UNITED NATIONS SYSTEM **SYSTEME DES NATIONS UNIES**

Chief Executives Board for Coordination

Conseil des chefs de secrétariat des organismes des Nations Unies pour la coordination

SUBMISSION: Conceptual Framework Exposure Draft 3: *Measurement of Assets and Liabilities in Financial Statements*

30 April 2013

Ms. Stephenie Fox
Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street West
Toronto Ontario Canada M5V 3H2

Dear Stephenie,

Conceptual Framework Exposure Draft 3

1 Thank you for the opportunity to comment on Conceptual Framework Exposure Draft 3 (CF–ED3), *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Measurement of Assets and Liabilities in Financial Statements*.

United Nations System Task Force on Accounting Standards

2 The United Nations System Task Force on Accounting Standards (Task Force) appreciates the work that the IPSASB is carrying out in developing accounting standards for public sector entities, including international organizations such as those making up the United Nations system. The Task Force is an inter-agency group consisting of directors of accounting, chief accountants and chief financial officers from United Nations System organizations. The comments below represent the views of Members of the Task Force. The individual organizations that provided comments on this submission and concurred with its submission to the IPSASB are listed in Appendix 1. Where an individual organization disagreed with a particular recommendation but agreed to the recommendation going forward to the IPSASB, this has been noted against the individual responses in Appendix 2.

General Comments

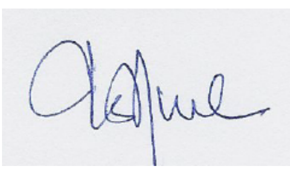
3 We support IPSASB's efforts in developing the Conceptual Framework, which establishes parameters for financial reporting under IPSAS and clarifies concepts not previously explicitly covered by the Standards. We note, however, that discussion in the CF-ED3 focuses mainly on specific attributes and challenges of governments, making it less useful and applicable for use by other public sector entities. This is also true for other documents issued as part of the IPSASB's Conceptual Framework project.

Specific Matters for Comments

4 Our detailed comments on the specific matters for comment identified in CF-ED3 are attached as Appendix 2.

5 Should you have any queries on our comments, please contact Ms. Dinara Alieva, Financial Analyst, System-wide IPSAS Project Team at alievad@un.org.

Yours sincerely,



Chandramouli Ramanathan

Deputy Controller, United Nations &
Chair, Task Force on Accounting Standards

ramanathanc@un.org

APPENDIX 1: UNITED NATIONS SYSTEM TASK FORCE ON ACCOUNTING STANDARDS

Task Force Members from the following organizations reviewed this submission and concurred with its contents.

Organisation	Agree (Disagree)
1. FAO	Agree
2. IAEA	Agree
3. ICAO	Agree
4. ILO	Agree
5. IMO	Agree
6. ISA	Agree
7. ITU	Agree
8. PAHO	Agree
9. UN	Agree
10. UNAIDS	Agree
11. UNDP	Agree
12. UNESCO	Agree
13. UNFPA	Agree
14. UNHCR	Agree
15. UNICEF	Agree
16. UNIDO	Agree
17. UNOPS	Agree
18. UNRWA	Agree
19. UPU	Agree
20. WFP	Agree
21. WHO	Agree
22. WIPO	Agree
23. WMO	Agree
24. WTO (Tourism)	Agree
25. UNWomen	Agree

APPENDIX 2: CONCEPTUAL FRAMEWORK FOR GENERAL PURSPOSE FINANCIAL REPORTING BY PUBLIC SECTOR ENTITIES: MEASUREMENT OF ASSETS AND LIABILITIES IN FINANCIAL STATEMENTS (CF-ED3 or Exposure Draft)

In response to the IPSASB's request for comments on these Specific Matters please find below comments of the Task Force:

Specific Matter for Comment 1

Do you 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? If you think that there should be a measurement objective please indicate what this measurement objective should be and give your reasons.

Response:

The Task Force has no objections against proposed selection of measurement basis based on the extent to which they meet the objectives of financial reporting. However application of this proposal in public sector environment might need to be further considered by the Board.

