



TE TAI ŌHANGA
THE TREASURY

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International Public Sector Accounting Standards Board
International Federation of Accountants
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CANADA

Dear Ross

EXPOSURE DRAFTS – IPSASB MEASUREMENT EDs 76, 77, 78 and 79

Thank you for the opportunity to respond to the IPSASB Exposure Drafts:

- ED 76 *Conceptual Framework Update: Chapter 7, Measurement of Assets and Liabilities in Financial Statements*;
- ED 77 *Measurement*;
- ED 78 *Property, Plant, and Equipment*; and
- ED 79 *Non-current Assets Held for Sale and Discontinued Operations*.

The New Zealand Treasury is responsible for the New Zealand Government's accounting policies that comply with NZ GAAP for the public sector, which is mainly based on IPSAS.

The four attachments to this letter set out NZ Treasury's response to the specific matters for comment.

Broadly the New Zealand Treasury:

- does not support ED 76 *Conceptual Framework Update*. We consider it poor process to update the Conceptual Framework as a type of consequential amendment in a project primarily aimed at producing a standard. We believe this approach has contributed to the lack of conceptual clarity in the resulting proposals. In our view, conceptual issues need lengthier debate and consideration than this process has allowed.

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- supports the ED 77 *Measurement* approach in aligning with IFRS 13 in respect of fair value and the first two levels of the fair value hierarchy.
- Consistent with our detailed comments on ED 76, rejects the proposed approach to a current operating value in favour of a current cost model approach, more clearly distinguished from fair value, and more appropriate to much measurement of property plant and equipment providing public services
- generally supports the proposals in ED 78 *Property, Plant, and Equipment* with some relatively minor suggestions for improvements, and
- supports ED 79 *Non-current Assets Held for Sale and Discontinued Operations* but has identified two public sector specific items for the consideration of the IPSASB.

We trust you will find this response useful in your further deliberations. If you have any queries regarding Treasury's comments, please contact Ken Warren or Angela Ryan by email to ken.warren@treasury.govt.nz or angela.ryan@treasury.govt.nz

Yours sincerely



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

Specific Matter for Comment 1: Measurement Hierarchy

ED 76 proposes a measurement hierarchy. Do you agree with the three-tier hierarchy? If not, why not? How would you modify it?

The Treasury disagrees with the depiction of measurement models, bases and techniques as a hierarchy. The common meaning of the term is “a system in which items are ranked according to relative status or authority”. Models, bases, and techniques are not items to be ranked. They are simply ways of describing a measurement, whether broadly, more specifically, or by reference to the methodology.

If the IPSASB wishes to propose a measurement hierarchy, it must identify its ranking preferences. This is what the IASB has done with its measurement hierarchy in IFRS 13 where the highest priority ranking is quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).

Furthermore, everyday use of the words: “models”, “bases” (and even “techniques”) are interchangeable, which means they are not intuitive. Historical cost for example, is both a model and basis in the suggested hierarchy, with no specified techniques identified.

The critical conceptual challenge with measurement is indeed to develop a hierarchy of approaches ranked in order of their merits in achieving the measurement objective. The current Conceptual Framework points to the way this must be done in BC5.65 and in BC7.1-BC7.12. The hierarchy proposal in this ED does not address this critical issue. Doing so at a framework level would require a far greater due process to obtain general acceptance than this project permits. Doing so at a standards level, which is what the framers of the current Conceptual Framework envisaged, will create a confusion of hierarchies. Consequently, the Treasury recommends that references to a hierarchy be dropped from ED 78.

Specific Matter for Comment 2: Fair value as a measurement base

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?

We accept the IPSASB's proposal to include the IASB's fair value as a measurement basis in the Conceptual Framework and to adopt the same definition of fair value as in IFRS 13. This basis is particularly important when measuring the financial capacity of assets, such as with financial instruments under IPSAS 41. It is important for the same term in IFRS and IPSAS to have the same meaning to avoid confusion, unless there is a public sector reason to depart.

But in deciding to introduce the IFRS 13's exit-based fair value definition and remove 'market value' (an entry and exit-based value), in our view, a discussion around entry and exit values should be more prominent in ED 76. We are disappointed the discussion and classification of measurement bases as either exit or entry values has been diluted in ED 76 relative to the current Chapter 7 in the IPSASB's Conceptual Framework. We recommend that the IPSASB state in ED 76 that the IFRS 13 fair value definition is an explicitly exit-based definition, which is acknowledged in paragraph BC7.25 of the Basis of Conclusion:

BC7.25 Shortly before the 2014 Conceptual Framework was finalized the IASB approved IFRS 13, Fair Value Measurement. IFRS 13 adopted an explicitly exit-based definition of fair value.

