Australian Government
Australian Accounting Standards Board

Staff Paper

Project:	**Fair Value Measurement for NFP Entities**	**Meeting:**	AASB June 2020 (M176)
Topic:	**Disclosures about discounts on restricted land**	**Date of this paper:**	26 May 2020
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		Project Priority:	Medium
		Decision-Making:	Medium
		Project Status:	Consider stakeholder feedback and draft amendments to AASB 13 and determine next steps

Objective of this agenda item

1. The objective of this agenda item is for the Board to:

- **consider** staff analysis and recommendations regarding key issues identified regarding the nature and scope of the proposed disclosures about discounts on restricted land (see Section 1);
- **consider** drafting of proposed amendments to AASB 13 *Fair Value Measurement* regarding the disclosures (see Agenda Paper 7.2);
- **decide** next steps of the project (see Section 2); and
- **note** feedback from stakeholders obtained during initial consultations regarding the proposed disclosures about discounts on restricted land (see Appendix).

Background

2. At its April 2020 meeting, the Board noted that the debate about the effects of restrictions on fair value measurements of assets of public sector NFP entities held primarily for their service capacity, and the fair value measurement of right-of-use assets arising under concessionary leases is likely to take a long time to resolve. The Board decided, as an interim step while it continues its deliberations about these measurement issues, to develop a limited-scope Exposure Draft for application by public sector not-for-profit (NFP) entities.

3. The Exposure Draft would propose the following amendments to AASB 13 in respect of assets held primarily for their service capacity (ie assets not held primarily for their ability to generate net cash inflows):

(a) in respect of land with material discounts for restrictions[1], for each class of land:

   i. the total carrying amount of land measured at a discount to the current market buying price of equivalent unrestricted land;

   ii. the total amount of the discount; and

   iii. the basis for calculating such discounts.

(b) additional guidance in respect of decisions previously made by the Board regarding assets measured at current replacement cost, addressing:

   - the nature of costs included in an asset's current replacement cost (see Action Alert of June 2019 AASB meeting);

   - the assumed location of land forming part of a facility (see Action Alert of June 2019 AASB meeting); and

   - identifying and measuring economic obsolescence (see Action Alert of April 2019 AASB meeting).

4. In making its decision about proposed amendments to AASB 13 referred to in paragraph 3, the Board focused on the likelihood (to be tested through outreach activities) that the proposed additional disclosures would not give rise to undue cost or effort, because they relate to inputs used in calculating estimates of fair value.

Reasons for bringing this agenda item to the Board at this meeting

5. The Board instructed staff to consult with public sector stakeholders and valuers regarding the proposed disclosures described in paragraph 3(a). Since the April meeting, staff reached out to the following stakeholders regarding the proposed disclosures about discounts on restricted land:

   - Four valuers, including two members of the Australian Valuation Standards Committee; and

   - Some representatives of the Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC).

   Staff plan consulting with representatives of the Financial Reporting and Accounting Committee (FRAC), a sub-group of the Australasian Council of Auditors General (ACAG), as well as other valuers and some users of financial statements prior to the 11th June AASB meeting. Staff expect to provide verbal feedback to the Board at the AASB meeting about the comments received from these consultations.

6. Initial feedback from some stakeholders indicated support for pursuing the principle of increased transparency about the amounts of discounts for restrictions in fair value measurements, and noted that valuation reports could provide the necessary information without undue cost or effort.

[1] Restrictions imposed on the land's use or the prices that may be charged for using the land.

Some stakeholders, however, noted various valuation techniques used in different jurisdictions, some without the discount to the current market buying price of equivalent unrestricted land as an explicit component of the fair value estimate; and have advised that distinguishing the effects of restrictions on land from other discounts (eg for contamination) might give rise to some practical and definitional issues. In addition, some stakeholders noted that land holdings of major public sector entities are revalued on a rolling basis over a five-year period.

Staff will perform further outreach to understand the likely cost and practical complexity of obtaining the information needed for the disclosures and their implications for the implementation of the disclosure proposals as an interim step.

7. Therefore, at this meeting, staff request the Board to:
   - form initial views on:
     - (i) the key issues arising from stakeholders' feedback regarding the basic features of the proposed disclosures described in paragraph 3(a); and
     - (ii) other key issues identified, which concern the scope of those proposed disclosures;
   - provide comments on staff's proposed drafting of amendments to AASB 13 regarding the proposed disclosures (Agenda Paper 7.2); and
   - provide direction on the next steps of the project.

8. In respect of the additional guidance described in paragraph 3(b), staff plan to include draft amendments to AASB 13 as part of a working draft Exposure Draft for the Board's consideration at a future meeting. Staff plan to also discuss with the Board at that meeting whether the guidance on these issues, regarding assets measured at current replacement cost, should be applicable to all NFP entities (ie not limited to NFP entities in the public sector).

Structure of this paper

9. This paper is structured as follows:

   (a) Section 1: Staff's analysis and recommendations about key issues identified regarding the scope of the proposed disclosures

   (b) Section 2: Proposed updated project milestones and timeline

   (c) Appendix: High-level summary of feedback from stakeholders on the proposed disclosures about discounts on restricted land (for noting)

Attachment

Agenda Paper 7.2: Staff's proposed draft amendments to AASB 13 regarding the proposed disclosures

Questions to the Board

10. Specific questions for the Board regarding staff's proposals are contained in each section of the paper, including the Appendix, as well as Agenda Paper 7.2.

