International Valuation Professional Board
41 Moorgate
London
EC2R 6PP

Per e-mail
26 May 2011

Dear Sirs,

PROPOSED TECHNICAL INFORMATION PAPER 2: DEPRECIATED REPLACEMENT COST

We welcome the opportunity to provide comment on the Proposed Technical Information Paper 2: Depreciated Replacement Cost issued by the International Valuation Professional Board.

The International Public Sector Accounting Standards Board (IPSASB) has recently issued a Consultation Paper Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Measurement of Assets and Liabilities in Financial Statements as part of a broader project to develop a public sector Conceptual Framework. The comment included in this letter has been formulated by comparing the principles in the IPSASB’s Consultation Paper to the Proposed Technical Information Paper.

Please do not hesitate to contact me should you wish to discuss any of our comment.

Yours sincerely

Erna Swart
Chief Executive Officer
General matters

1. Paragraph 4 of the Proposed Technical Information Paper (Paper) clarifies that the depreciated replacement cost (DRC) method is commonly used for the valuation of specialised assets where transactions are infrequent. It further clarifies that market information for such transactions may not be commonly available. Paragraph 55 however focuses on market derived information, which in our opinion, might not always be available for the reasons set out in paragraph 4. The IPSASB’s Consultation Paper also distinguishes replacement cost from a market value.

As paragraphs 4 and 55 might be seen as contradictory, we recommend that the Proposed Paper should clarify that DRC is current rather than a market value that reflects economic and financial conditions prevailing at the date of valuation.

2. Paragraph 3 states that in applying the DRC method, an entity needs to assess what the potential purchaser will pay to acquire or construct the asset. The IPSASB’s Consultation Paper on the other hand, considers the value of the asset to the owner. As the DRC method is commonly used for the valuation of specialised assets as explained in paragraph 4 of the Paper, we are of the view that the DRC method should rather consider the value of the asset to the owner, based on its use in delivering goods and services.

3. In addition, the service potential of the asset, and not only its ability to generate cash inflows, should be used in determining the DRC. This is particularly important if the method is to be applied to determine a value for public sector assets, as assets in the public sector are, not often, used to generate positive cash inflows or to earn a commercial return that reflects the risk involved in holding the asset. If the intention is to apply the principles in this Proposed Paper to public sector assets as well, the concept of the asset’s service potential, and how it should be determined in applying the DRC method, should be explained in the Proposed Technical Information Paper.