



Accounting Standards Board

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The Technical Director
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Per e-mail

29 September 2017

Dear John,

COMMENT ON CONSULTATION PAPER ON *FINANCIAL REPORTING FOR HERITAGE IN THE PUBLIC SECTOR*

We welcome the opportunity to comment on the Consultation Paper on *Financial Reporting for Heritage in the Public Sector*. We support the initiative from the IPSASB to develop guidance on accounting for heritage as this will address the divergent and inconsistent practices in the public sector.

Our responses to the preliminary views and specific matters for comment are included as Annexure A, while other comments are included as Annexure B to this letter.

The views expressed in this letter are those of the Secretariat and not the Accounting Standards Board (Board). In formulating its comments, the Secretariat consulted with a range of stakeholders including auditors, preparers, consultants, professional bodies and other interested parties.

Please feel free to contact me should you have any queries relating to this letter.

Yours sincerely

A handwritten signature in black ink, appearing to read 'J Poggiolini', written in a cursive style.

Jeanine Poggiolini, Technical Director

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ANNEXURE A – PRELIMINARY VIEWS AND SPECIFIC MATTERS FOR COMMENT

Specific Matters for Comment—Chapter 1 (following paragraph 1.8)

Do you agree that the IPSASB has captured all of the characteristics of heritage items and the potential consequences for financial reporting in paragraphs 1.7 and 1.8?

If not, please give reasons and identify any additional characteristics that you consider relevant.

Chapter 1 proposes certain characteristics for heritage items, while chapter 2 proposes a description for heritage items. We are unsure why the IPSASB requested comments on the characteristics and what it intends to do with this information given that a definition for heritage items has been developed.

Characteristics of heritage items (paragraph 1.7)

We broadly support the characteristics of heritage items listed in paragraph 1.7, but identified areas for potential improvement.

The characteristics should be expanded to indicate that the heritage item should be of particular significance to a community and/or jurisdiction and not only to the entity itself. If the heritage item is only significant to the entity and not the community and/or jurisdiction, there is no benefit in preserving the heritage item for present and future generations. We therefore recommend that the overall consideration of significance of the heritage item to the community and/or jurisdiction should be emphasised in the characteristics listed in paragraph 1.7.

We further recommend that, as the significance of an item to a particular community and/or jurisdiction can change over time, guidance should be provided on whether such changes will result in a reclassification of an item previously classified as a heritage item and vice versa. For example, a sculpture of a political leader (even if by a well-known artist) may be significant to a specific generation, but may not be to future generations, and as a result, that sculpture may no longer meet the characteristics and/or definition of a heritage item.

In addition, we propose that the following characteristics could be included in the list in paragraph 1.7:

- Heritage items may increase in value over time even if their physical condition deteriorates.
- Heritage items are protected, kept unencumbered, are cared for and preserved.

Consequences of the characteristics of heritage items (paragraph 1.8)

It is unclear what the difference is between the first and second consequence noted in this paragraph. As measurement involves attaching a monetary value to a heritage item, we recommend that the first and second consequence should be combined if these are included in any future guidance developed by the IPSASB. The concept of “heritage significance” is discussed in (b) on “value”, but (a) on “measurement” only refers to “service potential or their ability to generate economic benefits”. As a result, the two consequences seem to be contradictory in terms of what is being measured.

In addition, attaching a value to a heritage item could be challenging for the following reasons:

- Restrictions imposed on the disposal and/or transfer of the heritage item.
- Entities often indicate a reluctance to value heritage items as this may make the items more susceptible to theft.

We recommend that these aspects should also be addressed in the consequences dealing with measurement and/or valuation.

Preliminary View—Chapter 2.1 (following paragraph 2.11)

For the purposes of this CP, the following description reflects the special characteristics of heritage items and distinguishes them from other phenomena for the purposes of financial reporting:

Heritage items are items that are intended to be held indefinitely and preserved for the benefit of present and future generations because of their rarity and/or significance in relation, but not limited, to their archaeological, architectural, agricultural, artistic, cultural, environmental, historical, natural, scientific or technological features.

