The Chartered Institute of
Public Finance & Accountancy

IPSASB

Exposure Draft 75, *Leases*

Exposure Draft 76, *Conceptual Framework Update: Chapter 7, Measurement of Assets and Liabilities in Financial Statements*

Exposure Draft 77, *Measurement*

Exposure Draft 78, *Property, Plant, and Equipment*

Exposure Draft 79, *Non-current Assets Held for Sale and Discontinued Operations*

A response from the Chartered Institute of Public Finance and Accountancy

25 October 2021

CIPFA, the Chartered Institute of Public Finance and Accountancy, is the professional body for people in public finance. CIPFA shows the way in public finance globally, standing up for sound public financial management and good governance around the world as the leading commentator on managing and accounting for public money.

Further information about CIPFA can be obtained at www.cipfa.org

Any questions arising from this submission should be directed to:

Kirsty Stanners
Head of Policy and Technical
CIPFA
Level 3 Suite D
160 Dundee Street
Edinburgh
EH11 1DQ
Email: kirsty.stanners@cipfa.org

Steven Cain
Technical Manager
CIPFA
77 Mansell Street
London
E1 8AN

Email: steven.cain@cipfa.org

Our ref: Responses/ 211025 SC0265

Exposure Draft 76, *Conceptual Framework Update: Chapter 7, Measurement of Assets and Liabilities in Financial Statements*

Exposure Draft 77, *Measurement*

Exposure Draft 78, *Property, Plant, and Equipment*

Exposure Draft 79, *Non-current Assets Held for Sale and Discontinued Operations*

CIPFA is pleased to present its comments on these exposure drafts which variously consider issues around the measurement of public sector assets and liabilities. These have been reviewed by CIPFA's Accounting and Auditing Standards Panel.

General comments

As noted in various responses to consultations, including IPSASB's consultation on its strategy and workplan, CIPFA strongly supports the approach which IPSASB has taken to maintaining alignment with international frameworks. The resulting standards promote comparable treatments with private sector entities for those transactions and balances for which the underlying substance is similar, and set out different but conceptually consistent specific treatments for circumstances with specifically public sector characteristics.

Measurement is a particularly important aspect of this approach, but the alignment of the IPSASB and IFRS frameworks in this area has been problematic for some time, due to the different and somewhat out of step timescales in which the IPSASB and IASB issued their pronouncements on their conceptual frameworks, and the issuance by IASB of its standard IFRS 13 which has had no counterpart in the IPSASB canon. The latter standard made the read across between the frameworks more difficult because IPSAS were grounded in an 'old' definition of fair value which encompassed both entry and exit values, while IFRS fair value was more focussed on exit value. The IPSASB adopted a variety of handling mechanisms to manage the difference in vocabulary, including using the term 'market value' in the Conceptual Framework. The IPSAS standards continued to function effectively and for the most part maintaining appropriate alignment with IFRS, mostly because in those circumstances where the approaches give different results there are public sector specific reasons which support the difference in treatment. However, it has become evident in the intervening period that the variance in terminology detracts from the understandability of both the IPSASB conceptual framework and the individual IPSAS standards.

Against this background, we would note that IPSASB's project on measurement is not primarily intended to change the substance of financial statements prepared under IPSAS, but to provide greater clarity in the framework which underpins the standards, to make the read across with IFRS clearer in those circumstances where treatments are very similar or identical, and to be clearer and more understandable in those situations where public sector specific considerations justify a different (but conceptually consistent) treatment.

This additional clarity also provides a basis for guidance around the application of the standards to more difficult categories of asset which are encountered in public sector contexts, such as heritage assets and infrastructure assets.

Specific comments on ED 76 and ED 77

CIPFA generally supports the positions taken by the IPSASB Board in ED 76 and we do not support the alternative view expressed in relation to the definition of current operational value.

In relation to ED 77 we have some observations on the extent of when the income approach may be appropriate, but we do not support the alternative view which suggests that it is never appropriate.