Section 1 – Staff's analysis and recommendation about key issues identified regarding the nature and scope of the proposed disclosures

Reasons for proposing disclosures about discounts on restricted land

11. Throughout this Project, the Board has sought to address concerns that, in applying AASB 13 to fair value measurements of restricted land they hold primarily for its service capacity, public sector NFP entities sometimes measure such land at a heavily discounted value compared with its current market buying price (reflecting the estimated effect of the restriction on the entity's ability to directly generate net cash inflows through use of the land). In such cases, the application of AASB 13 implies market participant buyers would not be prepared to replace the asset's service potential because the net cash inflows the asset can generate directly through its restricted use would not recover the asset's current replacement cost (current market buying price). The Board was concerned that where fair value measurements of the restricted land differ materially from current market buying price, using the lower carrying amount causes a loss of accountability for the service potential being managed and deployed by the public sector NFP entity on behalf of the community.

12. The Board was of the view that, as an interim step, developing requirements to disclose the amount of discounts deducted from the current market buying price of unrestricted land should provide useful information for assessing:

- the current value of the land's service capacity (which is indicated by the current market buying price of equivalent unrestricted land); and
- the practical significance of the 'discounts' issue (which would be useful input to the Board's future decisions about the direction of the project).

Key issues identified during initial outreach

13. During consultations with stakeholders (see Appendix) staff identified some issues that require the Board's consideration regarding the nature and scope of the proposed disclosures. This Section contains staff's analysis of, and recommendations regarding, these issues.

14. As previously discussed with the Board, current practice by most public sector NFP entities is to apply a **discount**, either explicitly or implicitly, to the market value of a **reference parcel of unrestricted land** (ie reference land) to reflect **restrictions** (see paragraph 17) imposed on the parcel of land being valued. Examples include:

- using the price of adjacent/nearby land and explicitly deducting a discount for the effect of the restriction (explicit discount); and
- using the price of land with a much lower intensity of use—and, consequently, a much lower value—than adjacent/nearby land and not explicitly deducting a discount for the effect of the restriction because it is implicitly taken into account by using cheaper land in a lower-intensity-of-use location as a reference (implicit discount).

15. Staff think it is important to determine the scope (or meaning) of the following terms in the context of the proposed disclosures about discounts on restricted land:

- 'Restrictions' imposed on land (Issue 1); and

- ‘Reference land’ and ‘discounts’ deducted from reference land (in relation to ‘discounts’, address the implications of ‘implicit discounts’) (Issue 2).

Issue 1 – the scope of the term ‘restrictions’ imposed on land

16. Feedback from stakeholders indicated a need to consider the scope of the term ‘restrictions’ imposed on land in the context of the Board’s proposed disclosures, specifically:

    (a) Issue 1A – Does ‘restrictions’ on land refer only to legal restrictions? There might be situations where a parcel of land is not legally restricted (eg zoned for a commercial purpose) but a public sector entity has used the land as a recreational purpose and has applied a discount to the current market buying price of an equivalent unrestricted land. Should the proposed disclosure include such discounts?

    (b) Issue 1B – If an entity adjusts the fair value of a parcel of land to reflect adverse physical characteristics of the land (such as contamination, being flood-prone or lack of access), should the amounts being deducted for these physical characteristics of land be included in the proposed disclosures?

Staff analysis

Issue 1A – Does ‘restrictions’ on land refer only to legal restrictions?

17. Many stakeholders have expressed to staff that they believe a market participant buyer would consider restrictions imposed on the **land’s use or the prices** that may be charged for using the land; and therefore, in accordance with AASB 13 paragraph 11[2], they have deducted a discount to reflect these restrictions when measuring the fair value of restricted land.

18. In respect of Issue 1A in paragraph 16(a), staff think it is arguable whether restrictions that are not legal restrictions (as referred to in paragraph 28(b) of AASB 13[3]) should be factored into the land’s fair value measurement. Examples of these restrictions are those that are asserted to be intrinsic to the nature of particular assets and their purposes for being used by the public sector entity holding them (ie it has been argued in some jurisdictions that it is unnecessary to legally restrict the use of these assets because there is no prospect of redeploying them for a so-called ‘higher and best use’). That is, some argue that restrictions imposed on the use or disposal of an asset are a characteristic of that asset because most entities are mandated by government, ministerial directives, legal or administrative requirements to continue to provide the services that the assets assist them to provide. Staff think that, regardless of whether that argument is valid (the consideration of which is outside the scope of this ‘interim-step Exposure Draft’), if a public sector NFP entity deducts a discount for these other restrictions, they should be included in the discounts disclosed.

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[2] AASB 13 paragraph 11 states that “… when measuring fair value an entity shall take into account the characteristics of the asset … if market participants would take those characteristics into account when pricing the asset … at the measurement date. Such characteristics include … (b) restrictions, if any, on the sale or use of the asset.”

[3] AASB 13 paragraph 28 states that “The highest and best use of a non-financial asset takes into account the use of the asset that is … legally permissible … (b) A use that is legally permissible takes into account any legal restrictions on the use of the asset that market participants would take into account when pricing the asset (eg the zoning regulations applicable to a property).”

