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Dear Ms Fox

IPSASB Exposure Draft *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Measurement of Assets and Liabilities in Financial Statements*

The Australian Accounting Standards Board (AASB) is pleased to provide its comments on the above named Exposure Draft (ED). In formulating its comments, the AASB considered the views received from Australian constituents.

General Comments

The AASB's general comments on the IPSASB ED are highly similar to those made in the AASB's submission (dated 15 May 2013) on the IPSASB Conceptual Framework ED *Elements and Recognition in Financial Statements*, as they are generally pertinent to the IPSASB's Conceptual Framework project in its entirety.

Due process

The AASB recommends that the IPSASB issues an omnibus ED incorporating its proposed Conceptual Framework after it has redeliberated all of its Conceptual Framework EDs, rather than finalising its Conceptual Framework without further consultation. An omnibus ED would enable the IPSASB's constituents to comment on the IPSASB's latest thinking on all of its proposals in its Conceptual Framework project, and to have regard to recent developments in financial reporting (including developments in the IASB's Conceptual Framework project). This would enable the IPSASB's constituents to gain a holistic perspective together with greater context, and this should facilitate both internal consistency within the IPSASB's Conceptual Framework and either alignment with, or understanding of reasoning for differences from, the IASB Conceptual Framework.

Subsequent review and update of the IPSASB Conceptual Framework

The AASB recommends that the IPSASB should regard its Conceptual Framework as a living document, and thus should commit to reviewing and updating it from time to time in light of subsequent developments in financial reporting. The timing of such reviews should reflect the IPSASB's resources and priorities, and developments in conceptual thinking. This approach would be beneficial, for example, in respect of concepts of presentation and disclosure. The AASB considers that thinking on these concepts is still in the early stages of development, on the part of the IPSASB, the IASB and the international financial reporting community generally. Therefore, it seems likely that thinking on concepts of presentation and disclosure will continue to evolve further. Under circumstances such as these, it is important not to treat the IPSASB Conceptual Framework as an immutable document.

Relationship between the IPSASB and IASB Conceptual Framework projects

The AASB recommends that the IPSASB maximises its liaison with the IASB regarding those Boards' respective Conceptual Framework projects, in the context of the Memorandum of Understanding between the International Federation of Accountants and the IASB dated 22 November 2011.

Ideally, the IPSASB and IASB Conceptual Frameworks would be complementary, where the only differences are those warranted by differences in circumstances. This would support the development of International Public Sector Accounting Standards and International Financial Reporting Standards that differ only where necessary to deal with different economic phenomena. This approach is also likely to assist users of general purpose financial reports who read financial reports across all sectors in the economy, which is important given the fundamental objective of general purpose financial reporting to meet users' information needs.

In relation to measurement in particular, the AASB's encouragement of complementary concepts of the IPSASB and IASB is premised on the assumption that the IASB develops a comprehensive and conceptual ideal measurement model (see the AASB's comments below on the role of the Measurement chapter).

The AASB's arguments in relation to the IPSASB ED in this submission are mainly focused on technical issues, and not primarily on whether the IPSASB's proposals are consistent with the tentative thinking of the IASB in its Conceptual Framework project.

Specific Comments

The AASB's most significant specific comments regarding the issues in the ED are set out below and elaborated on in Appendix A.

Role of the Measurement chapter of the IPSASB Conceptual Framework

The AASB regards the IPSASB's Conceptual Framework project as an opportunity for the IPSASB to lead thinking regarding the identification of a comprehensive and conceptually ideal model for measurement. In that regard, the AASB disagrees with the role of the Measurement chapter proposed in the ED.

Specifically, the AASB disagrees with limiting the role of the Measurement chapter of the IPSASB Conceptual Framework to identifying factors that are relevant in selecting a measurement basis for particular assets and liabilities in specific circumstances (paragraph 1.7 of the IPSASB ED refers). The AASB considers the primary role of the Measurement chapter of the IPSASB Framework should be to identify a comprehensive and conceptually ideal model for measurement. The possibility of departing from that model can be contemplated at the Standards level. In this regard, the AASB notes that key reasons for a mixed measurement model asserted in paragraphs 4.2 and 4.3 of the IPSASB ED (even in "cases where one measurement basis is regarded as the most appropriate basis conceptually": see the first sentence of paragraph 4.2) seem to be Standards-level/application issues, which therefore do not seem to be reasons not to identify an aspirational conceptual ideal.