We would also note that in more difficult cases it is important to maintain a constructive dialogue with valuation professionals, who are particularly skilled in managing the complexities of the valuation process, but who need to be guided by the public sector accountants knowledge of the policy and service delivery contexts of assets to the extent that these are relevant. This may be particularly important in considerations of asset location.

Specific comments on ED 78

ED78 provides a good reframing of IPSAS 17 in line with the material in ED 76 and ED 77. The discussion of financial capacity and operational capacity is very helpful. CIPFA also supports the guidance for heritage assets and infrastructure assets.

Specific comments on ED 79

CIPFA supports the issuance of this standard and we agree with the proposals.

Detailed comments

Detailed comments on each of the SMCs are attached.

We hope this is a helpful contribution to the development of the revised and new pronouncements.

ANNEX A

ED 76 Specific Matters for Comment

Specific Matter for Comment 1 ED 76 proposes a measurement hierarchy. Do you agree with the three-tier hierarchy? If not, why not? How would you modify it?
CIPFA agrees with the proposed three-tier hierarchy in respect of subsequent measurement in the revised Chapter 7 of the Conceptual Framework. We believe that the three-tier hierarchy helps to clarify the measurement bases available should an entity chose the current value measurement model.
Specific Matter for Comment 2: Do you agree with the proposed inclusion of fair value as a measurement basis for assets and liabilities with the same definition as in IFRS 13, *Fair Value Measurement*, in the Conceptual Framework? If not, why not?
In line with our response to the Consultation Paper on Measurement, CIPFA agrees with the proposed inclusion of fair value as a measurement basis for assets and liabilities with the same definition as in IFRS 13, *Fair Value Measurement*, in the Conceptual Framework.
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?
CIPFA agrees with the proposed inclusion of current operational value as a measurement basis for assets and liabilities. It might be helpful to avoid using the term ‘value’ in the definition of current operational value as this may be confusing. We note that ‘value’ is not used in the definition of fair value which refers to ‘price to sell’. One approach might be to reframe the definition in terms of ‘worth to the entity’. While ‘worth to the entity’ is not as precise as ‘price to sell’ in some ways this may be an advantage. The term ‘worth to the entity’ has a strong read across to replacement cost given that for assets which the entity would replace if lost, the cost of replacement is a very relevant measure. At the same time, ‘worth to the entity’ encompasses other value providing factors such as market valuations and income generation capacity.

We have some observations on the specifics of how this basis is implemented in the proposed IPSAS on Measurement, which we provide in our observations on ED 77.

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?

CIPFA is content with this proposed change.

While the calculation of Value in Use does measure something, it is primarily part of the decision process for determining whether to recognise an impairment. The basis for measurement of the underlying asset will remain historical cost, fair value or current operational value.

Specific Matter for Comment 5:

Do you agree with the proposed deletion of the following measurement bases from the Conceptual Framework?:

Market value—for assets and liabilities

Replacement cost—for assets?

If not, which would you retain and why?

CIPFA agrees with the proposed deletion of Market Value. This basis was developed primarily to reduce the scope for confusion raised by the different approach to fair value in IFRS after the publication of IFRS 13 and extant IPSAS which reflected an approach grounded in older IFRS concepts of fair value.

CIPFA agrees with the proposed deletion of Replacement Cost given that it is included in and encompassed by Current Operation Value. Having said this, we do consider that it is an important part of the discussion of possible measurement bases. It is important to have a discussion of replacement cost in the Basis for Conclusions in the final standard, and for this reason we support the inclusion of the material in line with the current ED Basis for Conclusions.

Specific Matter for Comment 6: The IPSASB considers that the retention of certain measurement bases that were in the 2014 Conceptual Framework is unnecessary. Do you agree with the proposed deletion of the following measurement bases from the Conceptual Framework? Net selling price—for assets Cost of release—for liabilities Assumption price—for liabilities If not, which would you retain and why?
CIPFA agrees with the proposed deletion of these measurement bases from the Conceptual Framework.
Specific Matter for Comment 7: Are there any other issues relating to Chapter 7: Measurement of Asset and Liabilities in Financial Statements of the Conceptual Framework that you would like to highlight?
CIPFA has not identified any other issues that we would like to highlight in relation to Chapter 7.

