

**Meeting:** International Public Sector Accounting  
Standards Board

**Meeting Location:** Toronto, Canada

**Meeting Date:** December 5–8, 2023

# Agenda Item 4

For:

☐ Approval




☒ Discussion

☐ Information

## MEASUREMENT APPLICATION PHASE

<b>Project summary</b>	The project objective is to evaluate the applicability of current operational value in IPSAS not explicitly considered in phase one of the Measurement project.	
<b>Project staff leads</b>	<ul style="list-style-type: none"> <li>Agustina Llambi, Senior Manager</li> <li>John Stanford, Senior Advisor</li> </ul>	
<b>Task Force members</b>	<ul style="list-style-type: none"> <li>David Watkins, IPSASB Technical Advisor (Task Force Chair)</li> <li>Todd Beardsworth, IPSASB Member</li> <li>Liang Caroline Yang, IPSASB Member</li> <li>Takeo Fukiya, IPSASB Technical Advisor</li> <li>Rasmimi Ramli, IPSASB Technical Advisor</li> <li>Mark Wermuth, IPSASB Technical Advisor</li> <li>Shahad A. Alshehri, Ministry of Finance, Kingdom of Saudi Arabia</li> </ul>	
<b>Meeting objectives</b> <b>Project management</b>	<b>Topic</b>	<b>Agenda Item</b>
	<a href="#">Measurement Application Phase Dashboard</a>	<a href="#">4.1.1</a>
	<a href="#">Instructions up to Previous Meeting</a>	<a href="#">4.1.2</a>
	<a href="#">Decisions up to Previous Meeting</a>	<a href="#">4.1.3</a>
	<a href="#">Measurement Application Phase: Project Roadmap</a>	<a href="#">4.1.4</a>
<b>Decisions required at this meeting</b>	<a href="#">Amendment to IPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors</a>	<a href="#">4.2.1</a>
	<a href="#">Other Issues – IPSAS 12 and IPSAS 32</a>	<a href="#">4.2.2</a>
	<a href="#">Impairment of Non-Cash-Generating Assets: Recoverable Service Amount and Illustrative Examples</a>	<a href="#">4.2.3</a>
	<a href="#">Applicability of COV at Initial and Subsequent Measurements for Leases at Market Terms and at Below-Market Terms for Right-of-Use Assets</a>	<a href="#">4.2.4</a>

## MEASUREMENT APPLICATION PHASE DASHBOARD

Project Topic	Past Meetings	Dec 2023	Mar 2023
<b>Project Management</b>	✓		
<b>Review and Approval of Measurement Application Phase</b>			
Measurement – Applicability of current operational value			
• IPSAS 3, <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>			
• IPSAS 12, <i>Inventories</i>			
• IPSAS 16, <i>Investment Property</i>	✓		
• IPSAS 21, <i>Impairment of Non-Cash-Generating Assets</i>			
• IPSAS 26, <i>Impairment of Cash-Generating Assets</i>	✓		
• IPSAS 27, <i>Agriculture</i>	✓		
• IPSAS 31, <i>Intangible Assets</i>			
• IPSAS 32, <i>Service Concession Arrangements: Grantor</i>	✓		
• IPSAS 36, <i>Investments in Associates and Joint Ventures</i>	✓		
• IPSAS 37, <i>Joint Arrangements</i>	✓		
• IPSAS 40, <i>Public Sector Combinations</i>	✓		
• IPSAS 41, <i>Financial Instruments</i>	✓		
• IPSAS 43, <i>Leases</i>			
Current Value Disclosures			
Exposure Draft			
<b>Legend</b>			
✓	Task Completed		
	Planned IPSASB Discussion		
	Page-by-page Review		

## INSTRUCTIONS UP TO PREVIOUS MEETING

Meeting	Instruction	Actioned
June 2023	1. Include in the Basis for Conclusions the fact that biological assets in the scope of IPSAS 27 are held to generate economic benefits and therefore current operational value is not an applicable measurement basis.	1. To be drafted.
September 2023	2. Develop examples to illustrate how to determine recoverable service amount under both IPSAS 21, <i>Impairment of Non-Cash-Generating Assets</i> , and the staff proposals in Agenda Items 8.2.3 and 8.2.4.	2. See <a href="#">Agenda Item 4.2.3</a>
	3. Revise the initial measurement guidance in IPSAS 32 to put more emphasis on discounting of future cash flows technique and remove the reference to fair value.	3. See <a href="#">Agenda Item 4.2.2</a>
	4. Include a Specific Matter for Comment asking whether the income approach is necessary to measure a right of use asset.	4. To be drafted.
	5. Further analyze the applicability of COV for assets within the scope of IPSAS 12, <i>Inventories</i> , and IPSAS 43, <i>Leases</i> .	5. See <a href="#">Agenda Item 4.2.2</a> for IPSAS 12 and <a href="#">Agenda Item 4.2.4</a> for IPSAS 43.
	6. Develop a draft ED addressing the IPSASB's decisions to date.	6. In Progress.

## DECISIONS UP TO PREVIOUS MEETING

Meeting	Decision	BC Reference
September 2023	1. The IPSASB decided that COV is an applicable subsequent measurement basis for service concession assets accounted in accordance with IPSAS 45, <i>Property, Plant and Equipment</i> or IPSAS 31, <i>Intangible Assets</i> .	1. To be drafted.
	2. The IPSASB decided that the applicability of COV should be retained in the individual IPSAS as opposed to being included in IPSAS 40, <i>Public Sector Combinations</i> .	2. To be drafted.
	3. IPSAS 3, <i>Accounting Policies, Changes in Accounting Estimates and Errors</i> , should be updated to include the definition of accounting estimate and the 'measurement techniques' terminology introduced in IPSAS 46, <i>Measurement</i> , should be applied consistently throughout IPSAS.	3. To be drafted.
June 2023	1. The IPSASB decided that COV is not an applicable measurement basis for IPSAS 16, <i>Investment Property</i> .	1. To be drafted.
	2. The IPSASB decided that IPSAS 26, <i>Impairment of Cash-Generating Assets</i> should not be in the scope of the Measurement Application Phase.	2. To be drafted.
	3. The IPSASB decided that COV is not an applicable measurement basis for IPSAS 27, <i>Agriculture</i> .	3. To be drafted.
	4. The IPSASB decided that COV is not an applicable measurement basis for IPSAS 36, <i>Investments in Associates and Joint Ventures</i> .	4. To be drafted.
	5. The IPSASB decided that the applicability of COV should be retained in the individual IPSAS as opposed to being included in IPSAS 37, <i>Joint Arrangements</i> .	5. To be drafted.
	6. The IPSASB decided that COV is not an applicable measurement basis for IPSAS 41, <i>Financial Instruments</i> .	6. To be drafted.
	7. The IPSASB decided that the scope of the review of IPSAS 21 should be limited to the definition of 'recoverable service amount' and the components of 'recoverable service amount'.	7. To be drafted.
March 2023	1. The IPSASB decided the specific IPSAS in the scope of the Measurement Application Phase.	1. To be drafted.

## Agenda Item 4.1.3

December 2022	1. The potential application of COV across the existing suite of IPSAS should be added to the work program as a separate phase, with work to begin after the expected approval of IPSAS, <i>Measurement</i> , in March 2023.	1. Not applicable - Measurement: Application of COV has been added to the <a href="#">work program</a> .
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**MEASUREMENT APPLICATION PHASE:  
PROJECT ROADMAP**

Meeting	Completed Actions or Discussions / Planned Actions or Discussions:
December 2022	1. Application of COV - Phase 2 of the Measurement was added to the <a href="#">work program</a> .
March 2023	1. Discussion of Issues
June 2023	1. Discussion of Issues
September 2023	1. Discussion of Issues
December 2023	2. Discussion of Issues
March 2024	1. Discussion of Issues 2. Review of Exposure Draft (page flip) 3. Approval of Exposure Draft
April 2024 – August 2024	1. Document Out for comment
December 2024	1. Review Responses to Exposure Draft 2. Discuss Issues
March 2025	1. Review of Pronouncement (page flip) 2. Approval of Amendments

## Amendment to IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors*

### Question

- Does the IPSASB agree with the recommendation?