As a matter of logic, the AASB believes that, in considering the various alternative measurement attributes, the IPSASB should assume there are material differences between their amounts. The analysis should not be clouded by confusing amounts that may, in practice, happen to be similar (e.g. the measured amounts for items turning over quickly and for which historical and current values may not be far apart).

These comments are elaborated on below, and further in the AASB's response to Specific Matter for Comment 1 in Appendix A.

Concept of capital (wealth)

The AASB considers it vitally important that the IPSASB Conceptual Framework should aspire to identify the ideal measurement model, the application of which would result in measurements of amounts recognised in financial statements possessing the following qualities:

(a) they contribute to meeting the objectives of financial statements by providing the most relevant information that can faithfully represent the amounts of those recognised elements;

(b) they can meaningfully be added, subtracted and compared; and

(c) their economic significance, individually and collectively, is capable of being understood (for example, the economic significance of the surplus or deficit for the period can be understood).

The AASB considers a pre-requisite for identifying the ideal measurement model and achieving the qualities of measurements identified in paragraphs (a) – (c) above is identifying the most appropriate concept of capital (wealth). In the absence of identifying a single preferred concept of capital, the IPSASB ED's discussion of the relative merits of different measurement bases seems unlikely to serve as a basis for coherent choices between measurement bases, because there is no reference point with which to assess the options. Similarly, it seems unlikely that a Measurement chapter consistent with the ED would help the IPSASB make consistent measurement decisions when developing new or revised IPSASs.

Historical cost basis is likely to be less relevant than a current value basis

The AASB considers that the historical cost basis is likely to be less relevant than a current value basis for assets and liabilities when current prices differ materially from historical prices. This is because it is difficult to conceive of a resource allocation decision or accountability assessment that logically would be based on historical prices (which represent sunk costs) in preference to being based on current values (which reflect the current environment and operations of the reporting entity).

Whether a particular current value is, in concept, the most useful measurement basis for a particular asset or liability also depends on whether that value can faithfully represent the financial characteristics of the economic phenomena it purports to represent.

Fair value

The AASB strongly disagrees with the omission of fair value from the current value measurement bases for assets identified in Section 3 of the IPSASB ED and from the measurement bases for liabilities identified in Section 5 of that ED. It recommends resolving that problem by replacing the term 'market value' with 'fair value' as a measurement basis discussed in Sections 3 and 5 of the Measurement chapter. These comments are elaborated on in the AASB's responses to Specific Matters for Comment 2 and 4 in Appendix A.

The AASB's responses to all of the specific matters for comment in the ED are set out in Appendix A.

If you have any queries regarding matters in this submission, please contact me or Jim Paul (jpaul@aasb.gov.au).

Yours sincerely

K M Stevenson

Kevin Stevenson
Chairman and CEO

APPENDIX A

AASB's response to the Specific Matters for Comment on the ED

Specific Matter for Comment 1

Do you agree that the selection of a measurement basis should be based on the extent to which a particular measurement basis meets the objectives of financial reporting? If you think there should be a measurement objective, please indicate what this measurement objective should be and give your reasons.

The AASB agrees that the selection of a measurement basis should be based on the extent to which a particular measurement basis meets the objectives of financial reporting, together with meeting the qualitative characteristics. However, the AASB considers that assessing measurement bases should not occur on an item-by-item mixed measurement basis, as is strongly implied by paragraph 1.7 of the IPSASB ED. The AASB recommends, for conceptual purposes, identifying a measurement objective to guide the selection of measurement bases, and fleshing out that measurement objective by identifying an ideal concept of capital (wealth). These recommendations are explained below.

Qualities of desirable measurements

The AASB considers it vitally important that the IPSASB Conceptual Framework should aspire to identify the ideal measurement model, the application of which would result in measurements of amounts recognised in financial statements possessing the following qualities:

(a) they contribute to meeting the objectives of financial statements by providing the most relevant information that can faithfully represent the amounts of those recognised elements;

(b) they can meaningfully be added, subtracted and compared; and

(c) their economic significance, individually and collectively, is capable of being understood (for example, the economic significance of the surplus or deficit for the period can be understood).

