



30 June 2022

Dr Keith Kendall
Chair
Australian Accounting Standards Board
PO Box 204
Collins St West Victoria 8007
AUSTRALIA

Dear Dr Kendall

AASB Exposure Draft ED 320 *Fair Value Measurement of Non-Financial Assets of Not-for-Profit Public Sector Entities*

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to comment on AASB Exposure Draft ED 320 *Fair Value Measurement of Non-Financial Assets of Not-for-Profit Public Sector Entities*. The views expressed in this submission represent those of all Australian members of ACAG.

ACAG supports the Board's efforts to provide additional guidance to help public sector entities more consistently apply the principles in AASB 13 in relation to determining the fair value measurement of non-financial assets not held primarily for their ability to generate net cash inflows.

ACAG has some concerns that the draft implementation guidance may lead to divergent practices and other fair value measurement challenges. In particular, ACAG believes that the application guidance related to highest and best use and the current replacement cost approach can be further clarified to reduce these risks. More detail on these concerns is raised in our response to SMCs 5, 6 and 13.

ACAG has also included other suggestions and recommendations that we believe will help promote greater consistency and comparability of application across the public sector.

The attachment to this letter addresses the AASB's specific matters for comment outlined in the ED.

ACAG appreciates the opportunity to comment and trusts you find the attached comments useful.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Margaret Crawford', is written over a thin horizontal line.

Margaret Crawford
Chair
ACAG Financial Reporting and Accounting Committee

AASB Specific Matters for Comment

Scope

SMC 1

Do you consider that the proposed authoritative implementation guidance should be applicable also to NFP entities in the private sector? Please provide reasons to support your view.

ACAG is not commenting on the applicability of this guidance to the NFP private sector.

SMC 2

Do you agree with the AASB's conclusion that determining appropriate measurement techniques for measuring the fair value of land and improvements on land subject to public-sector-specific legal restrictions is best regarded as relating to detailed valuation assessments and should not be mandated in Australian Accounting Standards (see paragraphs BC164–BC170)? Please provide reasons to support your view.

ACAG agrees with the AASB's conclusion not to mandate a specific measurement technique for measuring the fair value of land and improvements on land subject to public sector legal restrictions.

Specifying a specific measurement technique for measuring land and improvements on land subject to public sector legal restrictions appears to conflict (from a standard-setting perspective) with:

- paragraph 61 of AASB 13 which requires an entity to select measurement techniques that:
 - are appropriate in the circumstances
 - for which sufficient data is available to measure fair value and
 - maximise the use of relevant observable inputs and minimise the use of unobservable inputs
- a principles based standard.

ACAG acknowledges paragraphs BC149 and BC 170 of the ED which state that if a Treasury or Finance Department (or other authority) and/or the Office of Local Government in a jurisdiction desires greater consistency in the valuation approach(es) used to measure the fair value of particular types or classes of non-financial assets in a jurisdiction, it may choose to designate a valuation approach for application to those assets held by public sector entities in its jurisdiction.

ACAG also notes that paragraph BC 166 of the ED states that:

'Despite the debate regarding fair value measurement of land subject to public-sector-specific legal restrictions, feedback from most stakeholders in targeted outreach and most feedback on ITC 45 indicated that, in practice, the fair value of each type or class of assets affected by this issue is being measured using a largely consistent approach – that is:

(a) for land subject to public-sector-specific legal restrictions, the market approach is used (although, as noted in paragraph BC168 below, at a more detailed level, different methods are being used to calculate the adjustments to reflect restrictions); and'

ACAG supports the above paragraph and believes that public-sector-specific restrictions (whether legal or implied socio-political restrictions) should be considered when valuing land by using the market approach with an adjustment to reflect the restrictions. In our view, this is consistent with the draft ED 320 because:

- Paragraph F9 states that an asset's current use is presumed to be its highest and best use unless this presumption is rebutted by management committing to a plan to sell or change the asset's use. Applying the requirements of paragraph F9 means the highest and best use of, for example, community parkland is its current use as a park (assuming this presumption cannot be rebutted) and therefore the valuation of the land should be based on its current use as a park, rather than by reference to surrounding land that may be used for residential, commercial or other uses. This is irrespective of whether or not there are legal restrictions on the use of the land as a park.