### Recommendation

- Task Force and staff recommend amending paragraph 40 in IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors* to clarify that a change between measurement models, instead of measurement basis, is a change in accounting policy choice to be consistent with IPSASB's decision when developing IPSAS 45, *Property, Plant, and Equipment*.

40. A change in the measurement ~~basis~~ **model** applied is a change in an accounting policy, and is not a change in an accounting estimate. ~~When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.~~

**40A.** When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.

### Background

- The introduction of COV as an additional current value measurement basis in IPSAS 45 has created an inconsistency with guidance in IPSAS 3 on how to account for a change in measurement basis. This is because an entity that elects the current value model in IPSAS 45 shall measure an item of property, plant, and equipment at current operational value (COV) or fair value, depending on the primary objective for which the entity holds the item of property, plant, and equipment.

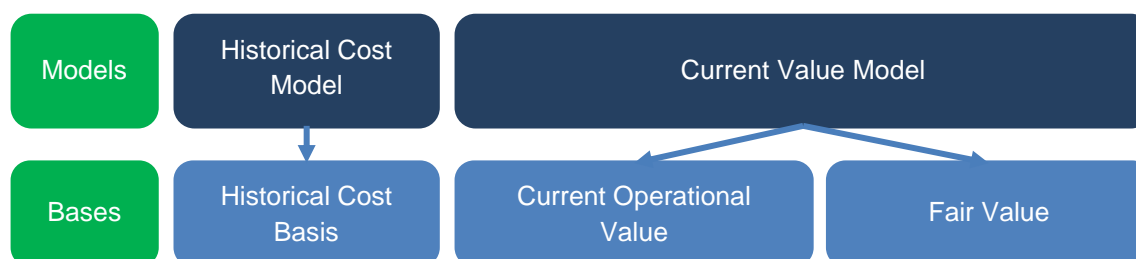


Figure 1. Subsequent Measurement Framework (This diagram only reflects measurement basis for assets.)

- In March 2023, the IPSASB instructed staff to explore guidance in IPSAS 3 and provide a recommendation on how to eliminate the inconsistency between these IPSAS.

### Analysis

#### IPSAS 3 Guidance

- IPSAS 3 notes that any change to the measurement basis applied in measuring an asset or liability should be accounted for as a change in an accounting policy<sup>1</sup>. A change in an accounting policy requires retrospective application as if that policy had always been applied.

<sup>1</sup> IPSAS 3 paragraph 40

*IPSAS 45 Guidance*

6. IPSAS 45 makes two measurement bases available for entities that choose to measure property, plant, and equipment using the current value model:
  - (a) Current operational value; and
  - (b) Fair value
7. The selection of measurement models – historical cost or current value – under IPSAS 45 is a choice available to the entity, however, which measurement basis to apply is based on the primary objective for which the entity holds the item of property, plant, or equipment. When the entity holds the asset for its operational capacity, it shall be measured at COV; however, when the asset is held for its financial capacity, it shall be measured at fair value (FV).
8. IPSAS 45 notes that when the primary objective for which the entity holds an item of property, plant, and equipment changes from operational to financial capacity, or vice versa, a change in measurement basis from COV to FV or from FV to COV is appropriate<sup>2</sup>. IPSAS 45.81 requires that an entity shall disclose that change and the reason(s) for making such a change.

*Analysis*

9. In September 2022, the IPSASB agreed it would not be appropriate to let an entity decide which current value measurement basis to apply considering that when an entity holds an asset for its operational capacity, COV is the measurement basis that most fairly reflects the transaction in a manner that is useful in holding the entity to account, and for decision-making purposes. Thus, the IPSASB decided, that the accounting policy choice is at the measurement model level (i.e., historical cost model and current value model) and not between current value measurement bases (i.e., current operational value and fair value).
10. This decision created an inconsistency with IPSAS 3, see paragraph 5 above. To ensure guidance between IPSAS 3 and IPSAS 45 are consistent with the IPSASB decision in September 2022, see paragraph 9, staff recommends amending paragraph 40 in IPSAS 3 to reflect that a change between measurement model rather than measurement basis is a change in an accounting policy:
  40. A change in the measurement ~~basis~~ model applied is a change in an accounting policy, and is not a change in an accounting estimate. ~~When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.~~
  - 40A. When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.

**Decision Required**

11. Does the IPSASB agree with the Task Force and Staff recommendation?

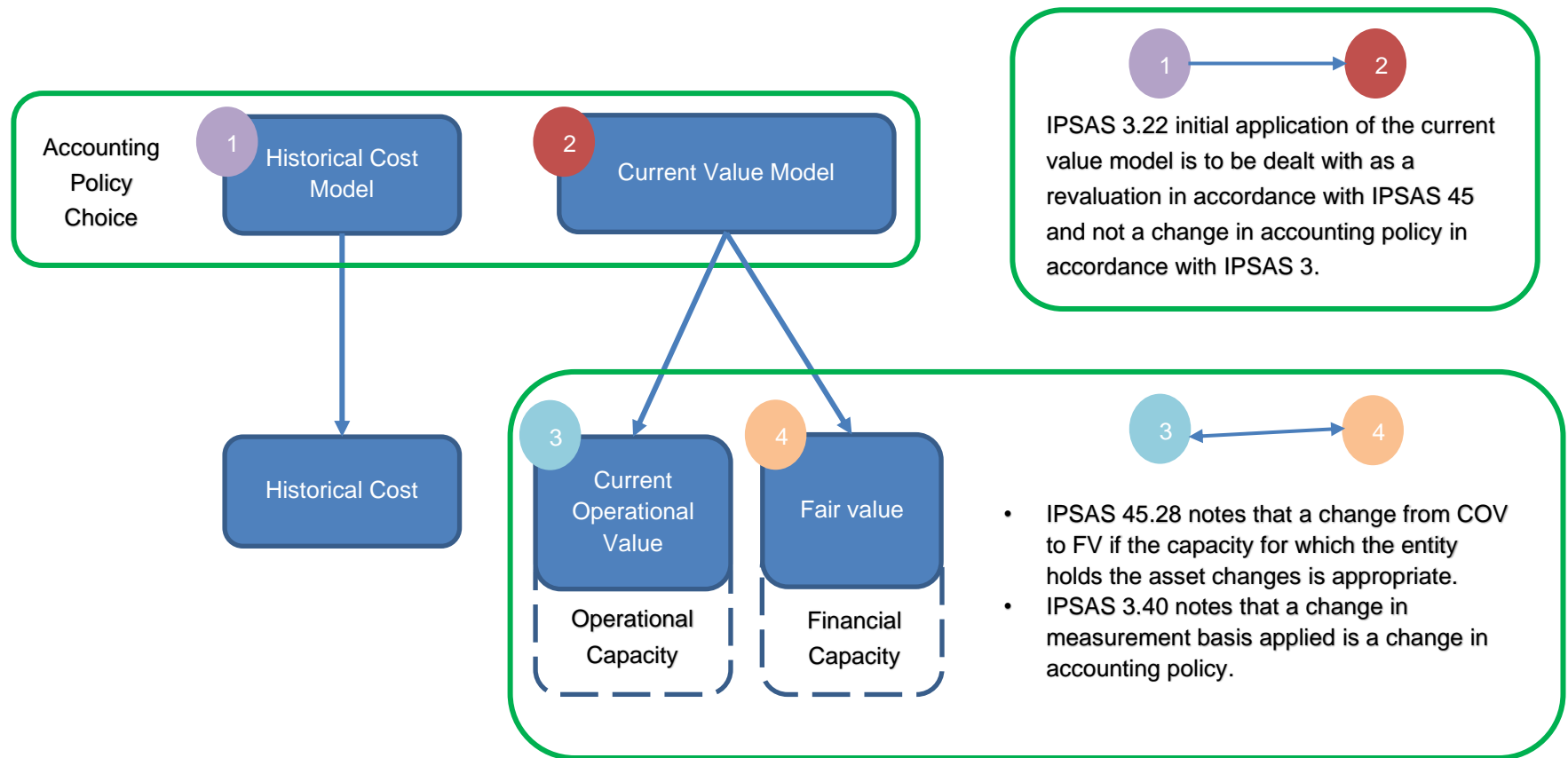
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<sup>2</sup> IPSAS 45 paragraph 28



## Agenda Item 4.2.1

### Appendix A – Illustration of Existing Inconsistency between IPSAS 3 and IPSAS 45



## **Other Issues – IPSAS 12 and IPSAS 32**

### **Question**

1. Does the IPSASB agree with the recommendation in paragraphs 2 and 3?

### **Recommendation**

2. Task Force and staff recommend that current operational value ('COV') replace current replacement cost ('CRC') in 'the lower of cost or CRC' for the measurement of inventories held for:
  - (a) Distribution at no charge or for a nominal charge; or
  - (b) Consumption in the production process of goods to be distributed at no charge or for a nominal charge; or
  - (c) Materials or supplies to be consumed or distributed in the rendering of services at no charge or for a nominal charge.
3. Task Force and staff recommend that the revision of IPSAS 32 initial measurement is out of the scope of the Measurement Application phase.