ANNEX B

ED 77 Specific Matters for Comment

Specific Matter for Comment 1 Do you agree an item that qualifies for recognition shall be initially measured at its transaction price, unless: • That transaction price does not faithfully present relevant information of the entity in a manner that is useful in holding the entity to account, and for decision-making purposes; or • Otherwise required or permitted by another IPSAS? If not, please provide your reasons, stating clearly what principles are more appropriate, and why.
CIPFA agrees that an item which qualifies for recognition shall initially be measured at its transaction price, except in the limited circumstances mentioned in the question. We expect that most of the cases where another approach is required (or permitted) by particular IPSAS are ones where transaction price would not (or might not) faithfully present relevant information.
Specific Matter for Comment 2 Do you agree after initial measurement, unless otherwise required by the relevant IPSAS, an accounting policy choice is made to measure the item at historical cost or at its current value? This accounting policy choice is reflected through the selection of the measurement model. If not, please provide your reasons, stating clearly what principles are more appropriate, and why.
CIPFA agrees that unless otherwise required by a relevant IPSAS, the decision to measure at historical cost or current value should be an accounting policy choice.

Specific Matter for Comment 3—Appendix A (paragraphs A1–A6): In response to constituents' comment letters on the Consultation Paper, Measurement, guidance on historical cost has been developed that is generic in nature (Appendix A: Historical Cost). 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.
CIPFA agrees that the guidance is appropriate for application by public sector entities.
Specific Matter for Comment 4—Appendix A (paragraphs A1–A6): Do you agree no measurement techniques are required when applying the historical cost measurement basis in subsequent measurement? If not, please provide your reasons, stating which measurement techniques are applicable to the subsequent measurement of an asset or liability measured at historical cost, and why.
CIPFA agrees that no measurement techniques are required when applying the historical cost measurement basis in subsequent measurement.
Specific Matter for Comment 5—(paragraph 6): 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.
CIPFA agrees that it is useful to characterise current operational value as "the value of an asset used to achieve the entity's service delivery objectives at the measurement date", although in line with our comment on ED 76 SMC 5, it may be clearer to avoid using the term 'value' in the description of current operational value.

Specific Matter for Comment 6—Appendix B (paragraphs B1–B41): 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.
CIPFA agrees that the general definition of current operational value proposed in the ED is appropriate for public sector entities although we do have some substantial observations on specific components of the definition which are explored in later SMCs. CIPFA also considers that some of the accompanying guidance is useful and appropriate, but that some needs considerable redrafting, as explained in responses to later SMCs.
Specific Matter for Comment 7—Appendix B (paragraphs B6–B7): 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.
CIPFA agrees that location is a relevant factor to the valuation of many public sector assets which deliver a service in a specified location. This may be for a variety of reasons including, but not limited to the asset being used to deliver a service: - to the local community where local provision contributes to the usefulness of the service - with a donated asset with legally restrictive covenants which restrict the use of that asset (normally a property asset) to a designated purpose in a designated location - where location is not so relevant to effective service delivery, but where government has additional policy objectives which are supported by siting the asset at that location. For example, the government may have an objective to employ people in a specific area, which siting the service in a building in that area supports. Given this we support the notion that, <u>where the location of the asset is and remains sufficiently important to the entity's service delivery objectives or policy objectives</u>, the valuation should assume that the notional replacement will be situated in the same location as the existing asset is situated or used. In practice, there can be complexities in determining the degree to which this applies, and there may be issues around whether valuation reflecting a replacement asset is referenced to an asset at exactly the same location or merely a geographically close location. This will need to be determined having regard to the circumstances (including the

policy context of the asset), and with close dialogue between valuation professionals and accountants.

