



**Australian Government**

**Australian Accounting  
Standards Board**

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Mr Ross Smith  
Program and Technical Director  
International Public Sector Accounting Standards Board  
International Federation of Accountants  
(submitted via the IPSASB website)

25 October 2021

Dear Ross,

### **IPSASB Exposure Drafts 76 and 77**

The Australian Accounting Standards Board (AASB) is pleased to provide its comments on Exposure Draft 76 *Conceptual Framework Update: Chapter 7, Measurement of Assets and Liabilities in Financial Statements (ED 76)* and Exposure Draft 77 *Measurement (ED 77)*.

For ease of reference in this letter, non-financial assets held primarily for their operational capacity are referred to as 'operational capacity assets'.

The AASB commends the IPSASB for developing proposed updated measurement concepts for public sector entities and a proposed Measurement IPSAS applying those updated concepts to a variety of measurement issues public sector entities face. This submission includes the AASB's views on selected proposals in ED 76 and ED 77, primarily regarding the current operational value measurement and fair value measurement of operational capacity assets.

The AASB issued an Invitation to Comment (ITC 45) on ED 76 and ED 77 and received six comment letters, which are available on the AASB's website.

Since 2013, Australian public sector for-profit and not-for-profit (NFP) entities have been applying AASB 13 *Fair Value Measurement*, which incorporates IFRS 13 *Fair Value Measurement*. Those entities apply AASB 13 to measure the current value of all their non-financial assets. Other than some disclosure relief in AASB 13 para. Aus93.1, the AASB did not make amendments to IFRS 13 for application by NFP public sector entities. Appendix A includes an overview of the experience of Australian NFP public sector entities in applying IFRS 13/AASB 13.

The AASB is yet to be convinced that the current value of operational capacity assets should be measured under the current operational value basis instead of the fair value basis, because it considers that:

- (a) the measurement objective for current operational value is not stated with sufficient clarity in ED 76 and ED 77; and
- (b) the IPSASB's explanation of why it concluded that fair value is appropriate for assets held primarily for their financial capacity but inappropriate for operational capacity assets should be expanded to provide better justification of that conclusion.

It is difficult to identify how current operational value should be measured or the extent to which measurements of current operational value and fair value would differ. This lack of a clear distinction between current operational value and fair value is exemplified by the proposal in ED 76 and ED 77 that the market, income or cost approach (or a combination of those approaches) may be used to measure an asset's current operational value, which is also a feature of fair value. The AASB considers that ED 76 and ED 77 do not provide sufficient explanation of how the application of these three approaches would

differ under current operational value and fair value. In addition, no detailed illustrative examples were included in ED 76 or ED 77 to help clarify these aspects.

Overall, there is insufficient information in the Exposure Drafts to explain why current operational value would be a better measurement basis than fair value for measuring the current value of operational capacity assets.

In addition to comments received on ITC 45, the AASB obtained feedback about fair value measurement as part of its ongoing Fair Value Measurement for Not-for-Profit Entities project. A significant majority of stakeholders across NFP public sector entities' financial statement preparers, auditors and valuers indicated that fair value under AASB 13 is appropriate for measuring the current value of non-financial assets held by NFP public sector entities and should remain the current value measurement basis. The Australian Federal Government and the Governments of each State and Territory have established policies and procedures to ensure consistent application of AASB 13 within each jurisdiction. Valuers have also established procedures in preparing valuation reports required for reporting under AASB 13.

These stakeholders also commented that they agree with applying the 'highest and best use' and 'market participants' concepts under fair value, although some stakeholders seek guidance to assist entities to understand better how these concepts should be applied in the NFP public sector context. They consider that applying the fair value basis to all non-financial assets, despite the need to exercise judgement in applying those concepts, would be preferable to applying two measurement bases, as proposed in ED 76 and ED 77. This is because it would avoid:

- (a) the need for financial statement preparers, auditors and valuers to understand the requirements of two measurement bases;
- (b) imposing potential additional costs and effort to assess which measurement basis is appropriate for each asset or class of assets, or to reassess the appropriate measurement basis when there is a change in how an entity uses an asset; and
- (c) reporting to users of financial statements of NFP public sector entities current values based on mixed measurement bases, which would reduce the comparability and understandability of the totals reported.

The AASB supports the proposed retention of conceptual guidance supporting the usefulness of historical-cost-based measurements for decision-making and accountability purposes referred to in ED 76 paras. 7.28 and 7.31. However, the AASB focused its comments on the current value measurement of operational capacity assets. As such, this submission does not include views on the historical cost measurement basis, the current value measurement of liabilities or assets held for their financial capacity (except in responding to Specific Matter for Comment 9 on ED 77).

Appendices B and C include the AASB's responses to selected Specific Matters for Comment in ED 76 and ED 77 related to:

- (a) the current operational value measurement basis; and
- (b) the removal of certain measurement bases from the IPSASB Conceptual Framework.

If you have any questions regarding this submission, please contact myself or Fridrich Housa, Deputy Technical Director ([fhousa@aab.gov.au](mailto:fhousa@aab.gov.au)).

Yours sincerely,



Dr Keith Kendall  
AASB Chair

## APPENDIX A

### Overview of the experience of Australian not-for-profit public sector entities in applying IFRS 13/AASB 13

Since AASB 13 *Fair Value Measurement*, which incorporates IFRS 13 *Fair Value Measurement*, became effective in the 2013-14 financial year, Australian public sector entities have been applying fair value to measure the current value of all their non-financial assets. This is because the Federal, State and Territory Governments in Australia, and many of their controlled entities, have been applying the revaluation model option in Australian Accounting Standards to align with the requirements in Government Finance Statistics (GFS) to measure assets and liabilities at market value. Adopting the revaluation model option in Australian Accounting Standards requires an entity to regularly revalue non-financial assets to fair value.

In 2016, as part of the feedback received on the AASB's Agenda Consultation 2017–2019, the AASB received requests for guidance to assist application of AASB 13 in the NFP public sector. Therefore, the AASB added the Fair Value Measurement for Not-for-Profit Entities project (FVM project) to its work program.

Although guidance has been requested to clarify certain principles in measuring the fair value of specialised operational capacity assets (such as identifying the market participants for the purchase or sale of a specialised operational capacity asset, and the highest and best use of such an asset), a significant majority of stakeholders agree that the fair value measurement basis is appropriate for measuring the current value of operational capacity assets. These stakeholders noted that the fair value basis in AASB 13 – with its three approaches to measuring fair value – caters for all non-financial assets held by public sector entities (including its incorporation of the cost approach, which is particularly appropriate for the variety of specialised assets held by public sector entities, as discussed further below). They also commented that applying the fair value basis to all non-financial assets would be preferable to applying two measurement bases, as proposed in ED 76 and ED 77. This is because it would avoid:

- (a) the need for financial statement preparers, auditors and valuers to understand the requirements of two measurement bases;
- (b) imposing potential additional costs and effort to assess which measurement basis is appropriate for each asset or class of assets, or to reassess the appropriate measurement basis when there is a change in how an entity uses an asset; and
- (c) reporting to users of financial statements of public sector entities current values based on mixed measurement bases, which would reduce the comparability and understandability of the totals reported.

