

AASB Invitation to Comment

**ITC XX**  
March 2021

# Request for Comment on IPSASB Exposure Drafts *Conceptual Framework – Limited-Scope Update and Measurement*

Comments to the AASB by XX June 2021

This is a draft version of the AASB Invitation for Comment (ITC) to be issued together with IPSASB Exposure Drafts ED 76 *Conceptual Framework – Limited-Scope Update* and ED 77 *Measurement*.

In addition to the draft AASB Specific Matters of Comment outlined in Agenda Paper 10.1, this document includes draft background information to provide context to constituents about the relationship between the IPSASB's Measurement project and the Board's Fair Value Measurement for Not-for-Profit Entities project. Questions to Board members about the draft AASB Specific Matters for Comment are set out in Agenda Paper 10.1.

## Question to Board members

Q6: Do Board members have any comments on the background information contained in this document?



**Australian Government**

**Australian Accounting  
Standards Board**

## **How to Comment on this AASB Invitation to Comment**

Constituents are strongly encouraged to respond to the AASB and the IPSASB. The AASB is seeking comment by XX June/July 2021 [a date 90 days after this ITC is issued]. This will enable the AASB to consider Australian constituents' comments in the process of formulating its own comments to the IPSASB, which are due by XX September 2021.

### **Formal Submissions**

Submissions should be lodged online via the “Work in Progress – Open for Comment” page of the AASB website ([www.aasb.gov.au/comment](http://www.aasb.gov.au/comment)) as a PDF document and, if possible, a Word document (for internal use only).

### **Other Feedback**

Other feedback is welcomed and may be provided via the following methods:

E-mail: [standard@aaasb.gov.au](mailto:standard@aaasb.gov.au)  
Phone: (03) 9617 7600

All submissions on possible, proposed or existing financial reporting requirements, or on the standard-setting process, will be placed on the public record unless the Chair of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

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## AASB REQUEST FOR COMMENTS

In light of the Australian Accounting Standards Board's (AASB's) decision to contribute to the work of the International Public Sector Accounting Standards Board (IPSASB), the AASB is inviting comments on:

- (a) any of the proposals in the attached IPSASB Exposure Drafts, including the specific question on the proposals as stated in the preface to the attached IPSASB Exposure Drafts; and
- (b) the 'AASB Specific Matters for Comment' and 'AASB General Matters for Comment' listed below.

Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents supplement their opinions with detailed comments, whether supportive or critical, on the major issues. The AASB regards both critical and supportive comments as essential to a balanced review and will consider all submissions, whether they address all specific matters, additional issues or only one issue.

### Relationship with the AASB's Fair Value Measurement for Not-for-Profit Entities Project

The AASB is undertaking its Fair Value Measurement for Not-for-Profit Entities project to develop guidance to assist the application of AASB 13 *Fair Value Measurement* in the not-for-profit sector. The AASB also decided that the scope of the project should include guidance to assist not-for-profit entities, in both the private and public sector, to measure the fair value of right-of-use assets arising from leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives (the requirement to measure these right-of-use assets at fair value has been deferred at least until further guidance has been developed to assist not-for-profit entities in measuring the fair value of right-of-use assets and the financial reporting framework for private sector not-for-profit entities has been finalised. The latter step will involve decision making regarding the tiers of reporting entities that should be subject to requirements to measure right-of-use assets at fair value).

The AASB has commenced deliberation of some fair value measurement issues raised by constituents and reached tentative views on some of those issues. In light of the IPSASB's project on public sector measurement, the AASB decided to consider the ongoing progress and outcomes of that IPSASB project before issuing its own consultation document potentially proposing amendments to AASB 13. Therefore, constituents' comments on the IPSASB's proposals, including comments on the AASB Specific and General Matters for Comment, are important to the AASB in deciding the direction of future work on its Fair Value Measurement for Not-for-Profit Entities project.

Further background information about the Fair Value Measurement for Not-for-Profit Entities project and its interaction with the IPSASB's Measurement project is contained in the Appendix.

### AASB Specific Matters for Comment

#### Note to Board members

AASB Specific Matters for Comment 1–15 are the same as those included in Agenda Paper 10.1.

The AASB would particularly value comments on the following in respect of **non-financial assets of a not-for-profit public sector entity not held primarily for their ability to generate net cash inflows** (i.e. assets held for their operational capacity). For ease of reference in this document, such assets are referred as **“operational assets”**:

## **In respect of the IPSASB's proposed 'current operational value' measurement basis**

### ***Service potential of operational assets***

1. In respect of operational assets, do you agree that a current value measurement should reflect the asset's service potential? Please explain your reasons.
2. In your opinion, would the IPSASB's proposed current operational value measurement basis result in an asset value reflecting the asset's service potential? Please explain your reasons.