We also note IPSASB's reasons for the dilution of discussion in respect of entry vs exit based value in ED 76:

BC7.19 The IPSASB is of the view that the key factor in selection of a measurement basis is the measurement objective; in particular, whether an asset is primarily held for its operational or financial capacity and the characteristics of a liability. The IPSASB concluded that the distinction between entry and exit values is useful in deciding whether a measure includes transaction costs, and, if so, whether on acquisition or disposal of an asset or the incurrence or disposal/settlement of a liability. The Conceptual Framework therefore includes a high-level discussion on entry and exit values but does not classify measurement bases as entry or exit. [Emphasis added]

We disagree with the IPSASB that the distinction between entry and exit values is only useful for considering transaction costs and believe it is a more fundamental characteristic of selecting a measurement basis. We support the previous IPSASB view in BC7.13 of the 2014 Conceptual Framework that *awareness of whether a measurement basis is an entry or exit value is useful in determining which measurement basis best meets the measurement objective.*

The IPSASB stance in BC7.19 of ED 76 also appears inconsistent with ED 77 where the classification of the two measurement basis for assets between entry and exit value is prominent. We note in paragraph 25 of ED 77, a useful explanation of the differences between COV and fair value, and that it clarifies COV is explicitly an entry value:

Current operational value differs from fair value because it:

- (a) *Is explicitly an entry value and includes all the costs that would necessarily be incurred when obtaining the asset; [emphasis added]*
- (b) *Reflects the value of an asset in its current use, rather than the asset's highest and best use (for example, a building used as a hospital is measured as hospital); and*
- (c) *Is entity-specific and therefore reflects the economic position of the entity, rather than the position prevailing in a hypothetical market (for example, the current operational value of a vehicle is less for an entity that usually acquires a large number of vehicles in a single transaction and is regularly able to negotiate discounts than for an entity that purchases vehicles individually).*

We recommend that IPSASB specify in ED 76 that

- fair value is explicitly an exit-based definition, and
- COV characteristic include the fact COV is explicitly an entry value (suggestion below underlined) and
- The term be replaced with the term *Current Cost* :

Current operational-value cost reflects the following characteristics. It:

- *Is based on an asset's current use;*
- *Assumes that an asset will continue to be used for service delivery rather than being sold; and*
- *Is explicitly an entry value, and*
- *Is entity-specific and therefore reflects the economic position of the entity, rather than the perspective of a market participant. For example, the current operational-value cost of a vehicle may be less for an entity that usually acquires a large number of vehicles in a single transaction and is regularly able to negotiate discounts than for an entity that purchases vehicles individually.*

Specific Matter for Comment 3: Current operational value as a measurement base

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?

Current operational value is the value of an asset used to achieve the entity's service delivery objectives at the measurement date.

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

The Treasury does not agree with the IPSASB's proposals in respect of current operational value (COV).

We agree with all the Alternative View on the proposed COV that the

- The definition is unclear
- The lack of clarity in the definition risks not achieving the qualitative characteristics of financial reporting; and
- The definition should focus on the cost of replacing an asset used for its service potential.

We strongly agree that the focus of a COV measurement basis should be on the cost of replacing an asset that is used for service potential, reflecting the concept that it is an entry value measure which is likely to be more appropriate when an asset is held primarily for its operational capacity to deliver services, rather than for their financial capacity. To reflect that, we propose this measurement basis be described as "Current Cost" rather than "Current Operating Value". What is being measured is not the public good value the asset provides, but what is the current cost for an asset to provide that public good value.

We believe the most relevant measure of an asset that is held primarily for its operational capacity to deliver services is the cost an entity would be required to incur to replace the asset for the following reasons:

- We acknowledge how difficult it is to measure public benefit and wellbeing generally and to do so would require a generally accepted approach to ex-post multi-criteria benefit analysis (to match the ex-ante multi-criteria benefit analysis used in cost benefit analysis).
- In the absence of a generally accepted framework for measuring public benefit and wellbeing, the Treasury believes a valuation approach to public sector assets based on fair value is not appropriate for measuring operating capacity and service potential (i.e. if fair value does not value public benefits, it is not fair, and it is likely either to make unrealistic market perspective assumptions, or just to be scrap value).
- In the absence of fair (public benefit) value the most useful (relevant and reliable) information we can provide users of public sector financial statements is the deprival value of assets such as property, plant and equipment.
- That follows from our view that users are interested in the operating capacity of the government to provide public benefits, and the cost of replacing that capital if the entity was deprived of it. Practically, this means that a depreciated replacement cost approach is likely to be the most appropriate current measurement basis in our view, and more detailed guidance would be aimed at providing information useful to an assessment of the cost of its deprival.

