

Comments to ED 78 - Property, Plant and Equipment (with references also to ED 77 - Measurement)

These comments express the Italian position on ED 78 with particular reference to the accounting treatment of heritage assets. Where relevant, they also convey observations referable to ED 77 on the subject of measurement of this kind of assets.

This paper is the result of the joint reflections within the Italian MEF State General Accounting Department adopted by the Executive Committee of the Governance Structure¹ established for the implementation of a single accrual accounting system for all the Italian public administrations.

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?

Comment:

The RGS-MEF expresses its deep appreciation and warmly welcomes the removal of heritage assets from the exclusions within the scope of application of IPSAS 17 and, consequently, the fact that heritage items that satisfy the definition of “asset” and meet the recognition criteria should be entered in the financial statements.

This view has always been strongly supported by Italy, as can also be seen from the previous letter of response to the Consultation Paper "Financial Reporting for Heritage in the Public Sector".

As part of the above-mentioned MEF-RGS Governance Structure, the Italian Standard Setter Board (SSB) is setting the Italian public sector accounting standards (ITASs), strongly inspired by IPSASs and based on recommendations from Eurostat EPSAS Working Group. In this work of ITASs setting, the SSB is moving in exactly the same direction, regulating the accounting treatment of heritage assets within the scope of the standard relating to Tangible Assets (ITAS 4) and requiring the accounting recognition of the heritage assets to the reporting entity that controls them.

It should be noted that in Italy there is a specific legislation, the *Codice dei beni culturali e del paesaggio* (the Cultural Heritage and Landscape Code), which sets out the list of the cultural properties and specifies the characteristics that they have to possess and the procedures that must be followed to qualify them as heritage items. In this context, the *Codice dei beni culturali e del paesaggio* considers in a uniform manner a plurality of heritage items (i.e., libraries, museums, picture-galleries) as an entirety of items with the same intended use, and not as a sum of individual items.

¹ Established in March 2020 within the State General Accounting Department of the Italian Ministry of Economy and Finance (MEF-RGS).

The amendments we intend to suggest are explained below

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.

Comment:

With regard to heritage assets, we note how – due to the particular characteristics of these assets – fair value could hardly be applied. In fact, it is an “exit value” and this implies that the asset is traded on the market.

Therefore, the current operational value model is applicable for heritage assets, as an entry value. In our opinion, it is correctly defined (par. 6 ED 77) as “*the value of an asset used to achieve the entity's service delivery objectives at the measurement date*”.

Appendix B of ED 77 identifies three main measurement techniques:

- 1) Market approach
- 2) Cost approach
- 3) Income approach

Since the **market approach** implies the existence of market transactions for identical or comparable assets, it is rarely applicable to heritage assets, whose characteristic is that they are nearly always unique and incomparable.

The **cost approach** takes into account the current replacement cost of the asset. This value is estimated by calculating the cost of a modern equivalent asset. This method could be applied to the so-called “operational heritage assets”. However, for the same reasons mentioned above, it is often difficult to identify a modern asset equivalent to a heritage asset, especially if it is a non-operational heritage asset. It should also be taken into account that in the art world a copy of a cultural-artistic item never has the same value as the original

On the other hand, the **income approach** takes into account the discounting of future financial flows through present value techniques. It is therefore applicable for those heritage assets that generate future economic benefits.²

In this regard, we note that Appendix B of ED 77 does not specify:

- a) whether only positive flows (inflows) or also negative ones (outflows) should be considered in the estimate of the present value;
- b) if, in addition to the flows directly referable to the heritage asset, it should be considered also those indirectly referable to the heritage asset but directly referable to the reporting entity in whose financial statements the asset will be recorded (i.e., those incremental flows that the reporting entity obtains thanks to the presence of the heritage asset in their own economy).

² Indeed, this method is already included in the Italian response letter to the Consultation Paper “Financial Reporting for Heritage in the Public Sector” and is one of the measurement methods also present in the ITAS 4 (Tangible Assets) under development.

With regard to point *a*), we think that net flows should be considered (difference between positive and negative flows).

With regard to point *b*), we think that both the flows directly referable to the heritage asset (e.g., entrance tickets, sponsorships, concessions over the asset, public and private contributions) and the flows indirectly referable to the heritage asset (e.g., all revenues connected to the economy generated by the presence of the heritage asset in a specific area in terms of higher tax revenues) should be considered.

For these flows, the presence of properly documentable data is an essential condition in order to put the relative value into the accounting information (measurement) rather than in the descriptive and extra-accounting information (disclosure).

In order to easily identify the financial flows that may result from the heritage asset, this should be considered as an “entirety of items” with the same intended use (i.e. libraries, museums, picture-galleries, etc.).