19. Staff think the scope of the proposed disclosure should include all deductions that an entity adjusts to reflect the limitations imposed on the land's use or the prices that may be charged for using the land as a result of the land's **public-sector-specific purpose**, even if it is not imposed by law or legislation.

20. Staff think the Board and users would find it useful to understand the nature of all discounts being deducted by preparers of financial statements and the amounts of discounts being deducted from a current measure of the land's service potential when measuring the land's fair value, when those discounts relate to the public-sector-specific purpose for holding the asset. This would be helpful for the Board's future deliberation about the measurement issue of restricted land.

Issue 1B – Should the amounts being deducted for the physical characteristics of land being included in the proposed disclosures?

21. In respect of Issue 1B in paragraph 16(b), staff think amounts deducted for adverse physical characteristics of the parcel of land being valued should not be included in the proposed disclosures. This is because these other deductions reflect physical characteristics of the land rather than public-sector-specific restrictions on the land's use or pricing, and are not unique to the public sector. An issue for future research and discussion is the practicality of separating these factors in a fair value measurement from the other adjustments to the current market buying price of equivalent unrestricted land.

Staff recommendations

22. Staff recommend clarifying in the Exposure Draft that the proposed disclosures about 'discounts' for 'restrictions' on land should:

- include discounts applied to reflect legal restrictions (eg to reflect the current zoning of the land) described in paragraph 28(b) of AASB 13[3]; and
- include any other restrictions that reporting entities deduct for in fair value measurements because of the **restricted public-sector-specific purpose** for holding the parcel of land being valued; but
- in principle, exclude amounts deducted to reflect adverse physical characteristics of the parcel of land because they do not arise from restrictions over the use of the land for a public-sector-specific purpose.

Question 1 to the Board
Do Board members agree with the staff recommendations in paragraph 22 to clarify the scope of the terms 'discounts' and 'restrictions' on land in the Exposure Draft?

Issue 2 – meaning of the terms 'reference land' and 'discounts'

23. As mentioned in paragraph 14, most public sector NFP entities would apply a **discount**, either explicitly or implicitly, to the market value of a **reference parcel of unrestricted land** (ie reference land) to reflect restrictions imposed on the parcel of land being valued.

24. An 'explicit discount' refers to using the price of adjacent/nearby land and explicitly deducting a discount for the effect of the restriction.

25. An 'implicit discount' refers to using the price of land that is not in the same proximity but has a lower intensity of use than the parcel of land being valued—and, consequently, a much lower value—than adjacent/nearby land. In this case, a valuer does not explicitly deduct a discount for the effect of the restriction because it is implicitly taken into account by using cheaper land in a low-intensity-of-use location as a reference (see example in paragraph 31).

26. Staff think the following issues need to be addressed to provide necessary guidance on the proposed disclosures:

   - Issue 2A – How should 'reference land' be defined?
   - Issue 2B – Should discounts that are implicitly deducted be disclosed and, if so, how should the amounts of those discounts be determined?

Staff analysis

Issue 2A – How should 'reference land' be defined?

27. Staff note that all land has a zoning restriction limiting its use for a specific purpose. For example, a parcel of land that has a commercial zoning cannot be used for a residential purpose. Therefore, any 'reference land' on which a valuer bases the fair value measurement might be subject to zoning restrictions that are not related to a public-sector-specific purpose.

28. Reflecting on initial comments received from valuers, staff are of the view that 'reference land' to which a discount is applied (either explicitly or implicitly) to reflect the limitations imposed on the land being measured for its restricted public-sector-specific purpose should be '**equivalent unrestricted land**', which is land:

   - in the same proximity as the land being valued, as the location of the land is a key aspect that valuers consider when measuring the value of land;
   - capable of providing the same services (or utility) as the parcel of land being measured (although not necessarily of the same dimensions, which can be adjusted for in the valuation); and
   - not restricted for the public-sector-specific purpose for holding the parcel of land being valued.

29. Staff reached this view because:

   - comments from valuers indicated that when measuring the fair value of restricted land using the 'explicit discount ' method described in paragraph 24, a valuer would usually start with a hypothetical assessment of the 'underlying zoning' of the land being valued (ie what would be the zoning of the land if it is not zoned for a public-sector-specific purpose) and then apply a discount to reflect the effect of the restriction for the public-sector-specific purpose; and

- staff are of the view that the Board and users are interested in understanding the amount being deducted from the value of the land in respect of the public-sector-specific purpose, which helps them to assess the current value of the land's service capacity.

Issue 2B –Should the discounts that are implicitly deducted be disclosed and, if so, how should the amounts of those discounts be determined?

30. Staff noted that identifying 'equivalent unrestricted land' is not formally included in the valuation process under the 'implicit discount' method described in paragraph 25. Therefore, disclosures based on 'equivalent unrestricted land' would require an additional formal step in the valuation process.

31. Using the 'implicit discount' method, the valuation is based on comparison with 'reference land' that is usually a parcel of land with a low-level utility in a different location (eg. grazing land or similar on the urban fringe of the metropolitan area with no foreseeable development or redevelopment potential at the measurement date). In this case, the 'discount' to reflect the public-sector-specific purpose is implicit in the market value of the reference land.