For those reasons, the Treasury believes a current cost measurement basis specifically to value the cost of replacing an asset used for its service potential should not be shoe-horned under the IFRS 13 exit-based fair value definition, so we support the IPSASB approach to developing a separate measurement base in general (albeit we do not support the definition of COV, nor the name as proposed).

However, we would have expected more discussion in Chapter 7 or the Basis of Conclusion on the conceptual differences between the cost approach under the IFRS 13 exit-based definition of fair value and a cost approach under a COV or Current Cost (CC) definition. The IPSASB acknowledges this issue in BC7.26 but unfortunately does not expand on it:

BC7.26 The 2014 Conceptual Framework included replacement cost as a current value measurement basis, envisaging that it would be appropriate for specialized assets. As noted in paragraph BC7.25 the IPSASB has adopted an exit-based definition of fair value. The cost approach, a measurement technique for fair value, has some similarities to replacement cost. These inter-related factors necessitated the development of a measurement basis that can be applied to assets held primarily for operational capacity. [Emphasis added]

We agree that these inter-related factors should lead to the IPSASB developing a separate cost measurement basis, but after reading BC7.27 of ED 76, we are left uncertain what the COV measurement basis is trying to achieve.

BC7.27 The IASB's 2018 Framework included current cost as a measurement basis for both assets and liabilities. The IPSASB considered whether current cost should be adopted as a current value measurement basis for assets that are primarily held for operational capacity (see paragraph BC7.68 for a discussion of current cost for liabilities). The IPSASB formed a view that a measurement basis similar to current cost is relevant in a public sector context for both specialized assets and non-specialized held for operational capacity. However, rather than the cost of an equivalent asset in the IASB's definition of current cost the IPSASB formed a view such a measurement basis should reflect an asset's existing use in delivering services. The IPSASB decided to use the term 'current operational value' for this measurement basis. Current operational value is a versatile measurement basis. For non-specialized assets, it can be supported by directly market-based measurement techniques with similarities to market value. For specialized assets, measurement techniques to determine the value of the asset may be applied. The updated Conceptual Framework therefore includes current operational value as a measurement basis for assets primarily held for operational capacity. [emphasis added]

In our view, the logical next step would have been for the IPSASB to develop a CC measurement basis relevant to the public sector for assets held for their service potential. But we are perplexed by the explanation in BC7.27 and are unable to follow

the reasoning. We are concerned that in proposing the COV measurement basis, the IPSASB has not explained in BC7.27:

- the rationale for developing a broad and versatile *current operational value* measurement basis, rather than developing a narrower replacement cost measurement basis
- what a measurement basis “*similar to current cost*” means
- what is meant by the phrase “*a measurement basis to reflect an asset’s existing use in delivering services*”
- why the concept of non-specialised and specialised assets has been introduced and why this categorisation is relevant to the COV definition
- what is meant by using market-based measurement techniques with similarities to market value for non-specialised assets, especially when market value is proposed to be deleted from the Conceptual Framework, and
- what the following unspecific statement means “*For specialized assets, measurement techniques to determine the value of the asset may be applied*”.

We request that the IPSASB revisit the conceptual basis for the COV and re-orientate the definition to focus on the cost of replacing an asset for measuring public benefit and service potential.

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 Treasury believes Value-In-Use is a measurement basis that should be retained in the Conceptual Framework, even if used infrequently.

The purpose of the Conceptual Framework is to establish the concepts that underpin general purpose financial reporting by public sector entities that adopt the accrual basis of accounting. That purpose is not served by ignoring the concept. The Treasury recognises that determining the value-in-use of a non-cash-generating asset is complex and subjective, but these are not reasons to give the concept less attention.

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?

We believe having both 'fair value' (as defined in IFRS 13) and 'market value' in the Conceptual Framework or IPSASs is likely to be confusing so for that reason we would generally support the removal of market value.

We would not support the deletion of the replacement cost basis until the IPSASB has clarified the COV measurement basis following our concerns raised in both SMC3 above and in our responses to ED77 below.

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?

