



NZ ACCOUNTING
STANDARDS
BOARD

10 October 2014

Mr Steven J. Sherman
Chairman
The International Valuation Standards Board
1 King Street
London EC2V 8AU
UNITED KINGDOM

Submitted to: CommentLetters@ivsc.org

Dear Mr Sherman

IVSC Standards Board's Agenda Consultation

The New Zealand Accounting Standards Board (NZASB) is pleased to submit its comments on the IVSC Standards Board's Agenda Consultation. We appreciate the opportunity to comment on the future work of the Standards Board.

The NZASB is a sub-board of the External Reporting Board, an independent Crown Entity responsible for financial reporting strategy and the development and issue of accounting and auditing and assurance standards in New Zealand. The NZASB has delegated authority from the External Reporting Board to develop (or adopt) and issue accounting standards for general purpose financial reporting in New Zealand.

The NZASB considers that the valuation profession plays a crucial role in contributing to the relevance and reliability of general purpose financial reporting. Financial statements include many items that are subject to uncertainty and which require the use of estimates. Both valuers and actuaries assist financial statement preparers and auditors in determining the amounts that are reported, both on the face of the financial statements and in the notes. The use of valuations obtained from a qualified valuer, undertaken in accordance with the IVSC's standards gives users confidence that the valuations are independent, objective and consistent with internationally recognised standards. This enhances the relevance and reliability of financial statements.

We note that internationally, there are two bodies developing financial reporting standards. The International Accounting Standards Board (IASB) develops International Financial Reporting Standards (IFRSs) which are designed to apply to the general purpose financial statements and other financial reporting of profit-oriented entities. Regulators in many jurisdictions have specified the use of IFRSs by private sector entities such as companies.

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International Public Sector Accounting Standards (IPSASs) are developed by the International Public Sector Accounting Standards Board (IPSASB) for use by public sector entities in the preparation of general purpose financial statements. IPSASs are applied mainly by governments but also by individual public sector entities and some international organisations.

In New Zealand we have a two sector, multi-tier accounting standards framework which distinguishes between for-profit entities and public benefit entities. The for-profit standards are based on IFRSs and the public benefit entity standards are based on IPSASs. We note that although there is a predominance of PBEs in the public sector in New Zealand, there are also a number of public sector for-profit entities. We consider that the distinction between for-profit entities and PBEs leads to a clear focus on those attributes of an entity that are important for financial reporting, such as the importance of the concept of service potential in relation to assets held by PBEs. We would encourage the IVSC in developing guidance to consider the distinctive characteristics of for-profit entities versus PBEs, rather than focusing on the differences between private and public sector entities.

We strongly encourage the IVSC Standards Board, in developing its agenda, to consult and work closely with the IASB and the IPSASB. Working with those Boards will help to identify topics or areas where additional valuation standards are required, or where existing valuation standards could be improved to work with the requirements in accounting standards. We would also encourage the IVSC Standards Board to refer to the requirements of both IFRSs and IPSASs when appropriate.

We note that the IFRS Foundation and the IVSC have a Statement of Protocols for co-operation on IFRS and International Valuation Standards. This Statement of Protocols was developed following an acknowledgment by the Trustees of the IVSC and the IFRS Foundation that interacting and exchanging information on how to measure fair values would be relevant and helpful in developing standards and guidelines on fair value measurement, which should lead to enhanced financial statements prepared in accordance with IFRS. We support the collaborative approach indicated by the Statement of Protocols.

We also note that the IVSC has a Memorandum of Understanding (MoU) with the International Federation of Accountants (IFAC). Given the increasingly widespread adoption of IPSASs by governments and public sector entities, we would encourage the IVSC to make use of this MOU with IFAC to support the identification of actions, by the IVSC and IFAC's standard-setting boards, that promote the credibility and acceptability of valuations prepared in accordance with the IVSs. For example, the IPSASB has recently completed its Conceptual Framework and in the context of its deliberations on that project, has signalled the possibility of undertaking further standards level work on measurement. This work might open up opportunities for discussions between the IVSC and the IPSASB.