The AASB considers that the proposal to limit the purpose of measurement concepts to assisting a choice of an appropriate measurement basis for an item, based on the extent to which applying a particular measurement basis would assist in meeting the objectives of financial reporting, would (if adopted) be inadequate because it would not provide a framework for achieving all of the qualities identified in paragraphs (a) – (c) above. Although various measurement bases can be relevant when viewed in relation to individual items, it would be exceedingly difficult to resolve trade-offs between those bases without an overall objective. Furthermore, it is possible that an item-by-item approach would not yield consistency of concept, thereby diminishing the likelihood that measurements will contribute to enabling the financial statements, as a whole, to serve decision making and accountability objectives. The likely result would be the *ad hoc* selection of measurement bases, leading to measurements that, when viewed collectively, lack the ideal qualities identified in (b) and (c) above.

Measurement objective and concept of capital (wealth)

Consistent with its comments in the paragraph immediately above, the AASB considers that identifying a comprehensive and conceptually ideal model for measurement would be assisted by identifying a measurement objective, broadly along the lines suggested by Mr Ken Warren in his Alternative View on pages 35 – 39 of the IPSASB ED (in particular, see paragraph AV7 thereof). However, in addition to identifying a measurement objective broadly along those lines, the AASB considers it essential that the most appropriate concept of capital (wealth) is identified, in order to develop an ideal measurement model, the application of which would result in measurements of amounts recognised in financial statements possessing all of the qualities described in (a) – (c) above. (See also the AASB's comments below regarding the notions of 'financial capacity' and 'operational capacity' referred to in the Alternative View of Mr Ken Warren.)

Examples of concepts of capital discussed in the accounting literature are invested money capital, current cash equivalents and operating capability. These concepts of capital are explained in further detail in the AASB's submission (dated 1 July 2011) on the IPSASB Consultation Paper *Measurement of Assets and Liabilities in Financial Statements*.

Each of these concepts of capital has a different objective and can provide a different picture of the entity's wealth. In this regard, 'wealth' is used with its broadest economic meaning, i.e. scarce resources that assist the entity in pursuing its objectives (whether for-profit or not-for-profit) less claims on those resources.

The AASB acknowledges that the IPSASB ED evaluates different measurement bases by reference to information they provide about 'operating capacity' and 'financial capacity'. However, the ED does not define these notions or indicate which of them should take precedence generally.

Without an articulation of the stock of an entity's wealth (however measured), it is difficult to define the reporting entity, the elements of its financial statements[1] or the appropriate measurement model. For example, in the absence of identifying a single preferred concept of capital, the IPSASB ED's discussion of the relative merits of different measurement bases seems unlikely to serve as a basis for coherent choices between measurement bases, because there is no reference point with which to assess the options. Similarly, it seems unlikely that a Measurement chapter consistent with the ED would help the IPSASB make consistent measurement decisions when developing new or revised IPSASs.

An example of a key issue dependent on the concept of capital is the treatment of revaluations (or other remeasurements) of assets and liabilities. The treatment of such remeasurements (i.e. whether the remeasurements are recognised in surplus or deficit for the period) reflects a view (implicitly or explicitly) of the nature of an entity's capital. This is on the basis that an entity's surplus or deficit for the period represents the change in the

[1] In relation to the elements of financial statements, this point was made in the AASB's submission (dated 15 May 2013) on the IPSASB Conceptual Framework ED *Elements and Recognition in Financial Statements* (page 7 thereof).

entity's capital (wealth), excluding ownership contributions and ownership distributions, recognised for the period. In its submission (dated 15 May 2013) on the IPSASB Conceptual Framework ED *Elements and Recognition in Financial Statements*, the AASB expressed the view that, if the IPSASB were to regard particular remeasurements of assets and liabilities excluded from surplus or deficit for the period[2] as repricing the same service potential or obligations to sacrifice service potential (instead of representing inflows/outflows or enhancements/diminutions of service potential), it would be logical for the Conceptual Framework to treat those remeasurements as capital maintenance adjustments. In that regard, the AASB noted that the IPSASB ED on Elements and Recognition does not identify 'capital maintenance adjustments' as elements. As mentioned above, the resolution of that issue would depend on the concept of capital (wealth) adopted.

'Financial capacity' and 'operational capacity'

As mentioned above, the AASB supports identifying a measurement objective, broadly along the lines suggested by Mr Ken Warren in his Alternative View on pages 35 – 39 of the IPSASB ED. However, the AASB does not support distinguishing 'financial capacity' and 'operational capacity' as if they are mutually exclusive, which paragraphs AV9 and AV10 of the Alternative View seem to do. Such a distinction would seem to inappropriately imply that a single concept of capital could not be applied to all of an entity's monetary and non-monetary resources (and monetary and non-monetary claims on those resources). This aspect is elaborated below.

