



Project:	Fair Value Measurement for Not-for-Profit Entities	Meeting:	AASB February 2021 (M179)
Topic:	AASB SMCs to accompany IPSASB EDs relating to Measurement	Date of this paper:	10 February 2021
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		Project Priority:	Medium
		Decision-Making:	High
		Project Status:	Decide on AASB SMCs to accompany the exposure of IPSASB ED 76 and ED 77 and consider stakeholder survey results

Objectives of this agenda item

1. The objectives of this agenda item are for the Board to:
 - (a) **decide** the content of the AASB Specific Matters for Comment (SMCs) and background information to be included in the AASB Invitation to Comment (ITC) on forthcoming IPSASB Exposure Drafts ED 76 *Conceptual Framework – Limited-Scope Update* and ED 77 *Measurement* (this Agenda Paper and Agenda Paper 10.2);
 - (b) **agree** project milestones and timeline (this Agenda Paper); and
 - (c) **note** a summary of comments from stakeholders about the specific aspects of fair value measurement for which guidance is most promptly needed (Agenda Papers 10.3 and 10.4).

The decisions sought in relation to objectives (a) and (b) are the subject of Questions for Board Members in this paper (Q1–Q5) and in Agenda Paper 10.2 (Q6). Agenda Paper 10.3 contains Questions for Board Members (Q7–Q8) regarding the process of addressing other measurement-related issues mentioned by survey respondents.

Background and reasons for bringing this agenda item to the Board at this meeting

AASB ITC

2. At its November 2020 meeting, the Board decided to consider the effect of cross-cutting projects of the AASB and international standard-setters, including the IPSASB's Measurement project, before proposing any not-for-profit (NFP) amendments to AASB 13 *Fair Value Measurement*.

3. The Board decided to respond to the IPSASB on its forthcoming Exposure Drafts, ED 76 and ED 77, and decided to add AASB SMCs when exposing the IPSASB Exposure Drafts for comment in Australia. The IPSASB is expected to issue ED 76 and ED 77 in March 2021 with a six months comment period.
4. At this meeting, staff ask the Board to **decide** the content of the AASB SMCs and the background information to be included in the ITC, with the aim to issue the ITC out of session to maximise the time in which constituents may respond. [Section 2](#) of this paper contains the draft AASB SMCs for the Board's consideration.
5. To provide a holistic view of all information that would be provided to constituents, staff have prepared a draft version of the ITC (Agenda Paper 10.2) for the Board's consideration. Agenda Paper 10.2 includes the same draft AASB SMCs as those outlined in [Section 2](#) of this paper. It also includes General Matters for Comment as part of the Board's usual due process, and background to the key issues deliberated in the Board's Fair Value Measurement for Not-for-Profit Entities project (FVM project).

Stakeholder survey

6. Staff sent a survey to members of the Fair Value Project Advisory Panel and stakeholders who originally requested guidance to assist NFP public sector entities in applying AASB 13. This survey was sent to implement the Board's instruction to consult with those stakeholders to understand:
 - (a) whether circumstances and the scope of guidance requested have changed since they originally requested guidance (e.g. the extent of diversity in applying AASB 13 in the NFP public sector changed); and
 - (b) the specific aspects of fair value measurement for which guidance is most promptly needed.
7. Agenda Paper 10.3 contains a high-level summary of stakeholders' feedback for the Board's noting. Aggregated survey results are contained in Agenda Paper 10.4 in the supplementary folder for the Board's reference. Since the Board has decided to consider IPSASB's Measurement project before proposing any NFP amendments to AASB 13, the focus of the next few meetings will be on considering the IPSASB's proposals and constituents' comments on those proposals. Therefore, staff do not propose discussing specific comments about the direction of the FVM project raised by survey respondents at this meeting.
8. A staff paper on the potential implications of the survey results for the scope and timing of the Board's future work on the FVM project is expected to be prepared for deliberation at the November 2021 meeting, after the Board has considered feedback on the ITC and finalised its submission to the IPSASB.

Attachments

- Agenda Paper 10.2: Draft AASB ITC to be issued together with IPSASB ED 76 and ED 77
- Agenda Paper 10.3: High-level summary of survey results (for noting)
- Agenda Paper 10.4: Aggregated survey results (in supplementary folder for reference)

Structure of this paper

9. This paper is structured as follows:
 - (a) [Section 1](#): The focus of the AASB SMCs
 - (b) [Section 2](#): Draft AASB SMCs
 - (c) [Section 3](#): Proposed project milestones and timeline

Section 1: The focus of the AASB SMCs

10. This Section provides background information and explanations why staff consider each of the draft AASB SMCs outlined in [Section 2](#) of the paper (also in Agenda Paper 10.2) important to inform the development of the Board's submission to the IPSASB on ED 76 and ED 77.