- BC62 states that the fair value of an asset would take into account the effect of restrictions that would transfer to market participants in a hypothetical sale transaction. Paragraph 140.5 of International Value Standards 104 *Bases of Value* states that '*to reflect the requirement to be legally permissible, any legal restrictions on the use of the asset, e.g., town planning/zoning designations, need to be taken into account as well as the likelihood that these restrictions will change*'. In the public sector, entities such as councils may not be able to remove zoning restrictions. For example, in NSW, community land cannot be sold by a local council unless it is converted to operational land. In most cases, councils do not have the sole ability to change the status of this land without a comprehensive planning process that requires the approval of third parties.
- Paragraph F4(b) of the draft ED states 'if the market selling price of an identical asset is not directly observable, the entity explicitly estimates the pricing assumptions that market participants would use by maximising the use of relevant observable inputs and minimising the use of unobservable inputs.' A market approach maximises the use of observable inputs and will usually be available even where there is no equivalent parcel of land with the same public-sector-specific restrictions in the marketplace. For example, while there may not be an equivalent parcel of land with the same zoning restrictions in the marketplace as a park being valued, there are other parcels of land that have market prices that provide a suitable reference point.

Two jurisdictions' additional view on valuations for GFS purposes

While two jurisdictions supported the proposals in ED 320, they would like the AASB to explore the notion of 'entry price' further and consider providing an optional relief from the requirements of paragraph 24 of AASB 13.

This is because under the ED proposals, which provide relief from current processes, entities will still need to go through a process of determining whether the revised relief applies, determining whether market observable inputs are available, and to document their findings.

These jurisdictions believe that an exemption would result in a more cost-efficient valuation and a fair value that reflects the non-financial benefits of providing needed services to beneficiaries that are not captured in a market-based exit price (which for assets like roads and land under roads can be a decrement to entry price approaching 100%).

Apart from land which is valued as per market approach with discounts in some jurisdictions, given many public sector infrastructure assets are valued at current replacement cost, the introduction of the entry price notion, or providing an exemption from paragraph 24 of AASB 13, will likely result in the same outcome, however, this would be subject to further research and impact analysis by the AASB. The jurisdictions believe that this valuation would still provide consistency with the International Monetary Fund Government Financial Statistics Manual 2014 (IMF GFSM) and the Australian Government Financial Statistics Manual (AGFSM) which governments are expected to follow when preparing their general government sector and whole of government sector financial statements. The IMF GFSM (paragraphs 7.20 – 7.31) and AGFSM (paragraphs 8.26 – 8.29, 8.34 – 8.39) regard the market value of assets as an entry price. Such an exemption would then provide clarity on the appropriate valuation technique to select for each asset class, including land.

Market participant assumptions

SMC 3	
In respect of the assumptions used in measuring the fair value of a non-financial asset of an NFP public sector entity not held primarily for its ability to generate net cash inflows, do you agree with the proposals in paragraphs F4–F7 that:	
(a)	if the market selling price of an identical asset is directly observable, that price (which incorporates implicitly the assumptions that other market participants would use when pricing the asset, negating the need to identify those assumptions) should be used to estimate the fair value of the asset; and
(b)	if the market selling price of an identical asset is not directly observable, the entity would need to explicitly estimate the pricing assumptions that other market participants would use.

In this case, to maximise the use of relevant observable inputs and minimise the use of unobservable inputs:

- (i) if all relevant information about other market participant assumptions needed to estimate the fair value of the asset is reasonably available, the entity should use those assumptions in measuring the fair value of the asset; or
- (ii) if not all relevant information about other market participant assumptions needed to estimate the fair value of the asset is reasonably available, the entity would need to develop unobservable inputs in measuring the fair value of the asset. When applying paragraph 89 to develop unobservable inputs, the entity should use its own assumptions as a starting point and make adjustments to those assumptions if reasonably available information indicates that other market participants would use different data; or
- (iii) if no relevant information about other market participant assumptions is reasonably available, the entity should use its own assumptions in measuring the fair value of the asset?

Please provide reasons to support your view.

ACAG agrees with the proposals in paragraphs F4-F7 as they are consistent with the requirements in paragraphs 61 and 89 of AASB 13.

One jurisdiction, while supporting the proposals (re-emphasis of paragraphs 22, 23, 61, 67 and 89 in F4 to F7), suggests including additional guidance as follows:

- the emphasis of using the entity's own data in the absence of other available data is highly relevant to the cost approach as entities have internal data about construction costs, the condition of their assets etc. This emphasis will provide little assistance for the market approach as entities do not usually have internal data about recent sales that is not also externally available. This jurisdiction therefore recommends that the implementation guidance include a further paragraph to the effect that the cost approach should be used when data that is relevant, reliable and current for the market approach is unavailable both externally and internally (and when the income approach is not appropriate because the asset is not held to generate net cash inflows)
- expanding paragraph F5(a), to state that a market participant is not readily identifiable when the entity is a monopoly service provider, on a not-for-profit basis, in their geographical area. This will avoid discussions on whether divergent assumptions made in other local governments/States are relevant.