### **Background**

4. To support the IPSAS 12 September 2023 recommendation that COV should replace current replacement cost when determining the recoverable amount of inventories, the IPSASB instructed staff to consider:
  - (a) Materials or supplies to be consumed or distributed in the rendering of services at no charge or for a nominal charge should also be subsequently measured at the lower of cost or COV;
  - (b) The benefits of COV against the potential complexities of replacing CRC with COV, considering constituents understand and apply CRC today when writing down inventory below cost;
  - (c) Assess whether the introduction of COV in IPSAS 12 impacts the cost of assets previously in scope of IPSAS 27, *Agriculture*; and
  - (d) Whether the timing of 'reporting date' used in CRC and "measurement date" used in COV can have the same timing.
5. IPSASB instructed staff to consider the revision of IPSAS 32 initial measurement to transaction price to align IPSAS 32 initial measurement guidance with IPSAS 46, *Measurement* initial measurement guidance.

### **Analysis**

6. [Appendix A](#) provides the analysis of the applicability of current operational value for certain inventories in the scope of IPSAS 12, *Inventories* discussed during the September 2023 meeting. Staff recommends reading [Appendix A](#) before reading paragraph 7.
7. Staff have actioned all instructions issued by the IPSASB on Agenda Item 8.2.2 from the September 2023 meeting and on IPSAS 32.

<b>Instructions</b>	Materials or supplies to be consumed or distributed in the rendering of services at no charge or for a nominal charge should be subsequently measured at the lower of cost or COV, like the inventories identified in Agenda Item 8.2.2-September 2023.
<b>Analysis</b>	<ul style="list-style-type: none"> <li>Materials or supplies to be consumed or distributed in the rendering of services are inventories in the scope of IPSAS 12. An IPSASB member noted that such inventories are consumed or distributed in the rendering of services at no charge or for a nominal charge, thus should also be measured at the lower of cost or COV.</li> <li>The Conceptual Framework (CF) for General Purpose Financial Reporting by Public Sector Entities defines a resource as a right to either service potential or the capability to generate economic benefits, or a right to both. Service potential is described in the CF as the capability of a resource to provide services or goods that contribute to achieving the entity's objectives. Service potential enables an entity to achieve its objectives without necessarily generating cash flows.</li> <li>Hospitals that render service at no charge or for a nominal charge enable an entity to achieve its objectives of providing universal healthcare. Such hospitals are expected to have medical materials and supplies (such as gauze, and antibiotics) to render such services at no charge or for a nominal charge.</li> <li>Therefore, the gauze and antibiotics (i.e., inventories) are held for their service potential and enable the hospital to achieve its objective of providing healthcare without generating cash flows. When the cost of such inventories cannot be recovered, the most relevant information is the amount the entity would pay for the remaining service potential of such asset. Therefore, staff recommends that these inventories should also be measured at 'the lower of cost or COV'.</li> </ul>
<b>Action proposed</b>	<p>Staff recommends amending paragraph 17 in IPSAS 12 as follows:</p> <p>17. Inventories shall be measured at the lower of cost and <del>current replacement cost</del> <u>current operational value</u> where they are held for:</p> <p>(a) Distribution at no charge or for a nominal charge; or</p> <p>(b) Consumption in the production process of goods to be distributed at no charge or for a nominal charge-; <u>or'</u></p> <p><u>(c) Distribution or consumption in the rendering of services at no charge or for a nominal charge.</u></p>

## Agenda Item 4.2.2

<b>Instructions</b>	Consider the benefits of COV against the potential complexities of replacing CRC with COV, taking into account constituents understand and apply CRC today when writing down inventory below cost.
<b>Analysis</b>	<ul style="list-style-type: none"> <li>The replacement of CRC with COV is not expected to present complexities that outweigh the benefits of applying COV, because: <ul style="list-style-type: none"> <li>As noted in paragraph 2(b) in <a href="#">Appendix A</a>, CRC and COV share key principles, therefore staff believes that replacing CRC with COV will not result in measurement differences;</li> <li>IPSAS 46 includes guidance on how to derive COV, discussing each of its principles (i.e., existing asset/use/location, entry price and least costly manner), thus reducing potential complexities of applying a new measurement basis; and</li> <li>Moreover, replacing CRC with COV aligns IPSAS 12 measurement guidance with the IPSASB's updated measurement methodology (i.e., IPSAS 46) that has evolved since IPSAS 12 was published in 2001 and ensures consistent application of measurement basis across IPSAS.</li> </ul> </li> </ul>
<b>Action proposed</b>	No action is proposed.

<b>Instructions</b>	Assess whether the introduction of COV in IPSAS 12, impacts the cost of assets previously in scope of IPSAS 27, <i>Agriculture</i> .
<b>Analysis</b>	<ul style="list-style-type: none"> <li>IPSAS 12.29 requires, in accordance with IPSAS 27, inventories comprising agricultural produce that an entity has harvested from its biological assets be measured on initial recognition at their fair value less costs to sell at the point of harvest. IPSAS 27 therefore establishes the cost of the inventories at that date for application of IPSAS 12.</li> <li>After the cost is established by IPSAS 27, inventories are measured at the lower of cost and net realizable value<sup>3</sup> or the lower of cost or current replacement cost (CRC)<sup>4</sup>.</li> <li>The applicability of COV in IPSAS 12 (i.e., replacing CRC) does not impact the link between IPSAS 12 and IPSAS 27, as the cost of agricultural produce harvested from biological assets is not changed and continues to be in accordance with IPSAS 27.</li> </ul>
<b>Action proposed</b>	No action is proposed.

<sup>3</sup> Inventories shall be measured at the lower of cost and net realizable value, except where Paragraph 16 or Paragraph 17 applies. [IPSAS 12.15]

<sup>4</sup> Inventories shall be measured at the lower of cost and current replacement cost where they are held for:

(a) Distribution at no charge or for a nominal charge; or

(b) Consumption in the production process of goods to be distributed at no charge or for a nominal charge. [IPSAS 12.17]

<b>Instructions</b>	CRC definition refers to 'reporting date' while COV definition refers to 'measurement date'. Does this present an issue if COV is to replace CRC?
<b>Analysis</b>	<ul style="list-style-type: none"><li>• 'Reporting date' refers to the last day of the reporting period to which the financial statements relate<sup>5</sup>, while 'measurement date' is the date at which the value of an asset or a liability is determined<sup>6</sup>. An entity at a minimum determines the current value of an asset or liability at its initial and subsequent measurement.</li><li>• Initial measurement refers to the date of the transaction date, which can take place at any time during the reporting period, while subsequent measurement refers to measurement in the Financial Statements, which takes time at the end of the reporting period. Therefore the 'reporting date' can be the 'measurement date', as such staff believes the recommendation in paragraph 2 is appropriate.</li></ul>
<b>Action proposed</b>	No action is proposed.

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<sup>5</sup> Defined in the IPSASB Glossary.

<sup>6</sup> Defined in the IASB Glossary.