Overview – IPSASB's Measurement project

11. The objective of the IPSASB's Measurement project is to establish a single comprehensive Standard that defines the measurement bases used in IPSAS. The IPSASB plans to:
 - (a) issue ED 77 to achieve this objective and to provide high-level guidance on the application of these measurement bases in the Measurement Standard; and
 - (b) issue ED 76 to consequentially amend the IPSASB's Conceptual Framework, which includes measurement concepts guiding the selection of measurement bases.
12. Consistent with current requirements in IPSAS, the IPSASB is expected to propose that an asset or a liability is initially measured at its transaction price, with limited exceptions. Because this proposed policy is generally accepted (e.g. it is required in AASB Standards such as AASB 116 *Property, Plant and Equipment*), and is unrelated to the current value focus of the Board's FVM project, this agenda paper focuses only on the IPSASB's proposals for subsequent measurement of assets and liabilities.
13. The current proposal is that IPSAS would have two measurement models: 'historical cost model' and 'current value model'. Within the 'current value model', there would be four measurement bases:
 - (a) fair value – for measuring assets primarily held for their financial capacity (and for measuring some liabilities). Fair value aligns with the concepts in IFRS 13 as a market-participants-based exit value and reflects the price that would be received to sell an asset;
 - (b) current operational value¹ – for measuring assets held primarily for their operational capacity (i.e. are non-cash-generating). Current operational value is an entity-specific entry value measurement that reflects prices in the market in which the entity would acquire a modern equivalent asset;

¹ The IPSASB proposes to define current operational value as "the value of an asset used to achieve the entity's service delivery objectives at the measurement date."

- (c) cost of fulfilment – for measuring liabilities the entity intends to settle in the normal course of operations; and
- (d) value in use – for determining impairment of assets.

Overview – AASB’s Fair Value Measurement for Not-for-Profit Entities project

14. In 2018–2020, the Board deliberated certain fair value measurement issues raised by stakeholders and the Fair Value Project Advisory Panel (the Panel) and formed tentative views on most of those issues. The Board considered three drafts of an AASB Exposure Draft of possible amendments to AASB 13 and a Basis for Conclusions reflecting those tentative decisions. The latest draft was included in [Agenda Paper 11.2](#) of the March 2020 meeting.
15. One of the key tentative decisions that the Board made was in relation to the fair value measurement of restricted assets held by NFP public sector entities primarily for their service capacity², including restricted land and NFP entity lessees’ right-of-use (ROU) assets under concessionary leases. The Board tentatively decided to propose that, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence, the fair value of such restricted assets:
 - (a) should be measured at the asset’s current replacement cost³ (i.e. the cost currently required to replace the service potential embodied in the asset);
 - (b) should not be reduced due to the restrictions because the restrictions would not reduce the amount the entity would need to incur to replace the service potential embodied in the asset;⁴ and
 - (c) this measurement should be deemed to be fair value.

² This paper refers to ‘service capacity’ and ‘service potential’ interchangeably. ‘Service capacity’ is referred to in paragraph B8 of AASB 13 (unamended from IFRS 13) and has been used in the Board’s working drafts of an ED on FVM for NFP entities mainly for that reason. ‘Service potential’ is used throughout the IPSASB’s [The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities](#) (paragraphs 5.7 and 5.8). This term is also described in paragraphs Aus49.1, Aus54.1 and Aus54.2 of the AASB’s [Framework for the Preparation and Presentation of Financial Statements](#). In light of the Board considering potential non-fair value measurements for assets held primarily for their service potential, the term ‘service potential’ might be appropriate for that broader measurement focus. However, this terminology issue is not the focal point of the issues raised in this paper and therefore not elaborated further.

The IPSASB uses the term ‘operational capacity’ in its draft ED 76 and ED 77. Therefore, the draft AASB SMCs on those draft IPSASB EDs refer to ‘operational capacity’ for consistency with those draft EDs.

³ The income approach would not be appropriate in measuring the fair value of such assets that are not primarily held to generate net cash inflows. Measuring the fair value of such restricted assets using the market approach is also not appropriate if an equivalent restricted asset is not obtainable in the marketplace at the measurement date and the resulting measure would differ from current replacement cost.

⁴ The Board tentatively concluded that if an equivalent restricted asset is not obtainable in the marketplace, the NFP public sector entity would need to compete with other market participants to purchase an equivalent asset (that reflects the same characteristics and provides services of the same nature as the asset being measured) that is not subject to the restrictions to provide the required services. In this hypothetical transaction, the cost that the NFP public sector entity would need to incur would not be reduced because the entity’s asset being measured is subject to restrictions. Accordingly, the current replacement cost of the restricted asset being measured would be unlikely to be reduced due to restrictions.