SMC 4

Paragraph F8 provides examples of assets for which:

- (a) market selling prices of an identical or a comparable asset are unlikely to be directly observable; and
- (b) no relevant information about different assumptions of other market participants is likely to be reasonably available.

Do you agree with the examples in paragraph F8? Please provide reasons to support your view.

ACAG agrees with the examples in paragraph F8 as market selling prices of an identical or a comparable asset are unlikely to be directly observable as they are either highly specialised assets or infrequently traded. However, defense weapons platforms are a mixture, as some off-the-shelf products are actively traded and have observable inputs whereas other assets (e.g. Collins Class submarines) are highly bespoke and so customized that it is difficult to identify any comparable traded assets.

ACAG believes that purpose-built hospitals and schools should also be included as examples, as these are commonly valued on a current replacement cost basis to construct the asset, and not based on market trading activity.

Highest and best use**SMC 5**

Do you agree with the proposal in paragraphs F9–F11 that, for a non-financial asset of an NFP public sector entity not held primarily for its ability to generate net cash inflows, the presumption in AASB 13 paragraph 29 that the asset's current use is its highest and best use should be rebutted when, and only when, the appropriate level of the entity's management is committed at the measurement date to a plan to sell the asset or to use the asset for an alternative purpose? Please provide reasons to support your view.

ACAG agrees with the proposals in paragraphs F9-F11 that for a non-financial asset of a NFP public sector entity not held primarily for its ability to generate net cash inflows, the presumption in AASB 13, paragraph 29 that the asset's current use is its highest and best use should be rebutted when, and only when, the appropriate level of the entity's management is committed at the measurement date to a plan to sell the asset or to use the asset for an alternative purpose. However, ACAG believes that in order for management to be committed to sell or use the asset for an alternative purpose, management should already have made the decision to do so i.e. for management to be committed to a plan to sell the asset or use an asset for an alternative purpose the sale or change in use needs to have been approved by the appropriate level of management. This will help reduce the judgement involved and likely disagreements between entities and auditors on whether or not the appropriate level of management has 'committed to a plan to sell the asset or use the asset for an alternative purpose'.

For the purpose of valuing an asset, ACAG believes that the considerations of physically possible, legally permissible and financially feasible need to be assessed as part of the decision/approval made by the appropriate level of management to sell or change the asset's existing use. ACAG therefore recommends the Board amends F9 to reflect that management's decision/approval at the measurement date to a plan to sell the asset or to use the asset for an alternative purpose needs to have considered what is physically possible, legally permissible or financially feasible. This is to avoid situations where management may be committed to a course of action, despite there being physical, legal or financial barriers existing that may prevent its success.

While ACAG supports the proposals that the current use of an asset is its highest and best use unless rebutted, we note that AASB 5 'Non-current Assets Held for Sale and Discontinued Operations' is a specific standard that has requirements for assets held for sale and adding a separate, but similar requirement in AASB 13 to rebut the highest and best use assumption may lead to possible confusion. Paragraph 8 of AASB 5 also refers to a commitment by management 'for a sale to be highly probable, the appropriate level of management must be committed to a plan to sell an asset.....'. We therefore recommend that the AASB clarifies and provides more guidance on whether there is any difference between a management commitment under the proposals and a management commitment under AASB 5.

Another ACAG jurisdiction also recommended that the AASB clarify that disclosures under paragraph 93(i) of AASB 13 when the current use is not highest and best use, apply the provisions of paragraph F9, to avoid negating the benefits provided by the relief by having to identify hypothetical situations of alternate highest and best use.

SMC 6

Do you agree with the example in paragraph F10 of steps that might, in some circumstances of a particular entity, need to be completed before the appropriate level of the entity's management is committed at the measurement date to a plan to sell the asset or use the asset for an alternative purpose, namely:

- (a) relevant field studies or a Ministerial briefing on whether there is a market for the asset (and, if so, its likely price) or for the alternative services that the asset could be used to provide;
- (b) initial due diligence processes to determine that a sale of the asset or an alternative use of the asset is possible within the current socio-economic environment and would maximise the asset's value; and

(c) development of project milestones and expected timelines to complete the sale or the plan to use the asset for the alternative purpose?

Please provide reasons to support your view.