<b>Instructions</b>	Consider the revision of initial measurement in IPSAS 32 from fair value to transaction price, as to align IPSAS 32 initial measurement guidance with IPSAS 46, <i>Measurement</i> .
<b>Analysis</b>	<ul style="list-style-type: none"> <li>Staff recommends that amending the initial measurement of IPSAS 32 is outside of the scope of the Measurement Application phase because: <ul style="list-style-type: none"> <li>The scope of the Measurement Application Phase is to evaluate the applicability of COV more broadly across IPSAS. COV is a subsequent measurement basis, that can be considered for initial recognition when the entity acquires an asset in a non-exchange transaction. Because service concession arrangements are exchange transactions rather than non-exchange transactions the applicability of COV at initial measurement is unnecessary.</li> <li>IPSAS 46 objective is the consistent application of measurement basis across IPSAS and making amendments to other IPSAS would be outside of the purpose of IPSAS 46<sup>7</sup>. The IPSASB decided when developing IPSAS 46 that would not make significant changes to measurement guidance in individual IPSAS, such as changing specific initial measurement guidance in IPSAS with IPSAS 46 terminology.</li> <li>Furthermore, the level of analysis needed to revise IPSAS 32 initial measurement from fair value to transaction price would be more appropriately fitted in a narrow scope project or be considered as a maintenance activity project, such as a post implementation review.</li> </ul> </li> </ul>
<b>Action proposed</b>	No action is proposed.

#### Decision Required

Does the IPSASB agree with the Task Force and Staff [recommendation](#)?

<sup>7</sup> IPSAS 46.BC10 and IPSAS 46.BC12

**Appendix A – Analysis and Recommendation in Agenda Item 8.2.2 from the IPSASB 2023  
September Meeting**

1. The IPSASB discussed [Agenda Paper 8.2.2 during the September 2023 meeting](#), which recommended:
  - (a) **Initial Measurement.** The cost of inventory acquired by means of a non-exchange transaction shall be measured at deemed cost.
  - (b) **Subsequent Measurement.** Replacing 'current replacement cost' with 'current operational value' in 'the lower of cost or current replacement cost' for the measurement of inventories held for:
    - (i) Distribution at no charge or for a nominal charge; or
    - (ii) Consumption in the production process of goods to be distributed at no charge or for a nominal charge.
2. Agenda Item 8.2.2 presented the analysis that CRC shall be replaced with COV for certain inventories because:
  - (a) Inventories held for distribution or consumption in the production process of goods to be distributed at no charge or for a nominal charge are held for their operational capacity. COV was specifically developed to measure assets held for its operational capacity. Thus, it is expected to most fairly reflect the transaction in a manner that is useful in holding the entity to account and for decision-making purposes;
  - (b) CRC and COV are both amounts that the entity would pay for the asset and share key principles—such as entry value and the current condition of the existing asset; and
  - (c) Replacing CRC with COV aligns IPSAS 12 measurement methodology with IPSAS 46, *Measurement*.

## **Impairment of Non-Cash-Generating Assets: Recoverable Service Amount and Illustrative Examples**

### **Question**

1. Does the IPSASB agree with the recommendation in paragraph 2?

### **Recommendation**

2. Task Force and staff recommend that:
  - (a) Members adopt a definition of recoverable service amount that is the higher of current operational value and fair value less costs to sell;
  - (b) The restoration cost approach and the services units approach in the current IPSAS 21, *Impairment of Non-Cash-Generating Assets*, should not be retained in an updated IPSAS 21; and
  - (c) The examples in [Appendix A](#) and [Appendix B](#) be included in a revised IPSAS 21, *Impairment of Non-Cash-Generating Assets*.

### **Background**

3. At the September 2023 meeting the IPSASB agreed that the scope of the limited-scope impairment project should focus on the components of recoverable service amount for non-cash-generating assets. The IPSASB instructed staff to develop examples to illustrate how to determine recoverable service amount under both IPSAS 21 and the revised approach proposed by staff.
4. The revised approach proposed was:
  - (a) The defined term 'value in use of a non-cash-generating asset'<sup>8</sup> will be replaced by current operational value<sup>9</sup> as a component of recoverable service amount; and
  - (b) The definition of fair value and assumptions in supporting guidance in IPSAS 46, *Measurement*, is to be the basis of fair value less costs to sell<sup>10</sup>.
5. Most members supported the retention of fair value less costs to sell as a component of recoverable service amount, although some had reservations that the determination of fair value less costs to sell would impose unnecessary costs on preparers. To illustrate the benefits of retaining fair value less costs to sell, Staff was instructed to emphasize that the cases in which fair value less costs to sell is higher than current operational value, and therefore the determinant of recoverable service amount, will be limited. In most cases it will be clear whether current operational value is higher than fair value less costs to sell.

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<sup>8</sup> Value in use of a non-cash-generating asset is the present value of the asset's remaining service potential.

<sup>9</sup> Current operational value is the amount that an entity would pay for the remaining service potential of an asset at the measurement date.

<sup>10</sup> The definition of fair value less costs to sell in IPSAS 21 is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.



**Analysis**

6. [Appendix A](#) shows four of the examples in existing IPSAS 21 in (a) their current format and (b) updated to reflect the use of current operational value rather than one of the techniques for value-in-use of a non-cash-generating asset in IPSAS 21 (see paragraph 10). In all these cases the reporting entity has adopted the cost model for measurement subsequent to recognition (subsequent measurement). The cost model has been renamed as the historical cost model in both the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* and IPSAS 46. In these examples the entity has formed a view that value in use of a non-cash-generating asset is higher than fair value less costs to sell. Similarly, the proposed revised approach assumes that current operational value is higher than fair value less costs to sell.
7. [Appendix B](#) provides four further examples for entities that have adopted the current value model for subsequent measurement. These include an example in which fair value less costs to sell is relevant to the determination of recoverable service amount.
8. In the first example in [Appendix B](#), there is an active market for an office building used for operational capacity. Despite the fact that there is a permanent decline in demand for the services provided by the asset it is clear that, in light of the buoyant commercial property market, the non-specialized nature of the asset, and the fact that there are no legal restrictions on the use of the asset, there is no impairment loss. Conversely, in the other examples, it is clear that current operational value is the relevant measurement basis to be applied. In these cases, the indication of impairment is evidence that current operational value should be determined in the reporting period, rather than at the next planned valuation in accordance with a rolling program of valuations. This will ensure that the carrying amount is materially accurate at the reporting date.
9. The examples highlight, the use of fair value less costs to sell and current operational value as components of recoverable service amount does not mean that an entity, which has adopted the historical cost model for subsequent measurement, is changing accounting policy. The purpose of determining recoverable service amount is to enable the entity to determine whether the resources invested in the asset for which there has been an indication of impairment are recoverable. In circumstances in which fair value less costs to sell is higher than carrying amount, the asset continues to be recognized at carrying amount. The asset is not revalued. However, a failure to determine fair value less costs to sell in circumstances such as those outlined in paragraph 8 may lead to recognition of an impairment loss when there is no loss.

*Approaches to Measuring Value in Use*

10. As indicated in the agenda papers for the June and September meetings, currently value in use of a non-cash-generating asset in IPSAS 21 is estimated by the application of one of three approaches:
  - (a) Depreciated Replacement Cost.
  - (b) Restoration Cost.
  - (c) Service Units Approach.
11. The next sub-sections of this agenda item consider the impact of using current operational value rather than the techniques to estimate value in use of a non-cash generating assets.

Depreciated Replacement Cost and Current Operational Value

12. Paragraph 45 of IPSAS 21 explains depreciated replacement cost:

“The replacement cost of an asset is the cost to replace the asset’s gross service potential. This cost is depreciated to reflect the asset in its used condition.”
13. In substance, depreciated replacement cost is the same as the cost approach, which is one of three measurement techniques for determining current operational value in IPSAS 46. Therefore, the use of current operational value as a component of recoverable service amount gives an outcome the same as the depreciated replacement cost approach in the current IPSAS 21.

Restoration Cost and Current Operational Value

14. IPSAS 21 describes restoration cost as “the cost of restoring the service potential of an asset to its pre-impaired level. Under this approach, the present value of the remaining service potential of the asset is determined by subtracting the estimated restoration cost of the asset from the current cost of replacing the remaining service potential of the asset before impairment.”
15. In [Appendix A](#) the example is a school bus, which is damaged in an accident. In the view of staff if an asset is damaged to the extent that it is incapable of delivering a service at the measurement date its current operational value at that date is zero, disregarding any scrap value.
16. A contrary argument, which underpins the restoration cost approach, is that the entity can mitigate any impairment loss by restoring the asset to its pre-impaired state and then determining the current replacement cost of the asset. In this view the cost of replacing the service potential of the school bus less restoration costs is a close approximation of current operational value. However, this approach relies on management intent, which is a questionable approach unless management are irrevocably committed to this at the reporting date.
17. Staff accepts that the impairment loss may be fully or partially reversed in a subsequent measurement period if the entity decides to restore the entity to its pre-impaired state before the damage was sustained. However, in the view of staff, while acknowledging the view in paragraph 17, the effect of such an event should be recognized in the reporting period when the restoration work takes place. Accordingly, staff recommends that the restoration cost approach should not be retained.

Service Units Approach and Current Operational Value

18. Under the service units approach “the present value of the remaining service potential of the asset is determined by reducing the current cost of the remaining service potential of the asset before impairment to conform with the reduced number of service units expected from the asset in its impaired state.” In the view of staff, a better estimate of the impairment loss is obtained by comparing the carrying amount of the underperforming asset with the amount that the entity would pay at the measurement date for an asset of similar age and condition providing the reduced service potential. In the example in [Appendix A](#) the relevant current operational value is that of a printer with the same reduced capacity as the asset in its impaired state. In [Appendix B](#) the example is a street sweeper with performance below that forecast at the time of acquisition. Accordingly, staff recommends that the service units approach should not be retained.

**Conclusion**

19. In the view of staff:

## Agenda Item 4.2.3

- (a) Fair value less costs to sell should be retained as a component of recoverable service amount;
- (b) Application of current operational value gives the same recoverable service amount and impairment as the depreciated replacement cost technique;
- (c) Application of current operational value does not give the same recoverable service amount and therefore the same impairment loss as the restoration cost approach and the service units approach in current IPSAS 21; and
- (d) The use of current operational value gives a more faithful representation of the monetary amount of an impairment loss than either the restoration cost approach or the service units approach, and these approaches should not be retained in an updated IPSAS 21.

### Decision Required

20. Does the IPSASB agree with the staff [recommendation](#) in paragraph 2?

**Appendix A - Illustrative Examples Comparing Approaches in IPSAS 21 and Proposed Approach for Updated IPSAS 21 in which Current Operational Value Replaces Value in Use of a Non-Cash-Generating Asset.**

21. These examples, including the fact patterns, are currently in IPSAS 21. In all these examples, the reporting entity has adopted the historical cost model for measurement subsequent to recognition (the cost model in current IPSAS 21.)

**Assumptions**

22. In the existing examples in IPSAS 21, it is assumed that fair value less costs to sell of the asset tested for impairment is less than the value in use of a non-cash-generating asset or is not determinable, unless otherwise indicated. Therefore, the asset's recoverable service amount is equal to its value in use. In these examples, the straight-line method of depreciation is used.
23. A similar assumption is made in the proposed revised approach, in which current operational value replaces value in use of a non-cash-generating asset. In all the updated examples the asset's recoverable service amount is equal to current operational value.

**Depreciated Replacement Cost Approach**

*Significant Long-term Change with Adverse Effect on the Entity in the Technological Environment—Underutilized Mainframe Computer.*

24. In 1999, the City of Kermann purchased a new mainframe computer at a cost of CU10 million. Kermann estimated that the useful life of the computer would be seven years, and that on average 80 percent of central processing unit (CPU) capacity would be used by the various departments. A buffer of excess CPU time of 20 percent was expected and needed to accommodate scheduling jobs to meet peak period deadlines. Within a few months after acquisition, CPU usage reached 80 percent, but declined to 20 percent in 2003 because many applications of the departments were converted to run on desktop computers or servers. A computer is available on the market at a price of CU500,000 that can provide the remaining service potential of the mainframe computer using the remaining applications.

**Evaluation of Impairment**

25. The indication of impairment is the significant long-term change in the technological environment resulting in conversion of applications from the mainframe to other platforms, and therefore decreased usage of the mainframe computer. (Alternatively, it can be argued that a significant decline in the extent of use of the mainframe indicates impairment.) Impairment loss is determined using the depreciated replacement cost approach as follows:

## Agenda Item 4.2.3

### Current approach in IPSAS 21

<b>a</b>	<b>Acquisition cost, 1999</b>	<b>10,000,000</b>
	<b>Accumulated depreciation, 2003 (<math>a \times 4 \div 7</math>)</b>	<b>5,714,286</b>
<b>b</b>	<b>Carrying amount, 2003</b>	<b>4,285,714</b>
<b>c</b>	<b>Replacement cost</b>	<b>500,000</b>
	<b>Accumulated depreciation (<math>c \times 4 \div 7</math>)</b>	<b>285,714</b>
<b>d</b>	<b>Recoverable Service Amount</b>	<b>214,286</b>
	<b>Impairment loss (b - d)</b>	<b>4,071,428</b>

### Approach under proposals for updated IPSAS 21

<b>a</b>	<b>Acquisition cost, 1999</b>	<b>10,000,000</b>
	<b>Accumulated depreciation, 2003 (<math>a \times 4 \div 7</math>)</b>	<b>5,714,286</b>
<b>b</b>	<b>Carrying amount, 2003</b>	<b>4,285,714</b>
<b>c</b>	<b>Replacement Cost of Asset</b>	<b>500,000</b>
	<b>Accumulated depreciation (<math>c \times 4 \div 7</math>)</b>	<b>285,714</b>
<b>d</b>	<b>Recoverable Service Amount (Current Operational Value)</b>	<b>214,286</b>
	<b>Impairment loss (b - d)</b>	<b>4,071,428</b>

### **Conclusion**

26. The only change is the use of the term 'current operational value'. Recoverable service amount and impairment loss are the same as currently in IPSAS 21.

### *Significant Long-term Change with Adverse Effect on the Entity in the Manner of Use—School Used as Warehouse*

27. In 1997, Lunden School District constructed an elementary school at a cost of CU10 million. The estimated useful life of the school is fifty years. In 2003, the school is closed because enrolments in the district declined unexpectedly due to a population shift caused by the bankruptcy of a major employer in the area. The school is converted to use as a storage warehouse, and Lunden School District has no expectation that enrolments will increase in the future such that the building would be reopened for use as a school. The current replacement cost for a warehouse with the same storage capacity as the school is CU4.2 million.

Evaluation of Impairment

28. Impairment is indicated, because the purpose for which the building is used has changed significantly from a place for instructing students to a storage facility, and this is not anticipated to change for the foreseeable future. The example in IPSAS 21 applies the depreciated replacement cost approach.

**Current approach in IPSAS 21**

<b>a</b>	<b>Acquisition cost, 1997</b>	<b>10,000,000</b>
	<b>Accumulated depreciation, 2003 (<math>a \times 6 \div 50</math>)</b>	<b>1,200,000</b>
<b>b</b>	<b>Carrying amount, 2003</b>	<b>8,800,000</b>
<b>c</b>	<b>Replacement Cost of storage facility of similar capacity</b>	<b>4,200,000</b>
	<b>Accumulated depreciation (<math>c \times 6 \div 50</math>)</b>	<b>504,000</b>
<b>d</b>	<b>Recoverable Service Amount</b>	<b>3,696,000</b>
	<b>Impairment loss (b - d)</b>	<b>5,104,000</b>

**Approach under proposals for updated IPSAS 21**

<b>a</b>	<b>Acquisition cost, 1997</b>	<b>10,000,000</b>
<b>b</b>	<b>Accumulated depreciation, 2003 (<math>a \times 6 \div 50</math>)</b>	<b>1,200,000</b>
<b>c</b>	<b>Carrying amount, 2003</b>	<b>8,800,000</b>
<b>d</b>	<b>Cost of a storage facility of similar capacity</b>	<b>4,200,000</b>
<b>e</b>	<b>Accumulated depreciation (<math>c \times 6 \div 50</math>)</b>	<b>504,000</b>
<b>f</b>	<b>Recoverable Service Amount (Current Operational Value)</b>	<b>3,696,000</b>
	<b>Impairment loss (c - f)</b>	<b>5,104,000</b>

**Conclusion**

29. The only change is the introduction of the term current Operational value for the depreciated storage facility. Current operational value is the recoverable service amount. Recoverable service amount and the impairment loss are the same as in IPSAS 21.