Do you agree with the IPSASB’s Preliminary View? If not, please provide your reasons.

We support the overall description of heritage items, but we are of the view that the list explaining what is deemed to be significant is too long and potentially repetitive. We recommend that the list be shortened by combining some aspects, for example environmental could form part of natural, and agricultural could form part of cultural.

We noted the following additional observations on the description of heritage assets:

- (a) We question where intangible cultural heritage, specifically intellectual property, as defined under UNESCO, is captured in the description.
- (b) The UNESCO description classifies heritage between cultural and natural heritage. Paragraph 2.4 explains that cultural heritage consists of man-made heritage. We question this statement as we are of the view that the two categories are not mutually exclusive. Some natural heritage could also have a cultural value, e.g. the “fynbos” nature reserves in the Western Cape of South Africa have cultural significance because of the plants’ medicinal properties and their role in traditional cuisine.

We therefore recommend that the IPSASB should consider the appropriateness of applying the UNESCO classification when developing future guidance as some natural heritage could either be man-made, and/or have a cultural value.

Preliminary View—Chapter 2.2 (following paragraph 2.12)

For the purposes of this CP, natural heritage covers areas and features, but excludes living plants and organisms that occupy or visit those areas and features.

Do you agree with the IPSASB’s Preliminary View? If not, please provide your reasons.

We support the view that natural heritage covers areas and features, and excludes living plants and organisms as they cannot be held indefinitely and preserved for present and future generations.

In certain instances the living plants and organisms contribute towards the heritage value of an area or feature. Therefore, guidance is needed to explain that, even though living plants and organisms do not meet the definition of heritage, they may contribute to the significance of an area or feature that result in classification as natural heritage. For

example, the Great Barrier Reef in Australia received world heritage status for its outstanding universal value. The guidance should also provide clarification on how, if at all, the living plants and organisms on the area or feature impact the measurement of the natural heritage.

Preliminary View—Chapter 3 (following paragraph 3.11)

The special characteristics of heritage items do not prevent them from being considered as assets for the purposes of financial reporting.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

We support the view that the special characteristics of heritage items do not prevent them from being considered as assets for the purposes of financial reporting.

However, paragraph 3.8 concluded that, even though knowledge-in-action falls within the description of a heritage item, it cannot be controlled by a single entity. The preliminary view, however, does not acknowledge that some types of heritage cannot be controlled by an entity. It is therefore unclear from the Consultation Paper how knowledge-in-action will be addressed in a future definition and/or guidance.

Specific Matters for Comment—Chapter 4.1 (following paragraph 4.17)

Do you support initially recognizing heritage assets at a nominal cost of one currency unit where historical cost is zero, such as when a fully depreciated asset is categorised as a heritage asset then transferred to a museum at no consideration, or an entity obtains a natural heritage asset without consideration?

If so, please provide your reasons.

Recognition of heritage assets at one currency unit

We do not support the approach to recognise items at one currency unit in any of the scenarios described in paragraph 4.16 and the specific matter for comment. We consider that paragraph 4.16 and the specific matter for comment aim to deal with issues related to the transfer and acquisition of heritage assets in a non-exchange transaction, as well as the potential reclassification of existing assets within an entity, e.g. when a heritage item is reclassified from an existing category of assets such as property, plant and equipment.

Paragraph 4.16 proposes that historical cost is zero where, for example, the asset was fully depreciated before being transferred to the entity. In our view the fully depreciated value of the asset will reflect the value of the asset for the entity transferring the asset. The entity receiving the asset should apply the principles in IPSAS 23 *Revenue from Non-exchange Transactions (Taxes and Transfers)* and measure the asset at fair value on initial recognition.

Recognising a heritage asset received at no or a nominal cost at one currency unit is different to the principles in other IPSASs that require all other assets received in a non-exchange transaction to be measured at fair value. We consider that the special characteristics of heritage resources do not preclude them from being measured in the same way as other assets, and therefore recommend that the same principle be applied to heritage.