While these factors appear to be relevant, ACAG believes that paragraph F10 could lead entities to assume meeting the list of activities in F10 might be considered sufficient to meet the criteria of management being committed to a plan to sell or change the purpose of an asset. ACAG believes the following clarifications would help to remove any ambiguity:

- clarify that the steps taken are examples of actions that may be required to confirm that there are no significant physical, legal or financial barriers to sell or change the asset's existing use prior to obtaining approval to sell or redeploy the asset (this links to our response in SMC 5)
- make explicit that in order for management to be committed to sell or use the asset for an alternative purpose the appropriate level of management should already have made the decision to do so. It is important that there is accountability at the transaction level upon the sale or intended sale of any public sector asset
- clarify whether it is one or all steps that need to be completed e.g. could be worded as 'The following one or more steps might....'

ACAG also notes that in a public sector context, a ministerial briefing may not be an approval, and depending on the subject asset, there may need to be ministerial approval, approval by Cabinet or a Cabinet committee or subject to another process.

ACAG believes the example in paragraph BC 51 where an appropriate level of an entity's management 'commits' to begin using an asset (such as equipment) for a commercial purpose (e.g. by leasing out that equipment) while awaiting approval of the asset's sale could be clarified further by including detail that the asset's valuation basis would likely become that alternative use, unless rebutted, as this is now its 'current use'.

SMC 7

Do you agree with the proposal in paragraph F12 that an entity is only required to assess whether a use of the asset is physically possible, legally permissible and financially feasible in accordance with paragraph 28 when (per paragraph F9) the presumption in AASB 13 paragraph 29 that the asset's current use is its highest and best use is rebutted? Please provide reasons to support your view.

While ACAG agrees with the proposal in paragraph F12 for the purpose of valuation of the subject asset, we believe that the considerations of physically possible, legally permissible and financially feasible need to be assessed as part of the decision/approval made by the appropriate level of management to sell or change the asset's current use. Refer to SMC 5 and 6 for further details.

SMC 8

Do you agree with the draft implementation guidance in paragraph F13 for applying the 'financially feasible use' concept described in AASB 13 paragraph 28(c), namely that, for a non-financial asset of an NFP public sector entity not held primarily for its ability to generate net cash inflows, a use is financially feasible if market participants (including NFP public sector entities) would be willing to invest in the asset's service capacity, considering both the asset's ability to be used to provide needed goods or services to beneficiaries and the resulting cost of those goods or services? Please provide reasons to support your view.

ACAG agrees with the draft implementation guidance in paragraph F13 for applying the 'financially feasible use'. This guidance is consistent with how financially feasible is assessed in the public sector and paragraph Aus49.1 of the *Framework for Financial Reporting* which states that 'future economic benefits is synonymous with the notion of service potential'.

Application of the cost approach

SMC 9

Do you agree with the proposal in paragraph F14(a) that the entity should assume the asset will be replaced in its existing location, even if it would be feasible to replace the asset in a cheaper location? Please provide reasons to support your view.

ACAG agrees that an entity should assume the asset will be replaced in its existing location. Generally, there will be reasons precluding the move to another location such as a social policy decision/legal restriction/operational requirements etc. that require the asset to be located in its existing location.

If market participants would relocate the asset (i.e. if the entity itself plans to relocate, given that the entity's own plans are the best evidence of market participant assumptions), then ACAG believes that it would be beneficial if the guidance clarifies that the:

- estimated remaining useful life/service potential of the improvements should reflect this plan, which in turn impacts the measurement of accumulated depreciation/obsolescence in a cost approach valuation
- valuation of the land may require an adjustment to reflect the costs required by the purchaser to remove structures after the service is relocated and land sold (if market approach is used).

ACAG also notes that as currently written, paragraph BC80 may give the impression that a public school or public hospital (including the land component) need be valued using the cost approach. We believe this paragraph should be clarified to state that if the land component is valued using the market approach while the improvements thereon are valued using the cost approach, the location issue for the land does not arise as the market approach always values the subject asset, i.e. the land, at its existing location.

SMC 10

Do you agree with the proposal in paragraph F14(b) that the entity should assume that the asset subject to measurement (the subject asset) presently does not exist; and therefore, all necessary costs intrinsically linked to acquiring or constructing the subject asset at the measurement date should be included in the asset's current replacement cost? Please provide reasons to support your view.

In principle, ACAG agrees with the proposal in paragraph F14(b) that the entity should assume that the asset subject to measurement (the subject asset) presently does not exist; and therefore, all necessary costs intrinsically linked to acquiring or constructing the subject asset at the measurement date should be included in the asset's current replacement cost for the reasons outlined in paragraphs BC95 and BC96. However, we are unclear how paragraph F14(b) interacts with paragraph F15(b). Refer to our comments in SMC 13.