**Restoration Cost Approach**

*Physical Damage—School Bus Damaged in Road Accident*

30. In 1998, North District Primary School acquired a bus at the cost of CU200,000 to help students from a nearby village to commute free of charge. The school estimated a useful life of 10 years for the bus. In 2003, the bus sustained damage in a road accident, requiring CU40,000 to be restored to a usable condition. The restoration will not affect the useful life of the asset. The cost of a new bus to deliver a similar service is CU250,000 in 2003.

## Evaluation of Impairment

31. Impairment is indicated because the bus has sustained physical damage in the road accident. Impairment loss using the restoration cost approach is illustrated followed by the approach under the revised proposals.

### Current approach in IPSAS 21

<b>a</b>	<b>Acquisition cost, 1998</b>	<b>200,000</b>
	<b>Accumulated depreciation, 2003 (<math>a \times 5 \div 10</math>)</b>	<b>100,000</b>
<b>b</b>	<b>Carrying amount, 2003</b>	<b>100,000</b>
<b>c</b>	<b>Replacement cost</b>	<b>250,000</b>
	<b>Accumulated depreciation (<math>c \times 5 \div 10</math>)</b>	<b>125,000</b>
<b>d</b>	<b>Depreciated replacement cost (undamaged state)</b>	<b>125,000</b>
	<b>Less: restoration cost</b>	<b>40,000</b>
<b>e</b>	<b>Recoverable Service Amount</b>	<b>85,000</b>
	<b>Impairment loss (b - e)</b>	<b>15,000</b>

### Approach under proposals for updated IPSAS 21

<b>a</b>	<b>Acquisition cost, 1998</b>	<b>200,000</b>
	<b>Accumulated depreciation, 2003 (<math>a \times 5 \div 10</math>)</b>	<b>100,000</b>
<b>b</b>	<b>Carrying amount, 2003</b>	<b>100,000</b>
<b>c</b>	<b>Recoverable Service Amount (Current Operational Value)</b>	<b>0</b>
	<b>Impairment loss (b - c)</b>	<b>100,000</b>

## Conclusion

32. Under the updated approach proposed for IPSAS 21 the entity determines the current operational value of the bus in its damaged state. Disregarding any scrappage value, because the bus is inoperable at the measurement date the current operational value of the bus is zero. This approach does not reflect management intent (see paragraph 16 in main paper). The impairment loss may be fully or partially reversed in a subsequent measurement period if the entity decides to restore the entity to its condition before the damage was sustained. However, the effect of such an event should be recognized in the reporting period when the restoration work takes place. The impairment loss under the proposed updated approach is therefore higher than that using the restoration approach in IPSAS 21.

**Service Units Approach**

*Evidence from Internal Reporting—Higher Cost of Operating the Printing Machine*

33. In 1998, Country X Education Department purchased a new printing machine at a cost of CU40 million. The Department estimated that the useful life of the machine would be 40 million copies of books to be printed over 10 years for use by elementary school students. In 2003, it was reported that an automated feature of the machine's function does not operate as expected, resulting in a 25 percent reduction in the machine's annual output level over the remaining 5 years of the useful life of the asset. The replacement cost of a new printing machine is CU45 million in 2003.

Evaluation of Impairment

34. Impairment is indicated by evidence from internal reporting that the service performance of the printing machine is worse than expected. Circumstances suggest that the decline in the service potential of the asset is significant and of a long-term nature. Impairment loss using the service units approach is determined followed by approach under the revised proposals:

**Current approach in IPSAS 21**

<b>a</b>	<b>Acquisition cost, 1998</b>	<b>40,000,000</b>
	<b>Accumulated depreciation (<math>a \times 5 \div 10</math>)</b>	<b>20,000,000</b>
<b>b</b>	<b>Carrying amount, 2003</b>	<b>20,000,000</b>
<b>c</b>	<b>Replacement cost</b>	<b>45,000,000</b>
	<b>Accumulated depreciation (<math>c \times 5 \div 10</math>)</b>	<b>22,500,000</b>
<b>d</b>	<b>Depreciated replacement cost before adjustment for remaining service units</b>	<b>22,500,000</b>
<b>e</b>	<b>Recoverable Service Amount (<math>d \times 75\%</math>)</b>	<b>16,875,000</b>
	<b>Impairment loss (<math>b - e</math>)</b>	<b>3,125,000</b>

**Approach under proposals for updated IPSAS 21**

35. Under the proposed approach recoverable service amount is estimated by reference to the cost of a printer with the same output as the impaired asset (30 million annual copies), rather than the replacement cost of the original asset (40 million annual copies). In this example Country X Education Department estimates the cost of a printer with an output of 30 million annual copies is 30,000,000 CU.



## Agenda Item 4.2.3

<b>a</b>	<b>Acquisition cost, 1998</b>	<b>40,000,000</b>
	<b>Accumulated depreciation (<math>a \times 5 \div 10</math>)</b>	<b>20,000,000</b>
<b>b</b>	<b>Carrying amount, 2003</b>	<b>20,000,000</b>
<b>c</b>	<b>Cost of Printer with Output of 30 million copies a year</b>	<b>30,000,000</b>
	<b>Accumulated depreciation (<math>c \times 5 \div 10</math>)</b>	<b>15,000,000</b>
<b>d</b>	<b>Recoverable Service Amount (Current Operational Value)</b>	<b>15,000,000</b>
<b>e</b>	<b>Impairment loss (b - d)</b>	<b>5,000,000</b>

### Conclusion

36. The impairment loss is higher than that determined by applying the service units approach in IPSAS 21. This is because the revised approach determines the current operational value of an asset providing the same service potential as the impaired asset, rather than estimating the replacement cost of the original asset and then reducing that amount to reflect a smaller number of service units.

**Appendix B - Impairment Examples for Entities on Current Value Model for Subsequent Measurement**

1. In all examples the entity is on the current value model for measurement subsequent to recognition. Depreciation is on straight-line basis.

*Cessation, or near cessation, of the demand or need for services provided by the asset.*

*Fact Pattern*

2. In 2003 Entity A acquired an office building with four floors in a central city area in which to house a number of educational support services for 700,000 CU. The building had an estimated useful life of 40 years. In 2020 there was a legislative change and schools were given greater discretion over the procurement of these services. Many sought alternative provision leading to a decline in demand for services provided by Entity A.
3. By 2023 demand for education support services had declined by about 75% from 2020 levels, so that the services can be provided in a building with about 25% of the floor area of the current building.
4. Because the office building is held for operational capacity it is measured at current operational value. The carrying amount is 500,000 CU. There are no restrictions on the building's use. There is a buoyant market for commercial property with average sale prices having increased by 25% in the 2020-2024 period. The entity therefore considers that fair value less costs to sell is the relevant metric for determining whether there is an impairment loss.

*Analysis*

<b>a. Acquisition Cost in 2003</b>	<b>700,000 CU</b>
<b>b. Current Operational Value in 2023 prior to impairment indication</b>	<b>1,000,000 CU</b>
<b>c. Accumulated Depreciation (20/40 * 1,000)</b>	<b>500,000 CU</b>
<b>d. Carrying Amount in 2023</b>	<b>500,000 CU</b>
<b>e. Fair Value less Costs to Sell in 2023</b>	<b>2,000,000 CU</b>
<b>f. Accumulated Depreciation (20/40 * 2,000)</b>	<b>1,000,000 CU</b>
<b>g. Recoverable Service Amount</b>	<b>1,000,000 CU</b>

**Conclusion**

5. There is no impairment loss as recoverable service amount (g) exceeds carrying amount (d). Although the asset's service potential has diminished, the resources invested in the asset can be recovered through sale in an active market, which is legally permitted and feasible. Therefore, Entity A continues to carry the building on its statement of financial position at 500,000 CU. There is no need to redetermine current operational value.