Particular care may also be needed for assets which are held for both their financial capacity and their operational capacity. While ED 78 has helpful guidance in relation to whether a property, plant or equipment asset is held primarily for one or the other of these, input from valuers may be useful in considering whether it is sensible and helpful to subdivide an asset into separate assets which reflect operational or financial capacity.

Specific Matter for Comment 8—(paragraphs B38–B39):

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.

Firstly we would note that the terminology ‘income approach’ may be misleading to some stakeholders, but we accept that this terminology is used in IFRS 13 to capture the net present value of flows arising from an asset or liability. For assets held for commercial purposes this will generally provide an estimate of net income (usually positive) associated with an asset, or negative net income associated with a liability.

Additionally we would note that the ED seems to be using this term to mean a calculation of the net present value of value flows in two different ways. In some cases this is a calculation of the net value of resources flowing to/from the entity as a result of <u>holding</u> an asset or liability (for example, in relation to tourist income in B38(b)). In other cases the calculation is of the net cost to the entity of <u>obtaining</u> an asset (for example in relation to a school in B38(a)). Both of these are relevant to valuations of the asset, but they capture rather different things. In our view, only the NPV of flows resulting from holding an asset (or liability) reflects net income in line with the intention of para C37(a) which provides more detail on the application of the income approach. The other calculation seems to be an elaboration of the cost approach.

The net income approach provides quite a natural measure of the income generation potential of an asset held for its financial capacity rather than operational capacity. For such assets the cash inflows (net of related outflows) correspond directly to value creation for the entity, and will often capture the majority of value creation. For this reason we are very content with the use of the income approach as one of the techniques which may be used to estimate the fair value of assets held for commercial purposes.

However, in CIPFA’s view the income approach will very rarely provide more than a very partial measure of the value of an asset held for operational purposes. The income generated by such an asset will generally not be set at a level designed to reflect the cost of the asset and may not even cover a significant fraction of that cost. Nevertheless, the asset will often be fully delivering services or achieving policy objectives in accordance with budgets and plans, suggesting that the ‘real’ value to the entity is much greater.

In line with the above, CIPFA would not rule out the use of the income approach to estimate current operational value, but we do have some significant reservations about the circumstances under which it might be appropriate.

We can see that it might be particularly useful when other methods fail. We would however note that the value information it provides under these circumstances may be very partial. Considerable explanation may be required so that readers of the financial statements do not mistake this for a more conventional valuation which they would consider fully captures the value of the asset.

CIPFA also considers that the explanatory material on the application of the income approach requires considerable redrafting.

Paragraph B38(a) is confusing and very difficult to understand. Inasmuch as it provides an example of a mixed measurement approach it appears not to be mixed, and not to reflect the intention of para C37(a)(or para B13(a) of IFRS 13) which sets out what the income approach is seeking to measure.

Additionally, in our view the example in B38(b) of ‘tourism income relating to cave painting heritage assets’ does not seem well chosen. We agree that there is no historical cost information, and market information will not generally be available because of legal restrictions. However, we doubt that many readers of the financial statements would consider the NPV of future tourism income to be a meaningful measure of the value of these assets. We therefore suggest that the Board provides a different example.

Specific Matter for Comment 9—Appendix C (paragraphs C1–C89):

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.

In its response to the consultation paper CIPFA supported Preliminary View 4 which proposed that fair value guidance should be aligned with IFRS 13, taking into account public sector financial reporting needs and the special characteristics of the public sector.

We have reviewed the material in C1-C89, much of which echoes material in IFRS 13. Appendix B. While there is little in this which specifically relates to public sector entities, we are content that taken together with other material in the ED, the guidance is appropriate for application by public sector entities.

Specific Matter for Comment 10—Appendix D (paragraphs D1–D48):

In response to constituents' comment letters on the Consultation Paper, Measurement, guidance on cost of fulfillment has been aligned with existing principles in the Conceptual Framework and throughout IPSAS (Appendix D: Cost of Fulfillment). 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.