[The term 'service potential' is used throughout the IPSASB's [\*The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities\*](#) (see paragraphs 5.7 and 5.8). This term is also described in paragraphs Aus49.1, Aus54.1 and Aus54.2 of the AASB's [\*Framework for the Preparation and Presentation of Financial Statements\*](#).]

### ***Measuring the current operational value of an asset based on its current use***

3. Do you agree with the IPSASB's proposal in ED 77 that the current operational value of an operational asset should be measured based on its current use, disregarding potential alternative uses and any other characteristics of the asset that could maximise its market value (paragraph B4)? Please explain your reasons.

### ***Using the income approach to estimate the current operational value of an operational asset***

4. Do you agree with the IPSASB's proposal in ED 77 that the income approach can be an appropriate measurement technique in certain circumstances to estimate the current operational value of an operational asset (paragraphs B24 and B37)? If you agree, please identify what those circumstances would be. Whether you agree or disagree, please explain your reasons for your view.

### ***Measuring the current operational value of restricted operational assets***

5. In respect of operational assets that are subject to restrictions, assuming that an equivalent restricted asset is not obtainable in the marketplace, do you agree with the IPSASB's proposal in ED 77 that the current operational value of such restricted operational assets should not be lower than the value of an equivalent unrestricted asset? Please explain your reasons.

### ***Assumed location of an operational asset when measuring its current operational value***

6. Do you agree with IPSASB's proposals in ED 77 that an asset's current operational value assumes that the entity will continue to meet its service delivery objectives from the same location in which the existing asset is situated (paragraph B12)? Please provide your reasons.

### ***Nature of component costs to include in an asset's current operational value***

7. Do you agree with ED 77 that, when measuring an asset's current operational value, the cost of a modern equivalent asset may in some circumstances exclude the following costs (paragraph B36)? Please explain your reasons.
  - Additional costs arising from extending an existing property;
  - Contract variation costs; and
  - Planning changes.

***Whether the current operational value of an asset should include borrowing costs***

8. Do you agree with ED 77 that if an entity does not capitalise borrowing costs in accordance with its accounting policy (as allowed under IPSAS 5 *Borrowing Costs* and in certain circumstances under AASB 123 *Borrowing Costs*), the entity should disregard any financing costs in measuring the modern equivalent asset as part of the current operational value estimate (paragraph B36(a))? Please explain your reasons.

***Consideration of surplus capacity and economic obsolescence***

9. Do you agree with ED 77 that the current operational value of an operational asset should assume the asset is used to its full capacity, subject to any obsolescence (paragraphs B11 and B12)? Please provide your reasons.
10. Do you consider the guidance in ED 77 to be clear and sufficient in distinguishing whether an asset's excess capacity should be treated either as:
- (a) surplus capacity, as described in paragraphs B11 and B12 (which is not adjusted for when measuring the asset's current operational value); or
  - (b) an indication of economic obsolescence, as described in paragraph B33(c) (which is deducted when measuring the asset's current operational value)?

Please provide your reasons.

***Overall comment on the IPSASB's proposed current operational value measurement basis***

11. Would you support the adoption of the IPSASB's proposed current operational value measurement basis – instead of fair value – for not-for-profit entities in Australia in measuring the current value of:
- (a) operational assets with restrictions; and
  - (b) other operational assets?

Please explain your reasons.

**In respect of the fair value measurement basis**

***Hypothetical market participant***

12. In respect of operational assets, do you agree with the AASB's initial tentative view to propose that, when measuring the fair value of an operational asset under AASB 13, hypothetical market participant buyers would include another not-for-profit entity that has similar service delivery objectives and would be willing to pay the lowest price for which it could replace the asset's service potential? Please explain your reasons.

***Measuring the current value of operational assets using the fair value model***

13. Do you agree with the IPSASB's conclusion in ED 77 that fair value is inappropriate to apply when measuring the current value of operational assets because the "highest and best use" and "maximising the use of market participant data"<sup>1</sup> concepts are generally not applicable (paragraph BC29)? (The AASB has not yet deliberated this issue.) Please explain your reasons.

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<sup>1</sup> In AASB 13, paragraph 67: "maximise the use of relevant observable inputs".

### ***Measuring the fair value of restricted operational assets***

14. Do you agree with the AASB's initial tentative view that, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence, the fair value of a restricted operational asset:
- (a) should be measured at its current replacement cost; and
  - (b) should not be reduced due to the restrictions, because the restrictions do not reduce the amount the entity would need to incur to replace the service potential embodied in the asset?

Please provide your reasons.