*Evidence of Physical Damage to An Asset*

*Fact pattern*

6. In 1993 Entity B constructed a school with an annual intake of 1,000 pupils. The cost was 2,000,000 CU. The school has an estimated useful life of 50 years. The carrying amount in 2023 was 1,600,000 CU. In 2023 the school sustained damage in high winds. As a result, the pupil intake has been reduced to 100 pupils per year. A legal restriction does not permit the building or site to be used for non-educational purposes.
7. Entity B revalues its educational property portfolio on a five-year rolling basis. The next valuation of the school is scheduled for 2025. However, because there is a black letter indication of impairment the revaluation of this building has been brought forward to 2023.
8. Because there is a legal restriction on the use of the building the entity concludes that fair value less costs to sell is lower than current operational value. It therefore estimates the up-to-date current operational value. Entity B receives a report from a valuer that the construction cost of a school with a capacity of 100 pupils is 3,000,000 CU.

*Analysis*

<b>a. Construction Cost in 1993</b>	<b>2,000,000 CU</b>
<b>b. Current Operational Value in 2023 prior to impairment indication</b>	<b>4,000,000 CU</b>
<b>c. Accumulated Depreciation (30/50 * 4,000,000)</b>	<b>2,400,000 CU</b>
<b>d. Carrying Amount in 2023</b>	<b>1,600,000 CU</b>
<b>e. Cost of school with capacity of 100 pupils</b>	<b>3,000,000 CU</b>
<b>f. Revised Accumulated Depreciation (30/50 * 3,000,000)</b>	<b>1,800,000 CU</b>
<b>g. Recoverable Service Amount (Current Operational Value)</b>	<b>1,200,000 CU</b>
<b>h. Impairment Loss d-g</b>	<b>400,000 CU</b>

**Conclusion**

9. Fair value less costs to sell is not the relevant component of recoverable service amount. The carrying amount of the asset in the statement of financial position is reduced to 1,200,000 CU. There is an impairment loss of 400,000 CU (d-g). Part of this impairment loss is debited to the revaluation reserve up to the level of previous revaluation gains. The remainder is debited to surplus/deficit.

## Agenda Item 4.2.3

*Significant long-term changes with adverse effect on the entity have taken place during the reporting period, or will take place in the near future, in the technological, legal, or government policy environment in which the entity operates.*

### Fact Pattern

10. Entity Z acquired a residential home for children in 2003 at a cost of 1,000,000 CU. The residential home had an estimated useful life of 50 years. Until 2023 the home had a capacity of 100 children. In 2023 Government regulations on occupancy-imposed restrictions on occupancy. As a result, the capacity was reduced to 50 children. Under the rolling program of valuations for assets on the current value model, the next valuation of the residential home is scheduled for 2026. The valuation is brought forward as a result of the impairment indication. A valuer's report indicates that a residential home of similar age and location for 50 children can currently be acquired for 2,000,000 CU.

### Analysis

<b>a. Acquisition Cost in 2003</b>	<b>1,000,000 CU</b>
<b>b. Gross Operational Value in 2023 prior to impairment indication</b>	<b>3,000,000 CU</b>
<b>c. Accumulated Depreciation (20/50 * 3,000)</b>	<b>1,200,000 CU</b>
<b>d. Carrying Amount (Current Operational Value) in 2023</b>	<b>1,800,000 CU</b>
<b>e. Revised Gross Operational Value following impairment indication</b>	<b>2,000,000 CU</b>
<b>f. Revised Accumulated Depreciation (20/50 * 2,000,000)</b>	<b>800,000 CU</b>
<b>g. Recoverable Service Amount (Current Operational Value)</b>	<b>1,200,000 CU</b>
<b>h. Impairment Loss d-g</b>	<b>600,000 CU</b>

### Conclusion

11. Fair value less costs to sell is not the relevant component of recoverable service amount. The carrying amount of the asset in the statement of financial position is reduced to 1,200,000 CU. There is an impairment loss of 600,000 CU. Part of this impairment loss is debited to the revaluation reserve up to the level of previous revaluation gains. The remainder is debited to surplus/deficit.

*Evidence is available from internal reporting that indicates that the service performance of an asset is, or will be, significantly worse than expected.*

### Fact Pattern

12. In 2018 Local Government Entity X acquired a street sweeper for 2,000 CU. The street sweeper has a useful life of 15 years. The street sweeper's carrying amount in 2023 was 1,800 CU. On acquisition the sweeper was estimated to cover 8,000 kilometres a year. Later in 2023 an assessment of the street sweeper's operational performance indicated that the sweeper was only covering 50% of the original estimate (4,000 kilometres a year). A street sweeper with an estimated coverage of 4,000 kilometres a year) of similar age can be purchased for 1,500 CU.

*Analysis*

<b>a. Acquisition Cost in 2018</b>	<b>2,000 CU</b>
<b>b. Gross Operational Value in 2023 prior to impairment indication</b>	<b>2,700 CU</b>
<b>c. Accumulated Depreciation (5/15 * 2700)</b>	<b>900 CU</b>
<b>d. Carrying Amount (Current Operational Value) in 2023</b>	<b>1,800 CU</b>
<b>e. Revised Gross Operational Value following impairment indication</b>	<b>1,500 CU</b>
<b>f. Accumulated Depreciation (5/15 *1,500)</b>	<b>500 CU</b>
<b>g. Recoverable Service Amount (Current Operational Value)</b>	<b>1,000 CU</b>
<b>h. Impairment Loss d-g</b>	<b>800 CU</b>

**Conclusion**

13. Fair value less costs to sell is not the relevant component of recoverable service amount. The carrying amount of the asset is reduced to 1,000 CU, which is the revised current operational value, The impairment loss of 800 CU split between the revaluation reserve to the extent of previous revaluation gains and surplus/deficit.

**Applicability of COV at Initial and Subsequent Measurements for Leases at Market Terms and at Below-Market Terms for Right-of-Use Assets**

**Question**

1. Does the IPSASB agree with the recommendation in paragraph 2?

**Recommendation**

2. Task Force and Staff recommend the IPSASB to agree that right-of-use assets acquired:
  - (a) At market terms, COV is unnecessary for initial measurement;
  - (b) At below market terms, ED 84 specific measurement technique is consistent with COV principles for initial measurement; and
  - (c) COV is applicable for subsequent measurement of right-of-use assets acquired at market terms and at below market terms if they are held primarily for operational capacity.

**Background**

3. At the September 2023 meeting, the IPSASB instructed staff to bring an agenda item with analysis on the possible applicability of COV at initial and subsequent measurements for leases at market terms and below market terms for right-of-use assets.

**Analysis**

4. [Appendix A](#) provides the analysis of the IPSAS 16, *Investment Properties*; IPSAS 45, *Property, Plant, and Equipment*; and IPSAS 46, *Measurement* requirements relevant to IPSAS 43, *Leases* and ED 84, *Concessionary Leases and Right-of-Use Assets In-Kind*. Staff recommends reading [Appendix A](#) before reading the paragraphs below.

*Measurement of Right-of-Use Assets under IPSAS 43*

5. Leases are contracts or part of contracts that convey the right to use an asset (underlying asset) for a period of time in exchange for consideration. Usually, leases involve payments in the future (the lease payments) for the duration of the lease contract.

**Initial Measurement**

6. For their initial measurement, IPSAS 43 requires the application of a measurement technique specifically designed to leases, as follows:
  - (a) The amount of the initial measurement of the lease liability, which includes the present value of the lease payments that are not paid at the commencement date;
  - (b) Any lease payments made at or before the commencement date, less any lease incentives received;
  - (c) Any initial direct costs incurred by the lessee; and
  - (d) An estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset, restoring the site on which it is located or restoring the underlying asset to the condition required by the terms and conditions of the lease, unless those costs are incurred to produce inventories. The lessee incurs the obligation for those costs either at the commencement date or as a consequence of having used the underlying asset during a particular period.

7. COV is unnecessary because it is undertaken in an orderly market transaction (see paragraph 1 of [Appendix A](#)). Furthermore, given the unique characteristics of a lease, guidance was developed so that the measurement technique explained in paragraph 6 is specifically designed to right-of-use assets acquired in leases at market terms.