Paragraph AV9 of the above-mentioned Alternative View says:

> "Financial capacity is represented by the resources that an entity has available to meet financial claims on the entity, or that can be transformed into operating capacity."; and
>
> "Operating capacity is represented by the resources that an entity has available to deliver services to meet the entity's service performance obligations."[3]

Unlike the descriptions of 'financial capacity' and 'operating capacity' in the IPSASB ED (which focus on different measurement attributes[4]), the notions of 'financial capacity' and 'operational capacity' in the Alternative View (as referred to in paragraph AV7) focus on different types of resources. Regardless of which concept of capital is considered appropriate[5], the AASB considers that a single concept of capital could be applied to an entity's 'financial capacity' and 'operational capacity' as referred to in paragraph AV7 and described in the quotes above from paragraph AV9. For example, the concept of operating capability in the accounting literature encompasses monetary and non-monetary resources,

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2 For example, increases in the carrying amounts of property, plant and equipment or intangible assets upon revaluation that are credited directly to revaluation surplus under paragraph 54 of IPSAS 17 *Property, Plant and Equipment* or paragraph 84 of IPSAS 31 *Intangible Assets.*

3 The AASB presumes that "operational", rather than "operating", was intended in paragraph AV9, for consistency with the measurement objective proposed in paragraph AV7 of the Alternative View.

4 Namely, immediate sale amount (i.e. current cash equivalent) and capacity to provide services in future periods: see paragraphs 2.7 and 2.6, respectively, of the IPSASB ED.

5 The AASB has not reached a conclusion, at this stage, regarding which concept of capital would be most appropriate.

and is wholly a financial concept [for example, non-monetary assets (such as items of property, plant and equipment) cannot be measured at amounts exceeding recoverable amount; and non-monetary liabilities (such as provisions for employee benefits) are measured by reference to the estimated amounts of cash necessary to settle them][6].

Because the notions of 'financial capacity' and 'operational capacity' in the Alternative View focus on different types of resources, the AASB considers that its view that identifying an ideal concept of capital is essential for the Measurement chapter of the IPSASB Conceptual Framework is compatible with supporting Mr Ken Warren's view that a measurement objective along the lines of that in paragraph AV7 should be specified in the Measurement chapter.

IPSASB ED's implicit adoption of particular concept(s) of capital

Despite not acknowledging the need for a concept of capital, and not explicitly identifying any concepts of capital in its discussion, the IPSASB ED includes arguments that imply adoption of particular concept(s) of capital. For example:

(a) paragraph 3.7 says that, in principle, market values fairly reflect the value of an asset to the entity. This is an empty statement unless the meaning of 'value to the entity' is defined. Because an empty statement would not have been intended, an underlying principle is implied;

(b) paragraph 3.26 refers to the usefulness of distinguishing the current cost of consumption from other price changes: this implies a particular concept of capital because it implies some price changes, but not others, are changes in an entity's wealth;

(c) paragraph 3.42 says the value of an asset's service potential is often greater than its replacement cost: this implies a particular notion of the value of an asset's service potential; and

(d) paragraph BC20 refers to an asset's service potential in a way that seems to incorrectly imply a concept of wealth has been articulated.

If some concept (or concepts) of capital are implicit in the mind of the IPSASB, the AASB thinks they should be made explicit.

The AASB's reasons for considering that an essential component of a Conceptual Framework chapter on Measurement is identification of an ideal concept of capital are explained in further detail in the AASB's submission (dated 1 July 2011) on the IPSASB Consultation Paper *Measurement of Assets and Liabilities in Financial Statements*.

Other considerations in choosing a measurement basis or bases

If, despite the AASB's views expressed above, the IPSASB decides on a mixed measurement model in concept, the AASB considers that the IPSASB should identify

6 In this regard, the AASB disagrees with the IASB Conceptual Framework's depiction of operating capability as adopting a physical concept of capital (see paragraph 4.57 of that *Framework*).

criteria for assisting in the appropriate choice of measurement basis in different circumstances. In addition, regardless of whether the IPSASB decides in concept on an ideal measurement model or a mixed measurement model, the AASB considers that the IPSASB should identify either:

(a) the key measurement methods (e.g. discount rates) consistent with applying the identified ideal measurement model; or

(b) criteria for assisting in the appropriate choice of key measurement methods under a mixed measurement model.

The AASB reiterates its comment, made in its submission (dated 8 June 2012) on the IPSASB Conceptual Framework CP *Presentation in General Purpose Financial Reports*, that the objectives of financial reporting need to be supported by identifying key aspects (e.g. stocks and flows) of an entity. In the context of Measurement concepts, identifying these aspects would help provide a focus for making choices between different measurement attributes or bases.

The AASB recommends that decisions about measurement bases should be made in conjunction with making decisions about how information, such as changes in values of assets and liabilities, should be presented in financial reports.

General observations about measurement bases

The AASB considers that the historical cost basis is likely to be less relevant than a current value basis for assets and liabilities when current prices differ materially from historical prices. This is because decisions about allocating scarce resources to a public sector entity (e.g. decisions by resource providers) and assessments of how a public sector entity used its resources and discharged its accountability for the resources provided to it (e.g. decisions by service recipients) are better served by information about the economic circumstances (including prices) prevailing during the reporting period than by information about the economic circumstances (including prices) prevailing in previous reporting periods. It is difficult to conceive of a resource allocation decision or accountability assessment that logically would be based on historical prices (which represent sunk costs) in preference to being based on current values (which reflect the current environment and operations of the reporting entity). The AASB acknowledges the view of some that the historical cost basis is useful for assessing accountability for expenditure of appropriated cash in the manner stipulated in the appropriation. However, the AASB considers that accountability for cash transactions can be assessed by using the statement of cash flows, and therefore should not be a factor in determining the basis for measuring assets and liabilities.

Whether a particular current value is, in concept, the most useful measurement basis for a particular asset or liability also depends on whether it can faithfully represent the financial characteristics of the economic phenomena it purports to represent. For example, if it were concluded that net selling price is generally the most relevant current value measurement basis for assets of a public sector entity, it might be impracticable to determine a faithful representation of the net selling price of particular assets such as defence weapons platforms and historical monuments. In its submission (dated 15 May 2013) on the IPSASB ED *Elements and Recognition in Financial Statements*, the AASB recommended including an explicit recognition criterion of 'faithful representation' in the Conceptual Framework chapter on Recognition and Elements (see page 20 thereof).

Specific Matter for Comment 2

Do you agree with the current value measurement bases for assets that have been identified in Section 3? If not, please indicate which additional measurement bases should be included or which measurement bases should not be included in the Framework.

The AASB generally agrees that the current value measurement bases for assets identified in Section 3 are a reasonably comprehensive range of candidate current value measurement bases on which to base the Measurement chapter. The AASB strongly supports the emphasis placed in Section 3 of the ED on the distinction between entry and exit values, which the AASB considers an important factor in choosing between measurement bases (particularly because entry and exit values generally reflect different concepts of capital). However, it has the following significant concerns regarding that range of measurement bases.

Fair value

The AASB strongly disagrees with the omission of fair value from the current value measurement bases for assets identified in Section 3 of the IPSASB ED, which inappropriately implies fair value is a less important current value measurement basis than those bases identified in Section 3. The AASB recommends addressing that problem by replacing the term 'market value' with 'fair value' as a current value basis discussed in Section 3. This recommendation is explained below.

The AASB observes that 'fair value' and 'market value', as used in the IPSASB's proposed Measurement chapter, both refer to exit and entry prices, albeit with different objectives in mind. This is because:

(a) consistently with the exit price notion of fair value in paragraph 4.5 of the IPSASB ED, fair value is defined in IFRS 13 *Fair Value Measurement* as an exit price; and IFRS 13 includes guidance that one of the valuation techniques for estimating an asset's exit price is its current replacement cost (under the 'cost approach' described in paragraphs B8 – B9 of that Standard)[7]; and

(b) 'market value' is described in paragraph 3.6 of the IPSASB ED as potentially reflecting either an entry or exit price perspective.