For example, it was noted that Exposure Draft derives three assessment criteria from objectives of financial reporting which include financial capacity, operational capacity and cost of services provided. Whereas operational capacity and cost of services appear to be clear and logical criteria, practical application of financial capacity as a criterion used to assess relevance of measurement bases appears to be more complex. An assessment of financial capacity requires information on the amount that would be received on sale of an asset to fund operating capacity of a reporting entity, i.e. its resources to support provision of services in future. However, most of the assets owned by public sector entities are used to provide services. If a public sector entity was to sell its assets it would not be able to support provision of services in future, i.e. would fail to meet requirements of operational capacity criterion. Although public sector entity might decide to sell an asset, it is usually because an asset is no longer required for provision of a service or a related service is no longer provided. In other words, the need to provide services determines what assets are kept or sold rather than the sale of an asset determines whether a service would be provided. Thus the proposed application of the criterion of financial capacity may not be as relevant to the public sector entities and useful to the users of GPFS as implied in the CF-ED 3. The Task Force recommends that the IPSASB reassesses relevance and usefulness of the financial capacity criterion as it is currently presented in CF-ED3. Perhaps it could be merged with the criterion of operational capacity which is defined as "physical and other resources available to support the provision of services in future periods" (para. 1.3). Assets owned by a reporting entity in public sector environment are typically part of such resources.

The Task Force also notes that the CF-ED3 does not prescribe a single measurement basis (or combination of bases), but rather identifies factors that are relevant in selecting a measurement basis. This proposed approach is in line with recommendations of the Task Force submitted to the IPSASB previously as feedback on draft CF-CP3. It was also noted that CF-ED3 reviews measurement bases used in financial statements and does not consider application of these bases to other GPFRs.

Specific Matter for Comment 2

Do you agree with the current value measurement bases for assets that have been identified in Section 3? If not, please indicate which additional measurement bases should be included or which measurement bases should not be included in the Framework?

Response:

The CF-ED3 proposes five measurement bases, including historical cost and four methods of current value measurement (market value, replacement cost, net seeling price and value in use). Many of these bases have been previously used and defined by the Board in previously issued IPSASs. The CF-ED3 also discusses strengths and weaknesses of each method, including their assessment against three criteria referred to in response to SMC 1 above. The IPSASB recognizes that most bases have limitations that outweigh potential benefits of their application and considers them as less relevant to non-cash generating assets of a public sector entity whose primary goal is provide service rather than maximize profits / return on investment. Among these bases with limited relevance are market value in markets that are not open, active and orderly, value in use and net selling price bases. As discussed in the main body of CF-ED3 and in the Basis for Conclusions (para. BC 19), the Board seems to favour replacement cost basis as it meets most criteria and qualitative characteristics (QC). The discussion also includes a reference to a combined use of historical and replacement cost (para. 3.27). However CF-ED3 does not include any evidence to support its assumption that use of replacement cost basis (on its own or in combination with historical cost basis) would result in a more superior outcome for users of financial statements than, for example, use of historical cost basis, while cost of switching to a new measurement basis may be very significant for preparers of financial statements.

In addition, replacement cost basis, along with most other proposed bases, does not meet requirements of the criterion of reporting on financial capacity. Only one basis out of five meets such criterion – the net seeling price basis. It does not, however, meet other criteria and is said to be relevant only where a reporting entity intends to sell asset(s).

Regardless of the above mentioned limitations, the net selling price basis is repeatedly referred to in the CF-ED3 as a basis for preparing supplementary information on asset values because it meets criterion of reporting on financial capacity. It is not clear whether IPSASB envisages that the net selling price basis would be applied to all assets of a reporting entity or only to those which an entity intends to sell. The Task Force expressed concern regarding relevance of the criterion of financial capacity to selection of measurement bases in response to SMC 1 above. Moreover, the need to use an additional measurement basis comes with considerable costs to preparers of financial statements. CF-ED3 does not include a discussion or a reference to the cost-benefit analysis of reporting asset values on the net selling price basis in addition to another measurement basis. For these reasons the Task Force does not consider use of the net seeling price basis to be essential for reporting asset values in financial statements, unless a reporting entity intends to sell the assets.

The Task Force is of the view that other current value measurement bases for assets identified in Section 3 of the CF-ED3 can be considered by preparers of financial statements along with historical cost basis for measurement of assets.