32. Because the 'discount' to reflect the restriction for a public-sector-specific purpose is implicit in the market value of the reference land in the case of 'implicit discount', it would create extra work to ask for disclosures in order for the Board and users to understand the amounts being deducted from the current market buying price of equivalent unrestricted land to reflect the restriction for a public-sector-specific purpose.

33. Staff identified the following options to address the treatment of 'implicit discounts':

- Option 1 – require entities (and therefore, valuers) to disclose the difference between the fair value measurement recognised for the land being valued and the current market buying price of adjoining/nearby land that would have the same 'underlying zoning' as the parcel of land being valued (ie the most likely zoning if it doesn't have the public-sector-specific purpose); and

- Option 2 – do not require disclosure of the amount of 'discounts' on land when 'implicit discounts' are used.

34. Table 1 below documents staff's analysis of the advantages and disadvantages of these options.

Table 1

Option	Advantages	Disadvantages
Option 1	• Achieves consistency in disclosures about discounts for restrictions to use land for a public-sector-specific purpose • The Board and users would be able to obtain information about the impact of the public-sector-specific purpose on the	• Potentially require more work of valuers and therefore incur additional costs in obtaining valuations Note: Feedback from initial consultations with some valuers indicates valuers should be able to obtain this information with minimal cost because valuers would typically obtain the value of

Option	Advantages	Disadvantages
	fair value measurement of land.	adjoining/nearby land as part of the valuation process (to perform a reasonableness check on the valuations obtained).
Option 2	• Would not require valuers to incur the time and cost of formally obtaining the value of adjoining/nearby land solely for the purpose of the new disclosure.	• Would not achieve consistency in disclosures about discounts on land • The Board and users would not be able to obtain all information about the impact of the public-sector-specific purpose on the fair value measurement of land.

35. Based on the above, and subject to further consultation with valuers regarding the costs involved in obtaining and disclosing the value of adjoining/nearby land in valuation reports, staff recommend adopting Option 1 – to require entities to disclose the difference between the fair value measurement recognised for the land being valued and the current market buying price of adjoining/nearby land that would have the same ‘underlying zoning’ as the parcel of land being valued.

Staff recommendation

36. Staff recommend clarifying in the Exposure Draft that ‘**<u>equivalent unrestricted land</u>**’ is a parcel of land that is:

- in the same proximity as the land being valued, because the location of the land is a key aspect that valuers consider when measuring the value of land;
- capable of providing the same services (or utility) as the parcel of land being measured (although not necessarily of the same dimensions, which can be adjusted for in the valuation); and
- not restricted for the public-sector-specific purpose as that applying to the parcel of land being valued.

37. Staff also recommend requiring disclosure of the difference between the fair value measurement recognised for the land being valued and the current market buying price of adjoining/nearby land that would have the same ‘underlying zoning’ as the parcel of land being valued, irrespective of the method used.

Questions to the Board
Q2: Do Board members agree with the principles for clarifying the meaning of ‘equivalent unrestricted land’ in the staff recommendation in paragraph 36?
Q3: Do Board members agree with the staff recommendation in paragraph 37 to require disclosure of the difference between the fair value measurement recognised for the land being valued and the current market buying price of adjoining/nearby land that would have the same ‘underlying zoning’ as the parcel of land being valued?

Issue 3 – Disclosures supplementing the amount of discounts deducted for the effects of restrictions over the use of land for a public-sector-specific purpose

38. At its meeting in April 2020, the Board decided to propose a requirement to disclose the basis for calculating the discount to the current market buying price of equivalent unrestricted land and instructed staff to undertake further outreach. Therefore, the Board did not discuss how detailed the disclosure requirement about the 'basis' for calculating the discount should be.

39. To provide perspective to the disclosure choices, the following staff analysis provides an overview of the existing and potential disclosure requirements pertaining to the basis for estimating the fair value of an asset. These existing and potential disclosure requirements seem relevant to evaluating which requirements should be included in AASB 13 regarding the basis for calculating these discounts.

Staff analysis

40. Agenda Paper 8.1 for the Board's meeting in April 2020 sets out staff's view that it would be useful if the financial statements were to disclose the key assumptions used to calculate the amount of the discount, such as the probability of the restriction being lifted and the estimated costs of obtaining rezoning, if those are factors in the methodology. It also noted that these disclosures might be more detailed than the disclosures that AASB 13 requires of for-profit entities.

41. Table 2 below sets out the following:

- current disclosure requirement of AASB 13 for for-profit entities and private sector NFP entities,
- current disclosure requirement of AASB 13 for public sector NFP entities, factoring in the disclosure relief in paragraph Aus93.1 of AASB 13;
- reporting requirements for valuation reports specified by International Valuation Standard IVS 103 *Reporting*; and
- staff proposed additional disclosure requirements that are not present in AASB 13 (nor IFRS 13) pertaining to the basis for calculating discounts to the current market buying price of equivalent unrestricted land.

