

CONSULTATION PAPER (CP)

MEASUREMENT

The Technical Director

International Public Sector Accounting Standards Board (IPSASB)

International Federation of Accountants

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October 14, 2019

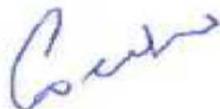
Dear Mr. John Stanford,

The Conselho Federal de Contabilidade (CFC) of Brazil welcomes the opportunity to collaborate with the consultation on *Measurement*. CFC, along with its regional arms - Regional Accounting Councils or Conselhos Regionais da Contabilidade (CRCs), is the Professional Accountancy Organization that carries out regulatory activities including the issuance standards of ethics, education for accountants, auditing and accounting for the private and public sectors and the overseeing of the accountancy profession throughout the country.

Our points of view and comments are included in the Appendix to this letter and was prepared by the Advisory Group for Public Sector Accounting Standards (GA/NBC TSP) of the CFC.

If you have any questions or require clarification of any matters in this submission, please contact: tecnica@cfc.org.br.

Regards,



Idésio S. Coelho
Technical Vice-President
Conselho Federal de Contabilidade

APPENDIX

1. Context and General Comments

The Brazilian Federation is composed by central, 26 states, the Federal District and more than 5,500 city governments. These levels of governments are responsible for formulating, implementing and evaluating public policies in cooperative and/or competitive arrangements.

In this document, we present the contributions for the consultation paper based on a practical approach applicable to our jurisdiction.

In general, we believe that most of the IPSASB propositions of the Measurement project are appropriated, however, we think that, at least, all measurement bases existing in specific IPSAS should be considered as part of the planned Measurement standard, including Value in Use and Net Realizable Value.

In addition, we share the opinion that it's important to identify the fair value as a measurement basis in the IPSASB's Conceptual Framework, clarifying what are the differences between Market Value and Fair Value, and also that borrowing costs that are directly attributable to the acquisition, construction, or production of a qualifying asset must be capitalized.

In the next section, we present our comments and answers on the preliminary views and specific matters for comment of the consultation paper.

2. Responses to the Preliminary Views and Specific Matters for Comment

Preliminary View 1 – Chapter 2 (following paragraph 2.6)

The IPSASB's Preliminary View is that the fair value, fulfilment value, historical cost and replacement cost measurement bases require application guidance.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons, stating clearly which measurement bases should be excluded from, or added to, the list, and why.

GA/CFC does not agree with Preliminary View 1. The measurement bases identified in Chapter 7 of the Conceptual Framework are: historical cost, market value, replacement cost, net selling price, and value in use, for assets; and, historical cost, cost of fulfilment, market value, cost of release, and assumption price, for liabilities. In deciding whether it needed to develop generic application guidance, the IPSASB considered how widely a particular measurement basis was used, excluding measurement bases whose specific IPSAS applies to specific transactions (e.g., value in use) and net realizable value (currently not considered necessary because this measurement basis is specific to inventories).

However, the IPSASB considers the possibility to select other bases in order to achieve this measurement objective (see Diagram 4.1 and 4.2). Considering this, it is expected a generic application guidance about the other bases with the purpose to allow constituents to evaluate the decision made by the IPSASB in providing guidance on application of measurement bases in existing and future IPSAS, and guidance on how to apply the measurement bases where specific IPSAS is not sufficient, and as a result the bases presented in Conceptual Framework should be used. In summary, at least, all bases presented in specific IPSAS require an application guidance.

Preliminary View 2 – Chapter 2 (following paragraph 2.6)

The IPSASB's Preliminary View is that the application guidance for the most commonly used measurement bases should be generic in nature in order to be applied across the IPSAS suite of standards. Transaction specific measurement guidance will be included in the individual standards providing accounting requirements and guidance for assets and liabilities.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons, and state what guidance should be included, and why.

GA/CFC agrees with Preliminary View 2. We believe that adding a specific guidance for a specific IPSAS within that IPSAS can be more methodologically appropriate to users, in accordance with the view that the new measurement standard should focus on generic principles rather than on the specificities of particular transactions or standards.

Preliminary View 3 – Chapter 2 (following paragraph 2.10)

The IPSASB's Preliminary View is that guidance on historical cost should be derived from existing text in IPSAS. The IPSASB has incorporated all existing text and considers Appendix C: Historical Cost–Application Guidance for Assets, to be complete.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons, stating clearly what you consider needs to be changed.

GA/CFC partially agrees with Preliminary View 3. In developing measurement guidance for historical cost in the Illustrative ED, the IPSASB consolidated guidance available in the Conceptual Framework, IPSAS 16 (Investment Property), and IPSAS 17 (Property, Plant, and Equipment), but the board did not address historical cost for liabilities.

Therefore, the proposal of carrying over the existing text from those IPSAS that is generic in nature directly into the Illustrative ED seems to be appropriate in relation to assets. However, for liabilities, a new guidance should be provided.

Preliminary View 4 – Chapter 2 (following paragraph 2.16)

The IPSASB's Preliminary View is 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. The IPSASB considers Appendix A: Fair Value–Application Guidance, to be complete.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons, stating clearly what you consider needs to be changed.

GA/CFC partially agrees with Preliminary View 4, considering some issues presented below.

Considering that fair value measurement requirements are most commonly referred to in IPSAS that are aligned with IFRS Standards (IPSAS 16 – Investment Property, IPSAS 17 – Property, Plant, and Equipment, and IPSAS 41 – Financial Instruments), and also that the relevance of fair value in the public sector is likely to be primarily limited to provide information on financial capacity, rather than information on operating capacity, and cost of services, it seems reasonable that fair value guidance should be aligned with IFRS 13 where applicable, without disregarding public sector financial reporting requirements in order to provide information to stakeholders.

Although GA/CFC shares the view that fair value as defined in IFRS 13 is relevant, we believe that measuring the fair value of some non-financial assets held by public sector entities based on its highest and best use by market participants is controversial, because it may not appropriately reflect the relevant service potential of asset to the public sector entity (indeed, in order to achieve the public interest, an entity may intend not to use the asset according to its highest and best use).

However, we believe that's important to consider the fair value as a measurement basis in the Conceptual Framework, and to identify what are the differences between fair value and market value. It is also important to describe the relationship between replacement cost as defined in the Conceptual Framework (as a measurement basis) and replacement cost as a measurement technique to determine fair value.

Preliminary View 5 – Chapter 2 (following paragraph 2.28)

The IPSASB's Preliminary View is that fulfilment value guidance should be based on the concepts developed in the Conceptual Framework, expanded for application in IPSAS. The IPSASB considers Appendix B: Fulfilment Value–Application Guidance, to be complete.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons, stating clearly what you consider needs to be changed.

GA/CFC agrees with Preliminary View 5. Since there are concepts developed on fulfilment value base in the Conceptual Framework, it seems to be appropriate that fulfilment value guidance should be defined from the perspective of the Conceptual Framework, expanding the related principles and developing guidance on how to apply it.

Preliminary View 6 – Chapter 2 (following paragraph 2.28)

The IPSASB's Preliminary View is that replacement cost guidance should be based on the concepts developed in the Conceptual Framework, expanded for application in IPSAS. The IPSASB considers Appendix D: Replacement Cost–Application Guidance, to be complete.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons, stating clearly what you consider needs to be changed.

GA/CFC partially agrees with Preliminary View 6. Since there are concepts developed on replacement cost basis in the Conceptual Framework, it seems to be appropriate that replacement cost guidance should be defined from the perspective of the Conceptual Framework, expanding the related principles and developing guidance on how to apply it.

However, as mentioned in the answer about PV4, we believe that it is important to describe the relationship between replacement cost as defined in the Conceptual Framework (as a measurement basis) and replacement cost as a measurement technique to determine fair value.

Preliminary View 7 – Chapter 3 (following paragraph 3.28)

The IPSASB's Preliminary View is that all borrowing costs should be expensed rather than capitalized, with no exception for borrowing costs that are directly attributable to the acquisition, construction, or production of a qualifying asset.

Do you agree with the IPSASB's Preliminary View?

If not, please state which option you support and provide your reasons for supporting that option.

GA/CFC does not agree with Preliminary View 7. We believe that all costs incurred to obtain the asset and get it ready for its intended use, including borrowing costs, should be included in the cost of an asset, so that expenses would be allocated to the reporting period which they are related, better supporting the assessment of the cost of services. Thus, we support the option 3.

In public sector, borrowing costs are often centralized and funding schemes to obtain an asset comes from a variety of sources which include tax revenues, service fees, debt and so on. In our jurisdiction, the financial information systems can generate segregated information that make the attribution of borrowing costs to qualifying assets possible in a reasonable and non-arbitrary manner. For this reason, we believe that there would be no operational limitation on applying it in many jurisdictions.

We also believe that capitalization of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset is appropriate based on the premise that historical cost is an entity-specific value. In other words, the capitalization of borrowing costs reflects economic opportunities that are not available to other entities and risks that are not experienced by other entities (which is in line with the Conceptual Framework – Chapter 7), including the entity’s financing choices.

In relation to the issue that capitalization of borrowing costs appears to incorrectly show to users of the financial statements that assets financed through borrowing have more service potential or future economic benefits compared to similar assets held by an entity that does not use debt to finance its asset acquisitions, it’s important to remember that one of the objectives of measurement, in accordance with the Conceptual Framework (Chapter 7), is enable users to assess the cost of services provided in the period, meaning, in the case of historical cost, the resources expended to acquire or develop assets consumed in the provision of services.

Regarding the issue that the capitalization of interest costs would “hide” the amount of borrowing costs, the disclosure in notes to the financial statements about the amount of interest capitalized allows users to calculate total borrowing costs for the period.

Finally, although one of the IPSASB’s stated objectives is to reduce unnecessary differences between IPSAS and GFS, the different objectives and focus on different reporting entities lead to the different treatment of some transactions and events. Thus, the option of all borrowing costs should be expensed, although aligned with the requirements in IPSAS 5 with GFS, seems not to be in line with the measurement objective of reflecting the costs of services, i.e., the amount of the resources expended to acquire or develop assets consumed in the provision of services, including the costs that are directly attributable to the acquisition, construction or production of a qualifying asset.

Preliminary View 8 – Chapter 3 (following paragraph 3.36)

The IPSASB’s Preliminary View is transaction costs in the public sector should be defined as follows: Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of an asset or liability and would not have been incurred if the entity had not acquired, issued or disposed of the asset or liability.

Do you agree with the IPSASB’s Preliminary View?

If not, please provide your reasons, and provide an alternative definition for the IPSASB to consider.

GA/CFC agrees with Preliminary View 8. We think that the proposed definition is aligned with the IFRS Standards, IVS and GFS definitions of transaction costs, highlighting that transaction costs are a direct result of the transaction accommodating an entry and exit price.

Considering that a number of IPSAS refer to such costs in different terms with different requirements and guidance, and generally do not call them “transaction costs”, we believe that is important to define “transaction costs” in the public sector in order to improve consistency in how transaction costs are accounted according to different IPSAS. In other words, we agree that a general definition of transaction costs would ensure a consistent meaning for transaction costs in all IPSAS suite of standards, while also supporting the understandability of IPSAS.

Preliminary View 9 – Chapter 3 (following paragraph 3.42)

The IPSASB's Preliminary View is that transaction costs should be addressed in the IPSAS, Measurement, standard for all IPSAS.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons and state how you would address the treatment of transaction costs in IPSAS, together with your reasons for supporting that treatment.

GA/CFC agrees with Preliminary View 9. Developing general measurement guidance in the IPSAS, Measurement, is an objective of the IPSASB in this project. We believe that the development of a general definition of transaction costs that applies consistently to all IPSAS supports the view that transaction costs are the same regardless of the nature of the transaction.

Preliminary View 10 – Chapter 3 (following paragraph 3.54)

The IPSASB's Preliminary View is that transaction costs incurred when entering a transaction should be:

- Excluded in the valuation of liabilities measured at fulfillment value;
- Excluded from the valuation of assets and liabilities measured at fair value; and
- Included in the valuation of assets measured at historical cost and replacement cost.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons and state how you would treat transaction costs in the valuation of assets and liabilities, giving your rationale for your proposed treatment.

GA/CFC partially agrees with Preliminary View 10.

We disagree with the exclusion from the valuation of assets and liabilities measured at fair value as in accordance with paragraphs 4.1.2A and 5.7.5 (and example in paragraph B5.2.2) of IFRS 9, the valuation of financial asset measured at fair value with changes through other comprehensive income does not exclude transaction costs.

So, IPSAS will be different from IFRS 9.

Preliminary View 11 – Chapter 3 (following paragraph 3.54)

The IPSASB's Preliminary View is that transaction costs incurred when exiting a transaction should be:

- Included in the valuation of liabilities measured at fulfillment value;
- Excluded from the valuation of assets and liabilities measured at fair value; and
- Excluded in the valuation of assets measured at historical cost and replacement cost.

Do you agree with the IPSASB's Preliminary View?

If not, please provide your reasons and state how you would treat transaction costs in the valuation of assets and liabilities, giving your rationale for your proposed treatment.

GA/CFC partially agrees with Preliminary View 11.