We have predominately commented on those questions where there issues or concerns specific to financial reporting in New Zealand.

If you have any questions or require clarification of any matters in this comment letter, please contact Joanne Scott (Joanne.Scott@xrb.govt.nz) or me.

Yours sincerely

A handwritten signature in black ink, appearing to read "Kimberley Crook". The signature is written in a cursive style with a large initial 'K' and a long, sweeping underline.

Kimberley Crook

Chair – New Zealand Accounting Standards Board

IVSC Standards Board Agenda Consultation

General Criteria for Content

Question 1a

Should the IVSC supplement its current standards with additional standards for subsets of assets that fall within the high level categories currently covered in IVSs 200 – IVS 250?

If yes, please indicate the nature of the subsets that you would like to see included and any criteria that you believe that the Board should take into account in determining the priority to be given to these.

Question 1b

Should the IVSC create additional standards to deal with the application of the principles in the existing IVSs to valuations for different purposes?

If yes, please indicate any purposes other than those already covered in IVSs 300 and 310 (Financial Reporting and Real Property for Secured Lending) that you would like to see included and any criteria that you believe that the Board should take into account in determining the priority to be given to these.

Although the requirements of IVS 300 *Financial Reporting* refer generally to financial reporting standards, the application guidance refers only to IFRSs. We accept that it would be impossible to address national requirements in this application guidance. However, we consider that given the increasing adoption of IPSASs, it would be helpful for the application guidance to also consider the requirements of IPSASs. At present the measurement requirements in IFRSs and IPSASs are broadly similar but there are some differences, and, over time, these differences may increase.

Extractive Industries

Question 2a

Do you or your organisation encounter valuations of assets in the Extractive Industries? If no, please proceed to Question 3a.

If yes, please indicate the nature of the assets involved and the purposes for which the valuations are required.

Question 2b

Do you have experience of problems or inconsistency in the way in which assets in the Extractive Industries are valued? If so please also indicate whether, in your experience, these are:

- i) specific to a particular country or jurisdiction or are common across borders,
- ii) arise across all the extractive industries or are specific to a particular sector (eg mining) or subsector (eg metal ores).

Question 2c

Please indicate whether you believe that this should be a high, medium or low priority for inclusion on the Board's agenda.

No comment on question 2.

Forestry

Question 3a

Do you or your organisation encounter valuations of forests or woodland used primarily for timber production? If no, please proceed to Question 4a.

If yes, please indicate the nature of the forests and geographic region involved and the purposes for which the valuations are required.

Question 3b

Do you have experience of problems or inconsistency in the way in which commercial forests or woodlands are valued? If yes please indicate whether, in your experience, these are:

- i) specific to a particular country or jurisdiction or are common across borders,
- ii) broadly applicable across all the types of commercial forest or to be specific to a particular sector or type of forest.

Question 3c

Please indicate whether you believe that this should be a high, medium or low priority for inclusion on the Board's agenda.

Forest valuation has been a significant issue in New Zealand, not least following the introduction of the Emissions Trading Scheme. We are aware that the New Zealand Institute of Forestry (NZIF) commented on the IVSC's 2012 ED *The Valuation of Forests*. That comment letter provided an overview of the nature of the forests and the purpose for which the valuations are required.

The NZIF has developed a standard on forest valuation to address areas where issues had arisen in practice and where inconsistencies could occur. The NZIF has also developed guidance on how to incorporate the impact of the Emissions Trading Scheme on forest and forest land valuation. Having regard to the issues that had previously been encountered in New Zealand, the NZIF suggested that the IVSC's project on forestry needed to address a broader range of issues, including those addressed in the NZIF Forest Valuation Standard, the Australian forest valuation standards (and any operative standards from other countries).

We would support further work on forestry valuations, having regard to the issues that have previously been identified by New Zealand constituents.

Trade Related / Going Concern Property

Question 4a

Do you or your organisation produce or rely on valuations of real property that is normally bought and sold at a price which reflects the potential earnings that can be made from operating a particular type of business from the property? If no, please proceed to Question 5a.

If yes, please indicate the type or types of real property that you are aware are generally valued using this approach.

Question 4b

Do you consider that it would be beneficial for the Board to produce guidance on the method of valuation of a real property interest that uses the income that can be generated by a business in occupation as an input?

Question 4c

If you have answered yes to question 4b, please indicate the issues that commonly cause difficulty or inconsistency in applying this approach.

Question 4d

Please indicate whether you believe that this should be a high, medium or low priority for inclusion on the Board's agenda.

No comment on question 4.

Specialised Public Sector Assets

Question 5a

Do you or your organisation value or rely on valuations of real property, plant and equipment held in the public sector? If no please proceed to question 6a.

If yes, please indicate the purpose or purposes for which the valuations are required.

Question 5b

Do you have experience of problems or inconsistencies in the way in which these assets are valued?

If yes, please indicate whether these:

- i) arise from the nature of the asset,
- ii) arise or are likely to arise across borders,
- iii) arise because of the need to comply with specific legislation or regulation. Question 5c.

Please indicate whether you believe that this should be a high, medium or low priority for inclusion on the Board's agenda.

Public sector entities (including central government, local government and many individual public sector entities) in New Zealand have been required to report in accordance with internationally-based financial reporting standards for many years. They have therefore been required to comply with the requirements of IAS 16 *Property, Plant and Equipment*, and more recently with IPSAS 17 *Property, Plant and Equipment*. Under both of these standards there has been widespread use of the revaluation model for subsequent measurement because this is seen as providing more relevant information than historic cost. There has also been widespread reliance on valuations to support the use of this model.

Depreciated replacement cost is widely used for the valuation of assets in both the private and public sectors in New Zealand. In particular, it is frequently used in the valuation of infrastructure assets, which represent a significant proportion of assets in the financial statements of public sector entities.

Standard setters have observed diversity in practice regarding the capitalisation of interest in valuations using the depreciated replacement cost approach. For this reason the Financial Reporting Standards Board, the previous financial reporting standard setter, encouraged the IVSC to include guidance on this in TIP 2 *The Cost Approach for Tangible Assets*. This remains a problem area in practice.

When the NZASB was developing the current suite of PBE Standards, specifically PBE IPSAS 17 *Property, Plant and Equipment*, it noted that there had been previous domestic guidance on the use of depreciated replacement cost by PBEs. This guidance had been developed to address aspects where diversity had been observed. The NZASB decided that guidance was still required and agreed to include application guidance in PBE IPSAS 17 on the estimation of fair value using the depreciated replacement cost method in the circumstances permitted by paragraph 48 of that Standard.

In developing PBE IPSAS 17 the NZASB noted that the International Valuation Standards Council had recently issued TIP 2 which provides guidance on the application of the cost approach to valuation, including application of the depreciated replacement cost method. The NZASB noted the desirability of aligning, to the extent possible, the guidance in PBE IPSAS 17 with that issued by the international valuation profession.

There were some areas where the NZASB considered that the guidance in PBE IPSAS 17 needed to differ from that in TIP 2 to adequately deal with the characteristics of public benefit entities, including the need in many cases to focus on the service potential of assets rather than their cash generating potential and the reality that there is often a very limited market for assets being valued on a DRC basis. For example, PBE IPSAS 17:

- (a) requires that the value of land reflect the fair value of the actual land held, in terms of both its size and location, and, where land is under-utilised, it requires that the fair value of the land be determined by reference to its highest and best use;
- (b) requires that application of depreciated replacement cost be based on the market price of inputs, but it does not refer to the costs that would be incurred by a typical market participant;
- (c) does not permit the inclusion of a profit to provide an adequate return on equity; and
- (d) specifically discusses how changes in the way goods and services are delivered in a sector may give rise to external obsolescence. It states that in considering demand for the asset or for the products or services produced from the asset, demand both by policy makers in seeking to further public policy objectives and demand evidenced by the recipients of the products or services produced by the asset should be taken into account.

Because most of our experience has been with issues surrounding the application of the cost approach, we have not commented on the need for guidance on the use of the income approach or market approach. However, we would urge that any valuation guidance that may be used for financial reporting purposes clearly explain the links between the terminology used in that guidance and the terminology used in financial reporting standards.

Derivatives

Question 6a

Do you or your organisation value or rely on valuations of derivatives? If no, please proceed to question 7a.

Question 6b

Please indicate which of the listed underlying asset classes you believe should be given priority in the next phase of the Derivatives project.

Both IFRSs and IPSASs specify requirements for accounting for derivatives. Many New Zealand entities report on their use of derivatives in accordance with these requirements. We note the increasing use of commodity-based derivatives in New Zealand over the last few years (for example, NZX has a Global Dairy Futures and Options market which assists farmers, producers, manufacturers and others to manage the price risk inherent in the global dairy industry). We therefore encourage the Standards Board to continue its work on this project and to address commodity derivatives in a subsequent phase of the project.

In addition, the market approach to the valuation of financial derivatives has undergone significant changes since the beginning of the global financial crisis and we note the importance for the valuation standards of addressing changes in market practice. Derivatives instruments are no longer measured using only risk free curves but are adjusted to reflect additional inherent risks such as foreign currency basis risk, counterparty credit risk, own credit risk and effect of collateralisation.

Funding Valuation Adjustments

Question 7a

Please indicate whether you have encountered problems or inconsistencies in the way in which funding valuation adjustments are applied. If not please proceed to question 8a.

Question 7b

Please indicate whether you believe that this should be a high, medium or low priority for inclusion on the Board's agenda.

No comment on question 7.

Valuations for Resolution and Recovery

Question 8a

Please indicate whether you or your organisation has to value or rely on valuations to support restructuring or corporate recovery. If no please proceed to question 9.

Question 8b

If yes, please indicate any valuation issues that you currently experience or anticipate arising under emerging regulations.

Question 8c

Please indicate whether you believe that this should be a high, medium or low priority for inclusion on the Board's agenda.

No comment on question 8.

Invitation to Suggest Projects

Question 10

Do you wish to suggest any additional projects for inclusion in the Board's agenda?

If yes, please identify the nature of the suggested project as precisely as possible and provide the information requested in para 42 above.

As noted in our response to question 1, we consider that the application guidance accompanying IVS 300 *Financial Reporting* should be expanded to consider the requirements of IPSASs.

Project criteria	Comment
Is the project one which addresses the needs of valuation users across different jurisdictions?	Yes. An increasing number of governments and public sector entities are adopting IPSASs or IPSASs-converged standards and will be seeking valuations in accordance with those standards. The requirements of some IPSASs differ from the equivalent IFRSs and, as the IPSASB addresses more public sector specific projects, there may be no IFRSs equivalent. The relevance and reliability of financial statements is heavily influenced by the appropriate application of valuation standards.
Is there evidence of diversity in practice that could be resolved by either introducing a new standard or other form of IVSC pronouncement or by amendments to a current standard or pronouncement?	Additional guidance in IVS 300, linking to the requirements in IPSASs, would make it easier for valuers and preparers to have a common understanding of the terms of the engagement.
Is there evidence that a broad spectrum of users and providers of valuations in the sector and across jurisdictions would support IVSC developing a standard or guidance on the topic?	The use of IPSASs has increased significantly over the last few years. In addition, IPSASs are frequently used as a reference point by jurisdictions developing national requirements.

Project criteria	Comment
Will the project produce an overall benefit for users and providers of valuations?	As noted above, we consider that clearly identifying the relevant requirements in IPSASs would assist in clear specification of the valuation required, and thereby enhance the relevance and reliability of amounts reported in the financial statements.
Will the project increase the possibility of achieving the convergence of valuation standards in different jurisdictions?	The inclusion of additional application guidance in IVS 300 is unlikely to impact on the convergence of valuation standards, but may impact on the convergence of valuation practice.
Is the project achievable with regard to current or attainable resources and other current work priorities?	Our suggestion could affect aspects of a number of projects (eg development process, structure and content). Rather than competing with resources for other projects, we consider that the development of such guidance could be useful to other projects.