Table 2

AASB 13 ref	Disclosure	Current requirement		Requir't of IVS 103	Staff's tentative view: restricted land
		FP & private NFP entities	Public NFP entities		
93(d)	Description of valuation technique(s) used	✓	✓	✓	✓
93(d)	Description of the inputs used	✓	✓	✓	✓
93(d)	For Level 3 measurements, quantitative information about significant unobservable inputs used (eg discount for the risk that public-sector-specific restriction will not be removed) • not required to be created if not developed by the entity • however, must be disclosed if reasonably available to the entity	✓	X	X	✓
n/a	Quantitative information about significant observable inputs used (eg [arguably] estimated unadjusted market values of land in a less closely settled environment; cost to adapt property to a higher and better use, including costs to remove contamination; the time value of the estimated period until the restriction is removed; and legal and other costs of the process of removing the restriction)				
	• Level 2 measurements	X	X	X[4]	X
	• Level 3 measurements	X	X	X	X
n/a	Quantitative information about the significant assumptions made:				
	• Level 2 measurements	X	X	X[5]	X
	• Level 3 measurements	X	X	X	X

42. In keeping with the general tenor of the Board's discussion of disclosures in April 2020, as referred to in paragraph 4, staff think the disclosure requirements supplementing disclosure of the amount of discounts should not be more detailed than the disclosures that AASB 13 requires

[4] IVS 103 para. 30.1(d) requires valuation reports to convey the key inputs used, but does not stipulate that the amounts of those inputs must be reported.

[5] IVS 103 para. 30.1(e) requires valuation reports to convey the assumptions made, but does not stipulate that the amounts of those assumptions must be reported.

of for-profit entities. Staff note that initial discussions with valuers have indicated that various components of the discount pertain to observable market inputs (for example, observable evidence often exists of the typical period to obtain rezonings or the cost to remove improvements in order to achieve a higher and better use). Requiring quantitative disclosure of all significant inputs to, and assumptions made in the calculation of, fair values would seem to have an objective of helping users to develop their own estimates of fair value. Such an objective would go beyond the disclosure objective in paragraph 91 of AASB 13 (which refers to helping users of financial statements to *assess* the valuation techniques and inputs used—which seems more related to helping users assess the quality and robustness of the fair value estimates). As the IASB stated in its Basis for Conclusions on IFRS 13 in respect of disclosing quantitative information about unobservable inputs used in a fair value measurement:

> "(for) a measurement categorised within Level 3 of the fair value hierarchy … disclosures about such information help users to understand the measurement uncertainty inherent in the fair value measurement. … the objective of the disclosure is not to enable users of financial statements to replicate the entity's pricing models, but to provide enough information for users to assess whether the entity's views about individual inputs differed from their own and, if so, to decide how to incorporate the entity's fair value measurement in their decisions. …" (paragraphs BC190 – BC192)

43. Land that is subject to restrictions would be measured at Level 2 or Level 3 of the fair value hierarchy (the unique location of each parcel of land means that Level 1 evidence will never be available). Staff observe that (as shown in Table 2 in paragraph 41 above), all entities are currently required by paragraph 93(d) of AASB 13 to disclose a description of the valuation technique(s) and inputs used in the fair value measurement. This would appear to involve, in the case of land restricted for use for a public-sector-specific purpose, disclosure of:

- whether the market approach, income approach or cost approach was used to measure the fair value of the land (typically, the market approach would be used);
- if the market approach or cost approach is used to estimate the fair value of each parcel of land, whether the reference land used to develop each fair value estimate is in the same area as the parcel of land being valued;
- the fact that a discount has been deducted for the risk that the restriction affecting the parcel of land being valued (but not the reference land) will not be able to be removed, if that valuation technique has been used; and
- if the fair value estimate includes adjustments for the cost to adapt the property to a higher and better use, the time value of the estimated period until the restriction is removed, and legal and other costs of the process of removing the restriction, the nature of those inputs to the fair value estimate.

Staff recommendation

44. For the reasons in paragraph 42, staff recommend that the supplementary *quantitative* information disclosed in addition to the amounts of discounts to the current market buying price of equivalent unrestricted land should be limited to quantitative information about significant unobservable inputs used (typically, the discount for the risk that a public-sector-specific restriction will not be removed). This would, in effect, reverse the exemption in paragraph Aus93.1 of AASB 13, but only in respect of land restricted for a public-sector-specific purpose.

Question to the Board

Q4: Do Board members agree that the supplementary *quantitative* information disclosed in addition to the amounts of discounts to the current market buying price of equivalent unrestricted land should be limited to quantitative information about significant unobservable inputs used?

Issue 4 – Classes of assets including land measured at fair value

45. Many public sector NFP entities recognise and disclose land (or 'land and other assets' eg land and buildings) as one class of assets in their property, plant and equipment note disclosure under AASB 116 *Property, Plant and Equipment*.

46. Public sector NFP entities have sub-classified land into different categories (eg. land under roads, land under hospitals or schools, Crown land) in their narrative fair value disclosure note[6]. However, the carrying amounts of these sub-classes of land are not separately disclosed.

47. Consistent with the level of disaggregation used for the balances of land (or land and other assets), staff's proposed disclosures about the carrying amount of land (or land and other assets) measured at fair value, and the adjustment deducted from the current market buying price of equivalent unrestricted land in arriving at that fair value carrying amount have been drafted to apply to **each class of land** (or land and other assets) within the scope of AASB 116.