Staff of the Australian Bureau of Statistics have informed the AASB that they consider fair value is the valuation basis most consistent with the GFS principle of market valuation. Any change from measuring assets at fair value might require data providers to keep separate records in order to provide the required GFS data. Since GFS is used internationally, this issue would be relevant across IPSASB jurisdictions in which revaluations of non-financial assets are undertaken for financial reporting, not just in Australia.

#### ***Identifying market participants and the highest and best use of a specialised asset***

Two of the key issues on which fair value guidance has been requested are:

- (a) identifying the market participants for the purchase or sale of a specialised operational capacity asset, in particular when an asset has legal restrictions (i.e. legal restrictions imposed on the use of an asset and/or the prices that may be charged for using an asset); and
- (b) identifying the highest and best use of a specialised asset, including how the physical characteristics

of an asset and legal restrictions should be considered when determining an asset's highest and best use.

The AASB has interpreted from ED 77 para. BC29 as indicating that the IPSASB decided fair value is not applicable to the current value measurement of operational capacity assets because it noted concerns from its constituents that the 'maximizing the use of market participant data'<sup>1</sup> and 'highest and best use' concepts are generally not applicable to such assets. However, the AASB observed that the IASB explained in its Basis for Conclusions on IFRS 13, in paras. BC78–BC79, how to consider market participant assumptions when measuring the fair value of a specialised non-financial asset, albeit in the context of a for-profit entity holding the asset for its financial capacity [emphasis added]:

BC78 Some respondents to the exposure draft expressed concerns about using an exit price notion for specialised non-financial assets that have a significant value when used together with other non-financial assets, for example in a production process, but have little value if sold for scrap to another market participant that does not have the complementary assets. They were concerned that an exit price would be based on that scrap value (particularly given the requirement to maximise the use of observable inputs, such as market prices) and would not reflect the value that an entity expects to generate by using the asset in its operations. However, IFRS 13 clarifies that this is not the case. In such situations, the scrap value for an individual asset would be irrelevant because the valuation premise assumes that the asset would be used in combination with other assets or with other assets and liabilities. Therefore, an exit price reflects the sale of the asset to a market participant that has, or can obtain, the complementary assets and the associated liabilities needed to use the specialised asset in its own operations. In effect, the market participant buyer steps into the shoes of the entity that holds that specialised asset.

BC79 It is unlikely in such a situation that a market price, if available, would capture the value that the specialised asset contributes to the business because the market price would be for an unmodified asset. When a market price does not capture the characteristics of the asset (eg if that price represents the use of the asset on a stand-alone basis, not installed or otherwise configured for use, rather than in combination with other assets, installed and configured for use), that price will not represent fair value. In such a situation, an entity will need to measure fair value using another valuation technique (such as an income approach) or the cost to replace or recreate the asset (such as a cost approach) depending on the circumstances and the information available.

Para. 29 of IFRS 13 and para. BC71 of the Basis for Conclusions on IFRS 13 provide guidance on identifying an asset's highest and best use [emphasis added]:

29 Highest and best use is determined from the perspective of market participants, even if the entity intends a different use. However, an entity's current use of a non-financial asset is presumed to be its highest and best use unless market or other factors suggest that a different use by market participants would maximise the value of the asset.

BC71 IFRS 13 does not require an entity to perform an exhaustive search for other potential uses of a non-financial asset if there is no evidence to suggest that the current use of an asset is not its highest and best use.

Based on the IFRS 13 requirements and the Basis for Conclusions quoted above, the AASB made the following observations regarding the 'hypothetical market participants' and 'highest and best use' concepts in respect of specialised operational capacity assets:

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1 This phrase differs slightly from the words used in IFRS 13 para. 61, which refer to "maximising the use of relevant observable inputs".

- (a) because ‘the market participant buyer steps into the shoes of the entity that holds that specialised asset’, in the context of specialised assets, market-participants-based assumptions under fair value would be the same as the assumptions of the NFP public sector entity holding the specialised asset (interpreting IFRS 13 para. BC78). The AASB considered that a ‘market participant buyer stepping into the shoes of the NFP public sector entity holding the operational capacity asset’ obtains value from that asset:
  - (i) by providing needed services to beneficiaries; and
  - (ii) through financial support (in the form of rates, taxes, grants and appropriations) and through any user charges;
- (b) the current use of a specialised operational capacity asset is presumed to be its highest and best use, unless there is evidence that a different use by the NFP public sector entity holding the asset (as a market participant) would maximise the value of the asset (IFRS 13 paras. 29 and BC 71); and
- (c) the income or the cost approach may be more appropriate than the market approach to measure the fair value of a specialised operational capacity asset because a specialised asset should not be measured at its scrap value if the asset contributes more to an entity when used together with other assets. The market approach would reflect the selling price of the asset to an entity without the complementary assets (IFRS 13 paras. BC78 and BC79).

The AASB is considering whether to develop NFP entity fair value guidance based on these observations.

#### ***Other aspects of fair value***

Australian NFP public sector stakeholders have also requested the AASB to provide guidance clarifying the following issues in measuring the fair value of operational capacity assets under AASB 13:

- (a) how restrictions imposed on the use of an asset and/or the prices that may be charged for using an asset should be considered when measuring fair value;
- (b) the assumed location of an operational capacity asset;
- (c) the nature of component costs to include in an asset’s current replacement cost;
- (d) whether the current replacement cost of a self-constructed asset should include borrowing costs; and
- (e) consideration of obsolescence.

The AASB noted that Appendix B of ED 77 proposes application guidance on these issues, albeit in the context of current operational value. The AASB’s views on these issues raised in Specific Matters for Comment 5–6 of ED 77 are contained in Appendix C of this submission.

## APPENDIX B

### The AASB's responses to selected Specific Matters for Comment in ED 76

The AASB's views on Specific Matters for Comment 3–5 in ED 76 are set out below.

**Specific Matter for Comment 3:**

Do you agree with the proposed inclusion of current operational value as a measurement basis for assets in the Conceptual Framework?

If not, why not?

*The Exposure Draft includes an Alternative View on current operational value.*

The inclusion of current operational value as a measurement basis, both in a revised IPSASB Conceptual Framework and in an IPSAS on Measurement, is premised on two IPSASB decisions about how to measure the current value of operational capacity assets on which the AASB wishes to comment, namely:

- (a) fair value is an inappropriate measurement basis; and
- (b) replacement cost would be an inappropriate alternative to fair value.