#### Subsequent Measurement

8. To subsequently measure right-of-use assets, IPSAS 43<sup>11</sup> cross refers to:
- (a) IPSAS 16, *Investment Property*, if the right-of-use assets meet the definition of investment property in IPSAS 16 and the lessee applies the fair value measurement basis in the current value model in IPSAS 16.
  - (b) IPSAS 45, if right-of-use assets relate to a class of property, plant and equipment to which the lessee applies the current value model in IPSAS 45 and elects to apply that current value model to all of the right-of-use assets that relate to that class of property, plant and equipment.
9. As noted in paragraph 8–10 of [Appendix A](#), COV is not applicable to right-of-use assets within the scope of IPSAS 16.
10. The measurement of right-of-use assets<sup>12</sup> within the scope of IPSAS 45, depends on the primary objective for which the entity holds them:
- (a) If held for operational capacity, then the right-of-use assets are measured at COV; and
  - (b) If held for financial capacity, then the right-of-use assets are measured at fair value.
11. Staff notes that assets are used in the same way in the entity's operations, irrespective of whether they are owned or leased. This means that the methodology to determine the subsequent measurement of assets under IPSAS 45 (COV or fair value) should not change depending on whether the asset is owned or leased.
12. In other words, the variables in the methodology used to compute the amount of subsequent measurement of right-of-use assets should take into consideration, for example, the following:
- (a) Right to the residual—with owned assets the entity has a right to the residual of the underlying asset that can be sold, whereas with right-of-use assets the right to acquire the residual of the underlying asset may be optional; and
  - (b) Useful life—owned assets are usually held for the whole useful life of the underlying asset, whereas right-of-use assets are held for the duration of the lease term, which may shorter than the useful life of the underlying asset.
13. This means that although the methodology to subsequently measure owned assets and right-of-use assets is the same, the resulting amounts may be different to reflect the different economic characteristics of both types of assets, similar to what already happens in IPSAS 45 to other types of assets.

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<sup>11</sup> IPSAS 43 also permits to apply the cost model, which is the cost of the right-of-use asset less any accumulated depreciation and any accumulated impairment losses and any adjustment for remeasurement of the lease liability.

<sup>12</sup> For further details see paragraph 8 in [Agenda Item 8.2.7—Analysis of COV Applicability to IPSAS 43, Leases](#) discussed in September 2023

*Measurement of Right-of-Use Assets under ED 84, Concessionary Leases and Right-of-Use Assets In-kind*

14. [Appendix B](#) provides ED 84 detailed requirements to measure right-of-use assets in concessionary leases. Staff recommends reading [Appendix B](#) before reading the paragraphs below.

Initial Measurement

15. ED 84 proposes to initially measure the right-of-use asset acquired in concessionary leases by applying a measurement technique specifically developed for concessionary leases, which is the *present value of payments for the lease at market rates based on the current use of the underlying asset as at the commencement date* (see [Appendix B](#) for further details).
16. The requirement *present value payments for the lease at market rates based on the current use of the underlying asset as at the commencement date* is consistent with COV principles and the economics of leases because the leases requirement:
- (a) Discounts the market lease payments that are to be made in the future to obtain the value of the right-of-use asset at **today's terms**<sup>13</sup>;
  - (b) Uses as inputs the observable prices in the market; and
  - (c) Is based on the existing use and condition of the asset (i.e., the market minimum lease payments represent the value of right-of-use asset in its existing use).

Subsequent Measurement

17. At the September 2023, the IPSASB requested staff to analyze the potential implication of the initially measure right-of-use assets in concessionary leases based on *payments for the lease at market rates* (which is non-entity specific) and subsequently measuring at COV, when the right-of-use assets relate to a class of property, plant, and equipment to which the lessee applies the current value model in IPSAS 45.
18. Staff and Task Force note that ED 84 does not propose changes to IPSAS 43 on subsequent measurement of right-of-use assets in concessionary leases. This means that the subsequent measurement guidance in IPSAS 43 is also applicable to right-of-use assets in concessionary leases and so are the conclusions (see paragraphs 8 to 13 in this agenda item).
19. As shown in paragraph 16, the application of the ED 84 specific measurement technique of right-of-use assets in concessionary leases is consistent with COV principles.

**Decision Required**

20. Does the IPSASB agree with the Task Force and Staff [recommendation](#)?

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<sup>13</sup> IE13B of ED 84 provides an example on the application of this part of the requirement.



**Appendix A – Analysis of the IPSAS 16, IPSAS 45, and IPSAS 46 requirements relevant to IPSAS 43 and ED 84**

*Measurement under Current Operational Value as per IPSAS 46*

1. COV was developed as a subsequent current value measurement basis for assets held for their operational capacity in its existing use, location, and current condition. However, COV can also be applied at initial measurement only when the transaction is not undertaken in an orderly market (for example, the transaction is at below-market terms).
2. When measuring COV under IPSAS 46, an entity shall determine the amount the entity would pay for the remaining service potential of an asset at the measurement date, with the conditions identified in paragraph 1.
3. To calculate COV an entity firstly applies the market approach if an active market with transactions involving identical or similar assets exists. If there is no active market for identical or similar assets, then the entity applies the cost approach.
4. The market approach uses prices from an orderly transaction in the principal market and other relevant information generated by market transactions involving identical or comparable (i.e., similar) assets, liabilities or a group of assets and liabilities.
5. The cost approach reflects the amount that would be required currently to replace the service provided by an asset (often referred to as current replacement cost) through the acquisition, construction, or development of a substitute asset of comparable utility, adjusted for obsolescence. If market transactions involving identical or similar assets does not exist, COV is the cost to develop or produce the identical, or similar, asset.

*Subsequent<sup>14</sup> Measurement of Assets under IPSAS 45, Property, Plant, and Equipment*

6. When an entity elects the current value model under IPSAS 45, the entity measures the asset:
  - (a) At COV, if it is held primarily for its operational capacity; and
  - (b) At fair value, if it is held primarily for its financial capacity.
7. As required by IPSAS 46, when subsequently measuring an item of property, plant, and equipment at COV, an entity firstly applies the market approach if an active market with transactions involving identical or similar assets exists. If there is no active market for identical or similar assets, then the entity applies the cost approach.

*Subsequent<sup>15</sup> Measurement of Assets under IPSAS 16, Investment Property*

8. When an entity elects the current value model under IPSAS 16, the entity measures the asset at fair value.

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<sup>14</sup> Initial measurement is not discussed in this Agenda Item because IPSAS 43 already provides a specific measurement technique to measure right-of-use assets and does not cross-refer to IPSAS 45.

<sup>15</sup> Initial measurement is not discussed in this Agenda Item because IPSAS 43 already provides a specific measurement technique to measure right-of-use assets and does not cross-refer to IPSAS 16.

9. According to IPSAS 16.49A, when a lessee uses the current value model to measure an investment property that is held as a right-of-use asset, it shall measure the right-of-use asset, and not the underlying asset, at fair value.
10. At the September 2023, the IPSASB decided that COV is not an applicable current value measurement basis for assets in the scope of IPSAS 16 because they are not held for their operational capacity.

**Appendix B – ED 84 Detailed Requirements to Measure Right-of-Use Assets in Concessionary Leases**

1. ED 84 proposes to measure the right-of-use asset acquired in concessionary leases by applying a measurement technique specifically developed for concessionary leases and is divided into four parts:
  - (a) Part 1: "present value of"—This requirement intends to apply the concept of time value of money embedded in the lease as normally leases entail a series of payments in the future, even if they are at below-market terms. The measurement technique "present value" is consistent with:
    - (i) Its applicability in IPSAS 43 for leases at market terms; and
    - (ii) The accounting principles in IPSAS 46, which measure the current economic value of assets and liabilities whether the cash flows occur at a point in time or in the future.
  - (b) Part 2: "payments for the lease at market rates"—This requirement intends to obtain the market lease payments as if the lease was made at market terms. The term "market rates" can be seen as a proxy or a way to estimate how much the lessee would have to pay if the lease was made at market rates.
  - (c) Part 3: "based on the current use of the underlying asset"—This requirement intends to be a restriction in the assessment of market rates that serves as a cost-relief to preparers, as preparers do not need to search for the highest and best use of the underlying asset.
  - (d) Part 4: "as at the commencement date"—This requirement intends to be consistent with the requirements in IPSAS 43 for leases at market terms and other items of property, plant, and equipment under IPSAS 45, *Property, Plant, and Equipment*.