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IPSAS Conceptual Framework

Measurement

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UK Government approach to Measurement

- UK Government has used IFRS since 1 April 2009 (local government from 1 April 2010)
- One economy; and transferable skills
- Adapted and interpreted for the public sector in the Government Financial Reporting Manual (and equivalent Manuals for health sector, devolved governments and local government)
- Support IPSAS – UK Technical Advisor works for HM Treasury
- Substantially follow IPSAS in UK Government
- Main issue – not for profit (non-exchange) transactions
- Two key aspects to UK approach:
    - Current value <u>not</u> historical cost (for non-current assets)
    - Replacement cost is a proxy for current value for assets

Conceptual Framework: Phase 3: Measurement: purpose of Consultation Paper

- Issued December 2010 – consultation closed June 2011
- To identify factors that should be considered in choosing measurement bases
- Examines measurement bases and approaches
  - ➢ Presumes mixed measurement model
  - ➢ Historical cost
  - ➢ Market values
  - ➢ Replacement cost
  - ➢ Deprival value approach
  - ➢ Relief Value Model – mirror for liabilities

General features of Measurement bases

- Historical or current
    - Historical: reflects an attribute at past date
    - Current: reflects economic and financial environment at reporting date
- Entry or exit perspective
    - Entry: reflects consideration payable (or receivable) for acquisition of asset (or assumption of liability)
    - Exit value: reflects amount that will be derived from asset from sale or service potential in fulfilling objectives of entity
- Market or entity-specific value
    - Market-based: may promote comparability as same asset reported at same amount by different entities
    - Entity-specific: reflects economic constraints and opportunities that determine possible use of asset or liability; some argue can be more relevant than market based approaches

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How do these features relate to the specific bases discussed in the Consultation Paper?

- Historical cost
  - Historical
  - Entry
  - Entity-specific
- Market value
  - Current
  - May be either entry or exit
  - Market
- Replacement cost
  - Current
  - Entry
  - Entity-specific

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Historical Cost: advantages and disadvantages

- Advantages suggested include:
  - High **verifiability**
  - **Understandable**, **timeliness** and **low cost** of obtaining information
  - Highly **relevant** as reflects actual transactions
  - **Faithful representation**
- Disadvantages suggested include:
  - Difficulty dealing with donated assets, assets provided on subsidised terms, assets held for long periods and collections of assets acquired in one transaction
  - **Questions about relevance** to assessment of future resource needs, and comparability

Market Values: advantages and disadvantages

Where an ideal market:

- Market value (MV) of asset is a ***relevant*** measure of its utility to entity
- MV provides ***faithful representation*** of value of asset
- MV provides values that are easy to ***understand***
- Information based on MV can normally be prepared quickly and with simple calculations, so ***timely***
- Amounts ***comparable*** *and* ***verifiable***

Where assets specialised:

- Unlikely to be a deep and liquid market, so estimation necessary - **reducing *comparability, verifiability* and und*erstandability***
- MVs may not be representative of the economic benefits/service potential the entity can derive from assets; ***relevance* is therefore questionable**
- Estimation may be possible, but excessively hypothetical, lacking ***relevance***

Replacement Cost: advantages and disadvantages

Replacement cost

- **Arguably highly relevant** for accountability and decision making in public sector:
  - reflects economic position of entity at reporting date
  - permits costs of providing services to be reported in current cost terms
- But can be complex and costly, with **impact on**:
  - **timeliness**
  - **comparability**
  - **verifiability**