The AASB's comments on (a) are set out below. Its comments on (b) are included in its response to Specific Matters for Comment 5 on ED 76.

The AASB recommends that the IPSASB expands its explanation of why it concluded that fair value is appropriate for assets held primarily for their financial capacity, but inappropriate for operational capacity assets, to provide better justification for that conclusion. Without detailed illustrative examples, it is difficult to identify how current operational value should be measured (notwithstanding ED 77's proposed Implementation Guidance on the use of experts and the meaning of 'modern equivalent asset') and, particularly, how measurements of current operational value and fair value would differ.

Because of the insufficiency of the justification provided, the AASB is yet to be convinced that the current value of operational capacity assets held by public sector entities should be measured under the current operational value basis instead of the fair value basis. In particular:

- (a) the measurement objective for current operational value is not clearly stated in ED 76 and ED 77, particularly whether current operational value is meant to be limited to the entry price of an asset and, where not, what the nature of the measurement is;
- (b) if reflecting an asset's entry value is not the sole objective of current operational value, then fair value, which measures an asset's exit value and uses the same three measurement techniques as current operational value, could be applied. As discussed in Appendix A, the IASB provided guidance (in IFRS 13 and its Basis for Conclusions thereon) for identifying market participant buyers of a specialised asset and the highest and best use of an asset when measuring fair value; and
- (c) if reflecting an asset's entry value is the sole objective of current operational value, then applying replacement cost in the IPSASB's existing Conceptual Framework would appear to achieve this objective better than the proposed current operational value measurement basis (since para. 6 of ED 77 defines entry price as "the price paid to acquire an asset ... in an exchange transaction" [emphasis added]. In this respect, the AASB considers that the alternative definition proposed in para. AV4 of ED 77 would appear to be a clearer and more accurate definition, because it clearly states that current operational value is "the cost to replace the service potential embodied in an asset at the measurement date".

**Specific Matter for Comment 4:**

It is proposed to substitute a general description of value in use (VIU) in both cash-generating and non-cash-generating contexts, for the previous broader discussion of VIU. This is because the applicability of VIU is limited to impairments. Do you agree with this proposed change?

If not, why not? How would you approach VIU instead and why?

The AASB considers there is merit in retaining value in use as a measurement basis in the IPSASB Conceptual Framework. The AASB's reasons for its views are:

- (a) value in use is identified as a measurement basis in the revised IASB *Conceptual Framework for Financial Reporting* (IASB Conceptual Framework), despite also being limited in IFRS to impairments of assets. In fact, this is the only measurement basis in the IASB Conceptual Framework without a parallel or equivalent measurement basis in the proposed updated IPSASB Conceptual Framework;
- (b) in relation to (a), the AASB is unaware of a public-sector-specific reason to differ from the IASB Conceptual Framework in this regard;
- (c) impairment concepts (including value in use) play an important role in understanding the measurement concepts proposed in ED 77. For example, ED 77 para. B11 would require an entity to consider impairment in measuring an asset's current operational value when surplus capacity exists. Retaining value in use in the IPSASB Conceptual Framework would support developing any requirements for value in use measurements in other IPSAS based on consistent concepts. In this regard, some important modifications of IFRS in IPSAS concern the measurement of impairments; therefore, omitting value in use as a measurement basis might detract from the central role of the IPSASB Conceptual Framework; and
- (d) it seems potentially confusing to exclude value in use from the measurement bases identified in the updated IPSASB Conceptual Framework but retain discussion of value in use in the Measurement chapter.

**Specific Matter for Comment 5:**

Noting that ED 77, *Measurement*, proposes the use of the cost approach and the market approach as measurement techniques, do you agree with the proposed deletion of the following measurement bases from the Conceptual Framework:

- Market value—for assets and liabilities; and
- Replacement cost—for assets?

If not, which would you retain and why?

**Deletion of market value**

The AASB agrees with the proposed deletion of market value from the IPSASB Conceptual Framework as a measurement basis for assets and liabilities in light of the IPSASB's proposals to:

- (a) include fair value as a measurement basis in the Conceptual Framework; and
- (b) conform the definition of fair value – both in the IPSASB Conceptual Framework and the Measurement IPSAS – to that used in IFRS 13, thus removing the need to use market value and thereby avoiding potential confusion from including the IPSAS definition of fair value in the Conceptual Framework rather than the definition in IFRS 13 (refer paras. BC7.31 and BC7.59–BC7.60 of the Basis for Conclusions on ED 76, and paras. BC51–BC54 of the Basis for Conclusions on ED 77).

### Deletion of replacement cost

The AASB considers that the reasons given in ED 76 and ED 77 for proposing to remove replacement cost as a current value measurement basis should be expanded to provide better justification for that proposal. Based on the reasons presented, a convincing argument has not been provided for removing replacement cost. This AASB view reflects the following aspects:

- (a) current operational value is meant to reflect an entry price (ED 77 para. B9);
- (b) the IPSASB's proposals include using the cost approach as a measurement technique to estimate current operational value (ED 77 para. 38); and
- (c) the IASB includes current cost (as a complement to fair value and value in use) – which is similar to replacement cost – as a current value measurement basis in its Conceptual Framework.

ED 76 para. BC7.33 states that the IPSASB considered that replacement cost is an appropriate measurement basis for specialised assets, but also that current operational value is a more versatile measurement basis as it can be applied to both specialised and non-specialised assets.

ED 76 para. BC7.27 states that the current operational value of a non-specialised asset can be supported by market-based measurement techniques with similarities to market value; whereas, the current operational value of a specialised asset can be determined using other measurement techniques.

The AASB interprets the IPSASB's rationale for not supporting replacement cost as a measurement basis, noted in the first sentence of the paragraph immediately above, to imply replacement cost is inapplicable to assets valued using market techniques. That is, the IPSASB's rationale seems to regard replacement cost and market prices as mutually exclusive values. If that is the IPSASB's reasoning, the AASB would not support it.

The AASB considers the notion of replacement cost (whether measured under the cost approach to fair value or under another measurement basis) can be applied to any asset, even when the asset's price is observable in an active market. Prior to adopting IFRS in Australia, various Australian public sector entities adopted a current-cost-based revaluation model (using guidelines similar to, or concordant with, Australian Statement of Accounting Practice SAP 1 *Current Cost Accounting*), under which the 'current cost' of some assets was measured using observable market prices or other observable market inputs. Therefore, the AASB considers that the notion of replacement cost is sufficiently robust to be applied to assets that are, or are not, traded in an active market.