CIPFA agrees that the guidance is appropriate for application by public sector entities.

Specific Matter for Comment 11:

Do you agree measurement disclosure requirements should be included in the IPSAS to which the asset or liability pertains and not in ED 77?

If not, please provide your reasons, stating clearly where the measurement disclosure requirements should be included, and why.

CIPFA agrees that measurement disclosure requirements should be included in the IPSAS to which the asset or liability pertains and not in ED 77.

Specific Matter for Comment 12: Are there any measurement disclosure requirements that apply across IPSAS that should be included in ED 77, Measurement? If yes, please provide your reasons, stating clearly what the disclosures are, and why.
CIPFA has not identified any measurement disclosure requirement that apply universally and would be appropriate to include in ED 77, Measurement rather than in individual IPSAS. We note our view that where there is a material difference between fair value and the carrying value of assets, there may sometimes be a need to disclose this. This is being addressed in the disclosure requirements in ED 79, Non-current Assets Held for Sale and Discontinued Operations, and in recommended disclosures in ED 78, Property, Plant and Equipment. There may be other asset or liability standards where this is a relevant consideration under particular circumstances.
Specific Matter for Comment 13: Do you agree current value model disclosure requirements should be applied consistently across IPSAS? For example, the same disclosure requirements should apply to inventory and property, plant, and equipment when measured at fair value. If not, please provide your reasons, stating clearly which IPSAS require more or fewer measurement disclosures, and why.
CIPFA generally agrees that current value model disclosure requirements should be applied consistently across IPSAS. However, we would not rule out the possibility that when reviewing the IPSAS on a standard by standard basis, the Board may identify situations where certain disclosures may not be material for the relevant category of asset or liability.
Specific Matter for Comment 14: Do you agree with the proposal disclosure requirements for items remeasured under the current value model at each reporting date should be more detailed as compared to disclosure requirements for items measured using the current value model at acquisition as proposed in Appendix E: Amendments to Other IPSAS. If not, please provide your reasons, stating clearly why disclosure requirements should be consistent for recurring items and non-recurring items measured using the current value model.

CIPFA agrees with this proposal.
Specific Matter for Comment 15: Do you agree fair value disclosure requirements should include requirements to disclose inputs to the fair value hierarchy? If not, please provide your reasons, stating clearly why disclosure requirements for inputs in the fair value hierarchy are unnecessary
CIPFA agrees with this proposal.

ANNEX C

ED 78 Specific Matters for Comment

Specific Matter for Comment 1: [Draft] IPSAS [X] (ED 78), Property, Plant, and Equipment proposes improvements to the existing requirements in IPSAS 17, Property, Plant, and Equipment by relocating generic measurement guidance to [draft] IPSAS [X] (ED 77), Measurement; relocating guidance that supports the core principles in this Exposure Draft to the application guidance; and adding guidance for accounting for heritage assets and infrastructure assets that are within the scope of the Exposure Draft. Do you agree with the proposed restructuring of IPSAS 17 within [draft] IPSAS [X] (ED 78)? If not, what changes do you consider to be necessary and why?
CIPFA strongly agrees with the restructuring of IPSAS 17, including • relocating generic measurement guidance to [draft] IPSAS [X] (ED 77), Measurement; • relocating guidance that supports the core principles in this Exposure Draft to the application guidance; and • adding guidance for accounting for heritage assets and infrastructure assets that are within the scope of the Exposure Draft
Specific Matter for Comment 2—(paragraphs 29-30): Do you agree that when an entity chooses the current value model as its accounting policy for a class of property, plant, and equipment, it should have the option of measuring that class of assets either at current operational value or fair value? If not, please provide your reasons, stating clearly which current value measurement basis would best address the needs of the users of the financial information, and why.
CIPFA supports this proposal.
Specific Matter for Comment 3—(paragraph AG3): Are there any additional characteristics of heritage assets (other than those noted in paragraph AG3) that present complexities when applying the principles of [draft] IPSAS [X] (ED 78) in practice? Please provide your reasons, stating clearly what further characteristics present complexities when accounting for heritage assets, and why.
CIPFA is content that the characteristics of heritage assets set out in the ED capture the complexities in accounting for these assets. While uniqueness is often cited as a key characteristic, this is encompassed within the ED discussion of non-replaceability.