The Treasury in principle disagrees with the deletion of these measurement bases from the Conceptual Framework as part of a limited scope review. While these measurement bases may not have been used in standards to date, it is noted they have only been available in the conceptual framework for six years, and most IPSAS simply refer to fair value. The case that they are not necessary has barely been tested, let alone proven.

A conceptual framework has a broader role than explaining the concepts in current standards. It should also help standard setters as they develop new standards and help preparers that are faced with situations not specifically addressed in standards.

These concepts for example may be useful in thinking about measuring carbon emission units. Assumption price has been a useful concept in New Zealand for public sector financial reporting when taking on large and unusual liabilities during financial crises. Without it, the measurement of the cost of such activity is rendered impossible.

Of the concepts listed, Net Selling Price appears to be a derivation from fair value, (i.e. fair value less costs to sell) and therefore a case could be made that it is not a separate concept. However, again the Treasury would expect that if what is intended of this measure is a 'disposal value' reflecting the cash proceeds a non-cash generating asset might generate, then a fuller assessment of the information value of such a concept would be more useful in making a determination.

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?

The Treasury has no further comments on ED 76.

Responses on Exposure Draft 77: *Measurement*

Specific Matter for Comment 1 (paragraphs 7–16):

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.

We agree with the principle but note that in existing IPSASB literature the term *deemed cost* (introduced in paragraph 10 of ED77) is widely understood in the context of first time adoption and in particular IPSAS 33 *First-time Adoption of Accrual Basis International Public Sector Accounting standards*.

The term is defined in IPSAS 33 as: *Deemed cost is an amount used as a surrogate for acquisition cost or depreciated cost at a given date.*

We think *deemed cost* should be a defined term in ED77 *Measurement* because

- the term is likely to be pervasive across a number of standards for initial recognition of non-exchange transactions
- of the prevalence of non-exchange transaction involving the acquisition of assets in the public sector, and
- the word “cost” in *deemed cost* may sound counter-intuitive to what the IPSASB intended, which is a current value measure, whereas the previous requirement to use *fair value* measurement provided an immediate awareness that the initial recognition of an asset in a non-exchange transaction was to be a current value at acquisition date.

It is also unclear to us if the IPSASB intended that the defined term in IPSAS 33 (above) exactly captures the proposals in paragraph 10 of ED77.

We also suggest that some of material in BC19 is brought forward into the actual standard because of the clarity this paragraph provides in respect of non-exchange transactions and deemed cost (especially the text underlined below):

BC19. A transaction price is applied, where appropriate, because transactions occurring in orderly markets are negotiated between parties at arm's length and are presumed to faithfully present the economics of the transaction. The transaction price is therefore useful for decision-making purposes and to the users of the financial information to hold decision-makers to account. Where transaction price is not appropriate, a deemed cost is calculated using a current value measurement technique to approximate the value of the asset or liability on the transaction date.

We are also surprised there is no discussion in the Basis of Conclusion explaining what we believe is a significant language change around the initial recognition of assets acquired in a non-exchange transaction, which under the existing suite of standards is generally measured at fair value. It seems clear in reading the list in paragraph 12 (i.e. the circumstances where a transaction price may not be observable or may not faithfully present relevant information) that the IPSASB intended the new language and descriptions in paragraph 10 to 13 to replace the term *non-exchange transactions*, but it would have been useful for that to be confirmed in the IPSASB's Basis of Conclusion and why this is the preferred approach.

We also noted there is no description or definition of *orderly market* in ED 77. Users would need to consult the Conceptual Framework, ED 76 for the following description of orderly market characteristics, which is located under the "Fair Value" section in Chapter 7:

Orderly Markets

7.40 Orderly markets have the following characteristics:

- *There are no barriers that prevent the entity from transacting in the market;*
- *There is sufficient frequency and volume of transactions to provide price information; and*
- *There are many well-informed buyers and sellers acting without compulsion, so there is assurance of "fairness" in determining current prices—including that prices do not represent distress sales.*

An orderly market is 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

Given the significance of this term in ED 77, we think it could be helpful to have a definition (or description) of orderly markets in the context of both COV(CC) and fair value in the measurement standard, to save users having to consult the fair value section of the Conceptual Framework for an explanation.

Specific Matter for Comment 2 (paragraphs 17):

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.

We agree with SMC 2

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.

We agree that the guidance in Appendix A: Historical Cost is appropriate for application by public sector entities. The omission of any discussion of depreciation in the section on subsequent measurement is however surprising.

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.