If fair value is not adopted for measuring the current value of operational capacity assets, an important advantage of retaining replacement cost as a current value measurement basis in the IPSASB Conceptual Framework, and including it in the IPSAS on Measurement, would be that many preparers, valuers and auditors of financial statements of public sector entities are familiar with replacement cost in the existing IPSASB Conceptual Framework and the existing role of depreciated replacement cost as a measure of fair value<sup>2</sup> in IPSAS 17 *Property, Plant and Equipment* (para. 48). Adopting a new measurement basis such as current operational value would involve those practitioners developing new measurement techniques and identifying exactly how current value measurements of operational capacity assets would change. This would be difficult in the absence of detailed illustrative examples of how to measure an asset's current operational value. In addition, if current operational value was intended to measure an asset's current entry value, it would seem that its differences from replacement cost should be minimal, in which case it is difficult to envisage how the benefits of changing to a subtly different current value measurement basis for operational capacity assets would exceed the resulting costs.

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2 Albeit, applying the cost approach involves using 'current replacement cost' (CRC) rather than 'depreciated replacement cost' (DRC). Replacing 'DRC' with 'CRC' would remove the potential for confusion regarding the distinction between those terms.

## APPENDIX C

### The AASB's responses to selected Specific Matters for Comment in ED 77

The AASB's views on Specific Matters for Comment 5–9 in ED 77 are set out below.

**Specific Matter for Comment 5:**

Do you agree current operational value is the value of an asset used to achieve the entity's service delivery objectives at the measurement date?

If not, please provide your reasons, stating clearly what principles more appropriate for the public sector, and why.

*The Exposure Draft includes an Alternative View on current operational value.*

**Specific Matter for Comment 6:**

Do you agree the proposed definition of current operational value and the accompanying guidance is appropriate for public sector entities (Appendix B: Current Operational Value)?

If not, please provide your reasons, stating clearly what definition and guidance is more appropriate, and why.

*The AASB's comments on the proposed core principle of current operational value (Specific Matter for Comment 5) and how the proposed definition of current operational value encapsulates that core principle (Specific Matter for Comment 6) are set out jointly below in Part A of the AASB's comments on those Specific Matters for Comment.*

*The AASB's comments on the proposed accompanying guidance on the cost approach under current operational value in Appendix B of ED 77 (Specific Matter for Comment 6) are set out below in Part B of the AASB's comments on those Specific Matters for Comment.*

**Part A: Proposed core principle and definition of 'current operational value'**

***Measurement objective and definition of current operational value***

The AASB considers that the meaning of current operational value warrants further clarification. Without further clarification, it is difficult to identify the measurement objective of current operational value and how it should be applied in all circumstances. Consequently, the AASB is unable to provide a definite answer on whether it agrees with current operational value. However, as mentioned in the covering letter in this submission, the AASB is not convinced that current operational value is preferable to fair value as a current value measurement basis for operational capacity assets.

ED 77 para. 25(a) states that current operational value is an entry value. Similarly, ED 77 para. B2(a) states that: "... current operational value reflects the amount an entity would incur at the measurement date to acquire its existing assets to be able to continue to achieve its present service delivery objectives ..." [emphasis added]. This states that current operational value reflects an asset's replacement cost.

However, ED 76 and ED 77 rejected replacement cost (and current cost in the IASB Conceptual Framework) as a possible alternative current value measurement basis to fair value for operational capacity assets. This indicates a measurement basis other than replacement cost would sometimes be used, but the Exposure Drafts do not identify the extent to which (or the circumstances in which) current operational value measurements would differ from replacement cost. It also implies a measurement objective other than replacement cost for some operational capacity assets, without identifying what that alternative objective might be. This is because the proposed definition of current operational value, as stated in ED 77 para. 6 ("the value of an asset used to achieve the entity's service delivery objectives at the measurement date") does not specify the type of 'value'.

Because ED 77 para. B2 states that “current operational value measures the value to the entity of an asset ...” [emphasis added], and ED 76 and ED 77 reject fair value (a market exit price) and replacement cost (a market entry price) as the current value measurement basis for operational capacity assets, a potential implication is that the Exposure Drafts propose some kind of intrinsic value measure of service potential for operational capacity assets. The AASB would not support using an intrinsic non-market current value measure because market prices are more objective and easier for users of financial statements to understand.

Having regard to paras. 25(a) and B2(a) of ED 77, if current operational value is intended by the IPSASB to be solely an entry value, the AASB would consider the permissibility of using the income approach to estimate an asset’s current operational value to be potentially inconsistent with that intention. The AASB supports the observations in the Alternative View in ED 77 (paras. AV11 and AV13) that using the income approach would result in an exit value that is generally inconsistent with the concept of the cost to replace the service potential embodied in the asset. Para. 6 of ED 77 defines entry price as “the price paid to acquire an asset ... in an exchange transaction” [emphasis added].

If the sole measurement objective of current operational value is to reflect an entry value of the asset, it would appear that the alternative definition proposed in para. AV4 of ED 77 might be closer aligned to that measurement objective, because the alternative definition clearly states that current operational value is “the cost to replace the service potential embodied in an asset at the measurement date” [emphasis added].

#### ***Current value measurement disregards an asset’s potential alternative uses***

Another potential ambiguity that might warrant clarification concerns the proposals that current operational value:

- (a) disregards potential alternative uses and any other characteristics of the asset that could maximise its market value (ED 77 para. B4); yet
- (b) “... provides a useful measure of the resources available to provide services in future periods ...” (ED 76 para. 7.53, emphasis added).

The AASB recommends that the IPSASB clarifies whether the phrase “resources available to provide services in future periods” in ED 76 para. 7.53 is meant to include the asset’s residual value (i.e. its potential to be sold for cash at the end of its useful life and be reinvested in other stores of service potential). Such an interpretation might be construed from the IPSASB’s replacement cost measurement basis in its existing Conceptual Framework, which the IPSASB treats in ED 76 para. BC7.33 as appropriate for specialised assets. Para. 7.37 of the IPSASB Conceptual Framework states that an asset’s replacement cost includes the amount that an entity will receive from disposal of the asset at the end of its useful life.

For example, those who interpret “resources available to provide services in future periods” in ED 76 para. 7.53 as including the asset’s residual value might consider that the current operational value of a post office (an operational capacity asset) in the centre of a large city with the potential to be used as a commercial building with a high resale value should exceed the current operational value of another post office located in an outer suburb with few potential alternative uses and a low resale value. Even if the two post offices have an identical capacity to provide postal services and identical remaining useful lives, the post office located in the city centre might be regarded as having the potential to provide more services (directly and indirectly) to the entity because the entity could choose to sell it and reinvest the cash in other post offices.

A related issue is that some may regard the stated objective of current value measurement in ED 76 para. 7.53, namely, to provide a “useful measure of the resources available to provide services in future periods”, as implying that the current measurement of an operational capacity asset should be based on the use of the asset that would maximise the value of the asset to the entity, in contrast with the rejection of the ‘highest and best use’ concept in ED 77. For example, a non-specialised building with harbour views currently being used by a public sector entity as a storage space has an alternative use as

a residential property without requiring a change of permitted use. If the market approach were applied to measure the building's current operational value, the building would be measured having regard to market prices of comparable buildings, which would be likely to be residential buildings.