ACAG notes that paragraph F15(c) directly contradicts the principle in F14(b) to assume that the asset presently does not exist. Therefore, paragraph F14(b) and/or F15(c) need to be changed to achieve consistency.

The proposal that the subject asset does not exist may provide practical challenges when a part, rather than the whole asset is replaced, particularly in relation to the costs to include. In the public sector it is common for parts of an asset to be replaced rather than the whole asset. This may occur multiple times over the life of the whole asset. For example, a local government may replace the road surface, but to do so will incur significant costs removing and disposing of the original surface. It is not clear to what extent these costs should be included and their impact on the value of the whole asset? ACAG suggests adding additional guidance in this area.

SMC 11

Do you agree with the proposal in paragraphs F14(b) and F14(c) that, when estimating the current replacement cost of the subject asset, the entity should estimate the replacement cost of a reference asset (ie a modern equivalent asset or a replica asset) as input and adjust the estimated

replacement cost of a reference asset for any differences between the current service capacity of the reference asset and the subject asset? Please provide reasons to support your view.

ACAG agrees with the proposals in paragraphs F14(b) and F14(c) as it is consistent with the requirements in paragraph B8-B9 and paragraph 70.6 of International Valuation Standard (IVS) 105 *Valuation Approaches and Methods*.

We note that a replica may be appropriate in the public sector for certain heritage, cultural or collection assets if market participants would require a direct replica rather than a modern equivalent.

ACAG notes that the paragraphs are very brief in providing guidance for how to measure obsolescence. We recommend the inclusion of additional paragraphs for how to measure each form of obsolescence, having regard to the guidance provided by IVS 105.80.

SMC 12

Do you agree with the proposal in paragraph F15(a) that once-only costs that would be expected to be necessarily incurred in a hypothetical acquisition or construction of the subject asset should be included in that asset's current replacement cost? Please provide reasons to support your view.

ACAG conceptually agrees with the proposal in paragraph F15(a) that once-only costs that would be expected to be necessarily incurred in a hypothetical acquisition or construction of the subject asset should be included in that asset's current replacement cost as, if an asset was to be acquired or constructed, these once-only costs at the measurement date would need to be included. However, while some entities may have actually incurred the once-only costs and therefore would have the relevant information, other entities may have inherited the land and infrastructure asset (e.g. from another public sector entity or a private sector developer) and therefore may not have the relevant information and would have to apply judgement and incur additional costs to estimate these hypothetical costs.

SMC 13

Do you agree with the proposal in paragraph F15(b) that, when estimating the current replacement cost of the subject asset, an entity should determine, based on the circumstances of the subject asset, whether the following costs would (among other costs) need to be incurred upon the hypothetical acquisition or construction of that asset at the measurement date:

- (a) unavoidable costs of removal and disposal of unwanted existing structures on land; and
- (b) any disruption costs that would hypothetically be incurred, when acquiring or constructing the subject asset at the measurement date, including costs of restoring an asset not controlled by the consolidated group (if any) to which the entity belongs?

Please provide reasons to support your view.

ACAG has concerns that, as currently drafted, the current guidance in paragraphs F15(b)(i) and paragraphs BC 99 – BC106 will lead to inconsistent practices being adopted across the public sector and implementation challenges.

Interaction between paragraphs F14(a), F14(b) and F15(b)(i) and determining unavoidable costs of removal and disposal of unwanted existing structures on land

Paragraph F15(b)(i) refers to the cost of removal and disposal of unwanted structures on land that would hypothetically need to be purchased to construct the asset when there are no vacant sites in the surrounding area and not the cost of removing and disposing of the asset being valued (for the purpose of replacement). The latter is discussed in BC104-BC106.

ACAG's concerns include:

- While some entities may have actually incurred the costs of removal and disposal of unwanted structures and therefore would have the relevant information, other entities may have inherited the land and infrastructure asset (e.g. from another public sector entity or a private sector developer) and therefore may not have the relevant information and would have to apply judgement and incur additional costs to estimate these hypothetical costs.