[7] In relation to non-financial assets, IFRS 13 (paragraph 32) says: "… a fair value measurement assumes that the market participant [to whom the reporting entity would sell the asset] already holds … complementary assets …". It appears that this assumption explains why, in some circumstances, market buying prices might provide the best evidence of an asset's market selling price (e.g. where sales activity for the asset only occurs for a larger unit of account including other assets used in combination with that asset to generate cash inflows) [see also paragraphs BC77 – BC79 of the IASB's Basis for Conclusions on IFRS 13]. Thus, in contrast with 'market value' (as described in paragraph 3.6 of the IPSASB ED), fair value has only an exit price perspective; but in common with 'market value', fair value would in some cases be determined by reference to entry prices.

Therefore, replacing 'market value' with 'fair value' as a current value basis would help simplify the discussion of current value measurement bases, by removing redundancy and helping avoid potential confusion (the first sentence of paragraph BC24 of the Basis for Conclusions on the IPSASB ED notes the likelihood of confusion resulting from the close similarity between fair value and market value). In view of the widespread use of 'fair value' in IPSASs (and IFRSs, including the extensive guidance on 'fair value' in IFRS 13), the AASB considers that if either 'fair value' or 'market value' were to be omitted from the Measurement chapter, 'fair value' would be the more appropriate term to retain.

For the same reasons, the AASB disagrees with excluding fair value from the measurement bases for liabilities discussed in Section 5 of the IPSASB ED (see the comments below on Specific Matter for Comment 4).

Regarding paragraph 1.10 of the IPSASB ED (as clarified by paragraph BC27 of the Basis for Conclusions on the ED), the AASB disagrees with limiting the role of fair value in the IPSASB Conceptual Framework to when market value is the most appropriate measurement basis and the market for the item is inactive. Fair value is defined and explained in IFRS 13 as a measure that can be applied to active and inactive markets – this seems equally valid in a private sector or public sector context. However, the AASB acknowledges that 'fair value', as defined and explained in IFRS 13, does not seem to reflect a clearly understandable measurement objective or concept of capital (see the next paragraph below for an explanation of this concern). Although this concern might be considered by some to be a reason not to adopt fair value as a measurement concept, it does not seem to be a reason for limiting the scope of the fair value measurement basis, in concept, to particular types of assets or liabilities. In addition, regardless of one's conclusions about this concern, the concern does not seem to warrant excluding fair value from the current value measurement bases considered in Section 3 of the proposed Measurement chapter.

As mentioned in the paragraph immediately above, the AASB acknowledges that 'fair value', as defined and explained in IFRS 13, does not seem to reflect a clearly understandable measurement objective or concept of capital. This is because, although 'fair value' is defined as an exit price, it is explained as being estimated using market selling prices or market buying prices, depending on the circumstances. As acknowledged above, IFRS 13 only uses market buying prices to estimate the fair value of a non-financial asset when they provide the best evidence of the asset's market selling price, using the assumption that the market participant buyer already holds complementary assets. However, market selling prices and market buying prices are fundamentally different in concept and reflect different concepts of capital. By assuming that the market participant buyer already holds complementary assets, the notion of 'fair value' in the guidance in IFRS 13 implicitly focuses on the price at which buyers and sellers meet, and does not address those fundamental conceptual differences (e.g. that when an entity holds highly specialised assets, there might not exist another market participant with complementary assets, in which case 'exit price' determined on the above-mentioned assumption would not faithfully reflect the 'current cash equivalent' concept of capital for the asset). The problem, in concept, with implicitly focusing on the price at which buyers and sellers meet is that preparers of financial statements are in either or both positions for an asset or liability (for example, an entity that buys goods from wholesalers and sells the goods and related services at a profit in a retail market). For them, entry and exit prices are not the same because they are found in different markets and, depending on the measurement basis, transaction costs are either added to or deducted from the market price. Therefore, in concept, it is necessary to choose between market selling prices and market buying prices for assets and liabilities if an ideal measurement model is to provide a basis for achieving the qualities of desirable measurements referred to in the AASB's comments on Specific Matter for Comment 1.

In view of the above-mentioned similarity between the notions of 'fair value' and 'market value', as described in the IPSASB ED, the AASB's concern in the paragraph immediately above applies equally to both notions. Since 'market value' was included in Section 3 of the IPSASB ED, logically the AASB's above-mentioned concern would not be a reason for excluding 'fair value' from Section 3 of the Measurement chapter.