### ***Current operational value of restricted operational capacity assets***

ED 77 para. B14(b) proposes that, 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 using the cost approach, at the price of an equivalent unrestricted asset without a reduction for the restrictions. Without greater elaboration, the AASB cannot identify the extent to which such a restricted asset's fair value would differ from its current operational value. The AASB's comments regarding the current value measurement of restricted assets are expressed mainly in the context of fair value. Under IFRS 13 para. 28(b), the highest and best use of a non-financial asset takes into account any legal restrictions on the use of the asset that market participants would take into account when pricing the asset.

The topic of fair value measurement of restricted land held by an NFP public sector entity for its operational capacity has attracted extensive debate in the AASB's FVM project. A key issue that has been debated is whether public-sector-specific restrictions (i.e. legally enforceable public-sector-specific restrictions over the use of land and/or the prices that may be charged for using that land,<sup>3</sup> such as a legal restriction that land in a prime location must be used solely for a naval base) that would transfer to market participants<sup>4</sup> would affect market participants' pricing of the restricted operational capacity land. A related subject of debate is whether this would depend on the approach adopted to estimate the land's fair value (in particular, whether the market approach or cost approach is applied). This seems to depend on whether the operational capacity land being measured is regarded as a specialised asset.

After conducting wide-ranging outreach, including targeted outreach activities and receiving feedback on AASB Invitation to Comment ITC 45 (on IPSASB ED 76 and ED 77), the AASB noted two views from Australian stakeholders.

#### **The minority view of Australian stakeholders**

A minority of Australian stakeholders who commented on this issue agree with the proposal in ED 77 para. B14(b). Their support was based on:

- (a) their view that when operational capacity assets are subject to public-sector-specific restrictions but an equivalent restricted asset is not obtainable in the marketplace at the measurement date for a price supported by observable market evidence, the restrictions cause the assets to be specialised; and
- (b) their interpretation of the IASB's views in IFRS 13 para. BC 78 and BC79 (quoted in Appendix A), regarding fair value measurement of specialised assets, that:

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3 That is, restricted for the public-sector-specific purpose of holding the entity's parcel of land being valued. The equivalent 'unrestricted' land might be restricted in use by zoning other than for a public-sector-specific purpose (e.g. it might be zoned for residential, commercial or light industrial use) or by an easement providing access to other services. This notion of 'restriction' is similar to that in ED 77 para. B13, the main exception being the addition here of the explicit reference to restrictions being 'public-sector-specific' (see also the related comment in the 'Other Matters' section of this Appendix).

4 The section on restricted assets in the Illustrative Examples accompanying IFRS 13 indicates that restrictions that would affect market participants' pricing of restricted assets are limited to those that are a characteristic of the asset (and thus are not specific to the entity holding the asset) and therefore would transfer to the market participant in a sale of that asset (e.g. Example 8, para. IE28 and Example 9, para. IE29).

- (i) many specialised assets might have little value if sold for scrap, but would have a significant value when used together with other non-financial assets; and
- (ii) the cost or income approach might be more appropriate in measuring an asset's fair value when the market price of the asset represents the use of the asset on a stand-alone basis rather than in combination with complementary assets.

Further, those stakeholders consider that, because the asset is held for its operational capacity, it would generally be inappropriate to apply the income approach as an alternative to the market approach and, consequently, the cost approach should be used to measure the fair value of the restricted operational capacity asset.

Those stakeholders consider that public-sector-specific restrictions cause the asset to be specialised because the effects of such restrictions are that:

- (a) unless the restrictions are lifted, the legally permissible use of the asset is limited to its current use. In this case, consistent with the IASB's views in IFRS 13 paras. BC 78 and BC79, the asset might have little value if sold (because of the restrictions on the asset's use or pricing), but would have a significant value when used together with other non-financial assets. Therefore, there is a lack of market inputs to support estimates of fair value using the market approach;
- (b) public sector market participant buyers would be prepared to pay (and in turn be compensated indirectly and directly through financial support e.g. in the form of rates, taxes, grants and appropriations and any user charges) for the asset assuming they will use it in combination with complementary assets to provide necessary services; and
- (c) for the reason in paragraph (b) immediately above, the highest and best use of the restricted asset would be obtained only by a market participant buyer stepping into the shoes of the entity holding the restricted asset, which is the viewpoint expressed by the IASB in respect of specialised assets in IFRS 13 paras. BC78 and BC79. Therefore, there is a scarcity of market inputs that would reflect the price that market participants would be prepared to pay for the restricted asset in its highest and best use.

IFRS 13 and ED 77 define the cost approach as “a valuation technique that reflects the amount that would be required currently to replace the service capacity of an asset ...” [emphasis added]. Consistent with the IPSASB's view explained in ED 77 paras. B17 and BC44, this minority of stakeholders commented that if the cost approach is applied, the current value measurement of a restricted asset would not be reduced for the effect of restrictions. This is because if an equivalent restricted asset is not obtainable in the marketplace, the entity would need to purchase an equivalent unrestricted asset to continue delivering services, and the existence of a restriction does not affect the price of this purchase.

This minority of stakeholders also argue that public-sector-specific restrictions over land would cause that land to be a specialised asset, because such a restriction would cause the highest and best use of the asset to only be its current use by the public sector entity holding the asset.

In its initial deliberations of this issue, the AASB had tentatively supported the above-mentioned views held by the minority of stakeholders, including that it would generally be inappropriate to apply the income approach as an alternative to the market approach; consequently, the AASB had tentatively decided to propose guidance that the cost approach should be used to measure the fair value of restricted operational capacity assets.

#### **The majority view of Australian stakeholders**

The AASB noted that a majority of Australian stakeholders who commented on this issue consider that:

- (a) restricted operational capacity assets' improvements are specialised assets, but restricted operational capacity land is not a specialised asset; and
- (b) consequently, there is no reason why restricted operational capacity land should not generally be measured using the market approach.

Those stakeholders disagree with applying the cost approach to measure the fair value of restricted operational capacity land because:

- (a) they do not consider land to be a specialised asset;
- (b) although an ‘equivalent’ parcel of land with the same restrictions (e.g. zoning restrictions) might not be obtainable in the marketplace at the measurement date for a price supported by observable market evidence, there are market transactions for other parcels of land that are suitable reference assets. Therefore, those stakeholders consider there are more relevant observable inputs for applying the market approach than the cost approach in measuring the fair value of restricted operational capacity land (consistent with the proposal in para. B23 of ED 77 to maximise the use of relevant observable inputs and minimise the use of unobservable inputs); and
- (c) many of them consider that restricted and unrestricted parcels of land cannot be equivalent assets because restrictions cannot be ignored when comparing land. That is, many Australian stakeholders do not agree with the notion of reference land being “equivalent, except for the effect of any restriction”, because public-sector-specific restrictions imposed on land are usually an inseparable characteristic of the land.