48. Another possible approach to the granularity of disclosures about the amounts of discounts for restrictions on land would be to require the carrying amounts and related discounts to be disclosed for each sub-class for which the fair value measurement techniques and inputs are described. An advantage of doing so would be that information about discounts (such as the percentage deduction applied for the risk of being unable to remove a public-sector-specific restriction) might be capable of being disclosed within narrower ranges.

49. Staff think that to disclose more meaningful information about the range of percentage adjustments to the current market buying price of land, an entity might voluntarily choose to disaggregate further some classes of assets including restricted land; however, staff do not recommend propose requiring such disaggregation in the Exposure Draft. Staff reached this view because:

- the primary focus of the proposed disclosures[7] is to enable users of financial statements to identify the amount by which the **carrying amounts of land** reflect an adjustment to the current market buying price of equivalent unrestricted land and, in turn, estimate the current value of the service capacity embodied in land held primarily for its service capacity. More granular information about discounts that would stem from requiring further disaggregation would provide further insights into the extent to which fair value measurements are dependent on estimates of the probabilities of restrictions being

[6] AASB 13 paragraph 93(d) includes a requirement to disclose a description of the valuation technique(s) and inputs used in fair value measurements categorised within Level 2 or Level 3 of the fair value hierarchy.

[7] For example, AASB 13 paragraph 91 states that the objective of fair value measurement disclosures is to help "… users of its financial statements assess … (b) for recurring fair value measurements using significant unobservable inputs (Level 3), the **effect of the measurements on profit or loss or other comprehensive income for the period**" (emphasis added)

lifted—however, users of financial statements would have very limited capacity to evaluate the reasonableness of those probability estimates; and

- any changes to requirements for identifying separate classes of assets, albeit for a limited-purpose objective, would be beyond the purpose of the proposed amendments. A counter-argument to this point is that any requirements to identify classes of assets at a more disaggregated level for the purpose of disclosures about discounts on restricted land could be precluded from affecting the boundaries of classes of assets in AASB 116 for the purpose of offsetting revaluation increases and decreases (this could be achieved by an explicit statement to this effect in the new text of AASB 13).

Staff recommendation

50. Based on the reasons in paragraph 49, on balance, staff recommend that the Exposure Draft's proposals:

    - should not specify how classes of assets that include land measured at fair value should be determined; and
    - should not require disaggregating further classes of assets in relation to discounts; but
    - should require disclosures about the carrying amount of land (or land and other assets) measured at fair value, and the adjustment deducted from the current market buying price of equivalent unrestricted land in arriving at that fair value carrying amount only in respect of each class of land (or land and other assets) for which the carrying amount is separately disclosed.

Question to the Board
Q5: Do Board members agree with staff recommendations in paragraph 50?

Issue 5 – Should land restricted for a public-sector-specific purpose and obtainable with the restriction be excluded from the disclosure requirements about discounts for restrictions?

51. The primary objective of the proposed disclosure requirements about discounts for restrictions on the use of land for a public-sector-specific purpose is to assist users of financial statements to identify the current value of the service capacity of land held primarily for its service capacity, when a fair value measurement may not (because of those restrictions) reflect faithfully the current value of the land's service capacity. Consequently, the benchmark value with which fair value measurements of restricted land are compared is the current market buying price of equivalent unrestricted land.

52. 'Unrestricted' land is used as a benchmark for the disclosure on the presumption that a market participant buyer (including another public sector entity with identical characteristics to the reporting entity) would be unable to acquire land with the restriction, ie for a price reflecting the loss of cash-generating ability arising from the restriction. That is, that benchmark presumes the reporting entity (and any other market participant) would be unable to take advantage of the restriction's adverse effect on the land's cash-generating ability that would be considered by for-profit market participants. However, in initial consultations about the proposed disclosures, feedback has been received that in some instances, market transactions occur for similarly restricted land in sufficiently close proximity to provide observable market evidence of the value of the entity's parcel of restricted land. An example is where a not-for-

profit public sector entity measures the fair value of a parcel of land restricted for use as a school by reference to the price of a parcel of land at an adjacent or nearby site that is also restricted for use as a school and available for purchase for a price supported by observable market evidence.

53. In the circumstances referred to in paragraph 52, it would be consistent with the Board's reasoning documented in paragraphs Aus66.1(a) and BC34 – BC35 of the March 2020 Draft Exposure Draft for this project (ie the broader-scope Draft Exposure Draft being considered by the Board) to treat the current value of the service capacity of such restricted land as being reflected by the observable market price for the similarly restricted (and available) land. Adopting that reasoning would mean that, in such circumstances, the price used as the benchmark should be the price for equivalent *restricted* land, which would be the fair value measurement adopted for that land by the reporting entity. In other words, no difference would exist between the land's fair value measurement and the current value of its service capacity. However, if the fair value of a parcel of restricted land is based on the value of equivalent restricted land obtainable in the marketplace for a price supported by observable market evidence, including that parcel of land in the scope of the disclosure requirement would lead to disclosure of the difference between the fair value measurement and the current market buying price of equivalent *unrestricted* land. This would overstate (albeit for disclosure purposes only) the current value of the land's service capacity.

Staff recommendation

54. Based on the reason in paragraph 53, staff recommend proposing in the Exposure Draft that a parcel of land restricted for a public-sector-specific purpose should be excluded from the disclosure requirements of draft paragraph Aus93.2 if its fair value estimate is based on the value of equivalent restricted land obtainable in the marketplace for a price supported by observable market evidence (see paragraph F31 of Agenda Paper 7.2).