### ***Consistency with other AASB Standards***

15. If you disagree with the AASB's initial tentative view in Specific Matter for Comment 14 – namely, that the fair value of a restricted operational asset should be measured at its current replacement cost without a deduction for the restrictions, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence – do you agree that, for logical consistency, changes to AASB 1059 *Service Concession Arrangements: Grantors* and AASB 136 *Impairment of Assets* would be warranted, so that the current values of all operational assets of not-for-profit entities are measured based on their current cash-generating ability? Please provide your reasons.

### **General matters for comment**

The AASB would also particularly value comments on the following general matters. If the IPSASB's proposals were to be adopted for Australian not-for-profit entities:

1. Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the IPSASB's proposals, including Government Financial Statistics (GFS) implications?
2. Whether, overall, the IPSASB's proposals would result in financial statements that would be useful to users?
3. Whether the IPSASB's proposals would be in the best interests of the Australian economy?
4. Unless already provided in response to general matters for comment 1 – 3 above, the costs and benefits of the IPSASB's proposals relative to the current Australian requirements for not-for-profit entities, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the IPSASB's proposals relative to the existing Australian requirements.

**Appendix: Background to the AASB’s Fair Value Measurement for Not-for-Profit Entities project and its interaction with the IPSASB’s Measurement project**

**Reasons for undertaking the Fair Value Measurement for Not-for-Profit Entities project**

Since 2014, most public sector entities (both for-profit and not-for-profit entities) have been measuring most of their non-financial assets at fair value in accordance with AASB 13 *Fair Value Measurement*. AASB 13 incorporates IFRS 13 *Fair Value Measurement*, which is an Accounting Standard issued by the International Accounting Standards Board (IASB) for for-profit entities (however, AASB 13 exempts not-for-profit public sector entities from some disclosure requirements in IFRS 13).

The Fair Value Measurement for Not-for-Profit Entities project was initiated by the AASB based on responses to the AASB’s *Agenda Consultation 2017-2019* that requested guidance to assist application of AASB 13 in the not-for-profit public sector. In particular, constituents requested guidance in respect of the fair value measurement of non-financial assets of a not-for-profit public sector entity not held primarily for their ability to generate net cash inflows (i.e. assets held for their ‘operational capacity’, to use the terminology of the IPSASB Exposure Drafts). For ease of reference in this Appendix, such assets are referred to as ‘operational assets’.

Having regard to advice from its Project Advisory Panel, the AASB has commenced deliberation and reached tentative views on some fair value measurement issues raised by the constituents, as summarised in the Table below.

<b>Topics</b>	<b>AASB’s tentative views</b>
<p>1. To what extent do restrictions on the use or pricing of the use of an operational asset affect the asset’s fair value?</p>	<p>The AASB tentatively decided to propose that, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence:</p> <p>(a) the fair value of such a restricted asset should be measured at the asset’s current replacement cost (i.e. the cost currently required to replace the service potential embodied in the asset). This is because:</p> <ul style="list-style-type: none"> <li>i. the income approach would be inappropriate in measuring the fair value of such an asset that is not primarily held to generate net cash inflows; and</li> <li>ii. measuring the fair value of such a restricted asset using the market approach would also be inappropriate if an equivalent restricted asset is not obtainable in the marketplace at the measurement date and the resulting measure would differ from current replacement cost;</li> </ul> <p>(b) the fair value of such a restricted asset should not be reduced due to the restrictions – this is because if an equivalent restricted asset is not obtainable in the marketplace, the not-for-profit public sector entity (or a not-for-profit public sector entity</p>

Topics	AASB's tentative views
	<p>market participant buyer 'stepping into its shoes of the entity that holds' the asset<sup>2</sup>) would need to compete with other market participants to purchase an equivalent asset (i.e. an asset that reflects the same characteristics and provides services of the same nature as the asset being measured) that is not subject to the restrictions to provide the required services. In this hypothetical transaction, the cost that the NFP public sector entity would need to incur would not be reduced because the entity's asset being measured is subject to restrictions; and</p> <p>(c) this measurement should be deemed to be fair value; however, this treatment might not be compliant with IFRS 13.</p> <p>If an equivalent restricted asset is obtainable in the marketplace at the measurement date for a price supported by observable market evidence, the fair value of the restricted asset should be based on the market price for that equivalent restricted asset. The market price for the equivalent restricted asset would incorporate the effect of the restriction; therefore, there would be no need to adjust that market price for the restriction.</p> <p>In respect of (a) above, prohibiting use of the income approach for a restricted asset, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence, would be consistent with the requirements in AASB 1059 <i>Service Concession Arrangements: Grantors</i> (to measure service concession assets at their current replacement cost) and amendments to AASB 136 <i>Impairment of Assets</i> (to exclude non-financial operational assets that are regularly revalued to fair value from the scope of AASB 136). Those requirements were developed to ensure operational assets are measured at amounts faithfully representing their service potential rather than at amounts reflecting their current cash-generating ability, which would often be their scrap values.</p>
2. How to apply the concept of 'highest and best use' to operational assets	<p>The highest and best use concept in AASB 13 should continue be applicable to not-for-profit entities.</p> <p>However, the 'financially feasible use' aspect of a non-financial asset's highest and best use (as described in paragraph 28(c) of AASB 13, consistently with IFRS 13) should not be applicable to restricted operational assets. This is because 'financially feasible' is described in terms of investment returns in the form of income or cash flows.</p>
3. Assumed location of an asset measured at	<p>Replacement of an asset should always be assumed to occur in its present location even if it would be feasible to relocate to a cheaper site. This is because an asset's service capacity includes its</p>

<sup>2</sup> To use the phrase in the last sentence of paragraph BC78 of the IASB's Basis for Conclusions on IFRS 13 *Fair Value Measurement*.



Topics	AASB's tentative views
current replacement cost	'reinvestment potential', i.e. the ability to sell the asset and reinvest the proceeds in other stores of service capacity.
4. Nature of component costs to include in an asset's current replacement cost	The current replacement cost of assets composing a self-constructed facility should include all necessary costs intrinsically linked to acquiring the facility at the measurement date. A not-for-profit public sector entity should assume that the facility presently does not exist and should take into account any make-good costs that must be incurred for surrounding facilities of another entity disturbed when the entity's facility is replaced.
5. Whether the current replacement cost of a self-constructed asset should include borrowing costs	<p>No guidance is proposed for AASB 13. The AASB considers that a not-for-profit entity should consider whether a market participant buyer of the asset would include borrowing costs in its pricing decisions about the asset.</p> <p>The AASB took the view that this issue affects for-profit and not-for-profit entities alike and, in light of AASB 13 not specifying the treatment of borrowing costs for fair value measurements by for-profit entities, it would be inappropriate to mandate a particular treatment for not-for-profit entities applying AASB 13.</p>
6. How to identify and measure economic obsolescence	<p>If an asset has suffered a reduction in demand for its services, the identification of its economic obsolescence should not require a formal decision to have been made to reduce the physical capacity of that asset.</p> <p>However, if an asset has apparent overcapacity in view of current demand for its services, economic obsolescence should not be identified for that asset if there is more than an insignificant chance that future increases in the demand for its services will largely eliminate that overcapacity within the foreseeable future.</p>

### Interaction with the IPSASB's Measurement project

The IPSASB's Measurement project seeks to identify and define measurement bases to be used in IPSAS to be applied by not-for-profit public sector entities. Public-sector-specific issues are not addressed in IFRS 13; therefore, in accordance with paragraph 20 of the AASB's policy document [The AASB's Approach to International Public Sector Accounting Standards](#), the AASB decided to provide formal feedback to the IPSASB on its Exposure Drafts ED 76 *Conceptual Framework – Limited-Scope Update* and ED 77 *Measurement*.

The IPSASB has reached a view that the fair value model under IFRS 13 would not be appropriate for measuring the current value of operational assets; instead, the IPSASB is proposing a different current value model – current operational value – for measuring the current value of operational assets. In contrast, the AASB has obtained feedback from most responding constituents that fair value is appropriate for measuring the current value of operational assets held by Australian public sector entities, but also that there is a need for

guidance to clarify some fair value application issues. A particularly contentious aspect of AASB 13 is how to measure the fair value of restricted operational assets. The AASB decided to research options for current value measurement bases other than fair value, primarily to address current value measurement issues arising in respect of restricted operational assets. Therefore, the AASB is particularly interested in the views of Australian constituents on the IPSASB's proposed current operational value measurement basis for measuring the current value of operational assets.

Appendix B of IPSASB ED 77 includes Application Guidance addressing the measurement topics (1)–(6) noted in the Table above, which the AASB has been deliberating. To date, the AASB has deliberated these topics in the context of fair value measurement, whereas the IPSASB has developed its proposals under its proposed approach to develop a current measurement basis that differs from fair value. Therefore, the AASB has included Specific Matters for Comment to elicit Australian constituents' views specifically on these measurement topics.

IPSASB Exposure Drafts ED 76 and ED 77 do not specifically address how to measure the current value of right-of-use assets arising from leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives (the scope of ED 77's proposed measurement requirements excludes leases accounted for in accordance with IPSAS 13 *Leases*). Therefore, this Invitation to Comment does not address that topic.