We agree that no discussion of measurement techniques are required in Appendix A when applying the historical cost measurement basis in subsequent measurement. Measurement techniques when applying historical cost are more likely to be applicable in making operating versus capitalisation decisions in initial measurement, but these are more appropriately covered in separate standards.

Specific Matter for Comment 5 (paragraphs 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.

The Exposure Draft includes an Alternative View on 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.

As explained in our response to SMC 3 of ED 76, the Treasury does not agree with the proposed definition of COV and the associated guidance as drafted.

The Treasury supports IPSASB's objective of developing a current measurement separate from fair value, but we support the development of a CC basis based on the cost to replace the service potential embodied in an asset at the measurement date as is proposed in the Alternative Views in ED 76 and ED 77.

We also support a replacement cost measurement basis because in our view, users are interested in the operating capacity of the government to provide public benefits, and we think users are best served if they know the cost of replacing that capital if the entity was deprived of it. As noted in our response to SMC 3 of ED 76, the Treasury believes that a depreciated replacement cost approach is commonly likely to be the most appropriate measurement in practice, and detailed guidance should be aimed at providing information useful to an assessment of the cost of its deprival.

Therefore, the Treasury agrees with the Alternative View that:

- The income approach is not appropriate as a measurement technique for COV (also refer SMC 8 for further comment)
- The lack of clarity in the proposed definition of COV risks not achieving the qualitative characteristics of financial reporting
- The proposed definition of COV could permit either entry or exit values; and
- The lack of clarity about the accounting for surplus capacity.

We have found the concept of COV, as expressed in ED 77 (and ED 76) is inconsistent and confusing in some parts. ED 77 lacks guidance relevant examples, which would

aid understanding of the principles proposed, particularly in relation to the current measurement of land assets in the public sector (refer to our comments below).

We note the reasons in BC15 for the IPSASB structure of ED 77 and the desire to minimise duplication in the standard

BC15. The IPSASB concluded this structure is appropriate because:

- (a) Core text stands alone. Including principle level guidance for measurement bases and measurement techniques in the core text allows it to be read and applied independently of the appendices.*

- (b) Minimal duplication. The most significant challenge to overcome in structuring the material was to reduce the duplication of measurement technique guidance between the core text and the appendices, and within the appendices. This was a challenge because some measurement techniques can be applied to more than one measurement basis. The structure of the [draft] Standard allows for key measurement techniques and principles to be included once in the core text, and application of those principles to each measurement basis to be included in the appropriate appendix (*emphasis added*)*

However we can envisage unintended interpretation challenges in practice when preparers are instructed to use the fair value guidance but to substitute certain concepts, such as in the income approach, to replace the requirement to assume a market participant perspective with an entity-specific perspective.

The fair value guidance initially drafted by the IASB holistically reflected exit-based principles and market participant perspectives. There will be challenges around when to use the fair value measurement guidance as authoritative support for specific guidance if there are gaps missing in the COV(CC) guidance, or where there are unique and complex valuations which require looking at a variety of authoritative support to develop a particular accounting policy. We also note that the COV(CC) guidance for the market approach techniques is minimal, but comprehensive under fair value.

The current proposal would therefore impose unnecessary cost for preparers, valuers and auditors in interpreting the different techniques in ED 77 and deciding what assumptions to fine-tune in their existing valuation models to reflect either an entity-specific entry price under COV(CC) or a market perspective exit price under the fair value guidance. Some of these differences could be subtle, while others could have a material impact on valuations. The interpretation challenges and judgements add complexity and cost to an already complex valuation process.

We would recommend that the IPSASB considers in ED 77:

- removing the cost approach measurement technique entirely from the Fair Value measurement basis

- having a single current (replacement) cost approach under the current operating value basis, with a primary focus on guidance to address public sector circumstances where the assets generate public good benefits, and
- removing the market approach and income approach measurement techniques from the COV measurement basis, and relying entirely on the fair value guidance for use of these techniques.

As explained earlier, we do not believe that the income approach is appropriate under COV, so we believe it should be removed anyway. We are also not convinced there is a need for a COV market approach (entry price) and a fair value market price (exit price) in practice as we are not convinced the need for a COV market approach is prevalent in the public sector. Also, as noted in our response to SMC 3 of ED 76, we do not see the conceptual justification for having a broad and versatile COV basis which incorporates three measurement techniques.

Surplus capacity

We agree with the alternative view that there is a lack of clarity in relation to the proposed treatment of surplus capacity. Currently, under the proposed COV guidance, paragraphs B10 to B12 of ED 77 require surplus capacity is included and measured as part of the asset, subject to impairment in accordance with IPSAS 21 and IPSAS 26, but under paragraph B36(c), IPSAS also require deductions for economic (external) obsolescence are made under the COV basis.