Accordingly, those stakeholders would be likely to disagree with the proposed non-mandatory implementation guidance in ED 78 *Property, Plant and Equipment* para. IG19(b), which states: “Land under or over infrastructure assets ... it will often be the case that the market approach will be challenging to apply, and that the asset will be more easily valued using the cost approach.”

In respect of specialised operational capacity improvements on land (e.g. a hospital building), including restricted improvements, a majority of Australian stakeholders would support applying the cost approach to measure their fair value. This is because identical or comparable assets might not be available in the marketplace and, as stated in IFRS 13 para. BC79 (discussed in Appendix A), a market price (using the market approach) – if available – might not capture the characteristics of the specialised asset and therefore might not represent fair value.

This majority of stakeholders argue that the fair value estimate (i.e. current replacement cost) of restricted improvements over or under land generally should not differ according to whether the improvements are subject to public-sector-specific restrictions. This is because those improvements generally are specialised and do not have a superior cash-generating ability or other utility in another use. Consequently, the cost approach is applied notwithstanding that the market approach is generally applied to measure the fair value of the land (whether restricted or unrestricted) under or over the specialised operational capacity improvements.

In contrast, this majority of stakeholders consider that the market value of land with a public-sector-specific restriction would be less than the market value of land that can provide the same services but is ‘unrestricted’ (i.e. is not subject to a public-sector-specific restriction). They consider that, if restricted land’s fair value was measured without an adjustment to the current price of equivalent unrestricted land, the measurement would lack comparability because it would depict different assets as having the same value. Thus, they would differ from the proposal in ED 77 para. B14(b) of measuring the land’s current value without a reduction for the restrictions.

Based on targeted outreach with valuers, financial statements preparers and auditors, the AASB noted that a clear majority of stakeholders undertake fair value measurements of restricted operational capacity land using the market approach. Under the market approach, the fair value measurements are less than the market price of equivalent unrestricted land because of the effect of the restrictions.

Australian stakeholders have also advised the AASB that different valuers use different methods in calculating the adjustments to be deducted from the market price of unrestricted land used as a reference asset, for example:

- (a) using the price of nearby unrestricted land and explicitly deducting an adjustment for the effect of the restriction (explicit adjustment); or

- (b) using the price of land with a much lower intensity of use – and, consequently, a much lower value – than that of nearby unrestricted land and not explicitly deducting an adjustment for the effect of the restriction because it is implicitly taken into account by using cheaper land in a lower-intensity-of-use location as a reference asset (implicit adjustment).

### **The AASB's observations**

Notwithstanding the interpretation of IFRS 13 paras. BC78–BC79 by a minority of stakeholders, in which they conclude that the cost approach would often be appropriate in measuring the fair value of restricted operational capacity land, the AASB observed that para. B23 of ED 77 proposes to require an entity to select measurement techniques:

- (a) that are appropriate in the circumstances;
- (b) for which sufficient data are available to measure current operational value; and
- (c) maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

IFRS 13 para. 61 has the same requirement for measuring an asset's fair value. A majority of Australian stakeholders commented that the ability to apply judgement in the circumstances in choosing among the market approach, income approach and cost approach (or a combination of those approaches) works well for measuring the fair value of an asset.

Despite the debate, feedback from most Australian stakeholders in targeted outreach and feedback on tentative Board decisions or ITC 45 indicated that, in practice, the fair value of each class of operational capacity assets is being measured using a largely consistent approach – that is:

- (a) for restricted operational capacity land, the market approach is used, and an adjustment is deducted to reflect the effect of restrictions<sup>5</sup> (although, as noted above, different methods are being used in applying the market approach); and
- (b) for restricted operational capacity improvements on land, an adjustment is not deducted to reflect the effect of restriction because the cost approach is used.

Although the AASB had reached a tentative view in 2019-20 to provide further guidance on the fair value measurement of restricted operational capacity assets that the cost approach should be used under certain circumstances, the AASB:

- (a) noted that a majority of Australian stakeholders do not consider restricted operational capacity land to be a specialised asset (and therefore do not consider IFRS 13 paras. BC78–BC79 to be applicable to such an asset); and
- (b) considers that determining appropriate valuation techniques for measuring the current value of an asset is best regarded as belonging within the role of valuation professionals and should not be mandated in accounting standards. Unless there is significant diversity in applying accounting principles in practice, there is no clear case for mandating the use of a particular valuation technique in measuring the current value of a particular asset or asset class.

### **Part B: Proposed accompanying guidance on the cost approach under current operational value**

#### ***Nature of component costs to include in an asset's current replacement cost***

ED 77 paras. B35(b)–B35(c) propose that some costs might not need to be included when considering the cost of a modern equivalent asset to estimate the current operational value of an asset.

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<sup>5</sup> For example, it was noted that the fair value of land under a hospital or a school would typically include a 20%–30% adjustment and land under reservoirs would typically include a 90% adjustment.

The AASB has received requests from Australian stakeholders for more general guidance on the nature of the component costs to include in the calculation of an asset's current replacement cost in the context of fair value. This includes guidance on whether:

- (a) once-only costs (e.g. formation costs for constructing a road) should be included;
- (b) the 'least costly manner' concept (consistent with the proposal in ED 77 para. B18) would include higher costs than those theoretically achievable where a more costly mode of replacement is necessary to meet community expectations;
- (c) it should be assumed that the site on which an asset would be replaced in the hypothetical replacement transaction is in an area with a similar degree of development, taking into account other facilities that would be disturbed upon replacement of the asset (e.g. drainage works disturbed upon replacing a road), necessitating the incurrence of make-good costs for those disturbed facilities; and
- (d) in relation to (c), if it were concluded that an asset's current replacement cost should include make-good costs for disturbing other facilities, whether the answer would depend on whether the facilities being disturbed are controlled by the public sector reporting entity or another entity.

The AASB considers that the IPSAS on Measurement should include general principles and illustrative examples for how to address these issues, in view of their pervasiveness in the NFP public sector. The AASB also considers that these issues affect the measurement of current replacement cost under the cost approach in the context of measuring either fair value or current operational value.

In view of the ambiguous nature of the concepts underlying current operational value, the AASB is unsure whether the treatment of the issues noted above should be the same for current replacement cost measurements under fair value and current operational value. The AASB notes below the tentative conclusions it has reached about these issues in the context of fair value measurement of operational capacity assets (as part of its FVM project):

- (a) the current replacement cost of an asset includes all necessary costs intrinsically linked to acquiring the asset at the measurement date (which would include the costs mentioned in ED 77 paras. B35(a)–B35(c)); and, consequently
- (b) a not-for-profit public sector entity should assume that the asset presently does not exist and needs replacing in its current environment. Therefore, the asset's current replacement cost should:
  - (i) include costs for land or permanent works, despite those components not being expected to be replaced, because current replacement cost assumes hypothetical replacement of the asset being measured, and is not limited to costs of replacements actually expected to be incurred in the future; and
  - (ii) take into account any make-good costs that must be incurred for surrounding assets of another entity disturbed when the entity's asset is replaced.