Initially recognising heritage assets received at no or a nominal cost at one currency unit where historical cost is zero (or in any situation) does not, in our view, meet the qualitative characteristics of relevance and faithful representation.

In addition, if the concerns raised in paragraph 4.16 relate simply to the re-categorisation of assets by an entity, any future guidance developed by the IPSASB on accounting for heritage could provide principles on measuring assets when there is a change in classification.

Treatment of subsequent expenditure

We are of the view that, irrespective of the value at which a heritage asset was initially recognised by an entity, any subsequent expenditure incurred should be accounted for in the same way as other assets, i.e. any subsequent expenditure incurred that will enhance the heritage asset's service potential and economic benefits should be capitalised. Furthermore, expensing subsequent costs on some heritage assets while capitalising the costs in other instances will, not result in relevant information to users of the financial statements for decision making.

As we consider that the special characteristics of heritage resources are no different to that of other resources, we recommend that the same principle on the treatment of subsequent expenditure that applies to other assets, should apply to heritage assets.

Preliminary View—Chapter 4.1 (following paragraph 4.40)

Heritage assets should be recognised in the statement of financial position if they meet the recognition criteria in the Conceptual Framework.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

As we are of the view that the special characteristics of heritage resources do not prevent them from being considered differently from other resources, we support the preliminary view that heritage assets should be recognised in the statement of financial position if they meet the recognition criteria in the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (Conceptual Framework).

Specific Matters for Comment—Chapter 4.2 (following paragraph 4.40)

Are there heritage-related situations (or factors) in which heritage assets should not initially be recognised and/or measured because:

- (a) it is not possible to assign a relevant and verifiable monetary value; or*
- (b) the cost-benefit constraint applies and the costs of doing so would not justify the benefits?*

If yes, please describe those heritage-related situations (or factors) and why heritage assets should not be recognised in these situations.

The Conceptual Framework requires that the benefits of financial reporting should justify the costs incurred to provide and use the information. However, we are of the view that the cost-benefit constraint should not impact the nature of information to be included on heritage assets in general purpose financial reports. All users will need information to understand the entity's custodial and other responsibilities to preserve heritage for present and future generations. We therefore do not support the use of cost-benefit as an argument to not initially recognise and/or measure heritage.

Factors that could prevent an entity from recognising and measuring a heritage asset in its financial statements, is (a) the absence of cost information on initial recognition, (b) the unavailability of market information in an active market to obtain a value for the heritage asset, (c) the absence of valuation techniques that can be applied to determine a market value for a heritage asset, and (d) when the range of market values are so diverse that the qualitative characteristics of relevance and faithful representation in the Conceptual Framework cannot be met.

Note: While we are aware that the Conceptual Framework requires measurement of an element to satisfy all the qualitative characteristics, we are of the view that the measurement of a heritage asset should faithfully portray the economic benefits, service potential and/or heritage significance of the resource in a way that provides relevant information to users of the financial statements to hold entities accountable and make decisions.

We therefore recommend that, in developing future guidance on financial reporting for heritage in the public sector, the IPSASB should consider providing guidance on:

- whether sector benchmarks and/or valuation techniques can be considered, as well as what types of inputs (e.g. directly observable market inputs, unobservable inputs, etc.) will be acceptable, to determine a market value for a heritage asset in the absence of an active market;
- how the significance of the heritage value of the item should be valued, if at all; and
- whether entities will be required to only disclose information to the users in the absence of determining a value for a heritage item that meets the qualitative characteristics of relevance and faithful representation in the Conceptual Framework (also refer to the note on the satisfaction of all qualitative characteristics above).

Preliminary View—Chapter 4.2 (following paragraph 4.40)

In many cases it will be possible to assign a monetary value to heritage assets. Appropriate measurement bases are historical cost, market value and replacement cost.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

We support the view that historical cost and market value are appropriate measurement bases to assign a monetary value to heritage assets.

We question whether replacement cost is an appropriate measurement basis. Applying replacement cost means that an entity replaces the operational value of the heritage asset. The heritage value and significance of the original heritage asset will however not be fully reflected by applying replacement cost. Furthermore, one of the characteristics of heritage items as noted in paragraph 1.7 of the Consultation Paper is that it is irreplaceable. Therefore applying replacement cost as a measurement basis to value the economic benefits or service potential of an asset, is not appropriate.