Consistent with the concerns raised in the Alternative View, we would like the IPSASB to clarify in ED 77:

- (a) how to classify a reduction in an asset's use resulting from a reduction in demand for its services - is it a potential source of impairment or is it a potential reduction in the measurement of an asset under COV(CC) (i.e. classified as economic (external) obsolescence)
- (b) how to classify a reduction in an asset's use resulting from a change in policies to supply services (e.g. reducing the maximum ordinary muster rate in prisons, or increasing spare ICU capacity in hospitals to cope with pandemics)
- (c) whether a difference in classification might cause a difference in the asset's carrying amount.

This lack of clarity could lead to COV(CC) being overstated or understated, depending upon how an entity interprets the proposed requirements.

Land

In this standard, the IPSASB should provide more and separate guidance and examples in ED 77 for measuring land held for operational capacity in delivering services, particularly land associated with specialised items of property, plant and equipment. Such examples would help clarify the COV(CC) principles in ED77 in paragraphs B5 to B16, which are not clear to us in some places.

The location of the asset (B6 & B&7)

We agree with the IPSASB that under COV(CC):

- the asset's COV(CC) assumes that the entity will continue to meet its service delivery objectives from the same location in which the asset is currently situated or used, and
- the COV(CC) of a building reflects the value of the building in its current location.

However, we note the example is focussed solely on the hospital building in its current location with a focus on construction costs and permits that would be incurred at that specific location.

In our view, the example would be improved if it also explain IPSASB's intention for the land associated with the hospital. For example, in our jurisdiction, current application guidance in PBE IPSAS 17 states in a case where specialised facilities are located in a prime central business district site but the operation would be able to be run from a smaller sized and/or less valuable alternative site offering the same service potential, the fair value of the land would be the market value of the entire central business district-located site (emphasis added). We noted that IPSASB has provided some guidance on land under or over infrastructure in paragraph *IG21 Implementation Guidance of ED 78 Property, Plant and Equipment*, but it would be helpful to have guidance on the principles of land under COV(CC) more generally in ED 77.

IG21. The replacement cost of the land is based on the current value of the land based on the existing site. For example, if the road runs through agricultural land, then the current value of the land under that section of the road will be agricultural and if the road runs through an industrial area, then the current value placed on the land under that section of the road will be industrial

Entity-Specific Value (B8 & B9)

The IPSASB states that an entity shall measure the COV of an asset using the assumptions from the entity's perspective and the asset's COV represents an entry price. Paragraph 24 of ED 77 also states:

24. In some cases, current operational value can be determined directly by observing prices in an active market. In other cases, it is determined indirectly. For example, if prices are available for a similar asset, the current operational value of the entity's asset might need to be estimated by adjusting the current price of the similar asset to reflect the unique aspects of the entity's asset in its current use.

We note the definition of entry price *is the price paid to acquire an asset in an exchange transaction.*

Applying the COV(CC) guidance proposed for public sector land assets held for service potential measured, we note in our jurisdiction that:

- there is unlikely to be an orderly market providing prices for public sector land reflecting the unique aspects of the entity's asset in its current use. at measurement date
- we are likely to observe an orderly market and fair value price for adjacent properties or property near the location of the public sector asset
- the starting point of measuring relevant public sector land is likely to be the price of the land next door, reflecting the value of its location
- consideration would likely be given as to whether any adjustments should be made to the fair value price of adjacent properties, to reflect the relevant characteristics of the public sector property being valued (e.g. its shape).

In ED 77 under the COV(CC) basis we are unsure if IPSASB's view is that, in the event that adjacent land use is different (e.g. agricultural, commercial or urban) from the public sector use (e.g. hospital, school or prison), is the land next door considered a similar asset in the context of paragraph 24 of ED 77.

In other words, the ED as currently drafted leaves open the question as to whether the different use of land by the public sector entity (in producing public goods) relative to the adjacent land use (in producing private goods) is a *unique aspect of the entity's assets in current use*, for which an adjustment to the land price should be considered, or whether the specific public sector use relates to the assets that are placed on that land.

Treasury has observed that some entities and valuers apply a discount to land that is applied for public sector specific purposes. The Treasury does not support such an approach. Generally, such discounts are arbitrary, and reflect a mistaken assumption that the use of land for a public sector purpose has a lower value than the use of adjacent land for cash generating purposes. It is arguable for example that the (public benefit) value of a park, is higher than the (future cash) value of apartments that overlook that park. If that was not the case, then the rational course of action for the public sector entity owning the park is to put the park up for sale. The inclusion of a discount, in our view, detracts from the information value of the measurement.