The AASB has yet to decide whether to develop fair value guidance based on these tentative views.

The AASB considers that 'once-only' costs should be included in the measurement of current replacement cost. This is because estimates of current replacement cost assume a hypothetical replacement transaction,<sup>6</sup> implicitly assuming that the entity (or a market participant buyer, in the context of fair value) does not possess the asset and is measuring the cost currently needed to be incurred to acquire an asset of equivalent service potential. Therefore, the components of an asset's

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6 This is consistent with the more general point in para. BC30 of the IASB's Basis for Conclusions on IFRS 13 that: "Like the previous definition of fair value, the revised definition assumes a hypothetical ... exchange transaction."

current replacement cost are not limited to actual replacement transactions expected to occur in the future. To conclude otherwise would logically imply that the current value of an asset measured under the cost approach would be zero if, at the measurement date, the asset is not expected by the entity (or a market participant buyer, in the case of a fair value measurement) to be replaced at the end of its useful life.

The AASB also considers that, in the measurement of current replacement cost, the ‘least costly manner’ principle should be applied in the context of the entity’s mode of replacement in the ordinary course of operations, which would take into account community expectations, operational mandates or other imperatives to incur costs additional to the theoretically cheapest-legally-permitted costs to the entity to maintain an adequate quality of services.

For example, where a replacement of the surface of a road would, in the ordinary course of operations, occur at night rather than during daytime to minimise disruption to drivers, the more costly night costs should be included in the asset’s replacement cost rather than the lower daytime costs. This is because it would be infeasible to avoid paying the higher night cost because replacement of the surface of the road in the daytime would be incompatible with community expectations on continuity of service. In the context of fair value, the AASB notes that a hypothetical market participant would be likely take into account the more costly night costs when pricing the asset.

#### ***Whether the current replacement cost of a self-constructed asset should include borrowing costs***

The AASB disagrees with the statement in ED 77 para. B35(a) that: “ ... A large site may have been developed in phases. ... If the entity does not capitalize borrowing costs in accordance with IPSAS 5, *Borrowing Costs*, the entity should disregard any financing costs in measuring the modern equivalent asset.” The AASB considers that the accounting policy choice regarding capitalisation of borrowing costs at the asset’s initial recognition under IPSAS 5 is irrelevant to how financing costs should be treated when subsequently measuring an asset that necessarily takes a substantial period of time to get ready for its intended use.

The current value of an asset is a current market phenomenon, which is not affected by an entity’s accounting policy choices concerning capitalisation of borrowing costs.

#### ***Consideration of obsolescence when determining current operational value***

The AASB concurs with the comments in para. AV16 of the Alternative View of Mr. Beardsworth and Mr. Blake on ED 77, particularly their comments that they:

“... are concerned that ED 77 does not provide guidance on (a) how to classify a reduction in an asset’s use resulting from a reduction in demand for its services as either a potential source of impairment or a potential reduction in the asset’s current operational value, and (b) whether a difference in classification might cause a difference in the asset’s carrying amount. ... [and] consider that this lack of clarity could lead to current operational value being overstated or understated, depending upon how an entity interprets the proposed requirements.”

The AASB recommends that the IPSASB provides greater clarity regarding whether a loss of utility of an asset should be treated as:

- (a) surplus capacity, as described in ED 77 paras. B10 and B11 (which is not adjusted for when measuring the asset’s current operational value); or
- (b) an indication of economic obsolescence, as described in ED 77 para. B36(c) (which is deducted when measuring the asset’s current operational value); or
- (c) an indication of impairment.

Specifically, in the example in ED 77 para. B10, the AASB requests the IPSASB to clarify why 20% of the building being left vacant would not be considered an indication of economic obsolescence or an indication of impairment; and thus, why the current operational value of the asset should not be reduced

accordingly. ED 77 has not adequately explained why current operational value of an asset assumes that the asset is used to its full capacity when there is apparent excess capacity.

Regarding the comments about severable surplus capacity in para. AV16 of the Alternative View on ED 77, some Australian stakeholders commented that bifurcating severable surplus capacity from an asset should occur only if and when:

- (a) the surplus capacity is presently severable from the rest of the asset; and
- (b) the entity has a plan to sell or lease that severable surplus capacity part of the asset or at least declared by the entity to be surplus (and does not merely have the right to sell or lease the asset, as indicated in ED 77 para. AV17).

Some stakeholders proposing the criterion in point (b) above noted that it appears to be similar to the proposed requirement in para. 13 of IPSASB ED 79 *Non-Current Assets Held for Sale and Discontinued Operations* that an asset should not be classified as ‘held for sale’ until (among other criteria) management has committed to a plan to sell the asset and the asset is actively marketed for sale.

The AASB recommends that any consideration of severable surplus capacity addresses the relationship between the timing of identifying obsolescence in respect of non-severable surplus capacity and bifurcating severable surplus capacity, to ensure ‘mismatches’ do not occur.

**Specific Matter for Comment 7:**

Do you agree the asset’s current operational value should assume that the notional replacement will be situated in the same location as the existing asset is situated or used?

If not, please provide your reasons, stating clearly why the asset should be measured at a different value.

The AASB agrees with the proposed principle that an asset’s current operational value should assume that the notional replacement will be situated in the same location as the existing asset is situated or used. The AASB also holds this view for any current entry value, such as a fair value measurement calculated by applying the cost approach in IFRS 13/AASB 13.

The AASB supports this proposed principle because:

- (a) if property has a higher market value in its current location than feasible alternative locations, from the perspective of market participant buyers, the property provides superior services. That is, market participant buyers are prepared to pay a premium for the service capacity of the property in its existing location (e.g. office space in a central business district location provides greater service capacity than office space in an inner suburb by, for example, having greater proximity to stakeholders and urban infrastructure, and by assisting the entity to attract and retain staff);
- (b) it would generally be very difficult to identify which location, of a potential variety of alternative locations with possibly significantly different market prices of properties, might be used as the assumed alternative location; and
- (c) the additional cost of potentially preparing multiple valuations and due diligence assessments would be unlikely to be justified by the benefits to users of the financial statements.

The AASB notes that, in stakeholder outreach, it was advised that the majority of public sector stakeholders measuring non-financial assets at fair value by applying the cost approach in AASB 13 assume that the notional replacement will be situated in the same location in which the existing asset is situated or used. However, in practice there might be situations in which replacing an asset in the same location would be impossible. The AASB recommends that the IPSASB provides guidance on how to

determine the assumed location of the asset in this situation when estimating an asset's current operational value.