We disagree with the exclusion from the valuation of assets and liabilities measured at fair value as in accordance with paragraphs 4.1.2A and 5.7.5 (and example in paragraph B5.2.2) of IFRS 9, the valuation of financial asset measured at fair value with changes through other comprehensive income does not exclude transaction costs.

So, IPSAS will be different from IFRS 9.

Specific Matter for Comment 1 – Chapter 2 (following paragraph 2.29)

Definitions relating to measurement have been consolidated in the core text of the Illustrative ED.

Do you agree that the list of definitions is exhaustive?

If not, please provide a listing of any other definitions that you consider should be included in the list and the reasons for your proposals.

GA/CFC does not agree. We understand that other definitions should be included in the list of definitions of the Illustrative ED:

- i) **Cost of services:** this concept is defined in the Conceptual Framework and means the cost of services provided in the period in historical or current terms.
- ii) **Operation capacity:** as defined in the Conceptual Framework, it means the capacity of the entity to support the provision of services in future periods through physical and other resources;
- iii) **Financial capacity:** this concept is also outlined in the Conceptual Framework, meaning the capacity of the entity to fund its activities.

As one of the objectives of the IPSAS, Measurement, standard is to define measurement bases that assist in reflecting fairly the cost of services, operational capacity and financial capacity of assets and liabilities (i.e., achievement of the objective of measurement), it seems to be reasonable that these concepts be defined in the list of definitions of the Illustrative ED.

- iv) **Impairment:** this concept is defined in the core text of the Illustrative ED, meaning the extent to which the service potential or ability to generate economic benefits provided by an asset have decreased due to changes in economic or other conditions, as distinct to

their consumption. It seems to be more methodologically appropriate this concept be carried out to the list of definitions.

- v) **Borrowing costs:** as defined in the IPSAS 5, Borrowing Costs, it means interest and other expenses incurred by an entity in connection with the borrowing of funds. Considering that we share the view that all costs incurred to get the asset ready for its intended use, including the cost of financing, be included in the cost of an asset, we think it's more appropriate the concept of *borrowing costs* be defined in the list of definitions of the Illustrative ED.

Specific Matter for Comment 2 – Chapter 3 (following paragraph 3.5)

Guidance in International Valuation Standards (IVS) and Government Financial Statistics (GFS) has been considered as part of the Measurement project with the aim of reducing differences where possible; apparent similarities between IPSAS, IVS and GFS have been noted.

Do you have any views on whether the IPSASB's conclusions on the apparent similarities are correct?

Do you agree that, in developing an Exposure Draft, the IPSASB should consider whether the concepts of Equitable Value and Synergistic Value should be reviewed for relevance to measuring public sector assets (see Addendum B)?

GA/CFC shares the view that it appears to be apparent similarities between IPSAS, IVS and GFS, especially in the discussion of Fair Value and Replacement Cost, between Net Selling Price measurement basis and the IVS Liquidation Value, and between the IPSAS concept of value in use for a cash generating asset and the IVS Investment Value.

GA/CFC agrees with the potential relevance of the concepts of Equitable Value and Synergistic Value for some public sector transactions. For example, the relationship between the Synergistic Value with the concept of *cash-generating unit* from IPSAS 26, *Impairment of Cash-Generating Assets* may represent an interesting issue to explore.

Specific Matter for Comment 3 – Chapter 4 (following paragraph 4.21)

Do you agree that the measurement flow charts (Diagrams 4.1 and 4.2) provide a helpful starting point for the IPSASB to review measurement requirements in existing IPSAS, and develop new IPSAS, acknowledging that other matters need to be considered, including:

- The Conceptual Framework Measurement Objective;
- Reducing unnecessary differences with GFS;
- Reducing unnecessary differences with IFRS Standards; and
- Improving consistency across IPSAS.

If not, should the IPSASB consider other factors when reviewing measurement requirements in existing IPSAS and developing new IPSAS? If so, what other factors? Please provide your reasons.

GA/CFC agrees that the measurement flow charts provide a helpful starting point for the IPSASB to review measurement requirements in existing IPSAS and develop new IPSAS. However, we believe that application guidance about the other measurement bases are necessary to decide about the appropriate basis. If the application guidance about the other measurement bases does not exist, it will be more difficult to evaluate if the bases other than historical cost, replacement cost, fulfillment cost and fair value are more appropriate. In addition, the detailed description regarding only four bases of measurement can generate bias in interpretation and application, since there is more knowledge about the selected ones.