AASB Exposure Draft **ED 262**

May 2015

Fair Value Disclosures of Not-for-Profit Public Sector Entities

Adverse Comments to the AASB by 4 June 2015

Australian Government

Australian Accounting Standards Board

Commenting on this AASB Exposure Draft

The AASB invites comments from constituents who hold a different view to those set out in this Exposure Draft by 4 June 2015.

Comments should be addressed to:

The Chair
Australian Accounting Standards Board
PO Box 204
Collins Street West   Victoria   8007
AUSTRALIA
E-mail: standard@aasb.gov.au

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

While comments may be lodged by email or by post, email lodgement is preferred. To enable the submissions to be accessible to all users of the website, including those with disabilities, please submit comments via email in an accessible Word format. An additional accessible and unsecured PDF version may also be submitted.

Enquiries

Phone: (03) 9617 7600
E-mail: standard@aasb.gov.au

ISSN 1030-5882

EXPOSURE DRAFT ED 262

FAIR VALUE DISCLOSURES OF NOT-FOR-PROFIT PUBLIC SECTOR ENTITIES

Introduction

This Exposure Draft proposes amending AASB 13 *Fair Value Measurement* to exempt not-for-profit public sector entities from certain requirements of the Standard.

These amendments arise from the AASB's short-term review of the disclosure requirements in AASB 13 applying to property, plant and equipment measured at fair value and categorised within Level 3 of the fair value hierarchy. Following that review, the AASB decided to propose interim relief for not-for-profit public sector entities from making certain specified disclosures about the fair value measurement of assets within the scope of AASB 116 *Property, Plant and Equipment* which are primarily held for their current service potential rather than to generate future net cash inflows. The relief is temporary pending the outcome of related current Board projects, including the review of the Reduced Disclosure Regime (Tier 2), Australian Reporting Framework, and Conceptual Framework.

Australian Accounting Standards

AASB 1053 *Application of Tiers of Australian Accounting Standards* establishes a differential reporting framework consisting of two tiers of reporting requirements for preparing general purpose financial statements:

(a) Tier 1: Australian Accounting Standards; and

(b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.

Tier 2 requirements comprise the recognition and measurement requirements of Tier 1 but substantially reduced disclosure requirements in comparison with Tier 1.

This Exposure Draft does not propose any amendments to existing Tier 2 requirements specified in AASB 13.

Exposure Drafts

The publication of an Exposure Draft is part of the due process that the AASB follows before making a new Australian Accounting Standard or amending an existing one. Exposure Drafts are designed to seek public comment on the AASB's proposals for new Australian Accounting Standards or amendments to existing Standards.

Proposals of this Exposure Draft

This Exposure Draft proposes inserting the following paragraph into AASB 13:

Aus93.1 Notwithstanding paragraph 93, in respect of not-for-profit public sector entities, for assets within the scope of AASB 116 *Property, Plant and Equipment* for which the future economic benefits are not primarily dependent on the asset's ability to generate net cash inflows, the following requirements do not apply:

(a) in paragraph 93(d) of AASB 13, the text "For fair value measurements categorised within Level 3 of the fair value hierarchy, an entity shall provide quantitative information about the significant unobservable inputs used in the fair value measurement. An entity is not required to create quantitative information to comply with this disclosure requirement if quantitative unobservable inputs are not developed by the entity when measuring fair value (eg when an entity uses prices from prior transactions or third-party pricing information without adjustment). However, when providing this disclosure an entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the entity.";

(b) paragraph 93(f); and

(c) paragraph 93(h)(i).

Main Features of this Exposure Draft

This Exposure Draft proposes relieving not-for-profit public sector entities from the following disclosures for assets within the scope of AASB 116 that are held primarily for their current service potential rather than to generate future net cash inflows:

(a) for recurring and non-recurring fair value measurements categorised within Level 3 of the fair value hierarchy, quantitative information about the significant unobservable inputs used in the fair value measurement;

(b) for recurring fair value measurements categorised within Level 3 of the fair value hierarchy, the amount of the total gains and losses for the period included in profit or loss that is attributable to the change in unrealised gains or losses relating to the assets held at the end of the reporting period, and the line item(s) in profit or loss in which those unrealised gains or losses are recognised; and

(c) for recurring fair value measurements categorised within Level 3 of the fair value hierarchy, a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs if a change in those inputs to a different amount might result in a significantly higher or lower fair value measurement. Where there are interrelationships between those inputs and other unobservable inputs used in the fair value measurement, the disclosure of a description of those interrelationships and of how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement will also not be required.

Application Date

It is proposed that the amendments be applicable to annual reporting periods beginning on or after 1 July 2016 with early adoption permitted for annual reporting periods beginning on or after 1 January 2005. No specific transitional provisions are proposed.

Request for Comments

Adverse comments are invited on any of the proposals in this Exposure Draft by 4 June 2015. If you disagree with the AASB's proposals, please supplement your submission with detailed comments on the major issues.