16. The Board noted that if an equivalent restricted asset is obtainable in the marketplace at the measurement date for a price supported by observable market evidence, the fair value of the restricted asset should be based on the sales price for that equivalent restricted asset. This sales price for the equivalent restricted asset would reflect what a market participant buyer (including public sector NFP entity market participant buyers)⁵ would consider in pricing the asset with an equivalent restriction; and therefore, there would be no need to adjust that sales price to reflect restrictions.
17. However, the Board received feedback from some stakeholders that they disagree with applying the tentative proposal described in paragraph 15 to measure restricted land at an amount deemed to be fair value (stakeholders generally agree with the proposal to measure other restricted assets at an amount deemed to be fair value). These stakeholders, including some members of the Panel, disagree that measuring land at current replacement cost without a deduction for the restriction would reflect the service potential of restricted land.
18. In light of the adverse feedback described in paragraph 17, at its March 2020 meeting, amongst other instructions to staff, the Board instructed staff to research options for measurement bases other than fair value to address the current value measurement issues regarding restricted assets held primarily for their service capacity.

The focus of the AASB SMCs should be on current operational value and fair value

19. The IPSASB's proposed 'current operational value' (COV) measurement basis is a current value that is not fair value. Therefore, in light of the Board's instruction described in paragraph 18, staff consider there is merit in assessing whether the proposed COV basis might be a suitable alternative measurement basis to address the restricted asset measurement issues in Australia.
20. This focus is important because ED 76 and ED 77 are also expected to propose other current value measurement bases (i.e. cost of fulfilment and value in use) as explained in paragraph 13, which are not directly relevant to the Board's FVM project. It would be appropriate to highlight the IPSASB proposals about COV and fair value to the Board's constituents.

Include an AASB SMC for each key fair value measurement issue on which the Board has been deliberating

21. IPSASB ED 77 will include Application Guidance addressing some of the measurement topics the Board has been deliberating. Albeit, the Board has deliberated those topics in the context of fair value measurement, whereas the IPSASB has developed its proposals under its proposed approach to develop a current measurement basis that differs from fair value. Staff consider it important to include AASB SMCs to elicit Australian constituents' views specifically on these measurement topics; in particular, topics for which the IPSASB has reached a different conclusion from the Board's tentative views.

⁵ The Board previously formed a tentative view that the market participant buyers of a non-financial asset of a public sector NFP entity held primarily for its service capacity would include similar public sector NFP entity market participants. This is noted here for completeness and consistency. In the particular case of an equivalent restricted asset being obtainable in the marketplace, including public sector NFP entities in the population of market participant buyers for a restricted asset should have no effect on the fair value measurement of that restricted asset. This is because if an equivalent restricted asset is obtainable, a public sector NFP entity market participant buyer would not be prepared to pay more for the restricted asset than the amount a for-profit entity market participant buyer would be prepared to pay.

22. A staff paper analysing the IPSASB's proposed COV measurement basis and related Application Guidance is expected to be prepared for the Board's deliberation at the April 2021 meeting.

Section 2: Draft AASB SMCs

23. In summary, based on the information in Section 1 of this paper, staff recommend the Board's ITC includes SMCs on:
- (a) specific aspects of the IPSASB's proposed COV measurement basis;
 - (b) the IPSASB's proposal not to apply the fair value model to measure the current value of assets held primarily for their operational capacity; and
 - (c) each key item of the IPSASB's Application Guidance addressing a measurement topic the Board has been deliberating (albeit based on the fair value model).
24. To assist the Board's review of the staff's draft AASB SMCs, for each draft SMC outlined in the Tables below, staff have included:
- (a) a summary of the IPSASB's relevant tentative decision on the COV measurement basis based on a working draft of ED 76 and ED 77⁶;
 - (b) where relevant, a summary of the Board's tentative view⁷ on the issue, in the context of fair value measurement (note that, where the Board has not considered the subject of an IPSASB proposal in its deliberations to date, or a Board view was only implicit in the context of another explicit view, those aspects are identified within the Table spanning SMCs 1 – 11); and
 - (c) an indication of whether the Board's tentative view to date is likely to be consistent with the IPSASB's tentative decision on the issue.
25. The draft SMCs contained in this Section are the same as those outlined in Agenda Paper 10.2. However, Agenda Paper 10.2 also includes other General Matters for Comment as part of the Board's usual due process and background to the key issues debated in the Board's FVM project. Staff have prepared Agenda Paper 10.2 to provide a holistic view of all information that would be provided to constituents.
26. As noted in the section in Agenda Paper 10.2 entitled 'Interaction with the IPSASB's Measurement project', IPSASB Exposure Drafts ED 76 and ED 77 do not specifically address how to measure the current value of right-of-use assets arising from leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives.

⁶ References to ED 76 and ED 77 are based on a working draft provided by IPSASB staff that has not yet been considered by the IPSASB. The working draft incorporates IPSASB decisions made at its December 2020 meeting. The IPSASB will meet on 25 February 2021; papers for that meeting were not yet available at the date of this agenda paper. Staff will provide a verbal update at the AASB meeting for any significant differences between those forthcoming papers and the content in the Table below.

⁷ The Table includes references to Action Alert documents and the [March 2020 draft AASB ED](#) for the FVM project. In 2019–2020, the Board discussed several working drafts of an Exposure Draft for the FVM project. The latest draft was presented at the March 2020 meeting, which reflects the Board's discussions up to then.

Therefore, although that topic is an important component of the Board’s FVM project, it is not the subject of an SMC in the draft Invitation to Comment.