Deprival value

Also in relation to paragraph 1.10 of the IPSASB ED, the AASB disagrees with limiting the use of deprival value to when the appropriate measurement basis is unclear from the objectives and qualitative characteristics. It is unclear to the AASB, on reading paragraphs BC28 – BC30 of the Basis for Conclusions on the IPSASB ED, why this limitation would be warranted. The two main criticisms of deprival value in the Basis for Conclusions seem to be that:

(a) "it would not usually be practicable for an accounting standard simply to require the use of the deprival value model for selection of the appropriate measurement basis" (paragraph BC29); and

(b) "the deprival value model addresses only the relevance of particular measurement bases" (paragraph BC30).

The criticism quoted in paragraph (a) above seems to be essentially a 'straw man' argument. It seems to inappropriately imply that identifying deprival value as a conceptually appropriate measurement model would be tantamount to requiring its use. This implicit argument blurs the distinction between accounting concepts, which are aspirational, and accounting standards, which are mandatory.

The AASB also disagrees with the criticism in paragraph (b) above. The example given in the last sentence of paragraph BC30 strongly implies that, to meet the accountability objective in the IPSASB Conceptual Framework, it would be more appropriate to adopt the historical cost basis, even if another basis is more relevant. The AASB has three main concerns with this argument:

(a) the argument seems to imply that information that is useful for assessing accountability is inherently less relevant than information that is useful for decision making, even though the IPSASB Conceptual Framework treats accountability and decision making as equally important objectives of public sector financial reporting. In view of those identified objectives, the AASB would not support such an implication;

(b) the AASB disagrees with the implication that different information would be useful for accountability and decision making purposes. This is because users assess accountability in order to make economic decisions (including voting and lobbying decisions) and because an entity's management is accountable for its management of resources (including changes in the entity's wealth), not just for the entity's transactions and stewardship of monies provided to it; and

(c) the illogical implication of the argument is that the historical cost basis would be more appropriate than any other measurement bases. Thus, under that argument, all current value measurement bases logically should, like deprival value, be discussed in section 4 of the Measurement chapter (as inferior measurement bases) – the AASB thinks this would be clearly inappropriate.

The AASB notes that each of the possible components of an asset's deprival value, namely, replacement cost, net selling price and value in use, is identified and analysed as a current value measurement basis in Section 3 of the IPSASB ED. The AASB considers it would therefore be logical to also identify and analyse deprival value as a current value measurement basis in Section 3 of the IPSASB ED.

Other noteworthy concerns with Section 3

The AASB also has the following less significant, but noteworthy, concerns regarding Section 3 of the IPSASB ED.

Classification of current value measurement bases as 'observable or unobservable in a market'

Regarding Table 1 and the related discussion of current value measurement bases in Section 3, the AASB considers it unnecessary to classify measurement bases as either 'observable in a market' or 'unobservable in a market'. Whether a measurement under a particular basis is observable is an issue of the evidence supporting the measurement (which is pertinent to the qualitative characteristic of verifiability and perhaps pertinent to determining which disclosures should be made about particular measurements). The AASB considers this issue is much less important than which economic characteristic(s) of the financial statement element the selected measurement basis is intended to represent.

Related to this concern, the AASB considers it is inherently difficult to classify with consistency the measurement bases according to whether the measures are observable or unobservable in a market. For example, for both a market value in an inactive market and for value in use, in some instances observable market inputs might be available – this is not well catered for in Table 1 (and this problem would be difficult to resolve in a summary format).

Replacement cost

The AASB disagrees with the distinction between replacement cost and reproduction cost made in the second sentence of paragraph 3.20 of the IPSASB ED. Ideally, the AASB would prefer that a more comprehensive term (like 'current cost') were used to encompass both replacement cost and reproduction cost. An asset's current cost is the price at which the asset's service potential can most economically be replaced, and thus is calculated as the lower of the cost of replacing that service potential with a modern equivalent asset or reproducing that service potential. Despite its above-mentioned preference, the AASB would support using 'replacement cost', provided that 'replacement cost' is explained as a broad term that encompasses reproduction cost.

In this regard, the AASB observes that the definition of 'replacement cost' in paragraph 3.17 of the ED refers to the most economic cost to replace the asset's service potential, which is consistent with the notion of 'current cost' explained above. Sometimes (for example, in the case of some self-constructed assets), reproduction is the most economic way in which to replace an asset's service potential; and may on occasion be the only feasible way to do so. Therefore, the second sentence of paragraph 3.20 seems to contradict the definition of 'replacement cost' in paragraph 3.17.