Question to the Board

Q6: Do Board members agree with staff recommendation in paragraph 54?

Terminology – 'Discounts' versus 'Adjustments deducted'

55. This Staff Paper refers to 'discounts', for continuity with the Board's tentative decision in April 2020 (see paragraph 3(a)). However, from initial consultation on the Board's tentative decision, feedback was received that 'discounts' is not a term used by valuers in the context of these disclosures, and is likely to cause confusion. One problem with referring to 'discounts' or 'discounting' is that the term is widely used to refer to discounting future cash flows to their present value—a meaning unrelated to the purpose of the Exposure Draft. Accordingly, staff's proposed drafting of amendments to AASB 13 in Agenda Paper 7.2 refers to 'adjustments deducted', consistent with the use of 'adjustments' by valuers in the context of the purpose of this Exposure Draft.

Section 2 – Proposed updated project milestones and timeline

57. Based on initial conversations with stakeholders (see Appendix), staff consider that further consultations with stakeholders is required to obtain further information about the following factors:

- whether there are any other methods, other than the 'implicit discount' and 'explicit discount' methods described in Section 1, used to measure fair value of restricted land;
- whether it would be possible, and the costs required, to separately disclose in valuation reports the adjustments made to reflect physical characteristics of the land (eg contamination, being flood-prone or lack of access);
- whether it would be possible, and the costs required, to obtain the necessary information to prepare the proposed disclosures for parcels of land that are outside of the valuation cycle; and
- whether the proposed disclosures about discounts on restricted land would be useful to users of public sector financial statements.

58. The IASB plans to expose proposed amendments to the disclosure requirements of IFRS 13 in the first half of 2021 as part of its *Disclosure Initiative – Targeted Standards-level Review of Disclosures* project. Staff will continue monitoring this project and assess how the Board might need to enlarge upon the IFRS wording to specify its proposed disclosures about discounts on restricted land.

59. The following table contains a proposed project timeline for the Board's consideration and comment. The milestones and timeline will periodically be reviewed and updated to ensure the project path remains appropriate and the project can be adequately resourced.

Meeting / Deliverable	**Project Milestones**
June – September 2020	Staff to continue consulting with stakeholders, including the project's Project Advisory Panel, about the proposed disclosures to obtain information about the factors noted in paragraph 57. Staff to consider options to progress the measurement issue about restricted land.
16-17 September 2020: Board meeting	Present staff analysis of possible options to progress the measurement considerations in respect of restricted land. Subject to feedback from stakeholders, staff to analyse the costs and effort required to prepare the proposed disclosures about discounts on restricted land. Board to consider a working draft of the interim-step ED, which would include staff's proposed amendments to AASB 13 about the proposed disclosures about discounts on land and to provide guidance regarding assets measured at current replacement costs.

Meeting / Deliverable	Project Milestones
September – November 2020	Subject to Board decisions at September meeting: • Staff to update draft ED based on decisions made in the September Board meeting; • Staff to perform further targeted consultation on any remaining key issues.
11-12 November 2020: Board meeting	Board to consider a pre-ballot draft of the ED reflecting outcome of further targeted consultations since September meeting.
18 November – 2 December 2020	Subject to Board decisions at November meeting, Board to vote on the Exposure Draft out of session with a two-week voting period. Voting period ends 2nd December 2020.
3 December 2020	Issue ED for public comment for a period of 90 days. Comment period ends 26 February 2021.
April 2021: Board meeting	Board to consider Staff paper and comments on the ED and decide on the amendments/guidance and next steps of the project.

Questions for Board members

Q7: Are there any other matters about which Board members would like staff to consult with stakeholders?

Q8: Do Board members agree with staff's proposed project milestones and timeline?

Appendix – High-level summary of feedback from initial outreach with stakeholders on the proposed disclosures about discounts on restricted land

A1. This Appendix contains a high-level summary of feedback from the initial outreach with the following stakeholders regarding the proposed disclosures about discounts on restricted land:

- Four valuers, including two members of the Australian Valuation Standards Committee; and
- Some representatives of the Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC).

A2. Staff plan consulting with representatives of the Financial Reporting and Accounting Committee (FRAC), a sub group of the Australasian Council of Auditors General (ACAG), as well as other valuers and some users of financial statements prior to the 11^{th} June AASB meeting. Staff expect to provide a verbal feedback to the Board at the AASB meeting about the comments received from these consultations.

Overall feedback

A3. Some valuers support the Board's proposal to require disclosures about discounts on restricted land particularly given the detailed reporting requirements in IVS 103. However, one valuer expressed concern that the Board seems to be asking for the value of a 'highest and best use' that is not achievable in practice and queried the usefulness of such a disclosure.

A4. Based on discussion with some representatives of HoTARAC, most jurisdictions seem to support the principle of promoting more transparency about discounts being applied on restricted land, if a reasonable timeframe is given to implement the requirement to make these disclosures. However, some jurisdictions commented that, due to the variety of methods used by valuers to measure fair value of land, the disclosures might be more complex to prepare than expected and might involve summing heterogeneous 'discounts' (see paragraph A6).