**Specific Matter for Comment 8:**

Do you agree the income approach is applicable to estimate the value of an asset measured using the current operational value measurement basis?

If not, please provide your reasons, stating clearly why the income approach is not applicable for measuring current operational value.

*The Exposure Draft includes an Alternative View on current operational value.*

As indicated in its response to Specific Matter for Comment 3 for ED 76 (in Appendix B), the AASB is not convinced that current operational value should be adopted as an alternative to fair value to measure the current value of operational capacity assets. The AASB also considers that, if fair value were adopted to measure operational capacity assets, an entity's selection of either the market approach, income approach or cost approach (or a combination of those approaches) should not be circumscribed in any way beyond the constraints of the general principles of IFRS 13.

As noted in Part A of the response to Specific Matters for Comment 5–6 for ED 77, the AASB considers it is unclear whether current operational value is solely intended to represent the asset's current entry value (paras. 25(a), B2(a) and B9 of ED 77) or to also include another value in particular circumstances.

If current operational value were solely intended to represent the asset's current entry value, the AASB would share the concerns raised by Mr. Beardsworth and Mr. Blake in para. AV14 of their Alternative View on ED 77 that the valuation resulting from applying the income approach might not reflect an entry price.

Para. BC47 of the IPSASB's Basis for Conclusions on ED 77 indicates the income approach would play a limited role in estimating an asset's current operational value. The AASB considers that:

- (a) the Basis for Conclusions should give greater emphasis to the income approach being inappropriate in most cases for estimating an asset's current operational value; and
- (b) clearer guidance on this limited role of the income approach should be included in the IPSAS on Measurement and not only acknowledging that limited role in the Basis for Conclusions.

**Specific Matter for Comment 9:**

In response to constituents' comment letters on the Consultation Paper, *Measurement*, guidance on fair value has been aligned with IFRS 13, *Fair Value Measurement* (Appendix C: Fair Value). Do you agree the guidance is appropriate for application by public sector entities?

If not, please provide your reasons, stating what guidance should be added or removed, and why.

The AASB agrees with the IPSASB's proposals in ED 77 that:

- (a) fair value is the appropriate current value measurement basis for non-financial assets held primarily for their financial capacity (although the AASB would not limit the application of fair value to those assets: this separate issue is addressed in the AASB's comments on Specific Matter for Comment 3 on ED 76); and
- (b) the definition of 'fair value' in IPSAS should conform to the definition of 'fair value' in IFRS 13 and guidance thereon should be consistent with the guidance on fair value in IFRS 13.

The AASB's reasons for supporting the IPSASB proposal noted in (a) above are that:

- (a) there does not appear to be a public-sector-specific characteristic of non-financial assets held primarily for their financial capacity that warrants differing from the current value measurement basis generally applicable in IFRS for non-financial assets (fair value); and

- (b) the experience of Australian public sector entities in applying fair value as the current value measurement basis for non-financial assets held primarily for their financial capacity is that it reports useful information for users of financial statements without creating issues involving diverse interpretation.

The AASB's reasons for supporting the IPSASB proposal noted in (b) above are that, as noted in para. BC54 of the IPSASB's Basis for Conclusions on ED 77:

- (a) it would avoid confusion about the meaning of 'fair value'; and  
 (b) it would support high quality current value measurements.

### **Other Matters**

As mentioned in its response to Specific Matters for Comment 5–6 for ED 77 (in Part A), the AASB considers that determining appropriate valuation techniques for measuring the current value of an asset is best regarded as belonging within the province of valuation professionals and should not be mandated in accounting standards. Therefore, the AASB does not support the proposals in ED 77 regarding current value measurement of restricted assets. However, if the IPSASB adopts those proposals in the IPSAS on Measurement, the following concepts in ED 77 para. B13–B17 may benefit from further clarification.

### ***Meaning of 'restricted assets' and 'equivalent restricted assets'***

The AASB recommends clarifying:

- (a) whether the restrictions referred to in ED 77 paras. B13–B17 are intended to include restrictions that would apply to any holder of the asset or restrictions relating only to a public-sector-specific purpose. Since all land is subject to some form of zoning restrictions, arguably the reference to 'equivalent unrestricted asset (i.e. land)' in ED 77 para. B14(b) might have no practical application, if the meaning of 'equivalent unrestricted asset' excludes assets with zoning restrictions that restrict the use or sale of an asset for any holder of the asset;
- (b) the meaning of 'equivalent' in relation to the references to equivalent restricted or unrestricted assets in ED 77 para. B14(b). The AASB has received stakeholder comments on ED 77 expressing concern that, in the case of land held and zoned for a specialised purpose (e.g. education), where other nearby land zoned for that purpose is unavailable, it is unclear whether the 'equivalent' unrestricted land referred to in para. B14(b) might be nearby land zoned for residential, commercial or industrial purposes. The market values of these differently-zoned types of nearby land could vary widely; and
- (c) the contaminated asset example noted in ED 77 para. B15. Using a contaminated asset as an example of an 'equivalent asset', without elaboration, might cause confusion. If a provision for restoration of the asset is recognised as a liability, the contamination should not be taken into account when measuring the current operational value of the contaminated asset. Doing so would double-count the effect of the contamination. The AASB recommends clarifying this aspect.

### ***The use of the market approach is applicable only when an equivalent restricted asset is obtainable in an 'orderly market'***

ED 77 para. B14(a) stipulates that the current operational value of a restricted asset shall be measured using the market approach only if that equivalent restricted asset is obtainable in an orderly market for a price supported by observable market evidence.

Consistent with para. 7.28 of the existing IPSASB Conceptual Framework, ED 76 paragraph 7.40 describes an orderly market as "one that is run in a reliable, secure, accurate and efficient manner. Such markets deal in assets that are identical and therefore mutually interchangeable, such as commodities,

currencies, and securities where prices are publicly available. In practice few, if any, markets fully exhibit all of these characteristics, but some may approach an orderly market” (emphasis added).

In relation to restricted land, one could argue that no land is identical or interchangeable because each parcel is distinct from another parcel<sup>7</sup>. Under this view, it would mean that the current operational value of restricted land would not be measured using the market approach under any circumstance, because ED 77 para. B14(a) cannot be met as there is no identical or mutually interchangeable land. The AASB recommends that the IPSASB clarifies this proposed requirement.

From a consistency perspective, this appears to be the only proposed measurement requirement in ED 77 for which market evidence is required to be found in an ‘orderly market’, which also seems more restrictive than any requirement in IFRS 13. The IASB did not adopt the notion of orderly market in IFRS 13 (the definition of ‘orderly transaction’ in IFRS 13 does not refer to identical assets).

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7 For example, International Valuation Standard IVS 400 *Real Property Interests* states that: “Property interests are generally heterogeneous (ie, with different characteristics). Even if the land and buildings have identical physical characteristics to others being exchanged in the market, the location will be different.” (para. 50.1)