BASIS FOR CONCLUSIONS

Background

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's considerations in reaching the conclusions in the Exposure Draft. Individual Board members gave greater weight to some factors than to others.

BC2 AASB 13 *Fair Value Measurement* applies to annual reporting periods beginning on or after 1 January 2013. In 2014, the Board received feedback about AASB 13 from not-for-profit public sector entities following their implementation of the Standard, including feedback about some of the specified disclosures. These constituents were concerned that the costs of presenting the disclosures specified by the Standard, including the disclosure overload to users of not-for-profit public sector general purpose financial statements, exceeded their benefits. The Board noted that it had considered similar issues in 2011 when making AASB 13, and had decided that no amendment to AASB 13 was necessary. However, following the feedback received, the Board decided, as a narrow scope project, to revisit whether some disclosure relief should be made available to not-for-profit public sector entities.

BC3 The Board undertook targeted outreach in late 2014 to further understand which disclosures were of concern to not-for-profit public sector entities, in particular, local governments, and the reasons for their concern. The Board's outreach activity included feedback from government entities, valuation experts and auditors.

BC4 The Board decided to limit its consideration of disclosure relief to:

(a) assets within the scope of AASB 116 *Property, Plant and Equipment* that are primarily held for their current service potential (for example, roads and water supply infrastructure) rather than to generate future net cash inflows; and

(b) disclosures in AASB 13 that apply solely to fair value measurements categorised within Level 3 in the fair value hierarchy. These disclosures help meet the objective noted in paragraph 91(b) of the Standard of providing users with information as to how fair value measurements using significant unobservable inputs affected profit or loss or other comprehensive income for the period, by requiring disclosure of information about the relative subjectivity of the fair value measurement.

BC5 The Board concluded that the feedback received did not suggest that a wider project scope was necessary to address matters raised (see also paragraphs BC6, BC17 and BC18). In April 2015, the Board evaluated these disclosures against its *Process for Modifying IFRSs for PBE/NFP* (‘*Process*’). The *Process* allows for departures from the requirements of the equivalent International Financial Reporting Standard where not-for-profit specific reasons for the departure exist. The Board concluded that, for the interim, in relation to these assets, it is appropriate to depart from its policy of transaction neutrality for cost-benefit reasons in relation to certain disclosures specified by the Standard.

BC6 The Board decided to propose amendments to AASB 13 to relieve not-for-profit public sector entities from disclosing, for assets within the scope of AASB 116 that are primarily held for their current service potential rather than to generate future net cash inflows:

(a) quantitative information about the significant unobservable inputs in fair value measurements categorised as Level 3 in the fair value hierarchy;

(b) the amount of the total gains and losses for the period included in profit or loss that is attributable to the change in unrealised gains or losses relating to assets held at the end of the reporting period, and the line item(s) in profit or loss in which those unrealised gains or losses are recognised; and

(c) information about the sensitivity of certain fair value measurements to changes in unobservable inputs.

The Board intends to revisit the relief pending the outcome of related current Board projects, including its projects on the review of the Reduced Disclosure Regime (Tier 2), Australian Reporting Framework, and Conceptual Framework, to assess the extent to which outcomes from those projects address the factors that led to the Board’s decisions noted above.

Significant Issues

Property, Plant and Equipment Held by Not-for-Profit Public Sector Entities

BC7 The Board discussed the prevailing practice in the Australian not-for-profit public sector of revaluing property, plant and equipment subsequent to initial measurement and recognition. It noted that assets such as road infrastructure and national parks were typically only held by public sector entities, but did not consider the nature of such assets in itself to be a sufficient sector specific differentiator, as assets held by private sector entities may similarly vary significantly across entities operating in different industries.

BC8 The Board noted that property, plant and equipment is primarily held for the purposes of delivering the not-for-profit entity's public service objectives rather than being held to generate net cash inflows. The Board observed that although private sector entities may similarly hold assets other than for the purpose of generating net cash inflows, the information needs of users of not-for-profit public sector general purpose financial statements about assets held for their current service potential were likely to be different from such assets held by the private sector.

BC9 The Board considered the extent and variety of long-lived assets measured on the fair value basis in the public sector and noted the resultant impact on the number of classes of assets determined for the purposes of satisfying the disclosure requirements of AASB 13. The Board observed that in many instances the valuation technique applied to these assets used unobservable inputs (Level 3 inputs) and that the assets were predominantly categorised within Level 3 in the fair value hierarchy for the purposes of making the disclosures specified by AASB 13.

Balance of Costs and Benefits

BC10 The Board concluded that it is appropriate to depart from its policy of transaction neutrality for assets within the scope of AASB 116 that are primarily held for their current service potential rather than to generate future net cash inflows for cost-benefit reasons. This conclusion takes into account the extent and variety of long-lived assets held by public sector entities measured on the fair value basis and categorised within Level 3 in the fair value hierarchy.