A5. Some HoTARAC representatives commented that only some parcels of land are valued every year and, depending on the length of the valuation cycle, it would take some time to obtain the required information for the disclosures even if valuers provide the necessary information in valuation reports. If the interim step of adding disclosure requirements about discounts for restrictions on land means the new disclosure requirements are only a temporary measure, these HoTARAC representatives questioned whether the cost and effort required to develop these disclosures would be justified.

A6. Some HoTARAC representatives commented that they engage different private sector valuers as well as valuers in the Valuer-General Office, and note that a variety of methods and discounts are being applied to similar types of land (for example, a range of discounts being applied to school land). They questioned the usefulness of aggregating these heterogeneous 'discounts' in a note disclosure. Some HoTARAC representatives commented that perhaps requiring disclosure of the objective of the discounts being applied to land might be more appropriate and useful than disclosing the amount being deducted, given the wide variety of discounts being applied. Some HoTARAC representatives wondered whether it might be more appropriate to remove the current disclosure relief in paragraph Aus93.1 of AASB 13.

A7. HoTARAC representatives mentioned that it is too early to comment on the costs involved in preparing the required disclosures because they would need to understand the scope of the disclosures and to have discussions with their valuers to ensure valuation reports have sufficient data for making these disclosures.

A8. One HoTARAC representative commented that, in its Post-Implementation Review of IFRS 13 *Fair Value Measurement*, the IASB deferred completing its consideration of the disclosures in IFRS 13 pending further progress with the IASB's 'Better Communication in Financial Reporting' project. The HoTARAC representative expressed concern that the IASB has decided to issue an Exposure Draft of amendments to the disclosure requirements of IFRS 13 (deferred until the first half of 2021 because of the Coronavirus pandemic), and might amend the disclosure requirements for fair value measurements in ways that contradict whichever disclosure requirements the AASB issues as an interim step for discounts in relation to restricted land. They suggested that the AASB takes an holistic view to disclosures related to fair value measurement, to avoid the risk of chopping and changing disclosure requirements (and consequential unnecessary costs for preparers, auditors and users of financial statements of public sector NFP entities). Another HoTARAC representative suggested that the AASB takes a conceptual approach to the objective of its disclosure requirements.

Valuation processes and the implications of 'implicit discounts'

A9. Some valuers mentioned that they typically apply the 'explicit discount' method described in paragraph 24 of Section 1 when measuring the fair value of restricted land. They would consult with town planners to identify the most likely 'underlying zoning' of the parcel of land being valued (ie the likely zoning of the land if it is not used for a public service). These valuers explained that the zoning of the surrounding land or nearby land (of the land being valued) would often be the underlying zoning of the land subject to measurement.

A10. Under two types of the 'explicit discount' method, valuers would consider the probability of the current zoning being changed, the time it takes for the zoning change to occur and the estimated cost of obtaining rezoning and adapting the asset to a higher and better use. Under one type of 'explicit discount', these three factors are separately identified in calculating the overall 'discount' being applied to the value of the 'reference land' in determining the fair value of the parcel of land subject to measurement. Under another type of 'explicit discount' to the value of the reference land, a single discount factor is used, based on guidelines reflecting overall historical experience with the individual factors affecting the class of land in question.

A11. One valuer explained that the current valuation reports they prepare already include the information about the 'reference land' and the discount being applied to the value of the reference land, and the rationale for applying the discount. Therefore, they do not expect additional work would be required to prepare valuation reports in order for financial statements preparers to make the proposed disclosures about discounts on land. Another valuer mentioned that this information is definitely needed in order to determine the value of the land being measured. Therefore, even if the information is not currently included in the valuation report, it would not require much additional work to include the required information in the future upon request.

A12. One valuer commented that where the 'implicit discount' method (as described in paragraph 25 of Section 1) is used to measure the value of land, additional work would be required to obtain information about the market value of the land adjacent to or near the parcel of land subject to measurement. However, two other valuers expressed a different view, namely, that it won't require too much additional work – this is because a valuer would have obtained market values of the land adjacent to or nearby the land subject to measurement in order to determine the adjustment factor to reflect that the land subject to valuation is in a different proximity to the reference land.

A13. One valuer added that if a valuer complies with International Valuation Standards (IVS), then all elements of the calculations to estimate an asset's fair value should be documented in valuation reports. Even if this information does not currently focus on the specific information the Board requires disclosure of, it would not create too much work (or too much additional cost) to report the information the Board requires of public sector NFP entities.

A14. Two valuers commented that it would be beneficial to specify in the Exposure Draft that the Board seeks disclosure of discounts being applied to reflect the land's 'restricted use', as distinct from other adjustments deducted for allowance for poor condition of the parcel of land.

A15. Two valuers also commented that if there is an easement running over the land subject to measurement, it is likely that the valuer would begin the valuation process by looking at the nearby land that also has an easement. In this case, the value of the reference land would have already factored in the 'easement discount', and the 'discount' for the easement would not be separately documented in valuation report. However, they noted that the discount for the easement – because is not specific to a public-sector purpose – would not be subject to the proposed disclosures.

A16. One valuer suggested that the Exposure Draft needs to specify the meaning of some of the key terms, for example: "current market buying price" and "equivalent unrestricted land", particularly because these terms are not typically used by valuers.