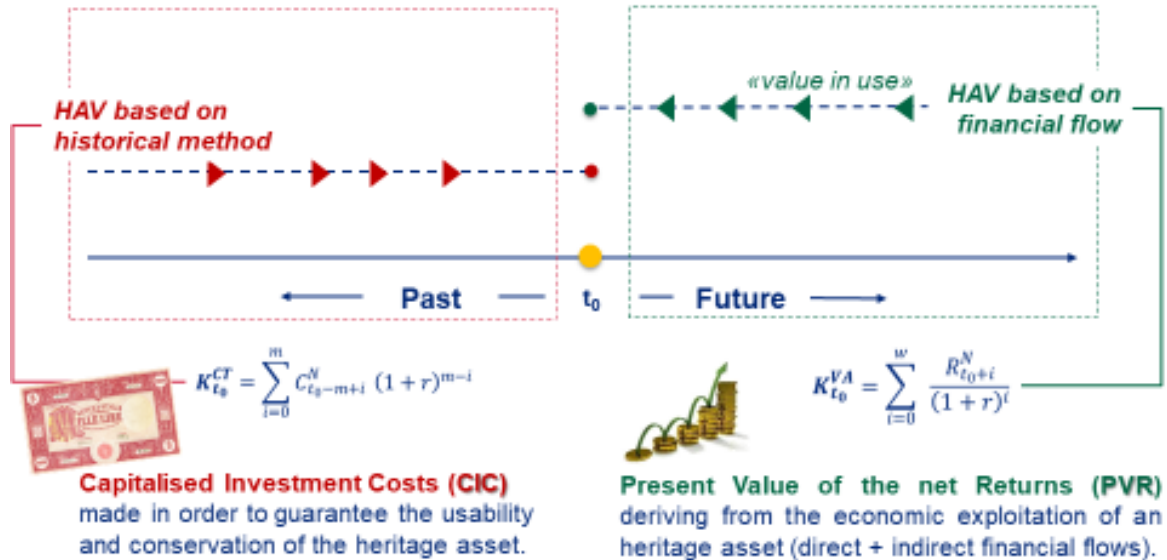
In this regard, it should be noted that the MEF-RGS, in the framework of the pilot project "Heritage in Financial Reporting", carried out experiments applying this method to evaluate some pilot heritage sites (Villa d'Este and Villa Adriana, Galleria Borghese, Pompeii).

Furthermore, again in the Italian response letter to the Consultation Paper "Financial Reporting for Heritage in the Public Sector", alongside the income approach (which allows to reach a significant value where the heritage asset begets future economic benefits), a method applicable to those heritage assets which, although not begetting future flows, have a service potential, is also proposed. This method is based on the capitalization of past costs.

The logic underlying this approach is linked to the concept of "usability" of the asset. In this sense, the evaluation of a heritage item as an asset can alternatively be based on two economic dimensions:

- the economic value of the usability of the heritage item over an infinite time horizon, in relation to the current state of the item and the related conditions of use (therefore estimate of the asset as the present value of the net returns – *income approach*);
- the resources invested in the past that have allowed the heritage item to be considered an asset and to be usable by present and future generations (therefore estimate of the asset as *capitalized investment costs - CIC*).

Alternative approaches: the value of the usability



We therefore propose to include this method in the measurement techniques of the current operational value.

It should also be noted that, with regard to unrecognized heritage properties, plants and equipment, ED78 provides for the possibility to capitalize subsequent expenditures exceeding a "capitalization threshold" fixed by the management. We support this approach.

In our opinion, this approach further supports the Italian proposal to proceed, only for heritage, to the capitalization of investments made in the past as an initial measurement basis.

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.*

Comment:

In relation to the applicability of the market approach and the cost approach in determining the current operational value, among the characteristics of the heritage assets to be included in the AG3, we suggest to add the following:

“They are often unique and incomparable”

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.

Comment:

We agree that this disclosure should be limited to heritage items.

On this point, we express our deep appreciation, as we believe it is appropriate to provide additional information relating to heritage assets that cannot be accounted for. For these assets, it is absolutely necessary to avoid the application of the "symbolic value" criterion equal to one unit current value.

In this sense, we suggest the following disclosure for heritage assets:

	Disclosure
	<i>Heritage assets</i>
#	In the disclosure, the entity must provide a description of the heritage assets distinguishing between those that - in addition to their cultural value - generate future economic benefits or a service potential (so-called <i>operational</i> or <i>non-heritage purpose</i>) and those that whose future economic benefits or service potential are limited to their cultural characteristics (so-called <i>non-operational</i> or <i>heritage purpose</i>).
#	With reference to heritage assets owned by the entity, regardless of their recording in the financial statements, disclosure shall set out: <ul style="list-style-type: none"> a) name, place, year, type (operational or non-operational), nature (e.g. historical, artistic, archaeological, archival, etc.) of the asset; b) acquisition mode, if known (i.e. discovery, gift, etc.); c) management mode (direct or indirect); d) information on the usability of the asset (access allowed or not allowed); e) if access is allowed, the number of annual visitors; f) if access is free or with an admission charge; g) the policies adopted by the entity and the budget allocated for acquisition, conservation, management or disposal.
#	With reference to heritage assets <u>recorded in the financial statements</u> , disclosure shall also set out: <ul style="list-style-type: none"> a) the date of first recording in the financial statements; b) the date of the last measurement; c) the measurement method adopted; d) the carrying amount; e) any possible alternative methods applicable; f) the reason why that method has been adopted; g) any significant limitations of the measurement; h) any additional information deemed relevant for the purposes of the measurement; i) any changes made in relation to the value of the asset at the beginning and at the end of the period.
#	With reference to heritage assets <u>not recorded in the financial statements</u> , disclosure shall also set out: <ul style="list-style-type: none"> a) the reasons why they are not recorded; b) any additional information on the assets, deemed relevant.
#	The disclosure required by paragraphs XX may be presented in aggregate form by groups or classes of heritage assets, provided that such aggregations are treated as a plurality of heritage items, in compliance with paragraph XX.

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.

Comment:

We are in favour of the inclusion of Implementation Guidance within ED78 for heritage assets, as we believe it is useful for providing further information on the correct application of the standard.

In this perspective, Italy will endeavour to facilitate the work of accounting operators by developing an Implementation Guidance that indicates, for each measurement model, a guided path, step-by-step, necessary to achieve a correct assessment of heritage assets.