BC11 As part of its considerations, the Board had regard to the benefits of the disclosures recognised by the International Accounting Standards Board (IASB) in its Basis for Conclusions to IFRS 13 *Fair Value Measurement*. The Board considered that the costs of requiring not-for-profit public sector entities to disclose quantitative information about the significant unobservable inputs in fair value measurements categorised within Level 3 in the fair value hierarchy, and the narrative description of the sensitivity of certain fair value measurements to changes in unobservable inputs, would generally be greater than they are for private sector entities. At the same time, the benefits would not be as great having regard to the number of specialised assets leading to a wide range of inputs within each class of assets for which disclosure is made and the information needs of users for such assets. The Board similarly considered the costs of making the disclosure specified by paragraph 93(f) of AASB 13 to exceed the benefits to users of the disclosure, having regard to the relative usefulness of the additional information to users of not-for-profit public sector general purpose financial statements.

BC12 As part of its consideration of the costs versus the benefits of presenting the disclosures proposed for relief, the Board observed that many not-for-profit public sector entities had only recently applied AASB 13. The Board discussed whether the concerns raised were reflective of underlying costs associated with implementing the Standard in a not-for-profit public sector environment, or whether the costs were largely transitional in nature. For example, the Board noted that the requirement to disclose a narrative description of the sensitivity of certain fair value measurements to unobservable inputs did not appear to be well understood in practice despite an example of the disclosure being included in the Illustrative Examples accompanying IFRS 13.

BC13 The Board also observed that IFRS 13 has not yet been incorporated into International Public Sector Accounting Standards (IPSASs) as issued by the International Public Sector Accounting Standards Board (IPSASB) of the International Federation of Accountants. Accordingly, for not-for-profit public sector entities, the extent of the disclosures specified by Australian Accounting Standards of the fair value measurements of property, plant and equipment held primarily for their current service potential presently exceeds those specified under IPSASs. The Board noted that future decisions of the IPSASB on public sector measurement and the accounting for heritage and infrastructure assets may prompt a need to revisit its present decisions on the costs versus benefits of the proposed relief provided (see also paragraph BC6).

BC14 The Board decided that it was not necessary to propose relief from disclosing the reconciliation of movements in each class of assets measured at fair value and categorised within Level 3 in the fair value hierarchy required by paragraph 93(e) of AASB 13 or the valuation processes used by the entity required by paragraph 93(g). The Board decided that these disclosures provided useful information without imposing significant additional ongoing costs. In particular, the Board considered that the information required to prepare the necessary reconciliations was likely in many cases to be available in the underlying accounting records.

BC15 The Board noted that entities would continue to be required to disclose a description of the inputs used in the fair value measurement in accordance with paragraph 93(d) of AASB 13. The Board expects, in most instances, that this disclosure together with other disclosures specified in AASB 13 and other Australian Accounting Standards (for example, AASB 101 *Presentation of Financial Statements* and AASB 116), would provide users of not-for-profit public sector general purpose financial statements with sufficient information about fair value measurements for decision-making purposes. The Board observed that its proposed relief does not override the general disclosure objective of AASB 13 described in paragraph 91 of that Standard.

BC16 The Board observed that the relief proposed does not prevent a not-for-profit public sector entity from presenting some, or all, of the disclosures specified in paragraphs 93(d), 93(f) and 93(h)(i) in its general purpose financial statements.

Other Issues

Extension of Relief to Other Assets Held by Not-for-Profit Public Sector Entities

BC17 The Board discussed whether the proposed relief from disclosure should be extended to include investment properties within the scope of AASB 140 *Investment Property* or financial assets held by not-for-profit public sector entities that are measured at fair value and categorised within Level 3 of the fair value hierarchy. The Board decided not to extend the relief to such assets as it did not regard there to be differences in the purposes these assets are held, whether held by a for-profit private sector entity or not-for-profit public sector entity. Further, the Board considered that, for such assets, the costs of providing the disclosures did not outweigh the benefits from making those disclosures in general purpose financial statements. The Board noted that, unlike property, plant and equipment, there was not necessarily a significant difference between the sectors with regards to the extent to which fair value measurement is applied to these assets.

BC18 The Board also discussed whether the proposed relief from disclosure should be extended to include other assets (besides financial assets and investment properties) held by not-for-profit public sector entities that are measured at fair value. The Board noted that it had decided to keep the scope of its project narrow, and observed the role of materiality when considering whether specified disclosures should be included in the general purpose financial statements.

Application Date and Transitional Provisions

BC19 The Board considered the application date of the proposed amendments to AASB 13. The Board decided to propose that the amendments apply to annual reporting periods beginning on or after 1 July 2016, and to permit early adoption of the amendments when finalised. The Board noted that early adoption would allow not-for-profit public sector entities to immediately access the proposed relief.

BC20 The Board decided that no specific transitional provisions were necessary as the amendments relate to providing relief from disclosure. Accordingly, the requirements of AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* apply to the amendments.