Specific Matter for Comment 3

Do you agree with the approaches proposed in Section 4 for application of:

(a) The fair value measurement model to estimate the price at which a transaction to sell an asset would take place in an active, open and orderly market at the measurement date under current market conditions? If not, please give your reasons; and

(b) The deprival value model to select or confirm the use of a current value measurement basis for operational assets? If not, please give your reasons.

(a) Fair value

As mentioned in its comments above on Specific Matter for Comment 2, the AASB disagrees with the comment in paragraph 1.10 of the IPSASB ED (as clarified by paragraph BC27 of the Basis for Conclusions on the ED) that the role of fair value in the IPSASB Conceptual Framework is limited to when market value is the most appropriate measurement basis and the market for the item is inactive. The AASB notes that fair value is defined and explained in IFRS 13 as a measure that can be applied to active and inactive markets – this seems equally valid in a private sector or public sector context.

For a similar reason, the AASB disagrees with indicating in paragraph 4.5 of the IPSASB ED that the objective of the fair value measurement model is to estimate the price at which a transaction to sell an asset would take place in an active, open and orderly market.

The AASB notes that conclusions regarding the relevance of fair value in light of an identified ideal concept of capital would have implications for all assets, not just those sold in an active, open and orderly market. This is because the purposes of identifying an ideal concept of capital include leading to measurements of amounts:

(a) that can meaningfully be added, subtracted and compared; and

(b) the economic significance of which, individually and collectively, is capable of being understood.

(b) Deprival value

As mentioned in its comments above on Specific Matter for Comment 2, the AASB disagrees with the comment in paragraph 1.10 of the IPSASB ED (as clarified by paragraph BC29 of the Basis for Conclusions on the ED) that the role of deprival value in the IPSASB Conceptual Framework is limited to when the appropriate measurement basis is unclear from the objectives and qualitative characteristics.

In addition, the AASB found unclear the comment in the first sentence of paragraph 4.9 of the IPSASB ED that: "The objective of the deprival value model is to select or confirm the use of a current measurement basis." In the context of the second sentence of paragraph BC29 of the Basis for Conclusions on the ED, the AASB construes the above-quoted sentence from paragraph 4.9 as indicating that deprival value provides a 'framework' for selecting when to apply particular current value measurement bases. If that interpretation is correct, it would be logical for deprival value to be included in Section 3 of the Measurement chapter. Otherwise, the Measurement chapter might imply that a mixed current value measurement model would be preferable to applying the 'framework' provided by deprival value.

Specific Matter for Comment 4

Do you agree with the proposed measurement bases for liabilities in Section 5? If not, please indicate which additional measurement bases should be included or which measurement bases should not be included in the Framework.

The AASB generally agrees that the measurement bases for liabilities proposed in Section 5 of the IPSASB ED are a reasonably comprehensive range of candidate measurement bases on which to base the Measurement chapter. The AASB strongly supports the emphasis placed in Section 5 of the ED on the distinction between entry and exit values, which the AASB considers an important factor in choosing between measurement bases (particularly because entry and exit values generally reflect different concepts of capital). However:

(a) for the same reasons indicated in its comments above on Specific Matter for Comment 2 regarding the omission of fair value from the current value measurement bases for assets identified in Section 3, the AASB:

 (i) strongly disagrees with the omission of fair value from the measurement bases for liabilities identified in Section 5; and

 (ii) recommends addressing that problem by replacing 'market value' with 'fair value' as a measurement basis discussed in Section 5; and

(b) the AASB finds the distinction between the 'market value' of a liability (discussed in paragraph 5.6 of the ED) and the 'cost of release' of a liability (discussed in paragraphs 5.7 – 5.11 of the ED) unclear. This is because, in explaining 'cost of release', paragraphs 5.7 and 5.9 refer to prices for transferring liabilities to third parties, which the AASB regards as the same as market value. In this regard, the AASB notes that IFRS 13 (paragraph 24) defines the fair value of a liability as the price that would currently be paid to transfer the liability. Paragraph 34 of IFRS 13 states that the transfer of a liability excludes settlement of the liability with the counterparty or other extinguishment of the liability without fulfilling the obligation. In recommending above that the term 'market value' for liabilities is replaced with 'fair value', the AASB assumes that, similarly to IFRS 13, the IPSASB Measurement chapter clearly distinguishes the 'fair value' and 'cost of release' of a liability.