- It is unclear how the requirements in paragraph F15(b)(i) are meant to interact with the requirements in paragraphs F14(a) and F14(b) whereby the asset is replaced in the existing location, and does not presently exist. While it is assumed the asset does not presently exist it is unclear what to assume are the conditions surrounding the asset and how wide the surrounding area could be when considering the availability of suitable vacant sites if a market participant buyer was to instead construct the subject asset. For example, would this need to be within an area that still allows the asset to meet its service objectives? Overall, ACAG believes the interaction between these assumptions should be further clarified to avoid inconsistent practice and measurement challenges.
- If we adopt the premise in paragraph BC102(b) that acquiring the subject asset would save a market participant buyer from incurring those removal and disposal costs, then what should an entity look to when estimating this cost? Should the entity be looking at the surrounding built environment to make an estimate of this cost (or to determine if it is required at all) or property directly adjacent to the subject asset or to the assets that were previously on the site (even if this was an asset of similar nature and use)?

As an example, a stadium has been demolished (old stadium) and a new stadium is constructed in its existing location. Based on the implementation guidance in the ED, when valuing the new stadium there is an assumption that the stadium will be replaced in its current location (paragraph F14(a)) and that it does not presently exist (paragraph F14(b)). However, it is not clear in this circumstance whether the costs of removing and disposing of unwanted structures at the measurement date would capture the cost of removal and disposal of the old stadium or if it would capture the cost of removal and disposal of typical structures that exist on surrounding properties? Or in this circumstance, if assessing from a market buyer perspective, would it be the approach that derives the lowest (avoided) cost outcome? An Illustrative Example would be helpful in clarifying this principle.

- In BC106, the Board did not rule out inclusion of the costs of dismantling the asset and restoring the site on which the asset is located. However, recognition of such costs would clearly contradict the principle that the asset does not presently exist. Therefore, it would seem appropriate to clearly articulate that these costs should not be recognised, unless an obligation has arisen under AASB 137 to restore the site, which would then trigger the accounting requirements in Interpretation 1.

Three ACAG jurisdictions also noted that the proposal in paragraph F15(b)(i) and BC102 was not common practice in those jurisdictions and sought clarification regarding whether the proposals being adopted were consistent with IVSC or similar requirements.

Determining disruption costs to other assets

ACAG notes that there may be some implementation challenges applying this principle, particularly for entities that control large, geographically dispersed infrastructure assets, such as roads authorities and local councils. ACAG also believes it would be appropriate to clarify the following with regard to F15(b)(ii):

- it is not written in a way that clearly excludes costs of restoring assets that are controlled by a consolidated group. It just clarifies that it includes (as part of the broader principle) costs of restoring an asset not controlled by the group. Paragraph BC112 indicates the intention is to exclude these costs. ACAG therefore suggest that paragraph F15(b)(ii) is re-written to 'any disruption costs that would hypothetically be incurred, when acquiring or constructing the subject asset at measurement date, excluding costs of restoring assets that are controlled by the consolidated group (if any) to which the entity belongs'
- that the costs of restoring disruption to the entity's own assets in paragraph F15(b)(ii) should not be double-counted with the entity's existing valuation for those other assets.

Overall, ACAG recommends the AASB revisit the requirements in paragraphs F15(b) and BC 99 – BC106 and Illustrative Examples to provide further clarity on how these costs should be measured. ACAG also questions whether, in the light of the implementation challenges identified above costs outweigh benefits in relation to the F15(b)(i) and (ii) proposals.

SMC 14

Do you agree with the proposal in paragraph F15(c) that an NFP public sector entity includes in the subject asset's current replacement cost all necessary costs required to be incurred in the context of the entity's expected manner of replacement in the ordinary course of operations, rather than necessarily including only the cheapest legally permitted costs to the entity? Please provide reasons to support your view.

Please note that Illustrative Examples 1 and 2 illustrate the application of paragraphs F14 and F15.

ACAG agrees with the proposal in paragraph F15(c) as a public sector entity may incur additional costs to meet community expectations, increase visitation to an asset or, through use of higher quality and cost materials, achieve a longer economic life for the subject asset.

However, as noted in SMC 10, paragraph F15(c) directly contradicts the principle in F14(b) to assume that the asset presently does not exist. The example in paragraph F15(c) of replacing the surface component contradicts the assumption under F14(b) that the whole road presently does not exist. Therefore, paragraph F14(b) and/or F15(c) need to be changed to achieve consistency.

Economic obsolescence**SMC 15**

Do you agree with the proposal in paragraph F16 that identifying economic obsolescence should not be limited to circumstances in which a formal decision has been made to reduce the asset's physical capacity? Please provide reasons to support your view.

ACAG agrees with the proposal in paragraph F16 that identifying obsolescence should not be limited to circumstances in which a formal decision has been made to reduce the asset's physical capacity as this is consistent with paragraph 22 of AASB 13 which requires an asset's fair value to be measured using the assumptions that market participants would use when pricing an asset. A market participant would not pay to replace an asset's existing capacity if they could replace its service potential with an asset with reduced capacity.

ACAG notes in practice that it may be very difficult to find evidence to support the valuation of obsolescence and that the wording in paragraph F16 'has suffered a reduction in demand for its services' is open to interpretation.

SMC 16

Do you agree with the proposal in paragraph F17 and the example in paragraph F18 that economic obsolescence should not be identified for any 'surplus capacity' of an asset that is necessary for stand-by or safety purposes (e.g. to deal with contingencies), even if it seldom or never is actively utilised? Please provide reasons to support your view.

ACAG agrees that surplus capacity of an asset that is necessary for stand-by or safety purposes should not be identified as economic obsolescence even if it seldom or never is actively utilised.

ACAG has concerns with the example provided in paragraph F18 that considers economic obsolescence of a school purely based on enrolment numbers and suggests expanding the example to provide greater insight into how the asset values have been attributed in the economic obsolescence adjustment such as listing the assets:

- that are retained at the same gross replacement cost, given those facilities will be needed regardless of the school's number of enrolments (such as the administration office, cafeteria, toilet blocks, library, gym etc.) and other items that would likely fall into this category e.g. classrooms
- where the economic obsolescence adjustment has been applied, how this adjustment has been determined and why.

Application of the proposed implementation guidance

SMC 17

Do you agree with the proposal in paragraph AusC6.1 that the proposed authoritative implementation guidance set out in Appendix F should be applied prospectively? Please provide reasons to support your view.

ACAG agrees with the proposal in paragraph AusC6.1 that the proposed authoritative implementation guidance should be applied prospectively as:

- this is consistent with the initial application of IFRS 13. ACAG agrees with the IASB conclusion that changes in the methods used to measure fair value would be inseparable from a change in the fair value measurements (i.e. as new events occur or as new information is obtained, e.g. through better insight or improved judgement)
- the Board noted that the proposed authoritative implementation guidance clarifies the requirements of AASB 13, rather than changing those requirements (paragraph BC 182) and the proposals do not indicate that entities changing practice in how they measure those assets made an error in applying the existing requirements of AASB 13 (paragraph BC22)
- the fair value of an asset or liability applying AASB 13 is considered to be an accounting estimate which are accounted for prospectively (paragraph 32(c) of amendments to AASB 108 in *AASB 2021-2 Amendments to Australian Accounting Standards – Disclosure of Accounting Policies and Definition of Accounting Estimates*).

SMC 18

If you agree with prospective application in Question 17, do you consider that it would be appropriate for the AASB to provide an option for an NFP public sector entity to elect to restate comparative information as if the authoritative implementation guidance in Appendix F had been applied from a preceding period? Please provide reasons to support your view.

Consistent with the initial application of IFRS 13, ACAG does not believe an option should be added to restate comparative information as if the authoritative implementation guidance has been applied from a preceding period.

In paragraph BC230 of IFRS 13 the IASB stated that the 'disclosures need not be presented in periods before initial application of the IFRS because it would be difficult to apply some of the requirements in IFRS 13 without the use of hindsight in selecting the inputs that would have been appropriate in prior periods.'

Restating comparative information is also inconsistent with the guidance in AASB 108 on applying changes to estimates which requires these to be adjusted prospectively.

SMC 19

If you consider it appropriate for the AASB to provide an option for an NFP public sector entity to restate comparative information (see Question 18), do you consider it appropriate that, if an entity elects to restate comparative information, it should be required to disclose the amount of the adjustment for each financial statement line item affected, as if the implementation guidance had:

- always been applied (ie full retrospective application in accordance with AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*); or
- been applied from a specific preceding period, for example, the beginning of the immediately preceding period presented in the financial statements (ie modified retrospective application)? If so, please specify which preceding period you think would be appropriate.

Please provide reasons to support your view.

ACAG does not believe it is appropriate to apply the implementation guidance retrospectively for the reasons outlined in SMC 18.

ACAG believes that option (a) full retrospective application will likely not be possible as valuations using the implementation guidance were not performed and sufficient data may not be available.

SMC 20

Further to Question 19, do you consider it would be appropriate for such optional restatements, if elected, to be required for all affected assets, except to the extent it is impracticable for the entity to determine either the period-specific effects of the implementation guidance or the cumulative effect of the change? Please provide reasons to support your view.

ACAG does not believe it is appropriate to apply the implementation guidance retrospectively for the reasons outlined in SMC 18.