The Task Force also notes with concern that proposed simultaneous application of multiple measurement bases might make information on asset values very complex and difficult to understand for users of financial statements. It may also affect comparability of information with other entities' financial statements since entities may choose different bases to measure similar assets arriving at significantly different results. It should therefore be considered weather use of multiple measurement bases, including simultaneous application thereof, to enhance usefulness of GPFS may actually detract from this goal due to complexity of the proposed approach.

The World Health Organization, a member of the Task Force, recommends expanding consideration of issues related to subsequent measurement of assets and liabilities in the CF-ED3.

Specific Matter for Comment 3

Do you 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. If not, please give your reasons; and

<u>Response:</u>

The Task Force notes IPSASB's conclusion that fair value should not be proposed as a measurement basis since it is very similar to market value and inclusion of both measurement bases is likely to be confusing (BC 24, BC 27). Instead fair value is used as a measurement model for the estimation of market value when the market is inactive. Fair value is currently defined in IPSAS as "the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction" (IPSASB Handbook 2012, Glossary of Defined Terms). Since concept of fair value in CF-ED3 appears to be aligned with that in previously issued pronouncements of the Board and CF-ED3 does not propose change in the definition of the fair value, the Task Force is inclined to support the approach proposed in Section 4 of the Exposure Draft. However it is noted that practical application of the fair value measurement model has not been thoroughly discussed in the CF-ED3 beyond introduction of assumptions to be used in this model.

(b) The deprival value model to select or confirm the use of a current measurement basis for operational assets. If not please give your reasons.

Response:

The Task Force notes IPSASB's decision not to require the use of the deprival value model. The Board concluded that this model can be used to assess the relevance of three measurement bases for operational assets – replacement cost, net seeling price and value in use (BC 29). It is important to note that the deprival value model addresses only the relevance of said measurement bases while objectives of financial reporting and QC continue to be the primary considerations in the selection of an appropriate basis (BC 30). Therefore even if deprival value model suggests a particular measurement basis a reporting entity may prefer a different measurement basis, for example, to achieve higher degree of compliance with QC.

Use of the deprival value method can be a complex and costly exercise as a reporting entity needs to calculate and compare outcomes of three possible measurement bases applied to the same asset and/or group of assets. This is a serious impediment for any reporting entity, but would be especially difficult for international public sector organizations which acquire assets through countless variations of special arrangements, including but not limited to donated assets and use of project assets, and often operate in areas with inactive markets.

The Task Force notes that CF-ED3 refers to use of a surrogate in cases where one measurement basis is regarded as the most appropriate conceptually, but another measurement basis may be used instead because it is considered to be not materially different or for other reasons. The Task Force supports this proposal.

Specific Matter for Comment 4

Do you 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?

Response:

The Task Force notes that Section 5 of the CF-ED3 proposes measurement bases for liabilities based on the same principles that it applies to measurement of assets. However measurement bases for liabilities have different limitations as compared to bases for measurement of assets. The discussion in Section 5 builds on but does not replicate material presented in Sections 2 and 3 of the CF-ED3.

It is noted that CF-ED 3 uses a recurring reference to resource-efficient course of action throughout the discussion in Section 5. Use of the most resource-efficient course of action implies that an entity would choose basis to measure its liability based on the most resource-efficient way to release such liability. For example, if the most resource-efficient course available to the entity is transfer of the liability, such liability is to be measured using ‘cost of release’ basis (which mirrors the net selling price basis for assets). The proposed approach does not seem to take into consideration that in public sector entities do not pursue maximization of profits, but are rather focused on provision of services and settling of obligations made to different parts of community, often on humanitarian grounds. Hence even if the most resource-efficient way for an entity would be to immediately release its liability by transferring it to the third party, it would probably still prefer to fulfill the said liability through provision of service to meet expectations of beneficiaries and donors. Hence realities of operating in public sector environment make concept of resource-efficient course of action significantly less relevant to selecting measurement basis for liabilities as compared to private sector operations. The Task Fore therefore recommends that the IPSASB reconsiders broad use of the concept of ‘resource-efficient course of action’ in CF-ED3 and proposes a different approach to selecting measurement basis for liabilities, which would be more relevant to the public sector entities. For example, reporting entities might be encouraged to select measurement basis depending on their intention towards settling a particular liability – through its fulfillment by provision of services or through its immediate release. This approach would likely result in a more realistic and therefore more useful presentation of entity’s liabilities to users of its financial statements.