes budget for deficits, occasionally for extended periods of time, and those deficits are financed by borrowing. In many jurisdictions outlays on qualifying assets are a relatively minor part of the government's annual outlays, the bulk of which are consumed by expenses, such as the payment of social benefits to individuals and households. This can be distinguished from the for-profit sector in which entities would normally budget for a loss only in unusual circumstances, and certainly not for an indefinite period. Therefore, in the public sector it is often difficult to distinguish financing from external borrowing and other sources of finance and there is often no meaningful way to attribute borrowing costs to qualifying assets.

- BC8. Governments and other public sector entities may borrow for public policy purposes, for example they may issue debt securities to provide liquidity in the capital markets. Often these securities form the benchmark security for the bond market and a common basis for pricing other securities.
- BC9. The reasons for public sector borrowing outlined in the preceding paragraphs mean that there is little linkage between these types of borrowing and the acquisition, construction or production of qualifying assets. For example, a government that has a policy of maintaining CU100 billion in bonds in the market, while not actually needing the cash, will find that, if it were required to capitalize borrowing costs, it would capitalize interest for any qualifying assets acquired, constructed or produced in any years in which bonds are outstanding. While it may be feasible to allocate these borrowings to qualifying assets, the IPSASB is of the view that doing so is unlikely to provide relevant and reliable information or enhance accountability. It is also likely that the cost to do so would exceed the related benefits, if any.
- BC10. In the public sector controlling entities may have a large number of controlled entities. Many of these controlled entities are responsible for acquiring, constructing or producing qualifying assets. Although there will be a general policy framework, many controlled entities are likely to have their own financial management systems, reflecting their own reporting needs. Funding for such controlled entities may be by means of appropriation from a central fund without regard to whether such appropriations are financed from taxes, borrowings or other sources. Any accounting system to track directly attributable borrowing costs and their application to qualifying assets is likely to be complex and resource intensive. The IPSASB is of the view that in these cases, the costs incurred in capitalizing borrowing costs would be likely to exceed the related benefits, if any.
- BC11. The IPSASB acknowledged, however, that there may be cases where public sector entities borrow specifically to finance the acquisition, construction or production of a qualifying asset, for example, where a municipality issues bonds specifically to finance an identified infrastructure project. The IPSASB considered that in such cases capitalizing borrowing costs may be appropriate and therefore entities should be permitted to capitalize borrowing costs specifically incurred for the acquisition, construction or production of a qualifying asset. However, because of cost-benefit considerations and issues associated with the relevance of the resulting information, the IPSASB concluded that the capitalization of borrowing costs should not be required, but instead should be optional in cases where a public sector entity borrows specifically to finance the acquisition, construction or production of a qualifying asset.

Specifically Incurred Borrowing Costs and Directly Attributable Borrowing Costs

- BC12. Having concluded that the option to capitalize borrowing costs should be limited to such costs related to financing specifically incurred for the acquisition, construction or production of a qualifying asset, the IPSASB considered whether the term “directly attributable” used in IAS 23 achieves this objective. In IAS 23, borrowing costs that are “directly attributable” to the acquisition, construction or production of qualifying assets are those borrowing costs that would have been avoided if the expenditure on the qualifying asset had not been made. Effectively, this means any borrowings of the entity are attributed to the acquisition, construction or production of qualifying assets. Such borrowings are not limited to funds borrowed specifically for the purpose of acquiring, constructing or producing a particular qualifying asset. Thus “directly attributable” borrowing costs may include costs related to general borrowing, including interest on

short-term borrowings such as bank overdrafts, which are not linked to any particular project. The IPSASB therefore concluded that the term “directly attributable” is broader than “specifically incurred” and that its use would not be in accordance with its conclusion that, in the public sector, the option to capitalize borrowing costs should be limited to those costs specifically incurred to finance the acquisition, construction or production of a qualifying asset. An approach of apportioning otherwise avoidable borrowing costs is also likely to be complex for the reasons outlined in paragraph BC10 and is likely to give rise to costs that exceed the related benefits.

- BC13. The IPSASB noted that some governments operate under fiscal rules that only permit them to borrow for capital purposes. The IPSASB concluded that the existence of such rules on their own is insufficient to create a strong enough link between borrowing and the acquisition, construction or production of specific qualifying assets for the option to capitalize borrowing costs to be exercised.

Non-Cash-Generating Assets and the Revaluation Model in IPSAS 17

- BC14. Under the requirements of IPSAS 17, “Property, Plant and Equipment,” many specialized non-cash-generating assets are revalued to fair value on the basis of a cost-based estimate of fair value such as depreciated replacement cost. Current guidance on such revaluation bases does not adequately address the issue of how borrowing costs should be incorporated into the calculation of fair value. In the absence of authoritative guidance on this issue the IPSASB was concerned at the prospect of a range of practices emerging in response to compulsory capitalization of borrowing costs, which would reduce the reliability of the information provided. The IPSASB therefore concluded that it would be inappropriate to require capitalization in respect of qualifying assets that are carried on the revaluation model in IPSAS 17.

Convergence with Statistical Bases of Reporting

- BC15. The IPSASB has a key strategic theme to converge IPSASs with statistical bases of reporting where appropriate. Under statistical bases of reporting borrowing costs are recognized as an expense in the period in which they are incurred. The IPSASB concluded that the approach to borrowing costs adopted in ED 35 furthers this strategic theme in an appropriate manner.

Overall Conclusion: Approach to Borrowing Costs, Qualitative Characteristics of Financial Reporting and Balance between Benefit and Cost

- BC16. For the above reasons the IPSASB concluded that requiring public sector entities to capitalize borrowing costs as part of the cost of qualifying assets would not satisfy the qualitative characteristics of general purpose financial reporting. In particular, the IPSASB believes that capitalizing borrowing costs generally would diminish the reliability of information reported in the financial statements of public sector entities while achieving, at best, a modest increase in the relevance of the information reported. Similarly, for these reasons, such a requirement generally would not enhance the accountability of public sector entities. The IPSASB also believes that, in many cases, the cost of capitalizing borrowing costs would likely exceed any benefits obtained.
- BC17. The IPSASB also concluded that, in view of the reasons for public sector borrowing (see paragraphs BC7–BC9), permitting public sector entities to capitalize borrowing costs that are directly attributable, but not specifically incurred, in relation to financing the acquisition, construction or production of a qualifying asset would not increase the

relevance and reliability of information reported in their financial statements and would not enhance their accountability.