We are seeking clarity in ED 77, because if the public sector considers its use of the land relative to the adjacent land to be a unique aspect of the land, the intention of paragraph 24 of ED 77 appears to be that adjustments would always be made to the reference price of the adjacent land, which in the Treasury's view would be inappropriate.

Restrictions

The guidance on restrictions in paragraph B13 is limited to where the restriction is legally enforceable and cannot be revoked unilaterally by the entity holding the asset. We are wondering if this is an overly narrow view of a land restriction in the public

sector, and whether the physical presence of the public sector operational asset sitting on the land means the land asset is “restricted” (also refer to our comments above under *Entity-Specific Value (B8 & B9)*)

We observe that particularly from a whole-of-government reporting perspective, restrictions can often be placed on land, for the purpose of protecting it in its current (public sector) use because that is considered the most beneficial, although it may not generate the highest cash returns.

IPSASB is requiring if there is an orderly market for an equivalent restricted asset, entities should use that price at measurement date. But if there is not, the asset is measured at the price of an equivalent unrestricted assets, without a reduction for the restriction. This appears to be a rule, rather than a principle, so the principle in respect to restrictions is not clear to us. As noted above, we think there will be limited circumstances where there is an orderly market for restricted assets in our jurisdiction, so in practice we suspect the rule means no adjustment for restrictions. We think not taking into account restrictions is inconsistent with the principles in:

- paragraph 24 of ED77 which states “*For example, if prices are available for a similar asset, the current operational value of the entity’s asset might need to be estimated by adjusting the current price of the similar asset to reflect the unique aspects of the entity’s asset in its current use.*”, and
- IG15 of ED 78 Property, Plant and Equipment where it is stated that restrictions on the use of heritage assets do not affect an entity’s ability to derive current values for them. However, restrictions will need to be taken into account when deriving a current value.

Surplus Capacity (B10 to B12)

As noted above we have general concerns with lack of clarity in the classification of surplus capacity, impairment and economic obsolescence. In respect of land associated with the asset measured under a COV(CC) basis, the IPSASB should clarify if surplus land associated with a public sector asset under COV(CC) measurement basis, should be measured as a separate unit of account for its financial capacity if it was capable of being sold or leased separately.

We think there are significant interpretation challenges with the measurement principles in respect to land asset under the COV(CC) basis, which the IPSASB could usefully explicitly address in ED 77 through use of illustrative examples.

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.

We agree that the asset's COV should assume that the notional replacement will be situated in the same location as the existing asset is situated or used. This is consistent with ensuring that the measure reflects the asset's current use and location.

However, we have concerns around the IPSASB proposed guidance in respect of surplus capacity, restrictions and measurement of land under COV(CC) – refer to our response to SMC 5 & 6 above.

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.

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

The Treasury does not agree that the income approach is an applicable measurement technique to estimate the value of an asset measured using the COV measurement basis for the reasons provided by Mr. Todd Beardsworth and Mr. Mike Blake in the Alternative view.

We also agree with the Alternative View that replacement cost would most commonly be an appropriate technique to use rather than the income approach for property, plant and equipment, as this would more appropriately reflect the service potential embodied in assets and the current cost of providing services using those assets.

Also refer to our responses to SMC 3 on ED 76 and SMC 5 & 6 on ED 77.

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.

We generally agree the guidance on fair value (that has been aligned with IFRS 13, Fair Value Measurement (Appendix C: Fair Value)) is generally appropriate for application by public sector entities.

However, we have suggested in our response to SMC 5 & 6 that IPSASB removes the cost approach measurement technique guidance entirely from IFRS 13 and focus on developing a single cost approach measurement technique specifically for the public sector in ED 77. This would simplify the number of measurement techniques available under the current value model which would be less complex for preparers, valuers, auditors and users of financial statements. It would also allow the IPSASB to develop single comprehensive guidance for a current cost approach without butting up against an overarching exit value definition of fair value.

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 fulfilment has been aligned with existing principles in the Conceptual Framework and throughout IPSAS (Appendix D: Cost of Fulfilment).

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 Treasury agrees the guidance is appropriate for application by public sector entities. We note that question as to whether a risk premium should be included in the calculation [of cost of fulfilment] will depend on guidance in the relevant IPSAS, and therefore that has not been settled by this project. We note that this can be a contentious issue for insurance and insurance-like activities that public sector entities undertake.