Specific Matters for Comment—Chapter 4.3 (following paragraph 4.40)

What additional guidance should the IPSASB provide through its Public Sector Measurement Project to enable these measurement bases to be applied to heritage assets?

Paragraph 4.18 notes that market values will be obtained for some heritage asset through reference to the market value of similar items if an active and orderly market exists. However, where heritage assets are unique, meaningful markets are unlikely to be available.

We recommend that guidance be provided to entities on how market value should be determined in the absence of an active market (also refer to our response to the specific matter for comment on chapter 4.2).

Preliminary View – Chapter 5 (following paragraph 5.14)

Subsequent measurement of heritage assets:

- (a) *Will need to address changes in heritage asset values that arise from subsequent expenditure, consumption, impairment and revaluation.*
- (b) *Can be approached in broadly the same way as subsequent measurement for other, non-heritage assets.*

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

We support the proposal that changes in heritage asset values that arise from subsequent expenditure, impairment and revaluation should be addressed in the same way as other assets.

Depreciation or amortisation

Depreciation or amortisation reflects the periodic consumption of an asset in an entity's operations. We question the recognition of depreciation or amortisation on heritage assets as the objective of holding heritage assets is to preserve them for present and future generations rather than to consume or use the asset in its operations.

We also note the following based on the characteristics of heritage items:

- A heritage item is expected to be available in future, and as such, most heritage items have an indefinite useful life as there is no finite period over which a heritage item is expected to be held by an entity.
- Paragraph 1.7 indicates that the heritage value of the item may appreciate over time, rather than depreciate.

We are therefore of the view that the depreciation or amortisation principles applicable to other assets are not relevant for heritage assets.

Specific Matters for Comment—Chapter 5 (following paragraph 5.14)

Are there any types of heritage assets or heritage-related factors that raise special issues for the subsequent measurement of heritage assets?

If so, please identify those types and/or factors, and describe the special issues raised and indicate what guidance IPSASB should provide to address them.

Calculating impairment losses

Based on our comment that cost and market value should be considered as the only measurement bases for heritage assets, consideration should be given to the impairment models that will be appropriate to assess impairment for heritage assets.

As most heritage assets are likely to be classified as non-cash generating assets, an entity will be required to measure the recoverable service amount at the higher of the asset's fair value less costs to sell and value in use. In terms of IPSAS 21 *Impairment of Non-cash Generating Assets*, value in use is determined by applying either (a) depreciated replacement cost, (b) restoration cost approach or (c) service units approach.

Based on our previous observations on depreciation and the application of replacement cost, we recommend that the IPSASB considers how the heritage asset's recoverable service amount should be calculated for purposes of impairment.

Preliminary View—Chapter 6 (following paragraph 6.10)

The special characteristics of heritage items, including an intention to preserve them for present and future generations, do not, of themselves, result in a present obligation such that an entity has little or no realistic alternative to avoid an outflow of resources. The entity should not therefore recognize a liability.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

We agree with the view that the special characteristics of heritage items, including an intention to preserve them for present and future generations, do not result in a present obligation for the entity.

We therefore agree that the entity should not recognise a liability.

Preliminary View—Chapter 7 (following paragraph 7.9)

Information about heritage should be presented in line with existing IPSASB pronouncements.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons and describe what further guidance should be provided to address these.

We agree with the view that information about heritage should be presented in line with the IPSASB's existing pronouncements.

In developing disclosure requirements for reporting on heritage in the public sector, we recommend that the following aspects should be considered in addition to the requirements in other asset standards:

- Subsequent expenditure incurred on heritage items that were not recognised by the entity.
- Judgements and assumptions applied to conclude that a heritage item does not meet the recognition criteria, or that a value could not be determined for a heritage asset.
- The extent to which experts were used to determine a value for a heritage asset.
- An indication of how the "heritage significance" of the item for the community and/or jurisdiction was assessed in determining the value for a heritage asset.
- Information that explains the entity's custodial responsibilities for heritage items.