SMCs relating to the IPSASB’s proposed current operational value measurement basis

The subject of SMC 1–15 below is non-financial assets of an NFP public sector⁸ entity not held primarily for their ability to generate net cash inflows (i.e. assets held for their operational capacity). For ease of reference in this paper, such assets are referred as “ operational assets ”.	
	Service potential of operational asset
AASB SMC 1	In respect of operational assets, do you agree that a current value measurement should reflect the asset’s service potential? Please explain your reasons.
AASB SMC 2	In your opinion, would the IPSASB’s proposed current operational value measurement basis result in an asset value reflecting the asset’s service potential? Please explain your reasons.
IPSASB’s tentative decisions	<p>Paragraph 7.43 of draft ED 76 states: “Fair value reflects the asset’s ability to generate economic benefits and the price expected to be received on sale. Therefore, it provides less useful information for the cost of services than current service operational value, which reflects the cost to replace the <u>remaining service potential provided by an asset.</u>” [emphasis added]</p> <p>Paragraph 7.53 of draft ED 76 states: “ ... current operational value provides a useful measure of the resources available to provide services in future periods, as it is focused on the current value of assets and their <u>service potential</u> to the entity.” [emphasis added]</p>
AASB’s tentative decisions [Consistent with IPSASB]	<p>At its meeting in November 2019, the AASB tentatively adopted the view that an asset of a NFP entity not held primarily to generate cash inflows provides service potential to the entity by having the capacity to satisfy the wants and needs of members of the community (beneficiaries) without necessarily receiving cash in exchange from those beneficiaries. Consistent with paragraphs Aus49.1, Aus54.1 and Aus54.2 of the AASB’s Framework for the Preparation and Presentation of Financial Statements, the AASB considers that those assets should be measured at amounts faithfully representing their service potential (i.e. measured at their service capacity).</p> <p>Reducing the value of a restricted non-financial asset because the entity that holds the asset has restrictions to charge for services, which would diminish the net cash inflows the asset can generate directly (but the asset’s service potential is unaffected), would be inconsistent with the principles of the Conceptual Framework.</p> <p>[Action Alert of November 2019 AASB meeting and staff’s draft text in paragraph BC9 of the March 2020 draft AASB ED]</p>

⁸ A staff paper to be considered at a future Board meeting will address whether there are any aspects of IPSASB ED 76 and ED 77 with different implications for *private sector* NFP entities. These aspects would not affect the Board’s submission on the IPSASB EDs but might affect whether any different measurement requirements should be developed for private sector NFP entities.

AASB SMC 3	<p>Measuring the current operational value of an asset based on its current use</p> <p>Do you agree with the IPSASB’s proposal in ED 77 that the current operational value of an operational asset should be measured based on its current use, disregarding potential alternative uses and any other characteristics of the asset that could maximise its market value (paragraph B4)? Please explain your reasons.</p>
IPSASB’s tentative decisions	<p>Paragraph B4 of draft ED 77 states: “Measuring the current use of an asset disregards potential alternative uses and any other characteristics of the asset that could maximize its market value. For example, the current use of a building operated as a school, is a school. Alternative uses, such as the operation of the building as an office block are not considered. The current use may be, but is not necessarily, the highest and best use.”</p>
AASB’s tentative decisions [Different from IPSASB]	<p>If a NFP entity measures an asset at fair value, the highest and best use concept in AASB 13 should continue be applicable to NFP entities.</p> <p>However, the ‘financially feasible’ use’ aspect of a non-financial asset’s highest and best use (as described in paragraph 28(c) of AASB 13) should not be applicable to restricted assets of NFP entities that are held primarily for their service capacity.</p> <p>[Action Alert of November 2019 AASB meeting and staff’s draft text in paragraph Aus28.1 of the March 2020 draft AASB ED]</p>
AASB SMC 4	<p>Using the income approach to estimate the current operational value of an operational asset</p> <p>Do you agree with the IPSASB’s proposal in ED 77 that the income approach can be an appropriate measurement technique in certain circumstances to estimate the current operational value of an operational asset (paragraphs B24 and B37)? If you agree, please identify what those circumstances would be. Whether you agree or disagree, please explain your reasons for your view.</p>
IPSASB’s tentative decisions	<p>Paragraph B37 of draft ED 77 states that the income approach may be applicable to estimate the current operational value when:</p> <ul style="list-style-type: none"> (a) the income approach is used to support the market or cost approach to discount future outflows to a current amount. This will occur when the timing of an outflow differs from the measurement date; or (b) information is unavailable to support the application of the market or cost approach. For example, heritage items that are naturally occurring, such as cave paintings, or natural resources are unlikely to have cost or market information related to the specific asset. However, the asset may generate cash inflows through tourism, a royalty stream, etc. that may be relevant in determining the current operational value.
AASB’s tentative decisions [appear different from IPSASB]	<p>The Board did not specifically discuss whether the income approach in AASB 13 is appropriate for measuring the current value of operational assets.</p> <p>Paragraphs 61 – 63 of AASB 13 states that, in some cases, multiple valuation techniques will be appropriate, reflecting the principle that fair value measurements are to maximise the use of relevant observable inputs. However, as noted in paragraph 15 above, the Board made a tentative decision that, for a restricted operational asset, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable</p>

	<p>market evidence, the asset should be measured at its current replacement cost without a deduction to the current market buying price of an equivalent but unrestricted asset (with the asset's current replacement cost deemed to be its fair value). Using the income approach would be incompatible with measuring an operational asset at its current replacement cost.</p> <p>In contrast, the Board tentatively decided that, for a restricted operational asset, if an equivalent restricted asset is obtainable in the marketplace at the measurement date for a price supported by observable market evidence, the asset should be measured at fair value based on the available market evidence. In such circumstances, using the income approach would be permissible, for example, where market rentals for an equivalent restricted asset are observable.</p> <p>Prohibiting use of the income approach for a restricted asset, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence, would be consistent with the requirements in AASB 1059 <i>Service Concession Arrangements: Grantors</i> (to measure service concession assets at their current replacement cost) and amendments to AASB 136 <i>Impairment of Assets</i> (to exclude non-financial operational assets that are regularly revalued to fair value from the scope of AASB 136). Those requirements were developed to ensure operational assets are measured at amounts faithfully representing their service potential rather than at amounts reflecting their current cash-generating ability, which would often be their scrap values.</p> <p>Therefore, staff propose including in the background information of the ITC a Board view (in line with its tentative decisions to date) that the income approach should not be used to estimate the fair value of restricted operational assets for which an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence. This aspect is the subject of Question 2 to Board members in this paper. In addition, a draft statement is included in Agenda Paper 10.2 (the AASB's tentative views in Topic 1 of the Table in the Appendix) for the Board's consideration.</p>
AASB SMC 5	<p>Measuring the current operational value of restricted operational assets</p> <p>In respect of operational assets that are subject to restrictions, assuming that an equivalent restricted asset is not obtainable in the marketplace, do you agree with the IPSASB's proposal in ED 77 that the current operational value of such restricted operational assets should not be lower than the value of an equivalent unrestricted asset? Please explain your reasons.</p>
IPSASB's tentative decisions	<p>To date, the IPSASB has not specifically discussed how restrictions would impact the measurement of current operational value. The IPSASB is expected to discuss this issue at its 25th February 2021 meeting.</p> <p>Based on discussions with IPSASB staff, it is expected that the draft ED 77 that will be presented at that IPSASB meeting will include draft paragraphs on restrictions along the following lines:</p> <p>The current operational value of restricted non-financial assets shall be measured as follows:</p> <p>(a) If an equivalent restricted asset is obtainable in an orderly market at the measurement date for a price supported by observable market evidence,</p>

	<p>the asset is measured based on the available market evidence for the equivalent restricted asset, without any further reduction for the restrictions; or</p> <p>(b) If an equivalent restricted asset is not obtainable in an orderly market at the measurement date for a price supported by observable market evidence, the asset is measured at the price of an equivalent unrestricted asset, without a reduction for the restrictions.</p> <p>The restrictions would not reduce the current entry price of the service potential embodied in the asset (the cost that the entity currently would need to incur) if the entity needs to purchase an unrestricted replacement asset to continue delivering services of the same nature and volume.</p>
<p>AASB's tentative decisions [as yet unknown whether the IPSASB decision will be consistent with the AASB's tentative decision]</p>	<p>Measure restricted operational assets, including restricted land, at current replacement cost without an adjustment deducted for restrictions if an equivalent restricted asset is not obtainable in the marketplace. This measurement is deemed to be fair value.</p> <p>Where an equivalent restricted asset is obtainable in the marketplace, the market price of an equivalent restricted asset would already reflect any effects that the restrictions have on the current price of the service potential embodied in the asset. That is, the restrictions have been taken into account in the measurement of the asset's fair value, but are implicit in the market price of the equivalent restricted asset, and therefore no explicit deduction would be necessary.</p> <p>[Action Alert of the April 2019 AASB meeting and staff's draft text in paragraph Aus66.1 of the March 2020 draft AASB ED]</p>
<p>AASB SMC 6</p>	<p>Assumed location of an operational asset when measuring its current operational value</p> <p>Do you agree with IPSASB's proposals in ED 77 that an asset's current operational value assumes that the entity will continue to meet its service delivery objectives from the same location in which the existing asset is situated (paragraph B12)? Please provide your reasons.</p>
<p>IPSASB's tentative decisions</p>	<p>Paragraph B6 of draft ED 77 states: "The asset's current operational value assumes that the entity will continue to meet its service delivery objectives from the same location as the current asset is situated."</p>
<p>AASB's tentative decisions [Consistent with IPSASB]</p>	<p>Service capacity of an asset includes 'reinvestment potential' i.e. the ability to sell an asset and reinvest the proceeds in other stores of service capacity. Therefore, replacement of an asset is always assumed to occur in its present location.</p> <p>[Action Alert of November 2019 AASB meeting and staff's draft text in paragraphs F26 and BC107–BC111 of the March 2020 draft AASB ED]</p>
<p>AASB SMC 7</p>	<p>Nature of component costs to include in an asset's current operational value</p> <p>Do you agree with ED 77 that, when measuring an asset's current operational value, the cost of a modern equivalent asset may in some circumstances exclude the following costs (paragraph B36)? Please explain your reasons.</p> <ul style="list-style-type: none"> • Additional costs arising from extending an existing property; • Contract variation costs; and • Planning changes.

<p>IPSASB's tentative decisions</p>	<p>Paragraph B36 of draft ED 77 proposes that an entity might not need to include the following costs when considering the cost of a modern equivalent asset to estimate the current operational value of an asset. It states:</p> <p>“(b) Additional costs arising from extending an existing property – These costs should be ignored, since the norm is that the valuation will be of a modern equivalent asset.</p> <p>(c) Contract variations – Additional construction costs because of design or specification changes should be ignored. The modern equivalent asset being valued will have the same service capacity as the existing asset in its current use.</p> <p>(d) Planning changes – Entities should consider whether planning consent would need to be obtained were the modern equivalent asset to be constructed on the actual site.”</p>
<p>AASB's tentative decisions [Different from IPSASB]</p>	<p>The current replacement cost of assets composing a self-constructed facility includes all necessary costs intrinsically linked to acquiring the facility at the measurement date.</p> <p>An NFP public sector entity should assume that the facility presently does not exist and should take into account any make-good costs that must be incurred for surrounding facilities of another entity disturbed when the entity's facility is replaced.</p> <p>[Action Alert of June 2019 AASB meeting and staff's draft text in Paragraph BC84 of the March 2020 draft AASB ED]</p>
<p>AASB SMC 8</p>	<p>Whether the current operational value of an asset should include borrowing costs</p> <p>Do you agree with ED 77 that if an entity does not capitalise borrowing costs in accordance with its accounting policy (as allowed under IPSAS 5 <i>Borrowing Costs</i> and in certain circumstances under AASB 123 <i>Borrowing Costs</i>), the entity should disregard any financing costs in measuring the modern equivalent asset as part of the current operational value estimate (paragraph B36(a))? Please explain your reasons.</p>
<p>IPSASB's tentative decisions</p>	<p>Paragraph B36(a) of draft ED 77 states: “ ... A large site may have been developed in phases. The cost of a modern equivalent asset would normally be based on a single-phase development, and this should be measured at the building cost at the measurement date. A single-phase development may still occur over an extended period of time. If the entity does not capitalize borrowing costs in accordance with IPSAS 5, <i>Borrowing Costs</i>, the entity should <u>disregard any financing costs</u> in measuring the modern equivalent asset.” [emphasis added]</p> <p>Section C.5 of draft ED 77 states: “... If the jurisdiction does not normally capitalize borrowing costs under IPSAS 5, <i>Borrowing Costs</i>, the entity should instruct the valuation expert to disregard any financing costs.”</p>
<p>AASB's tentative decisions</p>	<p>No guidance is proposed for AASB 13 because there is not a NFP-specific reason to issue guidance. The Board tentatively decided that, in determining whether borrowing costs should be included in the current replacement cost of a self-constructed asset, an NFP entity should consider whether a market participant</p>

<p>[Different from IPSASB]</p>	<p>buyer of the asset would include borrowing costs in its pricing decisions about the asset.</p> <p>The Board also tentatively decided that an entity’s decision whether to include borrowing costs in the current replacement cost of a self-constructed asset does not depend on the accounting policy choice made by the entity (under paragraph Aus8.1 of AASB 123) regarding whether to capitalise borrowing costs into the asset’s cost on initial recognition.</p> <p>[Action Alert of June 2019 AASB meeting]</p>
<p>Consideration of surplus capacity and economic obsolescence</p>	
<p>AASB SMC 9</p>	<p>Do you agree with ED 77 that the current operational value of an operational asset should assume the asset is used to its full capacity, subject to any obsolescence (paragraphs B11 and B12)? Please provide your reasons.</p>
<p>AASB SMC 10</p>	<p>Do you consider the guidance in ED 77 to be clear and sufficient in distinguishing whether an asset’s excess capacity should be treated either as:</p> <ul style="list-style-type: none"> (a) surplus capacity, as described in paragraphs B11 and B12 (which is not adjusted for when measuring the asset’s current operational value); or (b) an indication of economic obsolescence, as described in paragraph B33(c) (which is deducted when measuring the asset’s current operational value)? <p>Please provide your reasons.</p>
<p>IPSASB’s tentative decisions</p>	<p>Paragraph B12 of draft ED 77 states that: “Since current operational value reflects the value of the asset consumed in providing the service at the prevailing prices, current operational value assumes the asset is used to its full capacity, subject to any obsolescence.”</p> <p>Paragraph B11 of draft ED 77 provides an example of surplus capacity. It states: “Surplus capacity exists when an asset is not used to its maximum capacity. For example, an entity owns a building, but only utilizes 80% of the space available. The remaining 20% is left vacant.”</p> <p>Paragraph B33(c) of draft ED 77 states: “... Economic obsolescence relates to any loss of utility caused by economic or other factors outside the control of the entity. The loss of service capacity might be temporary or permanent.”</p>
<p>AASB’s tentative decisions [Consistent with IPSASB, to the extent discussed]</p>	<p>The Board has not discussed the implications, when measuring an asset’s current replacement cost, of an entity choosing not to fully utilise an asset’s capacity. This seems to be a different issue from identifying/measuring economic obsolescence. However, staff consider that the similarities and differences between surplus capacity and economic obsolescence warrant clarification by the IPSASB.</p> <p>Regarding economic obsolescence, the AASB is of the view that if an asset has suffered a reduction in demand for its services, the identification of its economic obsolescence does not require a formal decision to have been made to reduce the physical capacity of that asset. However, if an asset has apparent overcapacity in view of current demand for its services, economic obsolescence shall not be identified for that asset if there is more than an insignificant chance that future increases in the demand for its services will largely eliminate that overcapacity within the foreseeable future.</p>

	<p>[Action Alert of April 2019 AASB meeting and staff’s draft text in paragraphs F24–F25 and IE5 of the March 2020 draft AASB ED]</p> <p>(Note to Board members: Staff expect to analyse whether an entity choosing not to fully utilise an asset’s capacity would affect the asset’s current value for Board deliberation at the April 2021 meeting. Staff do not consider it necessary for the Board to reach a view on this issue prior to issuing the ITC.)</p>
AASB SMC 11	<p>Overall comment on the IPSASB’s proposed current operational value measurement basis</p> <p>Would you support the adoption of the IPSASB’s proposed current operational value measurement basis – instead of fair value – for NFP entities in Australia in measuring the current value of:</p> <p>(a) operational assets with restrictions; and</p> <p>(b) other operational assets?</p> <p>Please explain your reasons.</p>

SMCs relating to fair value measurement

AASB SMC 12	<p>Hypothetical market participant</p> <p>In respect of operational assets, do you agree with the AASB’s initial tentative view to propose that, when measuring the fair value of an operational asset under AASB 13, hypothetical market participant buyers would include another NFP entity that has similar service delivery objectives and would be willing to pay the lowest price for which it could replace the asset’s service potential? Please explain your reasons.</p>
IPSASB’s tentative decisions	<p>The IPSASB did not discuss this issue.</p>
AASB’s tentative decisions [Different from IPSASB]	<p>The Board tentatively reached the view that hypothetical market participant buyers would include another NFP entity with similar service delivery objectives. Such a market participant buyer would be willing to pay more than the amount on which it can generate a commercial rate of return for an asset it requires to fulfil its service delivery objectives. This is particularly pertinent to measuring the fair value of restricted assets.</p> <p>[Staff’s draft text in paragraph BC51(a) of the March 2020 draft AASB ED]</p>
AASB SMC 13	<p>Measuring the current value of operational assets using the fair value model</p> <p>Do you agree with the IPSASB’s conclusion in ED 77 that fair value is inappropriate to apply when measuring the current value of operational assets because the “highest and best use” and “maximising the use of market participant data”⁹ concepts are generally not applicable (paragraph B29)? (The AASB has not yet deliberated this issue.) Please explain your reasons.</p>

⁹ In AASB 13, paragraph 67: “maximise the use of relevant observable inputs”.

<p>IPSASB's tentative decisions</p>	<p>BC29 of ED 77 states: “ ... the IPSASB’s preliminary view [is] that fair value is relevant and applicable in measuring some assets and liabilities in the public sector. Constituents’ concerns with fair value related to the fact that when an item is held for its operational capacity, as is often the case in the public sector, fair value is difficult and inappropriate to apply because the following concepts generally are not applicable:</p> <p>(a) Highest and best use; and</p> <p>(b) Maximizing the use of market participant data.”</p>
<p>AASB's tentative decisions [Different from IPSASB]</p>	<p>When it originally issued AASB 13, the Board concluded that fair value is appropriate in measuring the current value of operational assets. The Board decided not to include any measurement-related NFP entity modifications to IFRS 13 in AASB 13 because it considered that a public sector entity would be able to measure the fair value of its operational assets at current replacement cost, under the cost approach in IFRS 13.</p> <p>Additionally, the Board considered that the highest and best use concept, other than the ‘financially feasible’ use aspect, should continue be applicable to NFP entities.</p> <p>The Board is of the view that a NFP public sector entity should be able to maximise the use of market participant data in estimating the fair value of an operational asset. In doing so, the Board considered that the hypothetical market participant buyer should include another NFP public sector entity with similar service delivery objectives.</p> <p>[Staff’s draft text in paragraphs BC4 and BC51(a) of the March 2020 draft AASB ED]</p>
<p>AASB SMC 14</p>	<p>Measuring the fair value of restricted operational assets</p> <p>Do you agree with the AASB’s initial tentative view that, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence, the fair value of a restricted operational asset:</p> <p>(a) should be measured at its current replacement cost; and</p> <p>(b) should not be reduced due to the restrictions, because the restrictions do not reduce the amount the entity would need to incur to replace the service potential embodied in the asset?</p> <p>Please provide your reasons.</p>
<p>IPSASB</p>	<p>This issue is outside the scope of the IPSASB’s decisions as it proposes not to apply fair value in measuring the current value of operational assets.</p>
<p>AASB's tentative decisions</p>	<p>The AASB considers that, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence, in a hypothetical sale in accordance with AASB 13, the hypothetical market participant buyers would include an entity needing to buy an equivalent <u>unrestricted</u> asset. In this case, the Board tentatively decided that the asset’s fair value should be estimated based on the current market buying price of the equivalent <u>unrestricted</u> asset, without a deduction for the restrictions, because the market participant buyer could not replace the asset for a lower price by acquiring an asset with an equivalent restriction.</p>