SMC 21

Do you agree that the proposed authoritative implementation guidance set out in Appendix F should be applied for annual periods beginning on or after 1 January 2024, with earlier application permitted? Please provide reasons to support your view.

Yes, ACAG agrees that if the proposed implementation guidance set out in Appendix F is issued by December 2022 that it should be applied for annual reporting periods beginning on or after 1 January 2024. This timeframe should provide enough time for universities to implement the proposals by 1 January 2024 and the majority of the public sector by 1 July 2024.

AASB General Matters for Comment**GMC 22**

Whether the *AASB Not-for-Profit Entity Standard-Setting Framework* has been applied appropriately in developing the proposals in this Exposure Draft?

Subject to our feedback on the SMCs, ACAG agrees that the NFP Framework has been applied appropriately.

GMC 23

Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, including Government Finance Statistics (GFS) implications?

ACAG has not identified any GFS implications arising from the proposals, but suggests that the Board consider any matters raised in any ABS submission on ED 320.

As stated in SMC 2, two ACAG jurisdictions suggest that a GFS compliant valuation could be achieved more cost efficiently by giving an exemption from using the exit price approach and using an entry price approach.

GMC 24

Whether, overall, the proposals would result in financial statements that would be useful to users?

ACAG believes overall that the proposals will result in financial statements that would be useful to users subject to the Board addressing our concerns outlined in SMC 5, SMC 6, SMC 13 and SMC 14.

One jurisdiction's view is that the implementation guidance, while an improvement, will not prevent the following differences in fair values derived by valuers:

- measurement of physical obsolescence – the guidance does not address how to measure physical obsolescence (e.g. proportion of useful life consumed to date or condition curve) and therefore valuers will continue with divergent practices. This jurisdiction suggests including additional paragraphs for how to measure each form of obsolescence, having regard to the guidance provided by paragraph 80 of IVS 105
- valuation of land subject to public sector specific restrictions – under the ED, valuers will continue with their previous judgements about the appropriate valuation technique to use and therefore material differences in fair value measurements will continue to occur. This jurisdiction has recommended changes that it believes will drive greater consistency in the selection of valuation techniques in SMC 2 and SMC 3.

This jurisdiction believes that the topics addressed by the guidance (market participants, highest and best use, greenfield versus brownfield; economic obsolescence) are often the subject of conceptual debate but in its experience have not led to material differences in outcomes between valuers. However, they believe the proposals for highest and best use (current use) and market participants are likely to reduce costs by not having to search for hypothetical situations.

This jurisdiction also believes that for non-financial assets not held primarily for their ability to generate net cash inflows, there are preferred alternatives to fair value that result in a similar outcome (including compliance with GFS) at a much lower cost. This jurisdiction recommends that the AASB amend AASB 116 to allow not-for-profit entities to use 'written-down current acquisition value' (paragraph 7.31 in the IMF GFSM and paragraph 8.38 of the AGFSM) for classes measured using the revaluation model. Written-down current acquisition value can be implemented by:

1. Expensing any inefficient costs from the cost of the asset at the time of construction
2. In each subsequent year:
 - (a) recognise depreciation expense against accumulated depreciation/other obsolescence for the year.
 - (b) revalue the gross carrying value for the subsequent change in a relevant and reliable construction index
 - (c) revalue accumulated depreciation/other obsolescence for any:
 - (i) change in gross carrying value
 - (ii) change in estimated useful life
 - (iii) obsolescence not captured by depreciation.

GMC 25

Whether the proposals are in the best interests of the Australian economy?
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ACAG is not able to comment on whether these proposals are in the best interests of the Australian economy.

GMC 26

Whether the proposals create any auditing or assurance challenges and, if so, an explanation of those challenges?

ACAG believes that the proposals may create auditing and assurance challenges in the following areas:

1. Market participant assumptions – ACAG notes that there may be an incentive for entities to assess that information about market participants is not 'reasonably available' when it may be available to avoid market valuations in order to adopt their own assumptions as holder of the asset.
2. Determining whether management is committed at the measurement date to a plan to sell the asset or to use the asset for an alternative purpose – refer to ACAG's comments at SMC 5, SMC 6 and SMC 7.
3. Valuation challenges and divergent practices associated with measuring the unavoidable costs of removal and disposal or unwanted structures on land and disruption costs for restoring other assets – refer to ACAG's comments at SMC 13.

GMC 27

Unless already provided in response to specific matters for comment above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.
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ACAG is not able to comment on costs and benefits of the proposals.