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.

The Treasury agrees 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.

We have not identified any measurement disclosure requirements that apply across IPSAS that should be included in the proposed standard on Measurement.

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.

The Treasury agrees that, where relevant, current value model disclosure requirements should be applied consistently across IPSAS, that is, the same disclosure requirements should apply to inventory and property, plant, and equipment when measured at fair value. This will allow for more consistent disclosure of information when the current value model is used in different standards.

Specific Matter for Comment 14

Do you agree with the proposed 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.

The Treasury agrees that the proposed 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.

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.

The Treasury agrees the fair value disclosure requirements should include requirements to disclose the significant inputs to the fair value hierarchy.

Responses on Exposure Draft 78: *Property, Plant and Equipment*

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?

The Treasury agrees with the proposed restructuring of IPSAS 17 within ED 78.

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.

The Treasury generally considers that as property, plant, and equipment is defined as tangible assets that are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and are expected to be used during more than one reporting period, then the measurement objective is more likely to be met by a current cost model than a fair value model. We consider that steer could be made clearer in the standard.

For example, the second sentence of paragraph 29 be strengthened to read (refer to underlined text below):

The primary objective for which an entity holds an asset guides determines the selection of the current value measurement basis (for example, reporting assets held for the supply of public goods are likely to best meet measurement objective if a current cost approach is used).

We do however consider the choice should be available. Some property plant equipment may be intended for sale or disposal, but not be expected to be able to be sold in less than a year, open and active markets for property and for some items of plant and equipment may mean that land is more easily valued on a fair value basis, and the difference between current cost and a fair value is negligible. In such cases the choice should be available to reporting entities.

Consistent with that thinking, Treasury also recommends that paragraph 30 be amended to clarify that a change in the current value measurement basis, for example, from COV to fair value, is appropriate only if there is a change to the primary objective for holding the asset, for example from operational capacity to financial capacity.

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.

The Treasury does not have additional characteristics of heritage assets (other than those noted in paragraph AG3) that we consider present complexities when applying the principles of ED 78 in practice.

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.

The Treasury observes that in New Zealand infrastructure is a broad term, defined in legislation as “physical infrastructure that is in New Zealand or that results in services in New Zealand” We would therefore not support further refining of the concept in the proposed standard.

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?

The Treasury agrees that such disclosures in respect of heritage property, plant, and equipment that is not recognized in the financial statements should be limited to heritage items in this standard. While it may be argued that similar disclosures may be required of other non-reported assets (e.g. intangibles, natural resources) such issues are better dealt with in separate standards.

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.

The Treasury is generally comfortable with the Implementation Guidance developed as part of this Exposure Draft for heritage assets.

However, the absence of market prices and/or the difficulty in obtaining reliable current values is likely to affect how heritage assets are measured. We question whether COV is a useable or relevant measurement base for certain irreplaceable heritage 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

The Treasury is generally comfortable with the Implementation Guidance developed as part of this Exposure Draft for infrastructure assets.

Responses on Exposure Draft 79: *Non-current Assets Held for Sale and Discontinued Operations*

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?

The Treasury agrees in general that there is no public sector specific reason to depart from the measurement requirements of IFRS 5 Non-current Assets Held for Sale and Discontinued Operations.

However, we recommend that the scope of the proposed standard be clarified to take an issue that is common in the public sector but rare in the private sector.

In the public sector, assets are often transferred between commonly controlled public entities with reporting obligations to comply with GAAP. Typically, in the private sector such "internal transfers" are made between subsidiaries that do not have public accountability reporting requirements

Such transfers can take place at full consideration, nominal consideration, below market consideration or no consideration. Where assets are transferred between commonly controlled entities at an entry value (COV/CC) that is above exit value (fair value), the accounting under the proposed standard will not be appropriate, as it would result in:

- an immediate loss for the transferor on classification of the asset as held for sale (resulting from measuring the assets at fair value less costs to sell); and
- an immediate write up in value of the asset for the transferee (resulting from measuring the assets back to COV/CC).

In New Zealand's case, other public sector specific examples include assets (for example, land and building) that are held for Treaty of Waitangi treaty settlements. These assets are non-current, are being held for disposal in accordance with a plan,

and disposal is highly likely. However, such assets could not be said to be actively marketed, and it is common that the negotiations that lead to the final disposal will take more than a year. It is unclear if these are considered to be non-current assets held for sale and therefore within the scope of the proposed standard.

