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Ms Stephanie Fox
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Our ref **KK/288**
Contact **Katja van der Kuij**

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Dear Ms Fox

Conceptual Framework Exposure Draft 3 for General Purpose Financial Reporting by Public Sector Entities: Measurement of Assets and Liabilities in Financial Statements

Summary comments

We appreciate the opportunity to respond to the International Public Sector Accounting Standards Board's ('IPSASB' or the 'Board') Exposure Draft ('ED') entitled *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Measurement of Assets and Liabilities in Financial Statements*, dated November 2012. We have consulted with, and this letter represents the views of, the KPMG network.

While we generally are supportive of the draft, we have identified specific matters that we believe merit further consideration. These follow below:

Overall Comments

The term "operational assets" is used throughout the exposure draft. A definition of operational assets should be included either in this document or in the 'Elements and Recognition in Financial Statements' section of the conceptual framework. Such definition could be "An operational asset is a non-financial asset which is held to provide services."

We disagree with the statement in paragraph 3.11, if the implication as drafted is that market value is representationally faithful with respect to reporting the cost of service. Market values report the cost that would have been incurred had the asset been purchased at the time the service was provided. It is therefore not representationally faithful to the transaction that actually occurred which was the cost at the time the asset was acquired, in particular for operational assets.

Much of the discussion in paragraph 5.9 appears to be a recognition issue rather than a measurement issue and should be excluded from this standard.

Providing examples of the application of the various measurement models may be helpful to users. For example, application of the deprival model may be enhanced if an example is provided of specific circumstances where it would be used. Many services provided by a government entity would be difficult to value. For example, a government entity provides a service in its office building. How would the service provided be valued to determine the value of the office building?

Specific Matter for Comment 1

You ask whether “*we agree that the selection of a measurement basis should be based on the extent to which a particular measurement basis meets the objectives of financial reporting and if so what should this measurement objective be*”.

We generally agree that the selection of a measurement basis should be based on the extent to which a particular measurement basis meets the objectives of financial reporting. No one measurement objective should be developed since the characteristics of the particular asset or liability should be considered when selecting the appropriate measurement basis. The overall financial statement objectives should be considered in the selection of a measurement basis as is outlined in the discussion in paragraph 1.3 and in Sections 3 and 4. This will ensure that the general purpose financial statements provide information that meets the objectives of financial reporting.

Table 1 on page 13 indicates that net selling price is an observable value. This value won't always be an observable value and when it is observable there may be a greater or lesser degree of transparency around the value depending on the circumstances. This should be indicated in the Table.

Paragraph 3.5 should be expanded to include a definition of an active market similar to that provided in Appendix A of IFRS 13.

Specific Matter for Comment 2

You ask whether “*we agree with the current value measurement bases for assets that have been identified in Section 3. If not, indicate which additional measurement bases should be included and which should not be included.*”

We agree with the current value measurement bases for assets that have been identified in Section 3. A clear discussion on the circumstances when one would use the measurement basis should be included for each basis similar to the discussion in paragraph 3.44 for “value in use”. Paragraph 3.22 should state that replacement cost is appropriate when it is greater than the value in use.

Paragraph 3.8 should clearly state that market value is not an appropriate measurement basis for operational assets that do not have an open and active market.

Specific Matter for Comment 3

You ask whether “*we agree with the approaches proposed in Section 4 for application of:*

(a) The fair value measurement model to estimate the price at which a transaction to sell an asset would take place in an active, open and orderly market at the measurement date under current market conditions.; and

(b) The deprival value model to select or confirm the use of a current measurement basis for operational assets.”

- (a) Paragraph 4.6(a) assumes that “the valuation of a non-financial asset is based on the premise that the asset will be used in its highest and best use.” Fair value determined in this manner would be a higher value than what is actually being derived by the entity. It does not reflect the actual use to which the asset is put. This would have a negative effect on the representational faithfulness of the transaction. The model needs to incorporate actual use of the underlying asset in order to reflect the entity’s actual circumstances.

Paragraph 4.6(b) assumes that “the transaction takes place in the principal (most advantageous) market”. While the entity holding the asset might desire that the transaction takes place in the most advantageous market, that is not always the case. Thus, the model needs to incorporate market’s real potential into its calculation in order to derive more value from the resulting calculation.

- (b) The Deprival Value Model has limited use in specific circumstances. Examples of when the deprival value model should be used should be included in the standard if it is to be used at all. Valuers use this model for long-term assets of a specialised nature or self-developed fixed assets where there is limited market replacement cost information or other market corroborative evidence. The deprival value model can be abused to justify a wide range of fair values so clear guidance needs to be given for its use. For example, a limitation on future cash flows used in estimating the value or explicit guidance to consider functional and technological obsolescence and age of the asset being valued. The deprival value model should be considered a last resort method of establishing value.

Specific Matter for Comment 4

You ask whether “*we agree with the proposed measurement bases for liabilities in Section 5? If not, please indicate which additional measurement bases should be included or which measurement bases should not be included in the Framework.”*



We agree with the measurement bases for liabilities that have been identified in Section 5. However, we note that much of the discussion in paragraph 5.9 appears to be a recognition issue rather than a measurement issue and should be excluded from this ED.

KPMG appreciates the opportunity to respond to this ED. Please contact Archie Johnston at +1 604 527-3757, Peter Greenwood at +1 604 691 3187 or Katja van der Kuij at +44 20 7694 8871 if you wish to discuss any of the issues in this letter.

Yours sincerely

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