Specific Matter for Comment 4—(paragraph AG5) Are there any additional characteristics of infrastructure assets (other than those noted in paragraph AG5) that present complexities when applying the principles of [draft] IPSAS [X] (ED 78) in practice? Please provide your reasons, stating clearly what further characteristics present complexities when accounting for infrastructure assets, and why.
CIPFA agrees that the characteristics set out in AG5 capture the key features of infrastructure assets which present complexities, especially when read in conjunction with paragraph AG4.
Specific Matter for Comment 5—(paragraphs 80-81 and AG44-AG45): This Exposure Draft proposes to require disclosures in respect of heritage property, plant, and equipment that is not recognized in the financial statements because, at initial measurement, its cost or current value cannot be measured reliably. Do you agree that such disclosure should be limited to heritage items? If not, please provide your reasons, stating clearly the most appropriate scope for the disclosure, and why.
CIPFA agrees that it is appropriate to require disclosure in relation to heritage assets that are not recognized in the financial statements because, at initial measurement, their cost or current value cannot be measured reliably. Given the current scope of IPSAS pronouncements, heritage assets are the only items for which we consider that this is appropriate. However, we understand that the IPSASB is considering extending its standards to encompass wider categories of assets, where issues around reliable measurement may raise similar issues. For example, natural resources. It would seem appropriate to review the need for this type of disclosure when such standards are developed.
Specific Matter for Comment 6—(paragraphs IG1-IG40): Do you agree with the Implementation Guidance developed as part of this Exposure Draft for heritage assets? If not, please provide your reasons, stating clearly what changes to the Implementation Guidance on heritage assets are required, and why.
CIPFA agrees with the Implementation Guidance developed for heritage assets. We specifically agree with IG 9 on capitalisation of subsequent expenditure, although it gives rise to a value which generally only captures part of the value of the asset. In the interests of understandability, we suggest that it is important that the financial statements clearly distinguish asset balances which represent only capitalised subsequent expenditure from those which reflect a valuation of the entirety of relevant assets.

Specific Matter for Comment 7—(paragraphs IG1-IG40): Do you agree with the Implementation Guidance developed as part of this Exposure Draft for infrastructure assets? If not, please provide your reasons, stating clearly what changes to the Implementation Guidance on infrastructure assets are required, and why.
CIPFA agrees with the content of the implementation guidance for infrastructure assets.

ANNEX D

ED 79 Specific Matters for Comment

Specific Matter for Comment The IPSASB decided that there was no public sector specific reason to depart from the measurement requirements of IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. However, the IPSASB considers that, where materially different, disclosures of the fair value of non-current assets classified as held for sale measured at a lower carrying amount would provide useful information to users of financial statements for accountability purposes. The additional proposed disclosure is shown at paragraph 52 of this ED. Do you agree with this disclosure proposal? If not, why not?
CIPFA strongly supports the introduction of an IPSAS on Non-current Assets Held for Sale and Discontinued Operations, using the measurement requirements of IFRS 5. CIPFA also supports the proposed disclosure of the fair value of non-current assets classified as held for sale if these are being measured at a materially lower carrying amount. We agree that this would provide useful information to users of financial statements In line with our response to ED 72 SMC 6 in IPSASB's consultation on revenue and transfer expenses, we would note that similar disclosures would be appropriate in circumstances where there are material differences between the fair value and carrying value of non-current assets which are transferred in a transfer not conducted under market conditions. Given which we suggest that a similar requirement should be incorporated into any standard on transfer expenses. We also note that ED 78 para 69 encourages a disclosure of this kind in respect of property, plant and equipment which is valued at historical cost and this is known to be materially different to the fair value.