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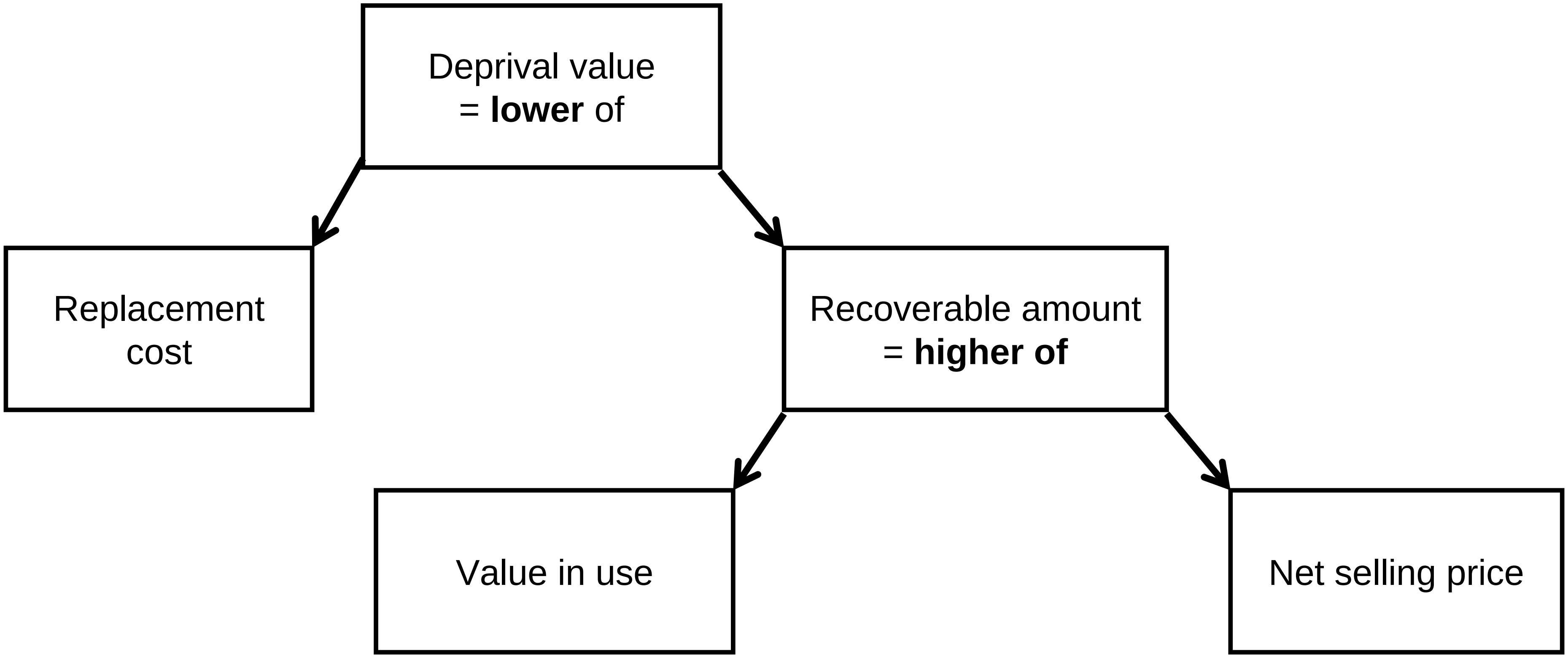
Deprival Value: What it is and is it useful?

- Deprival Value Model – a means of selecting relevant measurement basis
- Represents amount that would (just) compensate an entity for the loss of an asset:
    - replacement cost, except where recoverable amount is lower
    - recoverable amount is the higher of value in use and net selling price
- Suggests a basis that is highly **relevant**, but **does it reflect the other qualitative characteristics**?
- Determination of value in use is problematic in a non cash generating context
- Relief value model applies similar approach to liabilities

The Deprival Value Model for Assets



Other Issues

Own credit risk

- Take into account in measurement of liability at:
    - ➢ initial recognition
    - ➢ subsequent measurement

Alternative use

- Where asset use not restricted, should measurement reflect
    - ➢ only service potential relating to existing use
    - ➢ incremental value relating to possible sale for alternative use

IPSASB Measurement Consultation Paper: specific matters for comment

1. Should the framework identify relevant factors in selecting measurement bases or specify the measurement bases?
2. If there is one, what should a specific measurement basis be?
3. Does the Consultation Paper fairly describe the advantages and disadvantages of the various measurement bases?
4. Should an entity's own credit risk be reflected in the measurement of liabilities?
5. Should the alternative use value of assets be reflected in the statement of financial position (ie if more than existing service potential)?