AASB SMC 15	<p>Consistency with other AASB Standards</p> <p>If you disagree with the AASB’s initial tentative view in Specific Matter for Comment 14 – namely, that the fair value of a restricted operational asset should be measured at its current replacement cost without a deduction for the restrictions, if an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence – do you agree that, for logical consistency, changes to AASB 1059 <i>Service Concession Arrangements: Grantors</i> and AASB 136 <i>Impairment of Assets</i> would be warranted, so that the current values of all operational assets of not-for-profit entities are measured based on their current cash-generating ability? Please provide your reasons.</p>
AASB’s decisions	<p>AASB 1059 requires service concession assets to be measured at their current replacement cost. The amendments to AASB 136 made by AASB 2016-4 <i>Amendments to Australian Accounting Standards – Recoverable Amount of Non-Cash-Generating Specialised Assets of Not-for-Profit Entities</i> exclude non-financial operational assets of NFP entities that are regularly revalued to fair value from the scope of AASB 136. Both sets of requirements were developed to ensure operational assets are measured at amounts faithfully representing their service potential rather than at an amount reflecting their current cash-generating ability, which would often be their scrap values.</p>

Questions for Board members

Q1: Do Board members agree with staff recommendations in paragraph 23 that the focus of the AASB SMCs should be on:

- (a) specific aspects of the IPSASB’s proposed COV measurement basis;
- (b) the IPSASB’s proposal not to apply the fair value model to measure the current value of assets held primarily for their operational capacity; and
- (c) each key item of the IPSASB’s Application Guidance addressing a measurement topic the Board has been deliberating (albeit based on the fair value model).

Q2: In respect of SMC 4 above, do Board members agree with stating an explicit tentative view that the income approach should not be used to estimate the fair value of restricted operational assets for which an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence? [A draft statement is included in Agenda Paper 10.2 (the AASB’s tentative views in Topic 1 of the Table in the Appendix) for the Board’s consideration].

Q3: Do Board members have any comments on the draft AASB SMCs in the Tables above?

Q4: Are there any other SMCs that needs to be included in the Board’s Invitation to Comment?

Section 3: Proposed project milestones and timeline – Developing submission on IPSASB ED 76 and ED 77

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

Meeting / Deliverable	Project Milestones
March 2021	<p>Subject to the Board’s decisions at this meeting, staff recommend finalising and issuing the AASB ITC out of session to accompany the exposure of IPSASB ED 76 and ED 77. Staff propose for a subcommittee of the Board to review/approve the completed draft of the ITC for final approval by the Chairman.</p> <p>The IPSASB EDs are expected to have a six-month exposure period commencing in March 2021 and concluding in September 2021. Due to the timing of the IPSASB EDs vis-à-vis financial year-end activities, staff recommend a 90-day comment period for the ITC, which would close at the end of June or early in July, depending on when the IPSASB issues its Exposure Drafts.</p>
20–21 April 2021: Board meeting	Board to consider staff’s analysis of IPSASB’s proposed COV measurement basis and commence discussion of the content of its submission to the IPSASB.
May – June 2021	Outreach to stakeholders regarding the ITC, including a webinar and meetings with the FVM Panel, HoTARAC and ACAG.
21–22 June 2021: Board meeting	Board to consider: <ul style="list-style-type: none"> • comments received on the ITC from outreach activities; and • draft submission to the IPSASB
July – August 2021	Board Subcommittee to consider: <ul style="list-style-type: none"> • staff’s analysis of comment letters received on the ITC; and • updated draft submission to the IPSASB
8–9 September 2021: Board meeting	Board to consider: <ul style="list-style-type: none"> • comments received on the ITC from submissions and additional outreach activities; and • final draft submission to the IPSASB
10–11 November 2021: Board meeting	Board to consider implications of survey results and comments on the ITC for the direction of future work on the FVM project.

Question for Board members

Q5: Do Board members agree with the proposed project milestones and timeline, including to form a subcommittee and to finalise the ITC out of session?