In addition, we also recommend that consideration be given to the inclusion of a line item that reflects the repairs and maintenance costs incurred to preserve heritage items.

ANNEXURE B – OTHER COMMENTS

Public interest and financial reporting for heritage (paragraph 1.9)

Paragraph 1.9 notes that users may need information to (a) hold entities accountable for their preservation of the heritage item, and (b) make decisions on resources needed for heritage preservation.

In our view, users of general purpose financial statements also need information on an entity's custodial responsibilities. Users will also require information on heritage assets that have a dual purpose, i.e. those heritage assets that are significant for present and future generations, but which are also used by an entity in its day to day operations, for example, a historical building used as an administrative building. This information will enable the users to assess whether the heritage value of the asset is deteriorating or damaged through the use of the heritage asset in day to day operations.

We recommend that these two aspects should also be included in the discussion on information that users may need when the IPSASB develops future guidance on reporting for heritage in the public section.

Control of a resource (paragraphs 3.6 to 3.7)

Paragraph 3.7 explains the criteria to be applied by an entity to demonstrate its ability to control heritage resources. The explanations seem to focus on the entity's ability to direct physical access, rather than the entity's ability to direct how the economic benefits or service potential of the resource should be used by the entity and/or others.

We therefore recommended that any future guidance should clarify that, in assessing the entity's ability to access or deny or restrict access, the entity should assess whether it has the ability to decide how, and by whom the resource can be used. This right will demonstrate the entity's ability to direct the future economic benefits or service potential associated with the resource and should therefore not be limited to restricting or denying physical access to the resource.

Qualitative characteristics – comparability (paragraph 4.30)

Paragraph 4.30 states that comparability is the quality of information that enables users to identify similarities in, and differences between, two sets of phenomena. We question the relevance of comparability in relation to the recognition and/or measurement of heritage assets. As the nature of the heritage assets controlled by one entity is likely to differ from that of another entity, comparability may not be relevant in all instances.

We recommended that any guidance should explain how this qualitative characteristic will assist users to identify similarities between entities, particularly in relation to recognising and measuring heritage items as assets.

Constraints on information included in general purpose financial reports – materiality (paragraph 4.32)

The discussion of materiality in the Consultation Paper focuses mainly on the quantitative considerations and does not discuss qualitative considerations in relation to heritage assets sufficiently. Qualitative considerations may be more appropriate based on the nature of the

assets as users will need information to understand how an entity is fulfilling its custodial responsibility and other responsibilities.

We recommend that the application of both quantitative and qualitative materiality should be emphasised in developing any future guidance.

Constraints on information included in general purpose financial reports – cost benefit (paragraph 4.34)

Paragraph 4.34(c) notes that, one of the benefits of recognising heritage assets in the statement of financial position, is improved asset accountability and management. We do not agree with this observation as, in our view, recognising assets in the financial statements will not improve asset management necessarily. In our view the objective of financial reporting is not to improve asset management, but rather to provide information to the users of the financial statements about the entity that is useful to them to assess accountability and for decision-making purposes. Applying the principles in an accounting standard can therefore not by itself result in better asset management.

Depending on the nature of future guidance to be developed by the IPSASB on reporting on heritage, we recommend that this aspect should be reworded.

Other guidance needed – heritage assets with a dual purpose

As noted above, some heritage assets have more than one purpose, e.g. an historic building which, in addition to meeting the description and/or characteristics of a heritage item, is also used as office accommodation. This aspect has not been addressed in the Consultation Paper, but may be relevant in a number of instances.

Depending on the nature of future guidance to be developed by the IPSASB on reporting on heritage, we recommend that guidance should be included on the accounting considerations of heritage assets with a dual purpose. The guidance to be developed should consider, for example, whether a significant portion of the asset used or held meets the definition of heritage, or that of another type of asset, for example property, plant and equipment. The guidance to be developed could clarify that the asset should only be accounted for as a heritage asset to the extent that an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes.