

Meeting: International Public Sector Accounting
Standards Board

Meeting Location: Virtual Meeting

Meeting Date: December 7–10, and 14–15, 2021

Agenda Item 6

For:

☒ Approval

☐ Discussion

☐ Information

CONCEPTUAL FRAMEWORK–LIMITED SCOPE UPDATE (CF-LSU) – NEXT STAGE

Project summary	The project objective is to update the Conceptual Framework for a limited number of issues based on the criteria of urgency, consequences, feasibility, and prevalence, with an emphasis on the first three of these criteria.	
Board Sponsor	Ian Carruthers, IPSASB Chair	
Meeting objectives	Topic	Agenda Item
Project management	Conceptual Framework–Limited Scope Update (CF-LSU)–Next Stage: Project Roadmap	6.1.1
	Instructions up to Previous Meeting	6.1.2
	Decisions up to Previous Meeting	6.1.3
Decisions required at this meeting	Guidance on Rights in Context of a Resource	6.2.1
	Guidance on Unit of Account/Executory Contracts	6.2.2
	Structure of Section, <i>Liabilities</i>	6.2.3
	Specific Matters for Comment	6.2.4
	Approval of ED 81	6.2.5
Other supporting items	Draft ED 81, Conceptual Framework Update: Chapter 3, <i>Qualitative Characteristics</i> and Chapter 5, <i>Elements</i>	6.3.1

CONCEPTUAL FRAMEWORK–LIMITED SCOPE UPDATE (CF-LSU) – NEXT STAGE: PROJECT ROADMAP

Meeting	Completed Actions or Discussions / Planned Actions or Discussions:
Conceptual Framework–Limited-Scope Update	
March 2020	1. Approve Limited Scope Update of Conceptual Framework Project Brief
June 2020	1. Discussion of Issues
September 2020	1. Discussion of Issues 2. Review [draft] Exposure Draft 76, <i>Conceptual Framework Update: Chapter 7, Measurement</i>
October 2020	1. Discussion of Issues
December 2020	1. Approve Exposure Draft 76
February 2021	1. Finalize remaining instructions
March 2021	1. Discussion of Issues
June 2021	1. Discussion of Issues
September 2021	1. Discussion of Issues 2. Review [draft] Exposure Draft 81 <i>Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements</i>
October 2021	1. Discussion of Issues 2. Review [draft] Exposure Draft 81
December 2021	1. Approve Exposure Draft 81.

INSTRUCTIONS UP TO PREVIOUS MEETING

Meeting	Instruction	Actioned
Conceptual Framework–Limited-Scope Update		
October 2021	1. Delete the third sentence of paragraph 5.7 because it duplicates a subsequent bullet point.	1. Paragraph 5.7 has been deleted and replaced by a new paragraph 5.7A. See Agenda Items 6.2.1 and 6.3.1
	2. Work with Members and liaise with staff of the Australian Accounting Standards Board over drafting changes to paragraphs 5.7 and 5.8 and to the extent to which additional material from paragraphs 4.6-4.13 of the IASB 2018 Conceptual Framework should be included in the section on ‘A Resource’.	2. Paragraphs 5.7A-5.7F have been added. See Agenda Items 6.2.1 and 6.3.1.
	3. Consider how to make a cross-reference to the discussion of ‘sovereign rights’ in paragraph 5.13 of the section, ‘Past Events.’	3. Paragraph 5.7G has been added. See Agenda Item 6.2.1 and Agenda Item 6.3.1.
	4. Circulate a revised section on ‘A Resource’ out of session.	4. Circulated on November 15 th .
	5. Include a Specific Matter for Comment on whether the Framework should include a separate section on Executory Contracts/Executory Binding Arrangements.	5. Specific Matter for Comment 8. See Agenda Item 6.2.4 and ED 81 at Agenda Item 6.3.1.
	6. Modify paragraph 5.26G so that it establishes principles, rather than treating executory contract arrangements as examples of binding arrangements that establish both rights and obligations for the parties to the arrangement.	6. Wording of first sentence of paragraph 5.26G changed so that it does not include ‘An example is where’. See Agenda Items 6.2.2 and 6.3.1.
	7. Add ‘to the extent that’ in the second sentence of paragraph 5.26G.	7. As a result of restructuring this instruction now relates to paragraph 5.26I. Wording included in first sentence of paragraph 5.26I. Agenda Items 6.2.2 and 6.3.1.

Agenda Item 6.1.2

	8. Consider whether paragraph 5.26G should include material on onerous binding arrangements drawn from paragraph 4.57 of the IASB 2018 Framework, i.e., arrangements where the terms of exchange become favorable or unfavorable to the reporting entity prior to performance.	8. New paragraph 5.26H is drawn from paragraph 4.57. It provides guidance on arrangements where the terms of exchange become favorable or unfavorable to the reporting entity prior to performance. It does not include a reference to testing for an onerous contract, which is considered a standards-level issue. See Agenda Items 6.2.2 and 6.3.1.
	9. Explain more fully why the term 'contract' is problematic in paragraph BC5.36F.	9. Fuller explanation provided. See Agenda Item 6.3.1.
	10. Add 'or the remaining component' in paragraph 5.26C as it relates to an entity transferring part of an asset or part of a liability.	10. Wording added. See Agenda Items 6.2.2 and 6.3.1.
	11. Redraft paragraphs 5.26D(a)(iii) and 5.26D(a)(iv), reviewing the use of 'service potential'.	11. Paragraph 5.26D(a)(iii) has been shortened. Reference to 'service potential' has been retained in paragraph 5.26(a)(iv), but qualified by 'interdependent'. See Agenda Items 6.2.2 and 6.3.1.
	12. Modify paragraph 5.26D to indicate that not all the listed characteristics have to be present to justify selection of a particular unit of account.	12. Paragraph 5.26D has been modified. See Agenda Items 6.2.2 and 6.3.1.
	13. Make a general reference in the Basis for Conclusions that 'obligations' can include 'present obligations'.	13. Sentence added to paragraph 5.36C. See Agenda Item 6.3.1.
	14. Modify or remove the reference in paragraph BC5.36C to relevance and faithful representation as 'the most important qualitative characteristics in evaluating the usefulness of information on unit of account.'	14. Reference removed in paragraph 5.36C. See Agenda Item 6.3.1
	15. Circulate a revised section on Unit of Account out of session.	15. Circulated on November 15 th .

Agenda Item 6.1.2

September 2021	1. Add an explanation in the Basis for Conclusions (BC) that materiality impacts various QCs, including understandability.	1. Paragraph BC3.32C of Agenda Item 2.3.1.
	2. Review drafting of the sentence inserted in paragraph 3.32, replacing 'discretely' with a more understandable word, and linking more clearly with materiality.	2. "Discretely" replaced with 'separately' in paragraph 3.32A of Agenda Item 2.3.1.
	3. Specify uniform characteristics for when a particular information item becomes material in context of qualitative and quantitative materiality.	3. Paragraph 3.32A of Agenda Item 2.3.1.
	4. Split paragraph 3.32 into two paragraphs.	4. Addition of paragraph 3.32A in Agenda Item 2.3.1, which includes the second part of previous paragraph 3.32.
	5. Update the wording on regularity assertions/statements to note transactions, rather than just expenditures	5. Paragraph 3.32A of Agenda Item 2.3.1.
	6. Carry out a separate analysis on the use of 'item' in the description of a resource in paragraph 5.7 and consider the adoption of an approach wholly focused on rights, drawing on analysis in the IASB 2018 Framework.	6. Agenda Item 2.2.1. Paragraph 7 in Agenda Item 2.3.1.
	7. Review consistency and appropriate use of terminology, in particular the use of 'present obligations', 'obligations', 'items' and 'rights'.	7. Paragraphs 5.26A-5.26I discussed in Agenda Item 2.2.3 and Agenda Item 2.3.2.
	8. Ensure that the difference between 'unit of account' and 'offsetting' is clearly explained.	8. Agenda Item 2.2.3. Additional wording added to new paragraph 5.26I in Agenda Item 2.3.2.
	9. Review paragraph 5.26D (a) (iii) and 5.26 (a) (iv) to ensure that they fit the public sector context.	9. Agenda Item 2.2.3. Modifications to wording of paragraphs 5.26D (a) (iii) and 5.26D (a) (iv).
	10. Remove paragraph 5.26E discussing QCs other than relevance and faithful representation and add a paragraph to the BCs.	10. Agenda Item 2.2.3 and Agenda Item 2.3.2. Paragraph 5.26E deleted and paragraph BC5.36C inserted.

Agenda Item 6.1.2

	11. Replace the term 'binding arrangement' with a more neutral term such as 'arrangement'.	11. Agenda Item 2.2.1 and Agenda Item 2.3.2. Term 'arrangement' generally adopted. In paragraph 5.26G term 'binding arrangement is used'.
	12. Consider deletion of paragraph 5.26I listing possible units of account.	12. Agenda Item 2.2.3 and Agenda Item 2.3.2. Paragraph 5.26I deleted.
	13. Consider the extent to which the relevant circumstances of executory contracts are, or can be, reflected in the Unit of Account section prior to a decision on whether to include a section on Executory Contracts.	13. Agenda Item 2.2.2 and new paragraph 5.26G of Agenda item 2.3.2.
	14. Ensure that the change from 'capacity to provide services' to 'capability to provide services' is explained appropriately in BCs.	14. Paragraphs 5.7 and 5.8 in Agenda Item 2.3.2. Paragraph BC
	15. Update the first sentence of paragraph 5.7 to reflect that a resource may have both service potential and the capability to generate economic benefits.	15. Paragraph 5.7 in Agenda Item 2.3.2.
	16. Update the first sentence of paragraph 5.8 to link 'service potential' to 'a resource'.	16. Paragraph 5.8 in Agenda Item 2.3.2.
	17. Acknowledge that in the context of a principal-agent relationship an obligation to transfer to a third party a resource controlled by a principal, that obligation is not a liability of the agent.	17. Paragraph 5.15A added in Agenda Item 2.3.2.
	18. Consider the potential implications of: (a) Adopting the definition: (i) A present obligation of the entity for a to transfer resources that results from a as <u>a result of</u> past events.	18. Agreed at September 21 meeting. Paragraph 5.14 of Agenda Item 2.3.2.

Agenda Item 6.1.2

	19. Consider the implications of clarifying or shortening the reference to 'through fulfillment of an obligation or because of non-fulfillment of that obligation' in the context of no realistic alternative to avoid a transfer of resources in paragraph 5.15.	19. The references have been deleted in paragraph 5.15 of Agenda Item 2.3.2.
	20. Consider the implications of specifically linking 'taking an action' to 'a non-legally binding obligation' in paragraph 5.17A and, dependent on this analysis, the clarity of paragraph 5.17A(b).	20. Link has been deleted and 'taken an action' transferred to paragraph 5.17(a) in Agenda Item 2.3.2.
June 2021	1. Consider further the description of 'service potential' in paragraph 5.8 of the IPSASB Conceptual Framework in the context of the development of proposals on whether to amend the definition of an asset, especially whether to replace the word 'capacity' with an alternative word other than 'ability' e.g., 'capability'	1. Agenda Item 3.2.5, paragraphs 5.7, 5.8 and BC5.8A in Agenda Item 3.3.2, Revised Chapter 5, Elements.
	2. On prudence, starting from the drafting in the IASB Conceptual Framework, consider the need for changes due to the public sector context, drawing on suggestions from Board members.	2. Agenda Item 3.2.2, paragraphs 14A, 3.14B, BC3.17A-3.17E in Agenda Item 3.3.1, Revised Chapter 3, <i>Qualitative Characteristics</i> .
	3. Develop a further sentence on materiality by nature rather than amount (qualitative materiality).	3. Agenda Item 3.2.1, paragraph 3.32 in Agenda Item 3.3.1
	4. In the context of the discussion of regularity in the Basis for Conclusions, ensure that the respective responsibilities of preparers and auditors are appropriately identified.	4. Agenda Item 3.2.2, paragraph BC 3.32D in Agenda Item 3.3.1
March 2021	N/A	N/A
February 2021	1. All instructions provided up until February are reflected in the ED 76, Conceptual Framework Chapter 7, Measurement: Update	1. All instructions provided up until February are reflected in the ED 76, Conceptual Framework Chapter 7, Measurement: Update

DECISIONS UP TO PREVIOUS MEETING

Meeting	Decision	BC Reference
Conceptual Framework–Limited-Scope Update–First Stage		
October 2021	1. A rights-based focus should be adopted for the description of a resource.	1. Agenda Items 6.2.1 and 6.3.1' BC5.3A-BC5.3E
	2. Guidance on executory contract accounting principles should be included in the section on Unit of Account, rather than in a separate section.	2. Agenda Items 6.2.2 and 6.3.1 BC 5.36F
	1. Obscuring information' should be added to the factors influencing materiality.	1. Paragraph 3.32 in Agenda Item 2.3.1.
	2. The threshold for determining whether information is material should be softened.	2. Paragraph 3.32A in Agenda Item 2.3.1.
	3. Additional paragraphs 3.14A and 3.14B should be adopted.	3. Included in Agenda Item 2.3.1.
	4. A section on Unit of Account in a proposed revised Chapter 5 should be included.	4. Paragraphs 5.26A 5.26I in Agenda Item 2.3.2.
	5. The change from 'capacity to provide services' to 'capability to provide services' in paragraph 5.8 and conforming changes to 5.7 and 5.8 should be adopted.	5. Agenda Item 2.3.2.
	6. The revised definition of an asset should be: ○ <i>A resource presently controlled by the entity as a result of past events (<u>plural rather than singular as in current definition</u>).</i>	6. Paragraph 5.6 in Agenda Item 2.3.2.
	7. Additional guidance was necessary for: ○ The immediate receipt and consumption of a resource. ○ The use of a resource to extinguish or reduce a liability. ○ The principal-agent relationship.	7. Guidance provided in: ○ Paragraph 5.9A in Agenda Item 2.3.2; ○ Paragraph 5.7 in Agenda Item 2.3.2; and ○ Paragraph 5.12A in Agenda Item 2.3.2.
	8. Subject to consideration of any potential adverse impacts, the phrase 'as a result of past events' as part of a revised definition of a liability should be used. ○ <i>A present obligation of the entity for a to transfer resources that results from a as a result of past events.</i>	8. Agreed that no adverse impact at September 21 meeting. Paragraph 5.14 of Agenda Item 2.3.2.

Agenda Item 6.1.3

	9. Guidance on the transfer of resources in paragraphs 5.16A-5.16E should be included.	9. Agreed. Paragraphs 5.16A-5.16E of Agenda Item 2.3.2.
	10. The term 'transfer revenue' in the draft IPSAS under development from ED 71, <i>Revenue from Transactions without Performance Obligations</i> , should be adopted to remove the potential for confusion with the proposed use of 'transfers' in the Conceptual Framework, unless and until superior alternative term is identified.	10. To be taken forward in development of an IPSAS from ED 71
June 2021	1. Agreed to address prudence as a reinforcement of neutrality in the context of the qualitative characteristic (QC) of faithful representation, rather than adopting it as a separate QC.	1. Paragraphs 3.14A and 3.14B in Agenda Item 3.2.1
	2. Agreed to amend the description of materiality in paragraph 3.32 of the IPSASB Conceptual Framework to reflect the amendments to the IASB Conceptual Framework in late 2018.	2. Agenda Item 3.2.1 and paragraphs 3.32, BC3.32A and BC3.32B of Agenda Item 3.3.1
March 2021	1. Group the topics in the next stage of the Limited Scope Update according to whether then relate to Chapters 3 and 5 of the Conceptual Framework.	1. Topics grouped in accordance with March Agenda Paper 8.2.1 . Paragraphs BC3.17A-BC3.17C, BBC3.32A-BC3.32B, and BC5.2A and 5.2B provide rationale.
	2. Consider service potential in addition to the issues originally identified in the project brief approved in March 2020.	2. Item 3.2.5 considers service potential. Paragraphs 5.7 and 5.8 amended, Paragraph BC 5.8A provides rationale.
	3. Further work on capital maintenance and concepts of capital should be taken forward separately on a longer timeframe.	3. BC paragraph will be added to Chapter 7, <i>Measurement</i> , in development of final chapter from ED 76.
February 2021	1. All decisions provided up until February are reflected in the ED 76, Conceptual Framework Chapter 7, Measurement: Update.	1. All decisions provided up until February are reflected in the ED 76, Conceptual Framework Chapter 7, Measurement: Update.

Guidance on Rights in Context of a Resource

1. Does the IPSASB agree with the recommendations in paragraph 2 to action Board instructions at the October 2021 meeting?

Recommendations

2. The Board Sponsor and staff recommend that the IPSASB Framework adopt the revised section on 'Rights' in paragraphs 5.7A-5.7G of ED 81, *Conceptual Framework Update: Chapter 3, Qualitative Characteristics* and Chapter 5, *Elements* at Agenda Item 6.3.1.

Background

3. At the September meeting the IPSASB agreed to adopt a rights-based approach to a resource. At the October meeting Members reviewed an initial section on 'A Resource', which included two paragraphs drawn from the IASB 2018 Framework. Members instructed staff to work with Members and liaise with staff of the Australian Accounting Standards Board over (i) drafting changes to paragraphs 5.7 and 5.8 of the IPSASB Framework, and (ii) the extent to which further material from paragraphs 4.6-4.13 of the IASB 2018 Conceptual Framework should be included in a new section, *Rights*.

Analysis

4. In accordance with the instruction at the October meeting staff has further reviewed paragraphs 4.6-4.13 in the section, *Right*, of the IASB's 2018 Framework. Staff of the Australian Accounting Standards Board and the New Zealand External Reporting Board have provided detailed comments and have provided the template and some of the material for the table below paragraph 8. Staff is very grateful for this support.
5. Material drawn from six of these paragraphs have been included as paragraphs 5.7A-5.7F in the revised Chapter 5, *Elements*. Material from paragraphs 4.10 and paragraphs 4.13 has not been included, as it is considered unnecessary. Paragraph 4.10 discusses debt and equity instruments, which are not common in the public sector, and paragraph 4.13 discusses recognition, which is considered in Chapter 6, *Recognition*, of the IPSASB Framework.
6. Paragraph 5.7G has been added to cross-refer to the discussion of 'sovereign rights' in paragraph 5.13 in accordance with an instruction at the October meeting.
7. Staff circulated the revised section out of session on November 15th. Changes from that circulated version are shown in [Appendix A](#) in red with an accompanying explanation.
8. The table below details the paragraphs in the section, *Right*, in the IASB 2018 Framework and indicates whether, and if so, how these paragraphs have been included in the IPSASB Framework.

IASB 2018 Framework paragraph on Right	IPSASB Equivalent Paragraph	Notes
<p><u>Paragraph 4.6 – types of rights</u></p> <p>Rights that have the potential to produce economic benefits take many forms, including:</p> <p>(a) rights that correspond to an obligation of another party [...], for example:</p> <ul style="list-style-type: none"> (i) rights to receive cash. (ii) rights to receive goods or services. (iii) rights to exchange economic resources with another party on favourable terms. Such rights include, for example, a forward contract [...]. (iv) rights to benefit from an obligation of another party to transfer an economic resource if a specified uncertain future event occurs [...]. <p>(b) rights that do not correspond to an obligation of another party, for example:</p> <ul style="list-style-type: none"> (i) rights over physical objects, such as property, plant and equipment or inventories. Examples of such rights are a right to use a physical object or a right to benefit from the residual value of a leased object. (ii) rights to use intellectual property. 	<p><u>5.7A Rights to service potential or the capability to generate economic benefits take many forms, including:</u></p> <p><u>(a) Rights that correspond to an obligation of another party (see paragraph 5.16C), for example:</u></p> <ul style="list-style-type: none"> <u>(i) Rights to receive cash.</u> <u>(ii) Rights to receive services</u> <u>(iii) Rights to exchange resources with another party on favorable terms. Such rights include, for example, a forward contract to buy a resource on terms that are favorable.</u> <u>(iv) Rights to benefit from an obligation of another party to transfer a resource if a specified uncertain future event occurs (see paragraph 5.16A).</u> <p><u>(b) Rights that do not correspond to an obligation of another party, for example:</u></p> <ul style="list-style-type: none"> <u>(i) Rights over physical objects, such as property, plant and equipment or inventories. Examples of such rights are a right to use a physical object or right to benefit from a leased object; and,</u> <u>(ii) Rights to use intellectual property</u> 	<p>Includes references to service potential.</p>

Agenda Item 6.2.1

IASB 2018 Framework paragraph on Right	IPSASB Equivalent Paragraph	Notes
<p><u>Paragraph 4.7 – how rights are established</u></p> <p>Many rights are established by contract, legislation or similar means. For example, an entity might obtain rights from owning or leasing a physical object, from owning a debt instrument or an equity instrument, or from owning a registered patent. However, an entity might also obtain rights in other ways, for example:</p> <p>(a) by acquiring or creating know-how that is not in the public domain [...]; or</p> <p>(b) through an obligation of another party that arises because that other party has no practical ability to act in a manner inconsistent with its customary practices, published policies or specific statements [...]</p>	<p><u>5.7B Many rights are established by binding arrangement, legislation, or similar means. For example, an entity might obtain rights from owning or leasing a physical object, from owning a debt instrument such as a student loan, or from owning software or the right to use intellectual property. However, an entity might also obtain rights in other ways, for example:</u></p> <p><u>(a) By acquiring or creating know-how that is not in the public domain, such as a traffic management plan, or:</u></p> <p><u>(b) Through an obligation of another party that arises because that other party has no realistic alternative to avoid a transfer of resources (see paragraph 5.15).</u></p>	<p>'Binding arrangements' used rather than 'contracts'.</p> <p>'Example of traffic management plan' added in paragraph 5.7B(a).</p>
<p><u>Paragraph 4.8: immediate consumption of goods and services</u></p> <p>Some goods or services—for example, employee services—are received and immediately consumed. An entity's right to obtain the economic benefits produced by such goods or services exists momentarily until the entity consumes the goods or services.</p>	<p><u>5.7C Some goods and services—for example, employee services and services-in-kind—are received and immediately consumed. An entity's right to the service potential or economic benefits produced by such goods and services exists very briefly until the entity consumes the goods and services.</u></p>	<p>Included-previously agreed at September meeting. Paragraph number changed.</p> <p>Example of services-in-kind included as well as employee services.</p> <p>Service potential added.</p> <p>'Momentarily' replaced by 'very briefly' in accordance with September instruction.</p>

<i>IASB 2018 Framework paragraph on Right</i>	<i>IPSASB Equivalent Paragraph</i>	<i>Notes</i>
<p><u>Paragraph 4.9: not all rights are assets</u></p> <p>Not all of an entity's rights are assets of that entity—to be assets of the entity, the rights must both have the potential to produce for the entity economic benefits beyond the economic benefits available to all other parties [...]and be controlled by the entity [...]. For example, rights available to all parties without significant cost—for instance, rights of access to public goods, such as public rights of way over land, or know-how that is in the public domain—are typically not assets for the entities that hold them.</p>	<p>5.7D <u>Not all of an entity's rights are assets of that entity—to be assets of the entity, the rights must (i) have service potential or economic benefits beyond those available to all other parties (see paragraphs 5.8-5.10) and (ii) be controlled by the entity (see paragraphs 5.11-5.12). For example, rights available to all parties without significant cost—for instance, rights of access to public goods that are controlled by other entities, such as public rights of way over land controlled by other entities, or know-how that is in the public domain—are typically not assets for the entities that hold these rights.</u></p>	<p>Included. Minor drafting changes to emphasize the importance of control.</p>
<p><u>Paragraph 4.10: entity can't have right to obtain benefits from itself</u></p> <p>An entity cannot have a right to obtain economic benefits from itself. Hence:</p> <p>(a) debt instruments or equity instruments issued by the entity and repurchased and held by it—for example, treasury shares—are not economic resources of that entity; and</p> <p>(b) if a reporting entity comprises more than one legal entity, debt instruments or equity instruments issued by one of those legal entities and held by another of those legal entities are not economic resources of the reporting entity.</p>	<p>No equivalent</p>	<p>Judged to be unnecessary. This paragraph focuses on debt and equity instruments issued by the entity and either repurchased by the entity or held by an entity within the consolidated group – which are unlikely to be common in the public sector.</p>

Agenda Item 6.2.1

IASB 2018 Framework paragraph on Right	IPSASB Equivalent Paragraph	Notes
<p><u>Paragraph 4.11: rights are separate assets but may be treated as single asset</u></p> <p>In principle, each of an entity's rights is a separate asset. However, for accounting purposes, related rights are often treated as a single unit of account that is a single asset [...]. For example, legal ownership of a physical object may give rise to several rights, including:</p> <p>(a) the right to use the object; (b) the right to sell rights over the object; (c) the right to pledge rights over the object; and (d) other rights not listed in (a)–(c).</p>	<p><u>5.7E In principle, each of an entity's rights is a separate asset. However, for accounting purposes, related rights are often treated as a single unit of account that is a single asset (see paragraphs 5.26A–5.26I). For example, legal ownership of a physical object may give rise to several rights, including a right to:</u></p> <p><u>(a) Use the object;</u> <u>(b) Sell rights over the object; and</u> <u>(c) Pledge rights over the object.</u></p>	<p>Included. Necessary as a lead-in to paragraph 5.7F. Minor drafting changes. Point (d) in IASB paragraph considered unnecessary.</p>
<p><u>Paragraph 4.12: legal ownership rights accounted for as single asset</u></p> <p>In many cases, the set of rights arising from legal ownership of a physical object is accounted for as a single asset. Conceptually, the economic resource is the set of rights, not the physical object. Nevertheless, describing the set of rights as the physical object will often provide a faithful representation of those rights in the most concise and understandable way.</p>	<p><u>5.7F In many cases, the set of rights arising from legal ownership of a physical item is accounted for as a single asset. Conceptually, the resource is the set of rights, not the physical item. Nevertheless, describing the set of rights as the physical item will often provide a faithful representation of those rights in the most concise and understandable way.</u></p>	<p>Previously included in September version. Paragraph number changed. Minor drafting changes.</p>

<i>IASB 2018 Framework paragraph on Right</i>	<i>IPSASB Equivalent Paragraph</i>	<i>Notes</i>
<p><u>Paragraph 4.13: uncertainty over the existence of rights</u></p> <p>In some cases, it is uncertain whether a right exists. For example, an entity and another party might dispute whether the entity has a right to receive an economic resource from that other party. Until that existence uncertainty is resolved—for example, by a court ruling—it is uncertain whether the entity has a right and, consequently, whether an asset exists. (Paragraph 5.14 discusses recognition of assets whose existence is uncertain.)</p>	No equivalent.	<p>Judged unnecessary. Deals with existence uncertainty, which is addressed in Chapter 6, <i>Recognition</i>. Existence uncertainty is not in scope of Limited Scope Update.</p>

Way Forward

- Board Sponsor and Staff consider that the revised approach improves the guidance in the Rights section of Chapter 5 and explains the resource component in the asset definition.

Decision Required

- Does the IPSASB agree with the Board Sponsor and staff recommendation in paragraph 2?

GUIDANCE ON A RESOURCE AND RIGHTS

<p><i>'To obtain' deleted following member comment</i></p> <p><i>Minor change-tail 'or both' more appropriate' in paragraph 5.6A</i></p> <p><i>Lower case in paragraph 5.6B</i></p>	<p>Assets</p> <p>Definition</p> <p>5.6 An asset is:</p> <p style="padding-left: 40px;"><i>A resource presently controlled by the entity as a result of a past events.</i></p> <p>Resource</p> <p>5.6A A resource is a right to obtain service potential or the capability to generate economic benefits, or both.</p> <p>5.6B <u>This section discusses three components of this definition:</u></p> <p><u>(a) Rights (paragraphs 5.7-5.7F)</u></p> <p><u>(b) Service Ppotential and Eeconomic Bbenefits (paragraphs (5.8-5.10)</u></p> <p><u>(c) Present Ccontrol as a Rresult of Ppast Eevents (paragraph 5.11-5.13)</u></p> <p>5.1. A resource is a right to an item with service potential or the ability capability to generate economic benefits or both. Physical form is not a necessary condition of a resource. The service potential or capability ability to generate economic benefits can arise directly from the resource itself or arises from the rights to use the resource. Some resources embody an entity's rights to a variety of benefits including, for example, the right to:</p> <ul style="list-style-type: none"> • Use the resource to provide services¹; • Use an external party's resources to provide services, for example, leases; • Convert the resource into cash through its disposal; • Benefit from the resource's appreciation in value; or • Receive a stream of cash flows; or • Extinguish or reduce a liability by transferring the resource. 	<p><i>Framework Chapter 5 with amendments</i></p>
---	--	---

¹ References to "services" in the Conceptual Framework encompass "goods".

<p><i>'obtain' deleted</i></p> <p><i>'or both' deleted and moved to paragraph 5.6A</i></p> <p><i>'currently' added</i></p> <p><i>Editorials</i></p>	<p>Rights</p> <p>5.7A <u>Rights to obtain service potential or the capability to generate economic benefits, or both, take many forms, including:</u></p> <p><u>(a) Rights that correspond to an obligation of another party (see paragraph 5.16C), for example:</u></p> <p><u>(i) Rights to receive cash.</u></p> <p><u>(ii) Rights to receive service</u></p> <p><u>(iii) Rights to exchange resources with another party on favorable terms. Such rights include, for example, a forward contract to buy a resource on terms that are currently favorable.</u></p> <p><u>(iv) Rights to benefit from an obligation of another party to transfer a resource if a specified uncertain future event occurs (see paragraph 5.16A).</u></p> <p><u>(b) Rights that do not correspond to an obligation of another party, for example:</u></p> <p><u>(i) Rights over physical objects, such as property, plant and equipment or inventories. Examples of such rights are a right to use a physical object or right to benefit from a leased object; and,</u></p> <p><u>(iii) Rights to use intellectual property</u></p> <p>5.7B <u>Many rights are established by binding arrangement, legislation, or similar means. For example, an entity might obtain rights from owning or leasing a physical object, from owning a debt instrument such as a student loan, or from owning software or the right to use intellectual property . However, an entity might also obtain rights in other ways, for example:</u></p> <p><u>(a) By acquiring or creating know-how that is not in the public domain, such as a traffic management plan, or:</u></p> <p><u>(b) Through an obligation of another party that arises because that other party has no realistic alternative to avoid a transfer of resources (see paragraph 5.15).</u></p> <p>5.7C <u>Some goods and services—for example, employee services and services-in-kind—are received and immediately consumed. An entity's capability to obtain the service potential or economic benefits produced by such goods and services exists very briefly until the entity consumes the goods and services.</u></p>	<p>IASB 2018 Framework</p>
---	--	----------------------------

<p><i>Drafting changes.</i></p>	<p>5.7D <u>Not all of an entity's rights are assets of that entity—to be assets of the entity, the rights must both have (i) have service potential the potential for the entity to obtain services or economic benefits beyond those the services or economic benefits available to all other parties (see paragraphs 5.8-5.10) and (ii) be controlled by the entity (see paragraphs 5.11-5.12). and to be controlled by the entity (see paragraphs 5.11-5.12). For example, rights available to all parties without significant cost—for instance, rights of access to public goods held by other entities, such as public rights of way over land held by other entities, or know-how that is in the public domain—are typically not assets for the entities that hold these rights. them.</u></p>	
	<p>5.7E <u>In principle, each of an entity's rights is a separate asset. However, for accounting purposes, related rights are often treated as a single unit of account that is a single asset (see paragraphs 5.26A–5.26I). For example, legal ownership of a physical object may give rise to several rights, including a right to:</u></p> <ul style="list-style-type: none"> (a) <u>Use the object;</u> (b) <u>Sell rights over the object; and</u> (c) <u>Pledge rights over the object.</u> 	
	<p>5.7F <u>In many cases, the set of rights arising from legal ownership of a physical item is accounted for as a single asset. Conceptually, the resource is the set of rights, not the physical item. Nevertheless, describing the set of rights as the physical item will often provide a faithful representation of those rights in the most concise and understandable way.</u></p>	
<p><i>Added in accordance with October instruction.</i></p>	<p><u>5.7G The relationship between sovereign rights, resources and an asset is discussed in paragraph 5.13.</u></p> <p>Service Potential and Economic Benefits</p>	<p><i>Framework Chapter 5 with amendments</i></p>
	<p>5.8 Service potential is the capacity <u>capability</u> of a resource to provide services that contribute to achieving the entity's objectives. Service potential enables an entity to achieve its objectives without necessarily generating cash flows.</p>	

	<p>5.9 Public sector assets that embody service potential may include recreational, heritage, community, defense and other assets which that are held by governments and other public sector entities, and which are used to provide services to third parties. Such services may be for collective or individual consumption. Many services may be provided in areas in which market competition is limited or non-existent. where there is no market competition or limited market competition. The use and disposal of such assets may be restricted as many assets that embody service potential are specialized in nature.</p>	
	<p>5.9A <u>Some goods and services—for example, employee services and services-in-kind—are received and immediately consumed. An entity's capability to obtain the service potential or economic benefits produced by such goods and services exists momentarily briefly until the entity consumes the goods and services.</u> [Deleted]</p>	
<p><i>Added following discussion. Was previously in a version of now-deleted paragraph 5.7.</i></p>	<p>5.10 Economic benefits are cash inflows or a reduction in cash outflows. Cash inflows (or reduced cash outflows) may be derived from, for example:</p> <ul style="list-style-type: none"> • An asset's use in the production and sale of services; or • The direct exchange of an asset for cash. or other resources; or • <u>Extinguishing or reducing a liability by transferring the asset.</u> 	
<p><i>Change in title to reflect component of definition</i></p>	<p><u>Presently Controlled by the Entity As A Result of Past Events</u></p> <p>5.11 An entity must have control of the resource. Control of the resource entails the ability of the entity to use the resource (or direct other parties on its use) so as to derive the benefit of the service potential or economic benefits embodied in the resource in the achievement of its service delivery or other objectives.</p>	<p>Framework Chapter 5</p>

Agenda Item 6.2.1

	<p>5.12 In assessing whether it presently controls a resource, an entity assesses whether the following indicators of control exist:</p> <ul style="list-style-type: none"> • Legal ownership; • Access to the resource, or the ability to deny or restrict access to the resource; • The means to ensure that the resource is used to achieve its objectives; and • The existence of an enforceable right to service potential or the <u>capability</u> to generate economic benefits arising from a resource. <p>While these indicators are not conclusive determinants of whether control exists, identification and analysis of them can inform that decision.</p>	<p><i>Framework Chapter 5</i></p>
	<p><u>5.12A Sometimes one party (a principal) engages another party (an agent) to act on behalf of, and for the benefit of, the principal. For example, a principal may engage an agent to arrange the provision of services distribute goods controlled by the principal to eligible beneficiaries. If an agent has custody of a resource controlled by the principal, that resource is not an asset of the agent.</u></p>	<p><i>IASB 2018 Framework</i></p>

<p><i>Minor changes due to revised definition of an asset</i></p>	<p><u>Past Events</u></p> <p>5.13 The definition of an asset requires that a resource that an entity presently controls must have arisen from a one or more <u>past transactions</u> or other past events. The past transactions or other events that result in an entity gaining control of a resource and therefore an asset may differ. Entities can obtain assets by purchasing them in an exchange transaction or developing them. Assets may also arise through non-exchange transactions, including through the exercising of sovereign powers. The power to tax or to issue licenses and to access or restrict or deny access to the benefits embodied in intangible resources, like the electromagnetic spectrum, are examples of public sector-specific powers and rights that may give rise to assets. In assessing when an entity's control of rights to resources arise the following events may be considered: (a) a general ability to establish a power, (b) establishment of a power through a statute, (c) exercising the power to create a right, and (d) the event which gives rise to the right to receive resources from an external party. An asset arises when the power is exercised and the rights exist to receive resources.</p>	<p><i>Framework Chapter 5</i></p>
---	--	-----------------------------------

Basis for Conclusions Sections

	<p><u>BC5.2I The revised definition of an asset is therefore:</u></p> <p><u><i>A resource presently controlled by the entity as a result of past events.</i></u></p>	
	<p><u>BC 5.2J In the Limited Scope Update the IPSASB reviewed the sequencing of guidance and reconfigured the guidance so that it reflected the components of the definition of a liability more clearly.</u></p>	

	<p><i>A Resource</i></p> <p>BC 5.3 The 2014 Framework provided guidance that ‘a resource provides benefits to an entity in the form of service potential or the <u>capability ability to generate economic benefits or both</u>. In reaching its conclusions on the nature of a resource the IPSASB considered whether the benefits of the resource must have already flowed to an entity in order for a resource to exist. However, the IPSASB concluded that resources themselves embody benefits—benefits that can be accessed by the entity that controls the rights to these benefits. The IPSASB also considered the nature of the benefits (see paragraphs BC5.7 and BC5.8) and control (see paragraphs BC5.9–BC5.14).</p>	<p><i>Framework Chapter 5</i></p>
	<p><u>BC5.3A The IPSASB 2014 Framework distinguished service potential and the capability to generate economic benefits that can arise directly from the resource itself from service potential and the capability to generate economic benefits that arise from the rights to use the resource.</u></p>	
	<p><u>BC 5.3B The IASB 2018 Framework considered but decided not to make the distinction outlined in paragraph BC5.3A. The IASB took the view that ‘ownership of a physical object arises because of rights conferred by law and that, although they differ in extent, the rights conferred by full legal ownership of a physical object and by a contract to use an object for 99% (or 50% or even 1%) of its useful life are all rights of one kind or another.’ The IASB also considered that there may be inconsistencies of what constitutes legal ownership in different jurisdictions or at different dates. In summary, the IASB guidance reflects a view that legal ownership is a particular form of right rather than a separate phenomenon.</u></p>	
	<p><u>BC5.3C The Board IPSASB acknowledged the view that physical ownership gives rise to a specific type of control and that this should be reflected conceptually, and that, from an accountability perspective, a conceptual approach which might lead to underlying assets not being recognized risks not meeting the qualitative characteristic of understandability.</u></p>	

	<u>BC5.3D However, on balance the Board IPSASB decided to adopt a more overtly rights-based approach. In particular the IPSASB Board found the view that legal ownership is a type of right rather than a separate phenomenon persuasive.</u>	
<i>New paragraph.</i>	<u>BC5.3E The IASB 2018 Framework acknowledged that in many cases the set of rights arising from legal ownership of a physical object is accounted for as a single asset. The IPSASB inserted paragraph 5.8A7F providing guidance that describing the set of rights as the physical item will often provide a faithful representation of those rights in the most concise and understandable way.</u>	
	<p><u>BC5.3AFThe IPSASB considered whether it should augment the guidance on a resource with guidance drawn from the IASB 2018 Framework. The IPSASB decided that the following guidance should be added on issues on which the IPSASB 2014 Framework had previously been silent:</u></p> <ul style="list-style-type: none"> • <u>Rights can be classified as those that correspond to an obligation of another party and those that do not correspond to an obligation of another party. (paragraph 5.7A).</u> • <u>Ways in which rights can be established (paragraph 5.7B).</u> • <u>That when goods or services are received and immediately consumed an entity's right to obtain the service potential or/and economic benefits produced by such goods and services exists very briefly-until the entity consumes the goods or services.' This issue had arisen when the IPASB reconsidered the approach to recognition of in-kind services in its Revenue project (paragraph 5.7C).</u> • <u>Noting that not all rights are assets of an entity (paragraph 5.7D).</u> • <u>In principle each of an entity's rights is a separate asset (paragraph 5.7E).</u> • <u>In many cases the set of rights arising from legal ownership of a physical object is accounted for as a single asset (paragraph 5.7F).</u> • <u>That an entity can benefit from a resource by using it to extinguish or reduce a liability (added to paragraph 5.7)</u> 	IASB 2018 Framework

Guidance on Unit of Account/ Executory Contracts

Questions

1. Does the IPSASB agree with the recommendation on the approach to unit of account and executory contracts in paragraph 2?

Recommendation

2. Board Sponsor and staff recommend adopting the guidance in the section, *Unit of Account* in paragraphs 5.26A-5.26K of Chapter 5, *Elements*, of ED 81, *Conceptual Framework Update: Chapter 3, Qualitative Characteristics* and Chapter 5, *Elements* at Agenda Item 6.3.1.

Background

3. For the October meeting Staff incorporated material from paragraphs 4.56 and 4.58 of the section on *Executory Contracts* in the IASB's 2018 Framework into the *Unit of Account* section of the IPSASB Framework. Material from paragraph 4.57 was not included.
4. The IPSASB decided to include material on executory contracts in this section, but instructed staff to consider whether material on onerous binding arrangements drawn from paragraph 4.57 of the IASB 2018 Framework should also be included. Members also agreed to include a Specific Matter for Comment on whether the Framework should include a separate section on Executory Contracts/Executory Binding Arrangements. Those who favor a separate section consider that the IASB section on Executory Contracts is not just confined to unit of account issues but also addresses the point at which an asset or a liability arises under a binding arrangement.
5. Members also made a number of further instructions which are detailed in Agenda Item 6.1.2.
6. Staff circulated the revised section out of session on November 15th. Changes from that circulated version are shown in [Appendix A](#) in red with an accompanying explanation also in red.

Analysis

7. The table below shows the three paragraphs in the IASB 2018 Framework (4.56-4.58) in the section *Executory Contracts* and indicates whether, and how, that material has been imported into the IPSASB Framework.

Agenda Item 6.2.2

IASB 2018 Framework	Proposed New Text in Paragraphs 5.26G-5.26I of IPSASB Framework	Rationale for importation into IPSASB Framework
<p>4.56. An executory contract is a contract, or a portion of a contract, that is equally unperformed—neither party has fulfilled any of its obligations, or both parties have partially fulfilled their obligations to an equal extent.</p>	<p>5.26G Some binding arrangements, or portions of binding arrangements, may be equally unperformed—neither party has fulfilled any of its obligations or both parties have partially fulfilled their obligations to an equal extent.</p>	<p>Term ‘executory contract’ replaced by ‘binding arrangement’</p>
<p>4.57 An executory contract establishes a combined right and obligation to exchange economic resources. The right and obligation are interdependent and cannot be separated. Hence, the combined right and obligation constitute a single asset or liability. The entity has an asset if the terms of the exchange are currently favourable; it has a liability if the term of the exchange are currently unfavourable. Whether such an asset or liability is included in the financial statements depends on both the recognition criteria (see Chapter 5) and the measurement basis (see Chapter 6) selected for the asset or liability, including, if applicable, any test for whether the contract is onerous</p>	<p>5.26H The binding arrangements referred to in paragraph 5.26G establish a combined right and obligation to exchange resources. The right and obligation are interdependent and cannot be separated. Hence the combined right and obligation constitute a single asset or liability. The entity has an asset if the terms of the exchange are currently favorable; it has a liability if the term of the exchange are currently unfavorable. Whether such an asset is included in the financial statements depends on both the recognition criteria (see Chapter 6) and the measurement basis selected for the asset and liability (see Chapter 7).</p>	<p>Material from IASB Framework is now imported into paragraph 5.26H. Final clause on testing for onerous contracts has not been included as Board Sponsor and staff consider this is a standards-level issue.</p>

IASB 2018 Framework	Proposed New Text in Paragraphs 5.26G-5.26I of IPSASB Framework	Rationale for importation into IPSASB Framework
<p>4.58 To the extent that either party fulfils its obligations under the contract, the contract is no longer executory. If the reporting entity performs first under the contract, that performance is the event that changes the reporting entity's right and obligation to exchange economic resources into a right to receive an economic resource. That right is an asset. If the other party performs first, that performance is the event that changes the reporting entity's right and obligation to exchange economic resources into an obligation to transfer an economic resource. That obligation is a liability.</p>	<p>5.26I To the extent that either party fulfils its obligations under the binding arrangement, the binding arrangement changes character. If the reporting entity performs first under the binding arrangement that performance is the event that changes the reporting entity's right and obligation to exchange resources into a right to receive a resource. That right is an asset. If the other party performs first, that performance is the event that changes the reporting entity's right and obligation to exchange resources into an obligation to transfer a resource. That obligation is a liability.</p>	<p>As above, term 'executory' not used. First sentence actions October instruction, but has been drafted differently, because 'executory' not used.. Remainder of paragraph 4.58 has been imported with minor terminology change— 'contract'— replaced by 'binding arrangement'.</p>

8. Board Sponsor and Staff consider that the approach to unit of account and executory contracts is appropriate for the entities for which the IPSASB is developing standards and that it reflects public sector circumstances.

Decision Required

9. Does the IPSASB agree with the Board Sponsor and staff recommendation in paragraph 2?

UNIT OF ACCOUNT SECTIONS INCORPORATING EXECUTORY CONTRACT PRINCIPLES

Agreed to insert section at September 2021 meeting.	Assets and Liabilities Unit of Account	
Drawn from IASB 2018 Framework paragraph 4.48.	<u>5.26A The unit of account is the right or the group of rights, the obligation or the group of obligations, or the group of rights and obligations to which recognition criteria and measurement concepts are applied.</u>	IASB 2018 Framework
Drawn from IASB 2018 Framework paragraph 4.49.	<u>5.26B A unit of account is selected for an asset or liability when considering how recognition criteria and measurement concepts will apply to that asset or liability and to the related revenue and expense. In some circumstances it may be appropriate to select one unit of account for recognition and a different unit of account for measurement. For example, arrangements may sometimes be recognized individually but measured as part of a portfolio of binding arrangements. For presentation and disclosure, assets, liabilities, revenue and expense may need to be aggregated or separated into components.</u>	IASB 2018 Framework
Drawn from IASB 2018 Framework paragraph 4.50. 'and the retained component' inserted in accordance with October instruction reflecting IASB 2018 Framework wording.	<u>5.26C If an entity transfers part of an asset or part of a liability, the unit of account may change at that time, so that the transferred component, and the retained component, become separate units of account.</u>	IASB 2018 Framework

<p>Drawn from IASB 2018 Framework paragraph 4.51.</p> <p>Following October meeting:</p> <ul style="list-style-type: none"> • 'for example' added in paragraph 5.26(a). • paragraph 5.26D(a)(iii) shortened. • Interdependent moved in 5.26D (a) (iv) 	<p><u>5.26D A unit of account is selected to provide useful information, which implies that:</u></p> <p>(a) <u>The information provided about the asset or liability and about any related revenue and expense must be relevant. Treating a group of rights and obligations as a single unit of account may provide more relevant information than treating each item, each right or obligation as a separate unit of account if, for example, those rights and obligations:</u></p> <p>(i) <u>Cannot be or are unlikely to be the subject of separate transactions;</u></p> <p>(ii) <u>Cannot or are unlikely to expire in different patterns;</u></p> <p>(iii) <u>Have similar characteristics and risks, and hence are likely to have similar implications for service potential or for the prospects for future net cash inflows to the entity or net cash outflows from the entity.</u></p> <p>(iv) <u>Are used together in the operational activities conducted by an entity to provide service potential or to produce cash flows and are measured by reference to estimates of their interdependent service potential or interdependent future cash flows. I</u></p> <p>(b) <u>Information provided about the asset or liability and about any related revenue or expense must faithfully represent the substance of a transaction or other event from which they have arisen. Therefore, it may be necessary to treat rights or obligations arising from different sources as a single unit of account, or to separate the rights or obligations from a single source. Equally, to provide a faithful representation of unrelated, rights or obligations, it may be necessary to recognize</u> <u>The information provided about the asset or liability and about any related revenue or expense must faithfully represent the substance of a transaction or other event from which they have arisen. Therefore, it may be necessary to treat items, rights</u></p>	<p>IASB 2018 Framework</p>
---	---	----------------------------

Agenda Item 6.2.2

	<p><u>or present obligations arising from different sources as a single unit of account, or to separate the items, rights or present obligations from a single source. Equally to provide a faithful representation of unrelated items, rights or and obligations, it may be necessary to recognize and measure them separately and measure them separately.</u></p>	
<p><i>Drawn from IASB 2018 Framework paragraph 4.52. with drafting changes to align with discussion of cost-benefit constraint in Chapter 3 of IPSASB Framework.</i></p>	<p><u>5.26E In selecting a unit of account it is also important to consider the cost-benefit constraint of financial reporting discussed in Chapter 3. In general, the costs associated with recognizing and measuring assets, liabilities, revenue and expense increase as the size of unit of account decreases. Hence, in general, rights or obligations arising from the same source are separated only if the resulting information is more useful and the benefits outweigh the costs.</u></p>	<p>IASB 2018 Framework</p>
<p><i>Drawn from the first part of IASB 2018 Framework paragraph 4.53.</i></p> <p><i>Term 'executory contracts' changed to 'binding arrangements'.</i></p>	<p><u>5.26F Sometimes, both rights and obligations arise from the same source. For example, some binding arrangements establish both rights and obligations for each of the parties. If those rights and obligations are interdependent and cannot be separated, they constitute a single inseparable asset or liability and hence form a single unit of account.</u></p>	<p>IASB 2018 Framework</p>

<p><i>In accordance with October instruction the section on binding arrangements that are equally unperformed has been redrafted to include more material from paragraphs 4.56-4.58 of the IASB 2018 Framework.</i></p> <p><i>Notably most of paragraph 4.57 has now been included as paragraph 5.26H. Material from paragraph 5.26G has been moved into 5.26I. The inclusion of these additional paragraphs has necessitated a renumbering of paragraphs</i></p>	<p>5.26G An example, is where a <u>Some binding arrangements, or portions of binding arrangements, may be</u> has been entered into <u>equally unperformed</u>—neither party has fulfilled any of its obligations or both parties have partially fulfilled their obligations to an equal extent. Assets and liabilities of the reporting entity arise as either party fulfils its obligations under the binding arrangement. If the reporting entity performs first under the binding arrangement that performance is the event that changes the reporting entity's right and obligation to exchange resources into a right to receive a resource. That right is an asset. If the other party performs first, that performance is the event that changes the reporting entity's right and obligation to exchange resources into an obligation to transfer a resource. That obligation is a liability.</p>	<p>IASB 2018 Framework</p>
<p><i>Inserted following October instruction.</i></p> <p><i>Drawn from paragraph 4.57 of IASB 2018 Framework. But with no reference to 'executory contracts'. or 'onerous contracts'. Onerous contracts is considered a standards-level issue.</i></p> <p><i>Drafting change with cross-reference to paragraph 5.26G</i></p>	<p>5.26H Such <u>The binding arrangements referred to in paragraph 5.26G</u> establish a combined right and obligation to exchange resources. The right and obligation are interdependent and cannot be separated. Hence the combined right and obligation constitute a single asset or liability. The entity has an asset if the terms of the exchange are currently favorable; it has a liability if the term of the exchange are currently unfavorable. Whether such an asset is included in the financial statements depends on both the recognition criteria (see Chapter 6) and the measurement basis selected for the asset and liability (see Chapter 7).</p>	

<p><i>Inserted following October instruction and circulation of material</i></p> <p><i>Drawn from paragraph 4.58 of IASB 2018 Framework.</i></p>	<p>5.26I <u>To the extent that either party fulfills its obligations under the binding arrangement, the binding arrangement changes character.</u> If the reporting entity performs first under the binding arrangement that performance is the event that changes the reporting entity's right and obligation to exchange resources into a right to receive a resource. That right is an asset. If the other party performs first, that performance is the event that changes the reporting entity's right and obligation to exchange resources into an obligation to transfer a resource. That obligation is a liability.</p>	
<p><i>Drawn from the second part of paragraph 4.53 in IASB 2018 Framework. Minor editorial</i></p>	<p>5.26HJ <u>Conversely, if rights are separable from obligations, it may sometimes be appropriate to group the rights separately from the obligations, resulting in the identification of one or more separate assets and liabilities. In other cases, it may be more appropriate to group separable rights and obligations in a single unit of account treating them as a single asset or a single liability.</u></p>	
<p><i>Drawn from IASB 2018 Framework paragraph 4.54.</i></p> <p><i>Additional sentence added drawn from paragraph 7.10 of Chapter 7, Presentation and Disclosure of IASB 2018 Framework</i></p>	<p>5.26HIK <u>Treating a set of rights and present obligations as a single unit of account differs from offsetting assets and liabilities. Offsetting occurs when an entity recognizes and measures both an asset and liability as separate units of account, but groups them into a single net amount in the statement of financial position. Offsetting classifies dissimilar items together and therefore is generally not appropriate.</u></p>	<p><i>IASB 2018 Framework</i></p>

Basis for Conclusions Sections

	<p><u>Unit of Account and Executory Contracts</u></p> <p><u>Unit of Account</u></p> <p>BC 5.36A The IASB 2018 Framework describes unit of account as <u>'the right or the group of rights, the obligation or the group of obligations, or the group of rights and obligations, to which recognition criteria and management concepts apply.'</u></p>	
--	--	--

	<p><u>BC 5.36B The IPSASB took the view that unit of account was a standards-level issue during the development of the 2014 IPSASB Framework and there was no guidance on unit of account. Since 2014 the importance of decisions on the unit of account has been highlighted in a number of projects and led the IPSASB to reevaluate the case for high-level guidance.</u></p>	
<p><i>In accordance with October instruction sentence added that 'the term 'obligation' includes 'present obligations'</i></p> <p><i>Minor drafting change for clarification</i></p>	<p><u>BC5.36C The IPSASB decided that conceptual guidance in the Conceptual Framework would be beneficial in informing standards-level requirements and guidance on unit of account. The IPSASB drew on the IASB 2018 Framework for this guidance, which is in paragraphs 5.26A-5.26I. The term 'obligations' includes 'present obligations'. The guidance on consideration of how the selection of a unit of account provides useful information in the IASB 2018 Framework is in the context of the qualitative characteristics of relevance and faithful representation, because these are the most important qualitative characteristics in evaluating the usefulness of information on unit of account. Other QCs may need to be taken into account in assessing whether information is useful in determining the unit of account.</u></p> <ul style="list-style-type: none"> • Service potential, in addition to net cash flows, has been included as a factor that provides useful information in paragraph 5.26D(a)(iii). 	
	<p><u><i>Executory Contracts</i></u></p> <p><u>BC 5.36D The IPSASB 2014 Framework does not include guidance on executory contracts. The IPSASB evaluated whether guidance should be added to the Framework.</u></p> <p><u>BC5.36E The IASB 2018 Framework describes an executory contract is as 'a contract or a portion of a contract, that is equally unperformed—neither party has fulfilled any of its obligations, or both parties have partially fulfilled their obligations to an equal extent.'</u></p>	

Expanded explanation of why the term 'contract' has been problematic

in some jurisdictions.

'Generally' added as 'executory contracts' is defined in IPSAS 19, Provisions, Contingent Liabilities and Contingent Assets.

BC5.36F The IPSASB noted that the term 'contract' has been problematic in some jurisdictions. This because some public sector entities may not have powers to enter into contracts, although they may be able to enter into other binding arrangements with equivalent effect. Consequently, the term 'contract' ~~and that it~~ has not been used widely in the Conceptual Framework. At the standards level the term 'binding arrangement' has been generally used. The IPSASB concluded that the principles of executory contract accounting could be incorporated in the section on Unit of Account and that a separate section on Executory Contracts is unnecessary. This guidance is in paragraphs 5.26G-5.26I.

Structure of Section on Liabilities

Questions

1. Does the IPSASB agree with the recommendation on the restructuring of the section, *Liabilities*, of Chapter 5, *Elements*?

Recommendation

2. Board Sponsor and staff recommend that the Board adopt the revised and restructured section, *Liabilities*, in paragraphs 5.13-5.17G of ED 81, *Conceptual Framework Update: Chapter 3, Qualitative Characteristics* and Chapter 5, *Elements* at Agenda Item 6.3.1.

Background

3. At the June meeting the IPSASB agreed a revised definition of a liability (superseded text struck out and new text underlined):
A present obligation of the entity for ~~an outflow~~ a transfer of resources that results from a past events.
4. The IPSASB also decided to include guidance on 'A Transfer of Resources', drawn from the IASB 2018 Framework.
5. Board Sponsor and staff have reviewed the structure of the section, *Liabilities*, in draft Chapter 5, *Elements*, in light of that revised definition and the format of the IASB 2018 Framework.

Analysis

6. Board Sponsor and staff have concluded that the section will flow better if restructured and signposted, so that it aligns better with the definition. The section is now divided into the following sections:
 - Obligations (paragraphs 5.15-5.15F)
 - A Transfer of Resources from the Entity (paragraphs 5.16-5.16F)
 - Present Obligations as a Result of Past Events (paragraphs 5.17-5.17D)
7. The revised section is in [Appendix A](#). New text is underlined, deleted text is struck out and relocated text is double underlined.
8. The section on a Transfer of Resources was agreed by the IPSASB at the September 2021 meeting. Material from the 2014 Framework has been relocated; for example, the guidance on legal and non-legally binding obligations previously in paragraphs 5.18-5.26 of the 2014 Framework has been relocated to the Obligations section (previously paragraphs 5.18-5.23) and the section on Present Obligations as a Result of Past Events (previously paragraphs 5.24-5.26).

Way forward

9. Board Sponsor and staff consider that the revised section flows more logically and is more reader friendly.

Decision Required

10. Does the IPSASB agree with the Board Sponsor and staff recommendation in paragraph 2?

REVISED SECTION ON LIABILITIES

Liabilities

Definition

5.14 A liability is:

A present obligation of the entity for ~~an outflow~~ a transfer of resources that results from a past events.

5.14A For a liability to exist three criteria must all be satisfied:

- (a) The entity has an obligation (paragraphs 5.15-5.15F)
- (b) The obligation is to transfer a resource (paragraphs 5.16A-5.16E)
- (c) The obligation is a present obligation arising from ~~a~~ one or more past events (paragraphs 5.17-5.17D)

~~A Present Obligations~~

5.15 Public sector entities can have a number of obligations. Obligations are binding when an entity has little or no realistic alternative to avoid them. A present obligation is a legally binding obligation (legal obligation) or non-legally binding obligation, which an entity has little or no realistic alternative to avoid as a result of past events. ~~Obligations are not present obligations unless they are binding and there is little or no realistic alternative to avoid an outflow of resources.~~

~~Legal and Non-Legally Binding Obligations~~

5.15A Binding obligations can be legal obligations or non-legally binding obligations. Binding obligations can arise from both exchange and non-exchange transactions. An obligation must be to an external party in order to give rise to a liability. An entity cannot be obligated to itself, even where it has publicly communicated an intention to behave in a particular way. Identification of an external party is an indication of the existence of an obligation giving rise to a liability. However, it is not essential to know the identity of the external party before the time of settlement in order for a present obligation and a liability to exist.

5.15B Many arrangements that give rise to an obligation include settlement dates. The inclusion of a settlement date may provide an indication that an obligation involves an outflow ~~a transfer~~ of resources and gives rise to a liability. However, there are many agreements that do not contain settlement dates. The absence of a settlement date does not preclude an obligation giving rise to a liability.

Legal Obligations

5.15C A legal obligation is enforceable in law. Such enforceable obligations may arise from a variety of legal constructs. Exchange transactions are usually contractual in nature and therefore enforceable through the laws of contract or equivalent authority or arrangements. There are jurisdictions where government and public sector entities cannot enter into legal obligations, because, for example, they are not permitted to contract in their own name, but where there are alternative processes with equivalent effect. Obligations that are binding through such alternative processes are considered legal obligations in the Conceptual Framework. For some types of non-exchange transactions, judgment will be necessary to determine whether an obligation is enforceable in law. Where it is determined that an obligation is enforceable in law there can be no doubt that an entity has no realistic alternative to avoid the obligation and that a liability exists.

5.15D Some obligations related to exchange transactions are not strictly enforceable by an external party at the reporting date but will be enforceable with the passage of time without the external party having to meet further conditions— or having to take any further action—prior to settlement. Claims that are unconditionally enforceable subject to the passage of time are enforceable obligations in the context of the definition of a liability.

5.15E Sovereign power is the ultimate authority of a government to make, amend and repeal legal provisions. Sovereign power is not a rationale for concluding that an obligation does not meet the definition of a liability in this Framework. The legal position should be assessed at each reporting date to consider if an obligation is no longer binding and does not meet the definition of a liability.

Non-Legally Binding Obligations

5.15F Liabilities can arise from non-legally binding obligations. Non-legally binding obligations differ from legal obligations in that the party to whom the obligation exists cannot take legal (or equivalent) action to enforce settlement. Non-legally binding obligations that give rise to liabilities have the following attributes:

- The entity has indicated to other parties by an established pattern of past practice, published policies, or a sufficiently specific current statement that it will accept certain responsibilities;
- As a result of such an indication, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities; and
- The entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities.

An Outflow of Resources—A Transfer of Resources from the Entity

~~5.16—A liability must involve an outflow of resources from the entity for it to be settled. An obligation that can be settled without an outflow of resources from the entity is not a liability.~~

- 5.16A To satisfy the definition of a liability the obligation must have the potential to require the entity to transfer a resource to another party (or parties). For that potential to exist, it does not need to be certain, or even likely, that the entity will be required to transfer a resource—the transfer may, for example, be required only if a specified uncertain event occurs. It is only necessary that the present obligation exists, and that, at least in one circumstance, it would require the entity to transfer a resource.
- 5.16B An obligation can meet the definition of a liability even if the probability of a transfer of a resource is low. Nevertheless, that low probability might affect decisions about what information to provide about the liability and how to provide that information. Chapter 6 provides guidance on recognition and Chapter 7 provides guidance on measurement.
- 5.16C Obligations to transfer a resource include, for example:
- (a) Obligations to pay cash.
 - (b) Obligations to provide services or deliver goods.
 - (c) Obligations to exchange resources with another party on unfavorable terms. Such obligations include a forward contract to sell a resource on terms that are currently unfavorable or an option that entitles another party to purchase a resource from the entity.
 - (d) Obligations to transfer a resource if a specified uncertain future event occurs.
 - (e) Obligations to issue a financial instrument if that financial instrument will oblige the entity to transfer a resource.
- 5.16D Instead of fulfilling an obligation to transfer a resource to the party that has a right to receive the resource, entities may in some circumstances:
- (a) Settle the obligation by negotiating a release from the obligation.
 - (b) Transfer the obligation to a third party.
 - (c) Replace the obligation to transfer a resource with another obligation by entering into a new transaction.
- 5.16E In the situations identified in paragraph 5.16D an entity has an obligation to transfer a resource until it has settled, transferred, or replaced that obligation.
- 5.16F In a principal-agent relationship (see paragraph 5.12A), if the agent has an obligation to transfer to a third party a resource controlled by the principal, that obligation is not a liability of the agent. In such a case the resource that would be transferred is the principal's economic resource, not the agent's.

Present Obligations as a Result of Past Events

5.17 A present obligation is binding. To satisfy the definition of a liability, it is necessary that a present obligation arises as a result of one or more a past transactions ~~and~~ or other past events and requires ~~an outflow of resources~~ a transfer of resources from the entity. ~~The complexity of public sector programs and activities means that a number of events in the development, implementation and operation of a particular program may give rise to obligations. For financial reporting purposes it is necessary to determine whether such commitments and obligations, including binding obligations that the entity has little or no realistic alternative to avoid but are not legally enforceable (non-legally binding obligations) are present obligations and satisfy the definition of a liability. Where an arrangement has a legal form and is binding, such as a contract, the past event may be straightforward to identify. In other cases, it may be more difficult to identify the past event and identification involves an assessment of when an entity has little or no realistic alternative to avoid an outflow of resources from the entity. In making such an assessment an entity takes jurisdictional factors into account.~~

5.17A A present obligation exists as a result of past events only if:

- (a) The entity has already obtained service potential or economic benefits or taken an action; and
- (b) As a consequence, the entity will or may have to transfer a resource that it would not otherwise have had to transfer.

5.17B In the public sector, obligations may arise at a number of points. For example, in implementing a program or service:

- Making a political promise such as an electoral pledge;
- Announcement of a policy;
- Introduction (and approval) of the budget (which may be two distinct points); and
- The budget becoming effective (in some jurisdictions the budget will not be effective until an appropriation has been effected).

The early stages of implementation are unlikely to give rise to present obligations that meet the definition of a liability. Later stages, such as claimants meeting the eligibility criteria for the service to be provided, may give rise to present obligations that meet the definition of a liability.

5.17C The point at which an obligation gives rise to a liability depends on the nature of the obligation. Factors that are likely to impact on judgments whether other parties can validly conclude that the obligation is such that the entity has little or no realistic alternative to avoid a transfer an outflow of resources include:

- The nature of the past event or events that give rise to the obligation. For example, a promise made in an election is unlikely to give rise to a present obligation because an electoral pledge very rarely creates a valid expectation on the part of external parties that the entity has an obligation that it has little or no realistic alternative to avoid settling. However, an announcement in relation to an event or circumstance that has occurred may have such political support that the government has little option to withdraw. Where the government has committed to introduce and secure passage of the necessary budgetary provision such an announcement may give rise to a non-legally binding obligation;
- The ability of the entity to modify or change the obligation before it crystallizes. For example, the announcement of policy will generally not give rise to a non-legally binding obligation, which cannot be modified before being implemented. Similarly, if an obligation is contingent on future events occurring, there may be discretion to avoid an outflow of resources before those events occur; and
- There may be a correlation between the availability of funding to settle a particular obligation and the creation of a present obligation. For example, where both a budget line item has been approved and linked funding is assured through an appropriation, the availability of contingency funding or a transfer from a different level of government, a non-legally binding obligation may exist. However, the absence of a budgetary provision does not itself mean that a present obligation has not arisen.

5.17D “Economic coercion”, “political necessity” or other circumstances may give rise to situations where, although the public sector entity is not legally obliged to incur an outflow of resources, the economic or political consequences of refusing to do so are such that the entity may have little or no realistic alternative to avoid an outflow of resources. Economic coercion, political necessity or other circumstances may lead to a liability arising from a non-legally binding obligation.

Legal and Non-Legally Binding Obligations

~~5.18 — Binding obligations can be legal obligations or non-legally binding obligations. Binding obligations can arise from both exchange and non-exchange transactions. An obligation must be to an external party in order to give rise to a liability. An entity cannot be obligated to itself, even where it has publicly communicated an intention to behave in a particular way. Identification of an external party is an indication of the existence of an obligation giving rise to a liability. However, it is not essential to know the identity of the external party before the time of settlement in order for a present obligation and a liability to exist. [Deleted]~~

~~5.19—Many arrangements that give rise to an obligation include settlement dates. The inclusion of a settlement date may provide an indication that an obligation involves an outflow a transfer of resources and gives rise to a liability. However, there are many agreements that do not contain settlement dates. The absence of a settlement date does not preclude an obligation giving rise to a liability. [Deleted]~~

~~Legal Obligations~~

~~5.20—A legal obligation is enforceable in law. Such enforceable obligations may arise from a variety of legal constructs. Exchange transactions are usually contractual in nature and therefore enforceable through the laws of contract or equivalent authority or arrangements. There are jurisdictions where government and public sector entities cannot enter into legal obligations, because, for example, they are not permitted to contract in their own name, but where there are alternative processes with equivalent effect. Obligations that are binding through such alternative processes are considered legal obligations in the Conceptual Framework. For some types of non-exchange transactions, judgment will be necessary to determine whether an obligation is enforceable in law. Where it is determined that an obligation is enforceable in law there can be no doubt that an entity has no realistic alternative to avoid the obligation and that a liability exists. [Deleted]~~

~~5.21—Some obligations related to exchange transactions are not strictly enforceable by an external party at the reporting date but will be enforceable with the passage of time without the external party having to meet further conditions—or having to take any further action—prior to settlement. Claims that are unconditionally enforceable subject to the passage of time are enforceable obligations in the context of the definition of a liability. [Deleted]~~

~~5.22—Sovereign power is the ultimate authority of a government to make, amend and repeal legal provisions. Sovereign power is not a rationale for concluding that an obligation does not meet the definition of a liability in this Framework. The legal position should be assessed at each reporting date to consider if an obligation is no longer binding and does not meet the definition of a liability. [Deleted]~~

~~Non-Legally Binding Obligations~~

~~5.23—Liabilities can arise from non-legally binding obligations. Non-legally binding obligations differ from legal obligations in that the party to whom the obligation exists cannot take legal (or equivalent) action to enforce settlement. Non-legally binding obligations that give rise to liabilities have the following attributes:~~

- ~~•—The entity has indicated to other parties by an established pattern of past practice, published policies, or a sufficiently specific current statement that it will accept certain responsibilities;~~
- ~~•—As a result of such an indication, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities; and~~
- ~~•—The entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities. [Deleted]~~

- 5.24 In the public sector, obligations may arise at a number of points. For example, in implementing a program or service:
- ~~—— Making a political promise such as an electoral pledge;~~
 - ~~—— Announcement of a policy;~~
 - ~~—— Introduction (and approval) of the budget (which may be two distinct points); and~~
 - ~~—— The budget becoming effective (in some jurisdictions the budget will not be effective until an appropriation has been effected).~~
 - The early stages of implementation are unlikely to give rise to present obligations that meet the definition of a liability. Later stages, such as claimants meeting the eligibility criteria for the service to be provided, may give rise to obligations that meet the definition of a liability. [Deleted]
- 5.25 ~~—— The point at which an obligation gives rise to a liability depends on the nature of the obligation. Factors that are likely to impact on judgments whether other parties can validly conclude that the obligation is such that the entity has little or no realistic alternative to avoid an outflow of resources include:~~
- ~~—— The nature of the past event or events that give rise to the obligation. For example, a promise made in an election is unlikely to give rise to a present obligation because an electoral pledge very rarely creates a valid expectation on the part of external parties that the entity has an obligation that it has little or no realistic alternative to avoid settling. However, an announcement in relation to an event or circumstance that has occurred may have such political support that the government has little option to withdraw. Where the government has committed to introduce and secure passage of the necessary budgetary provision such an announcement may give rise to a non-legally binding obligation;~~
 - ~~—— The ability of the entity to modify or change the obligation before it crystallizes. For example, the announcement of policy will generally not give rise to a non-legally binding obligation, which cannot be modified before being implemented. Similarly, if an obligation is contingent on future events occurring, there may be discretion to avoid an outflow of resources before those events occur; and~~
 - ~~—— There may be a correlation between the availability of funding to settle a particular obligation and the creation of a present obligation. For example, where both a budget line item has been approved and linked funding is assured through an appropriation, the availability of contingency funding or a transfer from a different level of government, a non-legally binding obligation may exist. However, the absence of a budgetary provision does not itself mean that a present obligation has not arisen.[Deleted]~~
- 5.26 ~~—— “Economic coercion,” “political necessity” or other circumstances may give rise to situations where, although the public sector entity is not legally obliged to incur an outflow of resources, the economic or political consequences of refusing to do so are such that the entity may have little or no realistic alternative to avoid an outflow of resources. Economic coercion, political necessity or other circumstances may lead to a liability arising from a non-legally binding obligation.[Deleted]~~

Specific Matters for Comments

Question

1. Does the IPSASB approve the Specific Matters for Comments (SMCs) in ED 81, Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements.

Recommendation

2. Board Sponsor and Staff recommend that the SMCs in [Appendix A](#) and the Request for Comments section of ED 81 are adopted.

Background and Analysis

3. Staff has developed the SMCs in [Appendix A](#). SMC 8 asks respondents for views on whether a separate section on executory contracts is necessary. Members instructed that such a SMC should be included at the October meeting.
4. Because the change to the definition of an asset is very minor—past event is changed to past events—Staff does not consider that a SMC on the revised asset definition is necessary. SMC 3 asks for views on the rights-based approach to a resource adopted by the IPSASB at the October meeting.

Decision Required

5. Does the IPSASB agree with the Board Sponsor and Staff recommendation in paragraph 2?

APPENDIX A

PROPOSED SPECIFIC MATTERS FOR COMMENT IN ED 81

Specific Matter for Comment 1:

In paragraphs 3.14A and 3.14B the IPSASB has provided guidance on the role of prudence in supporting neutrality in the context of the qualitative characteristic of faithful representation. Paragraphs BC3.27A-BC3.17E explain the reasons for this guidance.

Do you agree with this approach? If not, why not? How would you modify these paragraphs?

Specific Matter for Comment 2:

In discussing materiality in paragraph 3.32 the IPSASB has added obscuring information to misstating or omitting information as factors relevant to materiality judgments. The reasons for this addition are in paragraphs BC3.32A and 3.32B.

Do you agree with the addition of obscuring information to factors relevant to materiality judgments? If not, why not?

Specific Matter for Comment 3:

ED 81 reflects a rights-based approach to the description of a resource in paragraphs 5.7A-5.7G. The reasons for this approach are in paragraphs BC5.3A-5.3F.

Do you agree with this proposed change? If not, why not?

Specific Matter for Comment 4:

The revised definition of a liability is in paragraph 5.13:

A present obligation of the entity for ~~an outflow~~ a transfer of resources that results from ~~a past events~~.

The reasons for the revised definition are in paragraphs 5.18A-5.18E?

Do you agree with the revised definition? If you do not agree with the revised definition, what definition do you support and why?

Specific Matter for Comment 5:

The IPSASB has included guidance on the transfer of a resource in paragraphs 5.16A-5.16F of the section on Liabilities. The reasons for including this guidance are in BC5.19A–5.19D.

Do you agree with this guidance? If not, how would you modify it?

Specific Matter for Comment 6

In addition to including guidance on the transfer of a resource the IPSASB has restructured the guidance on liabilities so that it aligns better with the definition of a liability. This guidance is in paragraphs 5.14A-5.17D. Paragraph BC 5.18H explains the reasons for this restructuring.

Do you agree with this restructuring? If not, how would you modify it?

Specific Matter for Comment 7

The IPSASB has added a section of Unit of Account in paragraphs 5.26A-5.26K. The reasons for proposing this section are in paragraphs BC5.36A-5.36D.

Do you agree with the addition of a section on Unit of Account and its content? If not, how would you modify it and why? If you have comments on executory accounting principles, please provide these in Specific Matter for Comment 8.

Specific Matter for Comment 8

The IPSASB took the view that guidance on executory accounting principles is necessary, but that a separate section on executory contracts is unnecessary. The principles of executory contract accounting are included in paragraphs 5.26G-5.36I of the section on Unit of Account. The explanation is at paragraphs BC5.36D-BC5.36F.

Do you agree that:

- (a) Guidance on executory accounting principles is necessary; and if so
- (b) Such guidance should be included in the Unit of Account section, rather than in a separate section.

Approval of ED 81, Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements

Question

1. Does the IPSASB approve ED 81, *Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements*, for exposure, subject to the normal editorial process?

Recommendation

2. Board Sponsor and Staff recommend that ED 81 is approved for exposure on a four-month consultation.

Due Process

3. The IPSASB approved a project brief for the *Limited Scope Update of the Conceptual Framework* in March 2020. The Consultative Advisory Group discussed and gave comments on an earlier draft version of the project brief at its December 2019 meeting. The initial stage of the project led to the approval of ED 76, *Conceptual Framework Update: Chapter 7, Measurement of Assets and Liabilities*. The consultation period for ED 76 ended on October 15th, 2021. Agenda Item 11, *Measurement Suite of EDs*, gives some high-level staff observations on the issues raised by respondents.

Next Steps

4. Subject to its approval at this meeting the text of ED 81 will be reviewed by an editorial group in early Q1 2021 prior to publication.

Decision Required

5. Does the IPSASB agree with the Board Sponsor and staff recommendation in paragraph 2?

Supporting Documents 1 – ED 81, *Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements*

Guidance in [draft] ***Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements*** at Agenda Item 6.3.1

Text has been updated to reflect:

- (a) IPSASB decisions made in June, September and October 2021;
- (b) IPSASB instructions made in June, September and October 2021; and
- (c) Board Sponsor and staff recommendations proposed in this Agenda Item 6.

REVIEW INSTRUCTIONS:

IPSASB members, Technical Advisors, and Observers are asked to note the following when reviewing ED 81:

- (a) Core Text
 - (i) A significant portion of ED 81 is imported from Chapters 3 and 5 of the Framework in the 2021 IPSASB Handbook and is unchanged. Unchanged text is neither crossed out or underlined.
 - (ii) Changes made to Chapters 3 and 5 are underlined (new text) and crossed out (deleted text) based on Board Decisions or Instructions to Staff provided in previous meetings. Relocated text is double-underlined.

Proposed Update to Conceptual Framework

Conceptual Framework Update:
Chapter 3, *Qualitative
Characteristics* and Chapter 5,
Elements

This document was developed and approved by the International Public Sector Accounting Standards Board® (IPSASB®).

The objective of the IPSASB is to serve the public interest by setting high-quality public sector accounting standards and by facilitating the adoption and implementation of these, thereby enhancing the quality and consistency of practice throughout the world and strengthening the transparency and accountability of public sector finances.

In meeting this objective the IPSASB sets IPSAS™ and Recommended Practice Guidelines (RPGs) for use by public sector entities, including national, regional, and local governments, and related governmental agencies.

IPSAS relate to the general purpose financial statements (financial statements) and are authoritative. RPGs are pronouncements that provide guidance on good practice in preparing general purpose financial reports (GPFRs) that are not financial statements. Unlike IPSAS RPGs do not establish requirements. Currently all pronouncements relating to GPFRs that are not financial statements are RPGs. RPGs do not provide guidance on the level of assurance (if any) to which information should be subjected.

The structures and processes that support the operations of the IPSASB are facilitated by the International Federation of Accountants® (IFAC®).

Copyright © January 2022 by the International Federation of Accountants (IFAC). For copyright, trademark, and permissions information, please see [page xx](#).

REQUEST FOR COMMENTS

This Exposure Draft (ED), *Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements*, was developed and approved by the International Public Sector Accounting Standards Board® (IPSASB®).

The proposals in this Exposure Draft may be modified in light of comments received before being issued in final form. **Comments are requested by May 31, 2022.**

Respondents are asked to submit their comments electronically through the IPSASB website, using the [“Submit a Comment”](#) link. Please submit comments in both a PDF file and a Word file. Also, please note that first-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the website. This publication may be downloaded from the IPSASB website: www.ipsasb.org. The approved text is published in the English language.

Objective of the ED

This ED aims to enhance the alignment between Chapters 3, *Qualitative Characteristics*, and 5, *Elements*, of its Conceptual Framework and the suite of IPSAS in the light of developments in the development and maintenance of IPSAS and other thinking on conceptual issues since the Framework was approved in 2014.

Guide for Respondents

The IPSASB would welcome comments on all of the matters discussed in this ED. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

The Specific Matters for Comment for the ED are provided below.

Specific Matter for Comment 1:

In paragraphs 3.14A and 3.14B the IPSASB has provided guidance on the role of prudence in supporting neutrality in the context of the qualitative characteristic of faithful representation. Paragraphs BC3.27A-BC3.17E explain the reasons for this guidance. Do you agree with this approach?

If not, why not? How would you modify these paragraphs?

Specific Matter for Comment 2:

In discussing materiality in paragraph 3.32 the IPSASB has added obscuring information to misstating or omitting information as factors relevant to materiality judgments. The reasons for this addition are in paragraphs BC3.32A and 3.32B.

Do you agree with the addition of obscuring information to factors relevant to materiality judgments? If not, why not?

Specific Matter for Comment 3:

ED 81 reflects a rights-based approach to the description of a resource in paragraphs 5.7A-5.7G. The reasons for this approach are in paragraphs BC5.3A-5.3F.

Do you agree with this proposed change? If not, why not?

Specific Matter for Comment 4:

The revised definition of a liability is in paragraph 5.13:

A present obligation of the entity for ~~an outflow~~ a transfer of resources that results from a past event.

The reasons for the revised definition are in paragraphs 5.18A-5.18E?

Do you agree with the revised definition? If you do not agree with the revised definition, what definition do you support and why?

Specific Matter for Comment 5:

The IPSASB has included guidance on the transfer of a resource in paragraphs 5.16A-5.16F of the section on Liabilities. The reasons for including this guidance are in BC5.19A-5.19D.

Do you agree with this guidance? If not, how would you modify it?

Specific Matter for Comment 6

In addition to including guidance on the transfer of a resource the IPSASB has restructured the guidance on liabilities so that it aligns better with the definition of a liability. This guidance is in paragraphs 5.14A-5.17D. Paragraph BC 5.18H explains the reasons for this restructuring.

Do you agree with this restructuring? If not, how would you modify it?

Specific Matter for Comment 7

The IPSASB has added a section of Unit of Account in paragraphs 5.26A-5.26K. The reasons for proposing this section are in paragraphs BC5.36A-5.36D.

Do you agree with the addition of a section on Unit of Account and its content? If not, how would you modify it and why? If you have comments on executory accounting principles, please provide these in Specific Matter for Comment 8

Specific Matter for Comment 8

The IPSASB took the view that guidance on executory accounting principles should be included in the Conceptual Framework, but that a separate section on executory contracts is unnecessary. The principles of executory contract accounting are included in paragraphs 5.26G-5.36I of the section on Unit of Account. The explanation is at paragraphs BC5.36D-BC5.36F.

Do you agree that:

- (a) Guidance on executory accounting principles is necessary; and if so
- (b) Such guidance should be included in the Unit of Account section, rather than in a separate section?

Note:

In ED 81, text deleted from the Conceptual Framework approved in 2014 is struck out. New text is underlined. Text that has been relocated is double underlined.

**EXPOSURE DRAFT 81, CONCEPTUAL FRAMEWORK UPDATE:
CHAPTER 3, QUALITATIVE CHARACTERISTICS AND CHAPTER 5,
ELEMENTS**

CONTENTS

	Page
CHAPTER 3: QUALITATIVE CHARACTERISTICS	7–22
CHAPTER 5: ELEMENTS.....	23–56

DRAFT

CHAPTER 3: QUALITATIVE CHARACTERISTICS

CONTENTS

	Paragraph
Introduction.....	3.1–3.5
Relevance	3.6–3.9
Faithful Representation	3.10–3.16
Understandability	3.17–3.18
Timeliness	3.19–3.20
Comparability	3.21–3.25
Verifiability	3.26–3.31
Constraints on Information Included in General Purpose Financial Reports	3.32–3.42
Materiality	3.32–3.34
Cost-Benefit	3.35–3.40
Balance Between the Qualitative Characteristics.....	3.41–3.42
Basis for Conclusions.....	BC3.1–BC3.35

Introduction

- 3.1 GPFRs present financial and non-financial information about economic and other phenomena. The qualitative characteristics of information included in GPFRs are the attributes that make that information useful to users and support the achievement of the objectives of financial reporting. The objectives of financial reporting are to provide information useful for accountability and decision-making purposes.
- 3.2 The qualitative characteristics of information included in GPFRs of public sector entities are relevance, faithful representation, understandability, timeliness, comparability, and verifiability.
- 3.3 Pervasive constraints on information included in GPFRs are materiality, cost-benefit, and achieving an appropriate balance between the qualitative characteristics.
- 3.4 Each of the qualitative characteristics is integral to, and works with, the other characteristics to provide in GPFRs information useful for achieving the objectives of financial reporting. However, in practice, all qualitative characteristics may not be fully achieved, and a balance or trade-off between certain of them may be necessary.
- 3.5 The qualitative characteristics apply to all financial and non-financial information reported in GPFRs, including historic and prospective information, and explanatory information. However, the extent to which the qualitative characteristics can be achieved may differ depending on the degree of uncertainty and subjective assessment or opinion involved in compiling the financial and non-financial information. The need for additional guidance on interpreting and applying the qualitative characteristics to information that extends the scope of financial reporting beyond financial statements will be considered in the development of any IPSASs and RPGs that deal with such matters.

Relevance

- 3.6 Financial and non-financial information is relevant if it is capable of making a difference in achieving the objectives of financial reporting. Financial and non-financial information is capable of making a difference when it has confirmatory value, predictive value, or both. It may be capable of making a difference, and thus be relevant, even if some users choose not to take advantage of it or are already aware of it.
- 3.7 Financial and non-financial information has confirmatory value if it confirms or changes past (or present) expectations. For example, information will be relevant for accountability and decision-making purposes if it confirms expectations about such matters as the extent to which managers have discharged their responsibilities for the efficient and effective use of resources, the achievement of specified service delivery objectives, and compliance with relevant budgetary, legislative and other requirements.
- 3.8 GPFRs may present information about an entity's anticipated future service delivery activities, objectives and costs, and the amount and sources of the resources that are intended to be allocated to providing services in the future. Such future oriented information will have predictive value and be relevant for accountability and decision-making purposes. Information about economic and other phenomena that exist or have already occurred can also have predictive value in helping form expectations about the future. For example, information that confirms or disproves past

expectations can reinforce or change expectations about financial results and service delivery outcomes that may occur in the future.

- 3.9 The confirmatory and predictive roles of information are interrelated—for example, information about the current level and structure of an entity's resources and claims to those resources helps users to confirm the outcome of resource management strategies during the period, and to predict an entity's ability to respond to changing circumstances and anticipated future service delivery needs. The same information helps to confirm or correct users' past expectations and predictions about the entity's ability to respond to such changes. It also helps to confirm or correct prospective financial information included in previous GPFRs.

Faithful Representation

- 3.10 To be useful in financial reporting, information must be a faithful representation of the economic and other phenomena that it purports to represent. Faithful representation is attained when the depiction of the phenomenon is complete, neutral, and free from material error. Information that faithfully represents an economic or other phenomenon depicts the substance of the underlying transaction, other event, activity or circumstance—which is not necessarily always the same as its legal form.
- 3.11 In practice, it may not be possible to know or confirm whether information presented in GPFRs is complete, neutral, and free from material error. However, information should be as complete, neutral, and free from error as is possible.
- 3.12 An omission of some information can cause the representation of an economic or other phenomenon to be false or misleading, and thus not useful to users of GPFRs. For example, a complete depiction of the item "plant and equipment" in GPFRs will include a numeric representation of the aggregate amount of plant and equipment together with other quantitative, descriptive and explanatory information necessary to faithfully represent that class of assets. In some cases, this may include the disclosure of information about such matters as the major classes of plant and equipment, factors that have affected their use in the past or might impact on their use in the future, and the basis and process for determining their numeric representation. Similarly, prospective financial and non-financial information and information about the achievement of service delivery objectives and outcomes included in GPFRs will need to be presented with the key assumptions that underlie that information and any explanations that are necessary to ensure that its depiction is complete and useful to users.
- 3.13 Neutrality in financial reporting is the absence of bias. It means that the selection and presentation of financial and non-financial information is not made with the intention of attaining a particular predetermined result—for example, to influence in a particular way users' assessment of the discharge of accountability by the entity or a decision or judgment that is to be made, or to induce particular behavior.
- 3.14 Neutral information faithfully represents the economic and other phenomena that it purports to represent. However, to require information included in GPFRs to be neutral does not mean that it is not without purpose or that it will not influence behavior. Relevance is a qualitative characteristic and, by definition, relevant information is capable of influencing users' assessments and decisions.
- 3.14A Neutrality is supported by the exercise of prudence. Prudence is the exercise of caution when making judgments under conditions of uncertainty. The exercise of prudence means that assets

and revenue are not overstated and liabilities and expense are not understated. Equally, the exercise of prudence does not allow for the understatement of assets or revenue or the overstatement of liabilities or expense. Such misstatements can lead to the overstatement or understatement of revenue or expense in future reporting periods.

- 3.14B The exercise of prudence does not imply a need for asymmetry; for example, a systematic need for more persuasive evidence to support the recognition of assets or revenue than the recognition of liabilities or expense. Particular standards may contain asymmetric requirements if this is a consequence of decisions intended to select the most relevant information that faithfully represents what it purports to represent.
- 3.15 The economic and other phenomena represented in GPFRs generally occur under conditions of uncertainty. Information included in GPFRs will therefore often include estimates that incorporate management's judgment. To faithfully represent an economic or other phenomenon, an estimate must be based on appropriate inputs, and each input must reflect the best available information. Caution will need to be exercised when dealing with uncertainty. It may sometimes be necessary to explicitly disclose the degree of uncertainty in financial and non-financial information to faithfully represent economic and other phenomena.
- 3.16 Free from material error does not mean complete accuracy in all respects. Free from material error means there are no errors or omissions that are individually or collectively material in the description of the phenomenon, and the process used to produce the reported information has been applied as described. In some cases, it may be possible to determine the accuracy of some information included in GPFRs—for example, the amount of a cash transfer to another level of government, the volume of services delivered, or the price paid for the acquisition of plant and equipment. However, in other cases it may not—for example, the accuracy of an estimate of the value or cost of an item or the effectiveness of a service delivery program may not be able to be determined. In these cases, the estimate will be free from material error if the amount is clearly described as an estimate, the nature and limitations of the estimation process are explained, and no material errors have been identified in selecting and applying an appropriate process for developing the estimate.

Understandability

- 3.17 Understandability is the quality of information that enables users to comprehend its meaning. GPFRs of public sector entities should present information in a manner that responds to the needs and knowledge base of users, and to the nature of the information presented. For example, explanations of financial and non-financial information and commentary on service delivery and other achievements during the reporting period and expectations for future periods should be written in plain language and presented in a manner that is readily understandable by users. Understandability is enhanced when information is classified, characterized, and presented clearly and concisely. Comparability also can enhance understandability.
- 3.18 Users of GPFRs are assumed to have a reasonable knowledge of the entity's activities and the environment in which it operates, to be able and prepared to read GPFRs, and to review and analyze the information presented with reasonable diligence. Some economic and other phenomena are particularly complex and difficult to represent in GPFRs, and some users may need to seek the aid of an advisor to assist in their understanding of them. All efforts should be undertaken to represent economic and other phenomena included in GPFRs in a manner that is

understandable to a wide range of users. However, information should not be excluded from GPFRs solely because it may be too complex or difficult for some users to understand without assistance.

Timeliness

- 3.19 Users of GPFRs are assumed to have a reasonable knowledge of the entity's activities and the environment in which it operates, to be able and prepared to read GPFRs, and to review and analyze the information presented with reasonable diligence. Some economic and other phenomena are particularly complex and difficult to represent in GPFRs, and some users may need to seek the aid of an advisor to assist in their understanding of them. All efforts should be undertaken to represent economic and other phenomena included in GPFRs in a manner that is understandable to a wide range of users. However, information should not be excluded from GPFRs solely because it may be too complex or difficult for some users to understand without assistance.
- 3.20 Some items of information may continue to be useful long after the reporting period or reporting date. For example, for accountability and decision-making purposes, users of GPFRs may need to assess trends in the financial and service delivery performance of the entity and its compliance with budgets over a number of reporting periods. In addition, the outcome and effects of some service delivery programs may not be determinable until future periods—for example, this may occur in respect of programs intended to enhance the economic well-being of constituents, reduce the incidence of a particular disease, or increase literacy levels of certain age groups.

Comparability

- 3.21 Comparability is the quality of information that enables users to identify similarities in, and differences between, two sets of phenomena. Comparability is not a quality of an individual item of information, but rather a quality of the relationship between two or more items of information.
- 3.22 Comparability differs from consistency. Consistency refers to the use of the same accounting principles or policies and basis of preparation, either from period to period within an entity or in a single period across more than one entity. Comparability is the goal, and consistency helps in achieving that goal. In some cases, the accounting principles or policies adopted by an entity may be revised to better represent a particular transaction or event in GPFRs. In these cases, the inclusion of additional disclosures or explanation may be necessary to satisfy the characteristics of comparability.
- 3.23 Comparability differs from consistency. Consistency refers to the use of the same accounting principles or policies and basis of preparation, either from period to period within an entity or in a single period across more than one entity. Comparability is the goal, and consistency helps in achieving that goal. In some cases, the accounting principles or policies adopted by an entity may be revised to better represent a particular transaction or event in GPFRs. In these cases, the inclusion of additional disclosures or explanation may be necessary to satisfy the characteristics of comparability.
- 3.24 Information about the entity's financial position, financial performance, cash flows, compliance with approved budgets and relevant legislation or other authority governing the raising and use of resources, service delivery achievements, and its future plans is necessary for accountability

purposes and useful as input for decision-making purposes. The usefulness of such information is enhanced if it can be compared with, for example:

- Prospective financial and non-financial information previously presented for that reporting period or reporting date;
- Similar information about the same entity for some other period or some other point in time; and
- Similar information about other entities (for example, public sector entities providing similar services in different jurisdictions) for the same reporting period.

- 3.25 Consistent application of accounting principles, policies and basis of preparation to prospective financial and non-financial information and actual outcomes will enhance the usefulness of any comparison of projected and actual results. Comparability with other entities may be less significant for explanations of management's perception or opinion of the factors underlying the entity's current performance.

Verifiability

- 3.26 Verifiability is the quality of information that helps assure users that information in GPFRs faithfully represents the economic and other phenomena that it purports to represent. Supportability is sometimes used to describe this quality when applied in respect of explanatory information and prospective financial and non-financial quantitative information disclosed in GPFRs—that is, the quality of information that helps assure users that explanatory or prospective financial and non-financial quantitative information faithfully represents the economic and other phenomena that it purports to represent. Whether referred to as verifiability or supportability, the characteristic implies that different knowledgeable and independent observers could reach general consensus, although not necessarily complete agreement, that either:
- The information represents the economic and other phenomena that it purports to represent without material error or bias; or
 - An appropriate recognition, measurement, or representation method has been applied without material error or bias.
- 3.27 To be verifiable, information need not be a single point estimate. A range of possible amounts and the related probabilities also can be verified.
- 3.28 Verification may be direct or indirect. With direct verification, an amount or other representation is itself verified, such as by (a) counting cash, (b) observing marketable securities and their quoted prices, or (c) confirming that the factors identified as influencing past service delivery performance were present and operated with the effect identified. With indirect verification, the amount or other representation is verified by checking the inputs and recalculating the outputs using the same accounting convention or methodology. An example is verifying the carrying amount of inventory by checking the inputs (quantities and costs) and recalculating the ending inventory using the same cost flow assumption (for example, average cost or first-in-first-out).
- 3.29 The quality of verifiability (or supportability if such term is used to describe this characteristic) is not an absolute—some information may be more or less capable of verification than other information. However, the more verifiable is the information included in GPFRs, the more it will assure users

that the information faithfully represents the economic and other phenomena that it purports to represent.

- 3.30 GPFRs of public sector entities may include financial and other quantitative information and explanations about (a) key influences on the entity's performance during the period, (b) the anticipated future effects or outcomes of service delivery programs undertaken during the reporting period, and (c) prospective financial and non-financial information. It may not be possible to verify the accuracy of all quantitative representations and explanations of such information until a future period, if at all.
- 3.31 To help assure users that prospective financial and non-financial quantitative information and explanations included in GPFRs faithfully represents the economic and other phenomena that they purport to represent, the assumptions that underlie the information disclosed, the methodologies adopted in compiling that information, and the factors and circumstances that support any opinions expressed or disclosures made should be transparent. This will enable users to form judgments about the appropriateness of those assumptions and the method of compilation, measurement, representation and interpretation of the information.

Constraints on Information Included in General Purpose Financial Reports

Materiality

- 3.32 Information is material if ~~its omission or misstatement~~ omitting, misstating or obscuring it could reasonably be expected to ~~could~~ influence the discharge of accountability by the entity, or the decisions that users make on the basis of the entity's GPFRs prepared for that reporting period. Materiality depends on both the nature and amount of the item judged in the particular circumstances of each entity. Where an entity judges that a material item is not separately displayed on the face of a financial statement (or displayed sufficiently prominently) an entity considers disclosure.
- 3.32A GPFRs may encompass qualitative and quantitative information about service delivery achievements during the reporting period, and expectations about service delivery and financial outcomes in the future. Consequently, it is not possible to specify a uniform characteristic or a uniform set of characteristics at which a particular type of information becomes material.
- 3.33 Assessments of materiality will be made in the context of the legislative, institutional and operating environment within which the entity operates and, in respect of prospective financial and non-financial information, the preparer's knowledge and expectations about the future. Disclosure of information about compliance or non-compliance with legislation, regulation or other authority may be material because of its nature—irrespective of the magnitude of any amounts involved. In determining whether an item is material in these circumstances, consideration will be given to such matters as the nature, legality, sensitivity and consequences of past or anticipated transactions and events, the parties involved in any such transactions and the circumstances giving rise to them.
- 3.34 Materiality is classified as a constraint on information included in GPFRs in the Conceptual Framework. In developing IPSASs and RPGs, the IPSASB will consider the materiality of the consequences of application of a particular accounting policy, basis of preparation or disclosure of a particular item or type of information. Subject to the requirements of any IPSAS, entities preparing GPFRs will also consider the materiality of, for example, the application of a particular accounting policy and the separate disclosure of particular items of information.

Cost-Benefit

- 3.35 Financial reporting imposes costs. The benefits of financial reporting should justify those costs. Assessing whether the benefits of providing information justify the related costs is often a matter of judgment, because it is often not possible to identify and/or quantify all the costs and all the benefits of information included in GPFRs.
- 3.36 The costs of providing information include the costs of collecting and processing the information, the costs of verifying it and/or presenting the assumptions and methodologies that support it, and the costs of disseminating it. Users incur the costs of analysis and interpretation. Omission of useful information also imposes costs, including the costs that users incur to obtain needed information from other sources and the costs that result from making decisions using incomplete data provided by GPFRs.
- 3.37 Preparers expend the majority of the effort to provide information in GPFRs. However, service recipients and resource providers ultimately bear the cost of those efforts—because resources are redirected from service delivery activities to preparation of information for inclusion in GPFRs.
- 3.38 Users reap the majority of benefits from the information provided by GPFRs. However, information prepared for GPFRs may also be used internally by management and result in better decision making by management. The disclosure of information in GPFRs consistent with the concepts identified in the Conceptual Framework and IPSASs and RPGs derived from them will enhance and reinforce perceptions of the transparency of financial reporting by governments and other public sector entities and contribute to the more accurate pricing of public sector debt. Therefore, public sector entities may also benefit in a number of ways from the information provided by GPFRs.
- 3.39 Application of the cost-benefit constraint involves assessing whether the benefits of reporting information are likely to justify the costs incurred to provide and use the information. When making this assessment, it is necessary to consider whether one or more qualitative characteristic might be sacrificed to some degree to reduce cost.
- 3.40 In developing IPSASs, the IPSASB considers information from preparers, users, academics, and others about the expected nature and quantity of the benefits and costs of the proposed requirements. Disclosure and other requirements which result in the presentation of information useful to users of GPFRs for accountability and decision-making purposes and satisfy the qualitative characteristics are prescribed by IPSASs when the benefits of compliance with those disclosures and other requirements are assessed by the IPSASB to justify their costs.

Balance Between the Qualitative Characteristics

- 3.41 The qualitative characteristics work together to contribute to the usefulness of information. For example, neither a depiction that faithfully represents an irrelevant phenomenon, nor a depiction that unfaithfully represents a relevant phenomenon, results in useful information. Similarly, to be relevant, information must be timely and understandable.
- 3.42 In some cases, a balancing or trade-off between qualitative characteristics may be necessary to achieve the objectives of financial reporting. The relative importance of the qualitative characteristics in each situation is a matter of professional judgment. The aim is to achieve an appropriate balance among the characteristics in order to meet the objectives of financial reporting.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, the Conceptual Framework.

Qualitative Characteristics of Information Included in General Purpose Financial Reports

- BC3.1 In developing IPSASs, the IPSASB receives input from constituents on, and makes judgments about, information that best satisfies the objectives of financial reporting and should be included in GPFRs. In making those judgments, the IPSASB considers the extent to which each of the qualitative characteristics can be achieved. Disclosure and other requirements are included in IPSASs only when the information that results from their application is considered to satisfy the qualitative characteristics and the cost-benefit constraint identified in the Conceptual Framework.
- BC3.2 Some respondents to the Exposure Draft issued in 2010 expressed concern about the application of the qualitative characteristics to all matters that may be presented in GPFRs, particularly those matters that may be presented in reports outside the financial statements. The IPSASB understands this concern. The IPSASB acknowledges that IPSASs and RPGs that deal with the presentation in GPFRs of information outside the financial statements may need to include additional guidance on the application of the qualitative characteristics to the matters dealt with.
- BC3.3 IPSASs and RPGs issued by the IPSASB will not deal with all financial and non-financial information that may be included in GPFRs. In the absence of an IPSAS or RPG that deals with particular economic or other phenomena, assessments of whether an item of information satisfies the qualitative characteristics and constraints identified in the Conceptual Framework, and therefore qualifies for inclusion in GPFRs, will be made by preparers compiling the GPFRs. Those assessments will be made in the context of achieving the objectives of financial reporting, which in turn have been developed to respond to users' information needs.
- BC3.4 Having in place accounting systems and processes that are appropriately designed and are operated effectively will enable management to gather and process evidence to support financial reporting. The quality of these systems and processes is a key factor in ensuring the quality of financial information that the entity includes in GPFRs.

Other Qualitative Characteristics Considered

- BC3.5 Some respondents to the 2010 Exposure Draft, expressed the view that additional qualitative characteristics should be identified. Those qualitative characteristics included "sincerity," "true and fair view," "credibility," "transparency," and "regularity".
- BC3.6 The IPSASB noted that "sincerity" as used in financial reporting has a similar meaning to "true and fair". The IPSASB took is of the view that sincerity, true and fair view, credibility, and transparency are important expressions of the overarching qualities that financial reporting is to achieve or aspire to. However, they do not exist as single qualitative characteristics on their own—rather, achieving these qualities is the product of application of the full set of qualitative characteristics identified in the Conceptual Framework, and the IPSASs that deal with specific reporting issues. Consequently, while important characteristics of GPFRs, they are not identified as separate individual qualitative characteristics in their own right. The IPSASB is also of took the view that the notion of "regularity" as noted by some respondents is related to the notion of "compliance" as used in the Conceptual Framework—therefore, regularity is not identified as an additional qualitative characteristic.

Relevance

- BC3.7 The Conceptual Framework explains that financial and non-financial information is relevant if it is capable of making a difference in achieving the objectives of financial reporting. As part of its due process the IPSASB seeks input on whether the requirements of a proposed IPSAS or any proposed RPGs are relevant to the achievement of the objectives of financial reporting—that is, are relevant to the discharge of the entity's obligation to be accountable and to decisions that users may make.

Faithful Representation

- BC3.8 The Conceptual Framework explains that to be useful information must be a faithful representation of the economic and other phenomena that it purports to represent. A single economic or other phenomenon may be faithfully represented in many ways. For example, the achievement of particular service delivery objectives may be depicted (a) qualitatively through an explanation of the immediate and anticipated longer term outcomes and effects of the service delivery program, (b) quantitatively as a measure of the volume and cost of services provided by the service delivery program, or (c) by a combination of both qualitative and quantitative information. Additionally, a single depiction in GPFRs may represent several economic phenomena. For example, the presentation of the item "plant and equipment" in a financial statement may represent an aggregate of all of an entity's plant and equipment, including items that have different functions, that are subject to different risks and opportunities and that are carried at amounts based on estimates that may be more or less complex and reliable.
- BC3.9 Completeness and neutrality of estimates (and inputs to those estimates) and freedom from material error are desirable, and some minimum level of accuracy is necessary for an estimate to faithfully represent an economic or other phenomenon. However, faithful representation does not imply absolute completeness or neutrality in the estimate, nor does it imply total freedom from error in the outcome. For a representation of an economic or other phenomenon to imply a degree of completeness, neutrality, or freedom from error that is impracticable for it to achieve would diminish the extent to which the information faithfully represents the economic or other phenomenon that it purports to represent.

Faithful Representation or Reliability

- BC3.10 At the time of issue of the 2010 Exposure Draft, Appendix A of IPSAS 1, *Presentation of Financial Statements* identified "reliability" as a qualitative characteristic. It described reliable information as information that is "free from material error and bias and can be depended on by users to represent faithfully that which it purports to represent or could reasonably be expected to represent." Faithful representation, substance over form, neutrality, prudence and completeness were identified as components of reliability. The *Conceptual Framework* uses the term "faithful representation" rather than "reliability" to describe what is substantially the same concept. In addition, it does not explicitly identify substance over form and prudence as components of faithful representation.
- BC3.11 Many respondents to the 2010 Exposure Draft supported the use of faithful representation and its explanation in the Exposure Draft, in some cases explaining that faithful representation is a better expression of the nature of the concept intended. Some respondents did not support the replacement of reliability with the term faithful representation, expressing concerns including that

faithful representation implies the adoption of fair value or market value accounting, and reliability and faithful representation are not interchangeable terms.

- BC3.12 The use of the term “faithful representation”, or “reliability” for that matter, to describe this qualitative characteristic in the Conceptual Framework will not determine the measurement basis to be adopted in GPFRs, whether historical cost, market value, fair value or another measurement basis. The IPSASB does not intend that use of faithful representation be interpreted as such. The measurement basis or measurement bases that may be adopted for the elements of financial statements are considered in Chapter 7, Measurement of Assets and Liabilities in Financial Statements. The qualitative characteristics will then operate to ensure that the financial statements faithfully represent the measurement basis or bases reflected in GPFRs.
- BC3.13 The IPSASB appreciated the concern of some respondents that the use of a different term may be interpreted to reflect different, and even lesser, qualities to those communicated by the term reliability. However, the IPSASB took is of the view that explanation in the Framework that “Faithful representation is attained when the depiction of the phenomenon is complete, neutral, and free from material error”, and the elaboration of these key features will protect against the loss of any of the qualities that were formerly reflected in the use of the term reliability.
- BC3.14 In addition, the IPSASB has been advised that the term “reliability” is itself open to different interpretations and subjective judgments, with consequences for the quality of information included in GPFRs. The IPSASB took is of the view that use of the term “faithful representation” will overcome problems in the interpretation and application of reliability that have been experienced in some jurisdictions without a lessening of the qualities intended by the term, and is more readily translated into, and understood in, a wide range of languages.

Substance over Form and Prudence

- BC3.15 Some respondents to the 2010 Exposure Draft expressed concern that substance over form and prudence are not identified as qualitative characteristics or that their importance is not sufficiently recognized or explained. Some also noted that prudence need not be incompatible with the achievement of neutrality and faithful representation.
- BC3.16 The Conceptual Framework explains that “Information that faithfully represents an economic or other phenomenon depicts the substance of the underlying transaction, other event, activity or circumstance—which is not necessarily always the same as its legal form.” Therefore, substance over form remains a key quality that information included in GPFRs must possess. It is not identified as a separate or additional qualitative characteristic because it is already embedded in the notion of faithful representation.
- BC3.17 The IPSASB ~~is of~~ took the view that the notion of prudence is also reflected in the explanation of neutrality as a component of faithful representation, and the acknowledgement of the need to exercise caution in dealing with uncertainty. Therefore, like substance over form, prudence is not identified as a separate qualitative characteristic because its intent and influence in identifying information that is included in GPFRs is already embedded in the notion of faithful representation.
- BC3.17A The IASB revised its approach to prudence in the 2018 Framework. The IASB did not include prudence as a qualitative characteristic, but, in the context of faithful representation, explained that ‘neutrality is supported by the exercise of prudence’ and that ‘prudence is the exercise of

caution when making judgments under conditions of uncertainty.’ The IASB characterized the approach adopted in the 2018 Framework as ‘cautious prudence’.

BC3.17B The IPSASB also noted that prudence had been the subject of much discussion in the European Public Sector Accounting Standards project.

BC3.17C Because of the above developments the IPSASB reconsidered the approach to prudence in the Conceptual Framework, in particular whether prudence should be included as a qualitative characteristic in its own right or whether guidance on prudence should be included in the context of neutrality and faithful representation.

BC3.17D The IPSASB considered that prudence is insufficiently distinct from faithful representation to justify inclusion as an additional qualitative characteristic. Practical application of the IPSASB Framework has not identified that the non-inclusion of prudence as a qualitative characteristic is problematic.

BC3.17E The IPSASB acknowledged the case for retaining the approach in the 2014 Framework on the grounds that an allusion to, and discussion of, prudence, adds little to the notion of neutrality, which itself conveys a lack of bias. However, the IPSASB concluded that clarifying that prudence entails caution in assessing uncertainty in the measurement of all elements would be beneficial and would respond to those who view the absence of references to prudence as a risk. The IPSASB is firmly of the view that caution should be applied consistently rather than focusing disproportionately on assets and revenue. The IPSASB therefore decided to include an explanation that, in the context of faithful representation, ‘neutrality is supported by the exercise of prudence’ and that ‘prudence is the exercise of caution when making judgments under conditions of uncertainty. This is consistent with the approach of the IASB in its 2018 Framework.

Understandability

BC3.18 Although presenting information clearly and concisely helps users to comprehend it, the actual comprehension or understanding of information depends largely on the users of the GPFRs.

BC3.19 Some economic and other phenomena are particularly complex and difficult to represent in GPFRs. However, the IPSASB is of the view that information that is, for example, relevant, a faithful representation of what it purports to represent, timely and verifiable should not be excluded from GPFRs solely because it may be too complex or difficult for some users to understand without assistance. Acknowledging that it may be necessary for some users to seek assistance to understand the information presented in GPFRs does not mean that information included in GPFRs need not be understandable or that all efforts should not be undertaken to present information in GPFRs in a manner that is understandable to a wide range of users. However, it does reflect that, in practice, the nature of the information included in GPFRs is such that all the qualitative characteristics may not be fully achievable at all times for all users.

Timeliness

BC3.20 The IPSASB recognizes the potential for timely reporting to increase the usefulness of GPFRs for both accountability and decision-making purposes, and that undue delay in the provision of information may reduce its usefulness for these purposes. Consequently, timeliness is identified as a qualitative characteristic in the Conceptual Framework.

Comparability

- BC3.21 Some degree of comparability may be attained by maximizing the qualitative characteristics of relevance and faithful representation. For example, faithful representation of a relevant economic or other phenomenon by one public sector entity is likely to be comparable to a faithful representation of a similar relevant economic or other phenomenon by another public sector entity. However, a single economic or other phenomenon can often be faithfully represented in several ways and permitting alternative accounting methods for the same phenomenon diminishes comparability and, therefore, may be undesirable.
- BC3.22 Some respondents to the Exposure Draft expressed concern that the explanation of the relationship between comparability and consistency may be read as presenting an obstacle to the on-going development of financial reporting. This is because enhancements in financial reporting often involve a revision or change to the accounting principles, policies or basis of preparation currently adopted by the entity.
- BC3.23 Consistent application of the same accounting principles, policies and basis of preparation from one period to the next will assist users in assessing the financial position, financial performance and service delivery achievements of the entity compared with previous periods. However, where accounting principles or policies dealing with particular transactions or other events are not prescribed by IPSASs, achievement of the qualitative characteristic of comparability should not be interpreted as prohibiting the entity from changing its accounting principles or policies to better represent those transactions and events. In these cases, the inclusion in GPFRs of additional disclosures or explanation of the impact of the changed policy can still satisfy the characteristics of comparability.

Verifiability

- BC3.24 Verifiability is the quality of information that helps assure users that information in GPFRs faithfully represents the economic and other phenomena that it purports to represent. While closely linked to faithful representation, verifiability is identified as a separate qualitative characteristic because information may faithfully represent economic and other phenomena even though it cannot be verified with absolute certainty. In addition, verifiability may work in different ways with faithful representation and other of the qualitative characteristics to contribute to the usefulness of information presented in GPFRs—for example, there may need to be an appropriate balance between the degree of verifiability an item of information may possess and other qualitative characteristics to ensure it is presented in a timely fashion and is relevant.
- BC3.25 In developing the qualitative characteristics identified in the Framework, the IPSASB considered whether “supportability” should be identified as a separate characteristic for application to information presented in GPFRs outside the financial statements. The IPSASB is of the view that identifying both verifiability and supportability as separate qualitative characteristics with essentially the same features may be confusing to preparers and users of GPFRs and others. However, the Conceptual Framework does acknowledge that supportability is sometimes used to refer to the quality of information that helps assure users that explanatory information and prospective financial and non-financial information included in GPFRs faithfully represent the economic and other phenomena that they purport to represent.
- BC3.26 Some respondents to the Exposure Draft expressed concern about the application of verifiability to the broad range of matters that may be presented in GPFRs outside the financial statements,

particularly explanatory information about service delivery achievements during the reporting period and qualitative and quantitative prospective financial and non-financial information. The IPSASB is of the view that the Conceptual Framework provides appropriate guidance on the application of verifiability in respect of these matters—for example it explains that verifiability is not an absolute and it may not be possible to verify the accuracy of all quantitative representations and explanations until a future period. The Framework also acknowledges that disclosure of the underlying assumptions and methodologies adopted for the compilation of explanatory and prospective financial and non-financial information is central to the achievement of faithful representation.

Classification of the Qualitative Characteristics and Order of their Application

BC3.27 Some respondents to the 2010 Exposure Draft expressed the view that the Conceptual Framework should identify:

- Relevance and faithful representation as fundamental qualitative characteristics, and explain the order of their application; and
- Comparability, verifiability, timeliness, and understandability as enhancing qualitative characteristics.

They noted that this would provide useful guidance on the sequence of application of the qualitative characteristics and reflect the approach adopted by the International Accounting Standards Board.

BC3.28 In developing the qualitative characteristics, the IPSASB considered whether some characteristics should be identified as fundamental, and others identified as enhancing. The IPSASB also considered whether the order of application of the characteristics should be identified and/or explained. The IPSASB is of the view that such an approach should not be adopted because, for example:

- Matters identified as “fundamental” may be perceived to be more important than those identified as “enhancing”, even if this distinction is not intended in the case of the qualitative characteristics. As a result, there may be unintended consequences of identifying some qualitative characteristics as fundamental and others as enhancing.
- All the qualitative characteristics are important and work together to contribute to the usefulness of information. The relative importance of a particular qualitative characteristic in different circumstances is a matter of professional judgment. As such, it is not appropriate to identify certain qualitative characteristics as always being fundamental and others as having only an enhancing or supporting role, or to specify the sequence of their application, no matter what information is being considered for inclusion in GPFRs, and irrespective of the circumstances of the entity and its environment. In addition, it is questionable whether information that is not understandable or is provided so long after the event as not to be useful to users for accountability and decision-making purposes could be considered as relevant information—therefore, these characteristics are themselves fundamental to the achievement of the objectives of financial reporting; and
- GPFRs of public sector entities may encompass historical and prospective information about financial performance and the achievement of service delivery objectives over a number of reporting periods. This provides necessary input to assessments of trends in

service delivery activities and resources committed thereto—for such trend data, reporting on a comparable basis may be as important as, and cannot be separated from, faithful representation of the information.

Constraints on Information Included in General Purpose Financial Reports

Materiality

- BC3.29 At the time of issue of the 2010 Exposure Draft, Appendix A of IPSAS 1 described materiality with similar characteristics to that described in the Conceptual Framework but identified materiality as a factor to be considered in determining only the relevance of information. Some respondents to the Exposure Draft noted that materiality may be identified as an aspect of relevance.
- BC3.30 The IPSASB has considered whether materiality should be identified as an entity-specific aspect of relevance rather than a constraint on information included in GPFRs. As explained in the Conceptual Framework, and subject to requirements in an IPSAS, materiality will be considered by preparers in determining whether, for example, a particular accounting policy should be adopted, or an item of information should be separately disclosed in the financial statements of the entity.
- BC3.31 However, the IPSASB is of the view that materiality has a more pervasive role than would be reflected by its classification as only an entity specific aspect of relevance. For example, materiality relates to, and can impact, a number of the qualitative characteristics of information included in GPFRs. Therefore, the materiality of an item should be considered when determining whether the omission or misstatement of an item of information could undermine not only the relevance, but also the faithful representation, understandability or verifiability of financial and non-financial information presented in GPFRs. The IPSASB is also of the view that whether the effects of the application of a particular accounting policy or basis of preparation or the information content of separate disclosure of certain items of information are likely to be material should be considered in establishing IPSASs and RPGs. Consequently, the IPSASB is of the view that materiality is better reflected as a broad constraint on information to be included in GPFRs.
- BC3.32 The IPSASB considered whether the Conceptual Framework should reflect that legislation, regulation or other authority may impose financial reporting requirements on public sector entities in addition to those imposed by IPSASs. The IPSASB is of the view that, while a feature of the operating environment of many public sector (and many private sector) entities, the impact that legislation or other authority may have on the information included in GPFRs is not itself a financial reporting concept. Consequently, it has not identified it as such in the Conceptual Framework. Preparers will, of course, need to consider such requirements as they prepare GPFRs. In particular, legislation may prescribe that particular item of information are to be disclosed in GPFRs even though they may not be judged to satisfy a materiality threshold (or cost-benefit constraint) as identified in the Conceptual Framework. Similarly, the disclosure of some matters may be prohibited by legislation because, for example, they relate to matters of national security, notwithstanding that they are material and would otherwise satisfy the cost-benefit constraint.

BC3.32A In its 2018 Improvements Project the IASB amended IAS 1, *Presentation of Financial Statements*, and IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, to clarify the definition of material in order to resolve difficulties that entities experience in making materiality judgements when preparing financial statements, and to align the definitions in both standards. Because of these changes the IASB made minor, but significant, amendments to Chapter 2, *Qualitative Characteristics of Useful Financial Information*, of its 2018 Conceptual Framework. First, an amendment complemented the guidance that information is material if omitting or misstating it could influence decision making with a reference to 'obscuring information'. A second amendment softened the threshold for determining that information is material.

BC3.32B In its Limited Scope Update project initiated in 2020 the IPSASB considered both changes in the context of public sector general purpose financial reporting. The IPSASB concluded that the reference to 'obscuring information' is relevant to the public sector as, amongst other practices, it suggests that the inclusion of immaterial disclosures can have a negative impact on users, rather than just being unnecessary. This is a relevant consideration for both the general purpose financial statements and other GPFRs. The IPSASB also concluded that modifying the wording on adversely influencing users by adding the words 'reasonably expected to influence' imposes a more realistic expectation on preparers' assessments of materiality. The IPSASB therefore decided to adopt these changes in its Conceptual Framework and amended paragraph 3.32 accordingly.

BC3.32C In the IASB's 2018 Framework materiality is an aspect of the qualitative characteristic of relevance, rather than a constraint on information in general purpose financial reports as in the IPSASB Framework. In the Limited Scope Update the IPSASB did not reassess this classification. The IPSASB did acknowledge that materiality can impact a number of qualitative QCs.

BC3.32D In the Limited Scope Update the IPSASB acknowledged that in a number of jurisdictions public sector entities are required to report on whether transactions have been recorded in accordance with governing legislation and regulations. In some jurisdictions such reports are referred to as a regularity assertion or statement. Auditors may be required to express an opinion on such statements, separate to that on the financial statements.

BC3.32E The IPSASB considered whether the Conceptual Framework should provide guidance on materiality considerations for regularity assertions/statements. Consistent with the reasoning in paragraph 3.32, the IPSASB concluded that additional guidance is not justified.

Cost-Benefit

BC3.33 Some respondents to the 2010 Exposure Draft expressed concern that the text of the proposed Conceptual Framework does not specify that entities cannot decide to depart from IPSASs on the basis of their own assessments of the costs and benefits of particular requirements of an IPSAS. The IPSASB is of the view that such specification is not necessary. This is because, as noted in paragraph 1.2 of the Conceptual Framework, authoritative requirements relating to recognition, measurement, and presentation in GPFRs are specified in IPSASs. GPFRs are developed to provide information useful to users and requirements are prescribed by IPSASs only when the benefits to users of compliance with those requirements are assessed by the IPSASB to justify their costs. However, preparers may consider costs and benefits in, for

example, determining whether to include in GPFRs disclosure of information in addition to that required by IPSASs.

- BC3.34 Some respondents to the 2010 Exposure Draft also expressed concern that the proposed Conceptual Framework did not recognize that cost-benefit trade-offs may differ for different public sector entities. They are of the view that acknowledgement of this may provide a useful principle to be applied when considering differential reporting issues. The IPSASB has considered these matters and determined that the Conceptual Framework will not deal with issues related to differential reporting, including whether the costs and benefits of particular requirements might differ for different entities.
- BC3.35 In the process of developing an IPSAS or RPG, the IPSASB considers and seeks input on the likely costs and benefits of providing information in GPFRs of public sector entities. However, in some cases, it may not be possible for the IPSASB to identify and/or quantify all benefits that are likely to flow from, for example, the inclusion of a particular disclosure, including those that may be required because they are in the public interest, or other requirement in an IPSAS. In other cases, the IPSASB may be of the view that the benefits of a particular requirement may be marginal for users of GPFRs of some public sector entities. In applying the cost-benefit test to determine whether particular requirements should be included in an IPSAS in these circumstances, the IPSASB's deliberations may also include consideration of whether imposing such requirements on public sector entities is likely to involve undue cost and effort for the entities applying the requirements.

CHAPTER 5: ELEMENTS

CONTENTS

	Paragraph
Introduction.....	5.1–5.5
Purpose of this Chapter	5.1
Elements and their Importance	5.2–5.4
Elements Defined	5.5
Assets.....	5.6–5.13
Definition	5.6
A Resource	<u>5.6A–5.7</u>
<u>Rights</u>	<u>5.7A–5.7G</u>
Service Potential and Economic Benefits	5.8–5.10
Presently Controlled by the Entity <u>as a Result of Past Events</u>	5.11–5.13
Past Event	5.13
Liabilities.....	5.14–5.26
Definition	5.14–5.14A
A Present Obligations	5.15
<u>Legal and Non-Legally Binding Obligations</u>	<u>5.15A–5.15F</u>
An Outflow of Resources <u>A Transfer of Resources</u> from the Entity	5.16–5.16F
<u>Present Obligations as a Result of Past Events</u>	5.17– 5.17D
Legal and Non-Legally Binding Obligations	5.18–5.26
Assets and Liabilities.....	5.26A–5.26K
Unit of Account	5.26A–5.26K
Net Financial Position, Other Resources, and Other Obligations.....	5.27–5.28
Net Financial Position, Other Resources, and Other Obligations	
5.27	As explained in paragraph 5.4, in some cases, in developing or revising an IPSAS, the IPSASB may determine that to achieve the objectives of financial reporting a resource or obligation that does not satisfy the definition of an element defined in the Conceptual Framework needs to be recognized in the financial statements. In these cases, the IPSAS may require or allow these resources or obligations to be recognized as other resources or other obligations, which are items additional to the six elements defined in this Framework.
5.28	Net financial position is the difference between assets and liabilities after adding other resources and deducting other obligations recognized in the statement of financial position. Net financial position can be a positive or negative residual amount.

Revenue and Expense	5.31–5.33
Definitions	5.31–5.33
Surplus or Deficit for the Period	5.34
Ownership Contributions and Ownership Distributions	5.35–5.39
Definitions	5.35–5.39
Basis for Conclusions.....	BC5.1–BC5.68

DRAFT

Introduction

Purpose of this Chapter

- 5.1 This Chapter defines the elements used in financial statements and provides further explanation about those definitions.

Elements and their Importance

- 5.2 Financial statements portray the financial effects of transactions and other events by grouping them into broad classes which share common economic characteristics. These broad classes are termed the elements of financial statements. Elements are the building blocks from which financial statements are constructed. These building blocks provide an initial point for recording, classifying and aggregating economic data and activity in a way that provides users with information that meets the objectives of financial reporting and achieves the qualitative characteristics of financial reporting while taking into account the constraints on information included in GPFRs.
- 5.3 The elements defined in this Chapter do not refer to the individual items that are recognized as a result of transactions and events. Sub-classifications of individual items within an element and aggregations of items are used to enhance the understandability of the financial statements. Presentation is addressed in Chapter 8, Presentation in General Purpose Financial Reports.
- 5.4 In some circumstances, to ensure that the financial statements provide information that is useful for a meaningful assessment of the financial performance and financial position of an entity, recognition of economic phenomena that are not captured by the elements as defined in this Chapter may be necessary. Consequently, the identification of the elements in this Chapter does not preclude IPSASs from requiring or allowing the recognition of resources or obligations that do not satisfy the definition of an element identified in this Chapter (hereafter referred to as “other resources” or “other obligations”) when necessary to better achieve the objectives of financial reporting.

Elements Defined

- 5.5 The elements that are defined in this Chapter are:
- Assets;
 - Liabilities;
 - Revenue;
 - Expense;
 - Ownership contributions; and
 - Ownership distributions.

Assets

Definition

- 5.6 An asset is:

A resource presently controlled by the entity as a result of ~~a~~ past events.

A Resource

5.6A A resource is a right to service potential or the capability to generate economic benefits, or both.

5.6B This section discusses three components of this definition:

- (a) Rights (paragraphs 5.7–5.7G);
- (b) Service potential and economic benefits (paragraphs 5.8–5.10); and
- (c) Present control as a result of past events (paragraph 5.11–5.13).

5.7 ~~A resource is an item with service potential or the ability to generate economic benefits. Physical form is not a necessary condition of a resource. The service potential or ability to generate economic benefits can arise directly from the resource itself or arises from the rights to use the resource. Some resources embody an entity's rights to a variety of benefits including, for example, the right to:~~

- ~~• Use the resource to provide services¹;~~
- ~~• Use an external party's resources to provide services, for example;~~
- ~~• Convert the resource into cash through its disposal;~~
- ~~• Benefit from the resource's appreciation in value; or~~
- ~~• Receive a stream of cash flows. [Deleted]~~

Rights

5.7A Rights to service potential or the capability to generate economic benefits take many forms, including:

- (a) Rights that correspond to an obligation of another party (see paragraph 5.16C), for example:
 - (i) Rights to receive cash.
 - (ii) Rights to receive services.
 - (iii) Rights to exchange resources with another party on favorable terms. Such rights include, for example, a forward contract to buy a resource on terms that are favorable.
 - (iv) Rights to benefit from an obligation of another party to transfer a resource if a specified uncertain future event occurs (see paragraph 5.16A).
- (b) Rights that do not correspond to an obligation of another party, for example:
 - (i) Rights over physical objects, such as property, plant and equipment or inventories. Examples of such rights are a right to use a physical object or right to benefit from a leased object; and
 - (ii) Rights to use intellectual property.

5.7B Many rights are established by binding arrangement, legislation, or similar means. For example, an entity might obtain rights from owning or leasing a physical object, from owning a debt instrument

¹ References to "services" in the Conceptual Framework encompass "goods".

such as a student loan, or from owning software or the right to use intellectual property. However, an entity might also obtain rights in other ways, for example:

- (a) By acquiring or creating know-how that is not in the public domain, such as a traffic management plan, or;
- (b) Through an obligation of another party that arises because that other party has no realistic alternative to avoid a transfer of resources (see paragraph 5.15).

5.7C Some goods and services—for example, employee services and services-in-kind—are received and immediately consumed. An entity's capability to obtain the service potential or economic benefits produced by such goods and services exists very briefly until the entity consumes the goods and services.

5.7D Not all of an entity's rights are assets of that entity—to be assets of the entity, the rights must (i) have service potential or economic benefits beyond those available to all other parties (see paragraphs 5.8-5.10) and (ii) be controlled by the entity (see paragraphs 5.11–5.12). For example, rights available to all parties without significant cost—for instance, rights of access to public goods that are controlled by other entities, such as public rights of way over land controlled by other entities, or know-how that is in the public domain—are typically not assets for the entities that hold these rights.

5.7E In principle, each of an entity's rights is a separate asset. However, for accounting purposes, related rights are often treated as a single unit of account that is a single asset (see paragraphs 5.26A–5.26I). For example, legal ownership of a physical object may give rise to several rights, including a right to:

- (a) Use the object;
- (b) Sell rights over the object; and
- (c) Pledge rights over the object.

5.7F In many cases, the set of rights arising from legal ownership of a physical item is accounted for as a single asset. Conceptually, the resource is the set of rights, not the physical item. Nevertheless, describing the set of rights as the physical item will often provide a faithful representation of those rights in the most concise and understandable way.

5.7G The relationship between sovereign rights, resources and an asset is discussed in paragraph 5.13.

Service Potential and Economic Benefits

5.8 Service potential is the ~~capacity~~ capability of a resource to provide services that contribute to achieving the entity's objectives. Service potential enables an entity to achieve its objectives without necessarily generating cash flows.

5.9 Public sector assets that embody service potential may include recreational, heritage, community, defense and other assets ~~which~~ that are held by governments and other public sector entities, and which are used to provide services to third parties. Such services may be for collective or individual consumption. Many services may be provided in areas in which market competition is limited or non-existent. ~~where there is no market competition or limited market competition~~. The use and disposal of such assets may be restricted as many assets that embody service potential are specialized in nature.

- 5.10 Economic benefits are cash inflows or a reduction in cash outflows. Cash inflows (or reduced cash outflows) may be derived from, for example:
- An asset's use in the production and sale of services;
 - The direct exchange of an asset for cash; ~~or other resources; or~~
 - Extinguishing or reducing a liability by transferring the asset.

Presently Controlled by the Entity as a Result of Past Events

- 5.11 An entity must have control of the resource. Control of the resource entails the ability of the entity to use the resource (or direct other parties on its use) so as to derive the benefit of the service potential or economic benefits embodied in the resource in the achievement of its service delivery or other objectives.
- 5.12 In assessing whether it presently controls a resource, an entity assesses whether the following indicators of control exist:
- Legal ownership;
 - Access to the resource, or the ability to deny or restrict access to the resource;
 - The means to ensure that the resource is used to achieve its objectives; and
 - The existence of an enforceable right to service potential or the capability to generate economic benefits arising from a resource.
- 5.12A Sometimes one party (a principal) engages another party (an agent) to act on behalf of, and for the benefit of, the principal. For example, a principal may engage an agent to arrange the distribution of goods controlled by the principal to eligible beneficiaries. If an agent has custody of a resource controlled by the principal, that resource is not an asset of the agent.

Past Event

- 5.13 The definition of an asset requires that a resource that an entity presently controls must have arisen from a one or more past transactions or other past events. The past transactions or other events that result in an entity gaining control of a resource and therefore an asset may differ. Entities can obtain assets by purchasing them in an exchange transaction or developing them. Assets may also arise through non-exchange transactions, including through the exercising of sovereign powers. The power to tax or to issue licenses and to access or restrict or deny access to the benefits embodied in intangible resources, like the electromagnetic spectrum, are examples of public sector-specific powers and rights that may give rise to assets. In assessing when an entity's control of rights to resources arise the following events may be considered: (a) a general ability to establish a power, (b) establishment of a power through a statute, (c) exercising the power to create a right, and (d) the event which gives rise to the right to receive resources from an external party. An asset arises when the power is exercised and the rights exist to receive resources.

Liabilities

Definition

- 5.14 A liability is:

A present obligation of the entity for ~~an outflow~~ a transfer of resources that results from a past events.

5.14A For a liability to exist three criteria must all be satisfied:

- (a) The entity has an obligation (paragraphs 5.15–5.15F)
- (b) The obligation is to transfer a resource (paragraphs 5.16A–5.16E)
- (c) The obligation is a present obligation arising from one or more past events (paragraphs 5.17–5.17D)

A-Present Obligations

5.15 Public sector entities can have a number of obligations. Obligations are binding when an entity has little or no realistic alternative to avoid them. A present obligation is a legally binding obligation (legal obligation) or non-legally binding obligation, which an entity has little or no realistic alternative to avoid. Obligations are not present obligations unless they are binding and there is little or no realistic alternative to avoid an outflow of resources.

Legal and Non-Legally Binding Obligations

5.15A Binding obligations can be legal obligations or non-legally binding obligations. Binding obligations can arise from both exchange and non-exchange transactions. An obligation must be to an external party in order to give rise to a liability. An entity cannot be obligated to itself, even where it has publicly communicated an intention to behave in a particular way. Identification of an external party is an indication of the existence of an obligation giving rise to a liability. However, it is not essential to know the identity of the external party before the time of settlement in order for a present obligation and a liability to exist.

5.15B Many arrangements that give rise to an obligation include settlement dates. The inclusion of a settlement date may provide an indication that an obligation involves an outflow a transfer of resources and gives rise to a liability. However, there are many agreements that do not contain settlement dates. The absence of a settlement date does not preclude an obligation giving rise to a liability.

Legal Obligations

5.15C A legal obligation is enforceable in law. Such enforceable obligations may arise from a variety of legal constructs. Exchange transactions are usually contractual in nature and therefore enforceable through the laws of contract or equivalent authority or arrangements. There are jurisdictions where government and public sector entities cannot enter into legal obligations, because, for example, they are not permitted to contract in their own name, but where there are alternative processes with equivalent effect. Obligations that are binding through such alternative processes are considered legal obligations in the Conceptual Framework. For some types of non-exchange transactions, judgment will be necessary to determine whether an obligation is enforceable in law. Where it is determined that an obligation is enforceable in law there can be no doubt that an entity has no realistic alternative to avoid the obligation and that a liability exists.

5.15D Some obligations related to exchange transactions are not strictly enforceable by an external party at the reporting date but will be enforceable with the passage of time without the external party

having to meet further conditions— or having to take any further action—prior to settlement. Claims that are unconditionally enforceable subject to the passage of time are enforceable obligations in the context of the definition of a liability.

5.15E Sovereign power is the ultimate authority of a government to make, amend and repeal legal provisions. Sovereign power is not a rationale for concluding that an obligation does not meet the definition of a liability in this Framework. The legal position should be assessed at each reporting date to consider if an obligation is no longer binding and does not meet the definition of a liability.

Non-Legally Binding Obligations

5.15F. Liabilities can arise from non-legally binding obligations. Non-legally binding obligations differ from legal obligations in that the party to whom the obligation exists cannot take legal (or equivalent) action to enforce settlement. Non-legally binding obligations that give rise to liabilities have the following attributes:

- The entity has indicated to other parties by an established pattern of past practice, published policies, or a sufficiently specific current statement that it will accept certain responsibilities;
- As a result of such an indication, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities; and
- The entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities.

An Outflow of Resources—A Transfer of Resources from the Entity

5.16 A liability must involve an outflow of resources from the entity for it to be settled. An obligation that can be settled without an outflow of resources from the entity is not a liability. [Deleted]

5.16A To satisfy the definition of a liability the obligation must have the potential to require the entity to transfer a resource to another party (or parties). For that potential to exist, it does not need to be certain, or even likely, that the entity will be required to transfer a resource—the transfer may, for example, be required only if a specified uncertain event occurs. It is only necessary that the present obligation exists, and that, at least in one circumstance, it would require the entity to transfer a resource.

5.16B An obligation can meet the definition of a liability even if the probability of a transfer of a resource is low. Nevertheless, that low probability might affect decisions about what information to provide about the liability and how to provide that information. Chapter 6 provides guidance on recognition and Chapter 7 provides guidance on measurement.

5.16C Obligations to transfer a resource include, for example:

- (a) Obligations to pay cash.
- (b) Obligations to provide services or deliver goods.
- (c) Obligations to exchange resources with another party on unfavorable terms. Such obligations include a forward contract to sell a resource on terms that are currently unfavorable or an option that entitles another party to purchase a resource from the entity.
- (d) Obligations to transfer a resource if a specified uncertain future event occurs.

- (e) Obligations to issue a financial instrument if that financial instrument will oblige the entity to transfer a resource.

5.16D Instead of fulfilling an obligation to transfer a resource to the party that has a right to receive the resource, entities may in some circumstances:

- (a) Settle the obligation by negotiating a release from the obligation.
(b) Transfer the obligation to a third party.
(c) Replace the obligation to transfer a resource with another obligation by entering into a new transaction.

5.16E In the situations identified in paragraph 5.16D an entity has an obligation to transfer a resource until it has settled, transferred, or replaced that obligation.

5.16F In a principal-agent relationship (see paragraph 5.12A), if the agent has an obligation to transfer to a third party a resource controlled by the principal, that obligation is not a liability of the agent. In such a case the resource that would be transferred is the principal's economic resource, not the agent's.

Present Obligations as a Result of Past Events

5.17 A present obligation is binding. To satisfy the definition of a liability, it is necessary that a present obligation arises as a result of one or more a past transactions and or other past events and requires an outflow of resources a transfer of resources from the entity. The complexity of public sector programs and activities means that a number of events in the development, implementation and operation of a particular program may give rise to obligations. For financial reporting purposes it is necessary to determine whether such commitments and obligations, including binding obligations that the entity has little or no realistic alternative to avoid but are not legally enforceable (non-legally binding obligations) are present obligations and satisfy the definition of a liability. Where an arrangement has a legal form and is binding, such as a contract, the past event may be straightforward to identify. In other cases, it may be more difficult to identify the past event and identification involves an assessment of when an entity has little or no realistic alternative to avoid an outflow of resources from the entity. In making such an assessment an entity takes jurisdictional factors into account.

5.17A A present obligation exists as a result of past events only if:

- (a) The entity has already obtained service potential or economic benefits or taken an action; and
(b) As a consequence, the entity will or may have to transfer a resource that it would not otherwise have had to transfer.

5.17B In the public sector, obligations may arise at a number of points. For example, in implementing a program or service:

- Making a political promise such as an electoral pledge;
- Announcement of a policy;
- Introduction (and approval) of the budget (which may be two distinct points); and

- The budget becoming effective (in some jurisdictions the budget will not be effective until an appropriation has been effected).

The early stages of implementation are unlikely to give rise to present obligations that meet the definition of a liability. Later stages, such as claimants meeting the eligibility criteria for the service to be provided, may give rise to present obligations that meet the definition of a liability.

5.17C The point at which an obligation gives rise to a liability depends on the nature of the obligation. Factors that are likely to impact on judgments whether other parties can validly conclude that the obligation is such that the entity has little or no realistic alternative to avoid a transfer ~~an outflow of resources~~ include:

- The nature of the past event or events that give rise to the obligation. For example, a promise made in an election is unlikely to give rise to a present obligation because an electoral pledge very rarely creates a valid expectation on the part of external parties that the entity has an obligation that it has little or no realistic alternative to avoid settling. However, an announcement in relation to an event or circumstance that has occurred may have such political support that the government has little option to withdraw. Where the government has committed to introduce and secure passage of the necessary budgetary provision such an announcement may give rise to a non-legally binding obligation;
- The ability of the entity to modify or change the obligation before it crystallizes. For example, the announcement of policy will generally not give rise to a non-legally binding obligation, which cannot be modified before being implemented. ~~Similarly, if an obligation is contingent on future events occurring, there may be discretion to avoid an outflow of resources before those events occur; and~~
- There may be a correlation between the availability of funding to settle a particular obligation and the creation of a present obligation. For example, where both a budget line item has been approved and linked funding is assured through an appropriation, the availability of contingency funding or a transfer from a different level of government, a non-legally binding obligation may exist. However, the absence of a budgetary provision does not itself mean that a present obligation has not arisen.

5.17D “Economic coercion,” “political necessity” or other circumstances may give rise to situations where, although the public sector entity is not legally obliged to incur an outflow of resources, the economic or political consequences of refusing to do so are such that the entity may have little or no realistic alternative to avoid an outflow of resources. Economic coercion, political necessity or other circumstances may lead to a liability arising from a non-legally binding obligation.

Legal and Non-Legally Binding Obligations

- 5.18 ~~Binding obligations can be legal obligations or non-legally binding obligations. Binding obligations can arise from both exchange and non-exchange transactions. An obligation must be to an external party in order to give rise to a liability. An entity cannot be obligated to itself, even where it has publicly communicated an intention to behave in a particular way. Identification of an external party is an indication of the existence of an obligation giving rise to a liability. However, it is not essential to know the identity of the external party before the time of settlement in order for a present obligation and a liability to exist. [Deleted]~~

- 5.19 ~~Many arrangements that give rise to an obligation include settlement dates. The inclusion of a settlement date may provide an indication that an obligation involves an outflow of resources and gives rise to a liability. However, there are many agreements that do not contain settlement dates. The absence of a settlement date does not preclude an obligation giving rise to a liability. [Deleted]~~
- 5.20 ~~A legal obligation is enforceable in law. Such enforceable obligations may arise from a variety of legal constructs. Exchange transactions are usually contractual in nature and therefore enforceable through the laws of contract or equivalent authority or arrangements. There are jurisdictions where government and public sector entities cannot enter into legal obligations, because, for example, they are not permitted to contract in their own name, but where there are alternative processes with equivalent effect. Obligations that are binding through such alternative processes are considered legal obligations in the Conceptual Framework. For some types of non-exchange transactions, judgment will be necessary to determine whether an obligation is enforceable in law. Where it is determined that an obligation is enforceable in law there can be no doubt that an entity has no realistic alternative to avoid the obligation and that a liability exists. [Deleted]~~
- 5.21 ~~Some obligations related to exchange transactions are not strictly enforceable by an external party at the reporting date but will be enforceable with the passage of time without the external party having to meet further conditions—or having to take any further action—prior to settlement. Claims that are unconditionally enforceable subject to the passage of time are enforceable obligations in the context of the definition of a liability. [Deleted]~~
- 5.22 ~~Sovereign power is the ultimate authority of a government to make, amend and repeal legal provisions. Sovereign power is not a rationale for concluding that an obligation does not meet the definition of a liability in this Framework. The legal position should be assessed at each reporting date to consider if an obligation is no longer binding and does not meet the definition of a liability. [Deleted]~~

Non-Legally Binding Obligations

- 5.23 ~~Liabilities can arise from non-legally binding obligations. Non-legally binding obligations differ from legal obligations in that the party to whom the obligation exists cannot take legal (or equivalent) action to enforce settlement. Non-legally binding obligations that give rise to liabilities have the following attributes:~~
- ~~• The entity has indicated to other parties by an established pattern of past practice, published policies, or a sufficiently specific current statement that it will accept certain responsibilities;~~
 - ~~• As a result of such an indication, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities; and~~
 - ~~• The entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities. [Deleted]~~
- 5.24 ~~In the public sector, obligations may arise at a number of points. For example, in implementing a program or service:~~
- ~~• Making a political promise such as an electoral pledge;~~
 - ~~• Announcement of a policy;~~
 - ~~• Introduction (and approval) of the budget (which may be two distinct points); and~~

- ~~The budget becoming effective (in some jurisdictions the budget will not be effective until an appropriation has been effected).~~
 - ~~The early stages of implementation are unlikely to give rise to present obligations that meet the definition of a liability. Later stages, such as claimants meeting the eligibility criteria for the service to be provided, may give rise to obligations that meet the definition of a liability.~~
[Deleted]
- 5.25 ~~The point at which an obligation gives rise to a liability depends on the nature of the obligation. Factors that are likely to impact on judgments whether other parties can validly conclude that the obligation is such that the entity has little or no realistic alternative to avoid an outflow of resources include:~~
- ~~The nature of the past event or events that give rise to the obligation. For example, a promise made in an election is unlikely to give rise to a present obligation because an electoral pledge very rarely creates a valid expectation on the part of external parties that the entity has an obligation that it has little or no realistic alternative to avoid settling. However, an announcement in relation to an event or circumstance that has occurred may have such political support that the government has little option to withdraw. Where the government has committed to introduce and secure passage of the necessary budgetary provision such an announcement may give rise to a non-legally binding obligation;~~
 - ~~The ability of the entity to modify or change the obligation before it crystallizes. For example, the announcement of policy will generally not give rise to a non-legally binding obligation, which cannot be modified before being implemented. Similarly, if an obligation is contingent on future events occurring, there may be discretion to avoid an outflow of resources before those events occur; and~~
 - ~~There may be a correlation between the availability of funding to settle a particular obligation and the creation of a present obligation. For example, where both a budget line item has been approved and linked funding is assured through an appropriation, the availability of contingency funding or a transfer from a different level of government, a non-legally binding obligation may exist. However, the absence of a budgetary provision does not itself mean that a present obligation has not arisen.~~[Deleted]
- 5.26 ~~“Economic coercion,” “political necessity” or other circumstances may give rise to situations where, although the public sector entity is not legally obliged to incur an outflow of resources, the economic or political consequences of refusing to do so are such that the entity may have little or no realistic alternative to avoid an outflow of resources. Economic coercion, political necessity or other circumstances may lead to a liability arising from a non-legally binding obligation.~~ [Deleted]

Assets and Liabilities

Unit of Account

- 5.26A The unit of account is the right or the group of rights, the obligation or the group of obligations, or the group of rights and obligations to which recognition criteria and measurement concepts are applied.
- 5.26B A unit of account is selected for an asset or liability when considering how recognition criteria and measurement concepts will apply to that asset or liability and to the related revenue and expense.

In some circumstances it may be appropriate to select one unit of account for recognition and a different unit of account for measurement. For example, arrangements may sometimes be recognized individually but measured as part of a portfolio of binding arrangements. For presentation and disclosure, assets, liabilities, revenue and expense may need to be aggregated or separated into components.

5.26C If an entity transfers part of an asset or part of a liability, the unit of account may change at that time, so that the transferred component and the retained component, become separate units of account.

5.26D A unit of account is selected to provide useful information, which implies that:

(a) The information provided about the asset or liability and about any related revenue and expense must be relevant. Treating a group of rights and obligations as a single unit of account may provide more relevant information than treating, each right or obligation as a separate unit of account if, for example, those rights and obligations:

(i) Cannot be or are unlikely to be the subject of separate transactions;

(ii) Cannot or are unlikely to expire in different patterns;

(iii) Have similar characteristics and risks;

(iv) Are used together in the operational activities conducted by an entity to provide service potential or to produce cash flows and are measured by reference to estimates of their interdependent service potential or future cash flows.

(b) Information provided about the asset or liability and about any related revenue or expense must faithfully represent the substance of a transaction or other event from which they have arisen. Therefore, it may be necessary to treat rights or obligations arising from different sources as a single unit of account, or to separate the rights or obligations from a single source. Equally, to provide a faithful representation of unrelated, rights or obligations, it may be necessary to recognize and measure them separately.

5.26E In selecting a unit of account it is also important to consider the cost-benefit constraint of financial reporting discussed in Chapter 3. In general, the costs associated with recognizing and measuring assets, liabilities, revenue and expense increase as the size of unit of account decreases. Hence, in general, rights or obligations arising from the same source are separated only if the resulting information is more useful and the benefits outweigh the costs.

5.26F Sometimes, both rights and obligations arise from the same source. For example, some binding arrangements establish both rights and obligations for each of the parties. If those rights and obligations are interdependent and cannot be separated, they constitute a single inseparable asset or liability and hence form a single unit of account.

5.26G Some binding arrangements, or portions of binding arrangements, may be equally unperformed—neither party has fulfilled any of its obligations or both parties have partially fulfilled their obligations to an equal extent.

5.26H The binding arrangements referred to in paragraph 5.26G establish a combined right and obligation to exchange resources. The right and obligation are interdependent and cannot be separated. Hence the combined right and obligation constitute a single asset or liability. The entity has an asset if the terms of the exchange are currently favorable; it has a liability if the term of the exchange

are currently unfavorable. Whether such an asset is included in the financial statements depends on both the recognition criteria (see Chapter 6) and the measurement basis selected for the asset and liability (see Chapter 7).

- 5.26I To the extent that either party fulfills its obligations under the binding arrangement, the binding arrangement changes character. If the reporting entity performs first under the binding arrangement that performance is the event that changes the reporting entity's right and obligation to exchange resources into a right to receive a resource. That right is an asset. If the other party performs first, that performance is the event that changes the reporting entity's right and obligation to exchange resources into an obligation to transfer a resource. That obligation is a liability.
- 5.26J Conversely, if rights are separable from obligations, it may sometimes be appropriate to group the rights separately from the obligations, resulting in the identification of one or more separate assets and liabilities. In other cases, it may be more appropriate to group separable rights and obligations in a single unit of account treating them as a single asset or a single liability.
- 5.26K Treating a set of rights and present obligations as a single unit of account differs from offsetting assets and liabilities. Offsetting occurs when an entity recognizes and measures both an asset and liability as separate units of account, but groups them into a single net amount in the statement of financial position. Offsetting classifies dissimilar items together and therefore is generally not appropriate.

Net Financial Position, Other Resources, and Other Obligations

- 5.29 As explained in paragraph 5.4, in some cases, in developing or revising an IPSAS, the IPSASB may determine that to achieve the objectives of financial reporting a resource or obligation that does not satisfy the definition of an element defined in the Conceptual Framework needs to be recognized in the financial statements. In these cases, the IPSAS may require or allow these resources or obligations to be recognized as other resources or other obligations, which are items additional to the six elements defined in this Framework.
- 5.30 Net financial position is the difference between assets and liabilities after adding other resources and deducting other obligations recognized in the statement of financial position. Net financial position can be a positive or negative residual amount.

Revenue and Expense

Definitions

- 5.31 Revenue is:
Increases in the net financial position of the entity, other than increases arising from ownership contributions.
- 5.32 Expense is:
Decreases in the net financial position of the entity, other than decreases arising from ownership distributions.
- 5.33 Revenue and expense arise from exchange and non-exchange transactions, other events such as unrealized increases and decreases in the value of assets and liabilities, and the consumption of assets through depreciation and erosion of service potential and ability to generate economic

benefits through impairments. Revenue and expense may arise from individual transactions or groups of transactions.

Surplus or Deficit for the Period

- 5.34 The entity's surplus or deficit for the period is the difference between revenue and expense reported on the statement of financial performance.

Ownership Contributions and Ownership Distributions

Definitions

- 5.35 Ownership contributions are:

Inflows of resources to an entity, contributed by external parties in their capacity as owners, which establish or increase an interest in the net financial position of the entity.

- 5.36 Ownership distributions are:

Outflows of resources from the entity, distributed to external parties in their capacity as owners, which return or reduce an interest in the net financial position of the entity.

- 5.37 It is important to distinguish inflows of resources from owners, including those inflows that initially establish the ownership interest, and outflows of resources to owners in their capacity as owners from revenue and expense. In addition to the injections of resources and the payment of dividends that may occur, in some jurisdictions it is relatively common for assets and liabilities to be transferred between public sector entities. Where such transfers satisfy the definitions of ownership contributions or ownership distributions they will be accounted for as such.
- 5.38 Ownership interests may arise on the creation of an entity when another entity contributes resources to provide the new entity with the capacity to commence operational activities. In the public sector, contributions to, and distributions from, entities are sometimes linked to the restructuring of government and will take the form of transfers of assets and liabilities rather than cash transactions. Ownership interests may take different forms, which may not be evidenced by an equity instrument.
- 5.39 Ownership contributions may take the form of an initial injection of resources at the creation of an entity or a subsequent injection of resources, including those where an entity is restructured. Ownership distributions may be: (a) a return on investment; (b) a full or partial return of investment; or (c) in the event of the entity being wound up or restructured, a return of any residual resources.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, the Conceptual Framework.

Scope of Chapter

- BC5.1 Respondents to the 2010 Consultation Paper, *Elements and Recognition in Financial Statements* (the 2010 Consultation Paper), questioned why the IPSASB was only addressing elements for the financial statements in this phase of the Framework. They suggested that IPSASB should also develop elements for economic and other phenomena in the more comprehensive areas of financial reporting outside the financial statements. The IPSASB acknowledges the merits of these views and the need to develop such elements in the future. However, the IPSASB decided that in order to put its future standard-setting activities for the financial statements on a sound and transparent footing it is important to deal firstly with the development of elements for the financial statements.
- BC5.2 The IPSASB acknowledges a view that cash inflows and cash outflows should be defined as elements of the cash flow statement. The IPSASB took the view that cash inflows and cash outflows are components of the elements identified in this Chapter, and that further guidance should be provided at standards level.

Limited Scope Update of Conceptual Framework

- BC5.2A In March 2020 the IPSASB initiated a Limited Scope Update of the Conceptual Framework. The Limited Scope Update reviewed the definitions of an asset and a liability against the definitions in the International Accounting Standards Board's Conceptual Framework, which was finalized in 2018. The guidance supporting the definitions was also reviewed to take account of experience in applying the Framework in standards development and maintenance.
- BC5.2B The Limited Scope Update also evaluated the case for including guidance on unit of account and executory contracts. The Conceptual Framework approved in 2014 did not address these issues.

Assets

The definition of an asset

- BC5.2C The definition of an asset in the 2014 Conceptual Framework approved was:
A resource presently controlled by the entity as a result of a past event
- BC5.2D The definition of an asset in the IASB's 2018 Framework is: A present economic resource controlled by the entity as a result of past events.
- BC5.2E Neither the IPSASB nor the IASB definitions included wording that could be interpreted as recognition thresholds, such as 'expected to flow.'
- BC5.2F The 2014 IPSASB and 2018 IASB definitions contain the same components—a resource/an economic resource; control; and a past event/past events. The only differences were:
- (a) The IASB uses the term 'economic resource', whereas the IPSASB uses the term 'resource'. The IPSASB took the view that a resource is inherently economic and that the

term 'economic resource' could be confusing in light of the guidance that items with service potential are resources as well as those with the capability to generate economic benefits.

- (b) The IASB attaches 'present' to 'economic resource' whereas the IPSASB Framework attaches 'presently' to control. The IASB's use of 'present economic resource' mirrors a present obligation for a liability. The use of 'presently controlled' in the IPSASB Framework is to emphasize that control of a resource has to be evaluated at the reporting date. The prospect of control in the future is not sufficient to meet the asset definition.
- (c) The IASB uses 'past events' (plural). The IPSASB used 'past event' (singular). The IPSASB formulation indicated that there need be only one past event in order for the definition to be met.

BC5.2G The IPSASB reaffirmed the rationale for using the terms 'resource' and 'presently controlled'.

BC5.2H The IPSASB considered that the use of the plural 'past events' rather than the singular 'past event' better conveys the point that resources can accumulate over time due to an initial past event and further past events. An example is a binding arrangement for the delivery of services. Recipients of resources from transfer providers accumulate assets as they incur eligible expenditure or complete specified activities in accordance with the binding arrangement. The term 'past events' includes a single past event.

BC5.2I The revised definition of an asset is therefore:

A resource presently controlled by the entity as a result of past events.

BC5.2J In the Limited Scope Update the IPSASB reviewed the sequencing of guidance and reconfigured the guidance so that it reflected the components of the definition of a liability more clearly.

A Resource

BC5.3 The 2014 Framework provided guidance that 'a resource provides benefits to an entity in the form of service potential or the capability ability to generate economic benefits or both. In reaching its conclusions on the nature of a resource the IPSASB considered whether the benefits of the resource must have already flowed to an entity in order for a resource to exist. However, the IPSASB concluded that resources themselves embody benefits—benefits that can be accessed by the entity that controls the rights to these benefits. The IPSASB also considered the nature of the benefits (see paragraphs BC5.7 and BC5.8) and control (see paragraphs BC5.9–BC5.14).

BC5.3A The 2014 Framework distinguished service potential and the capability to generate economic benefits that can arise directly from the resource itself from service potential and the capability to generate economic benefits that arise from the rights to use the resource.

BC5.3B The IASB 2018 Framework considered but decided not to make the distinction outlined in paragraph BC5.3A. The IASB took the view that 'ownership of a physical object arises because of rights conferred by law and that, although they differ in extent, the rights conferred by full legal ownership of a physical object and by a contract to use an object for 99% (or 50% or even 1%) of its useful life are all rights of one kind or another.' The IASB also considered that there may be inconsistencies of what constitutes legal ownership in different jurisdictions or at different dates. In summary, the IASB guidance reflects a view that legal ownership is a particular form of right rather than a separate phenomenon.

BC5.3C The IPSASB acknowledged the view that physical ownership gives rise to a specific type of control and that this should be reflected conceptually, and that, from an accountability perspective, a conceptual approach which might lead to underlying assets not being recognized risks not meeting the qualitative characteristic of understandability.

BC5.3D However, on balance, the IPSASB decided to adopt a more overtly rights-based approach. In particular the IPSASB found the view that legal ownership is a type of right rather than a separate phenomenon persuasive.

BC5.3E The IASB 2018 Framework acknowledged that in many cases the set of rights arising from legal ownership of a physical object is accounted for as a single asset. The IPSASB inserted paragraph 5.7F providing guidance that describing the set of rights as the physical item will often provide a faithful representation of those rights in the most concise and understandable way.

BC5.3F The IPSASB considered whether it should augment the guidance on a resource with guidance drawn from the IASB 2018 Framework. The IPSASB decided that the following guidance should be added on issues on which the 2014 Framework had previously been silent:

- Rights can be classified as those that correspond to an obligation of another party and those that do not correspond to an obligation of another party (paragraph 5.7A).
- Ways in which rights can be established (paragraph 5.7B).
- That when goods or services are received and immediately consumed an entity's right to obtain the service potential or/and economic benefits produced by such goods and services exists very briefly-until the entity consumes the goods or services.' This issue had arisen when the IPASB reconsidered the approach to recognition of in-kind services in its Revenue project (paragraph 5.7C).
- Noting that not all rights are assets of an entity (paragraph 5.7D).
- In principle each of an entity's rights is a separate asset (paragraph 5.7E).
- In many cases the set of rights arising from legal ownership of a physical object is accounted for as a single asset (paragraph 5.7F also noted above in paragraph BC5.3E).

Unconditional Rights and Executory Contracts

BC5.4 Unconditional rights to resources typically result from contracts or other binding arrangements that require provision of resources to the entity in the future. The IPSASB notes that there can be a large number of such rights and acknowledged that unconditional rights that represent service potential or the ability to generate economic benefits that are controlled by the entity as a result of a past event give rise to assets. Whether such assets are recognized depends on whether the recognition criteria have been satisfied. The IPSASB concluded that the consequences of application of the definition of an asset to unconditional rights should be addressed at standards level.

~~BC5.5 Executory contracts are binding arrangements where there is an unconditional right to receive resources and an equal present obligation to transfer resources to the counterparty in the future. Public sector entities are likely to engage in a large number of such arrangements. The IPSASB acknowledges the view that such arrangements may give rise to both assets and liabilities, as there is a right to receive resources and a present obligation to sacrifice resources, which the entity has no realistic alternative to avoid. [Deleted]~~

~~BC5.6 The IPSASB also acknowledges the view that recognizing assets and liabilities from executory contracts would involve the inclusion of potentially very large amounts of assets and liabilities in the statement of financial position and the statement of financial performance and that this may conflict with the qualitative characteristic of understandability. Whether assets and liabilities arise from rights and obligations in executory contracts will be determined by an assessment of whether those rights and obligations satisfy the definitions of elements and recognition criteria identified in the Conceptual Framework. Such assessments, and the approach to presentation in the financial statements of any elements arising from executory contracts, are considered at standards level. [Deleted]~~

Service Potential and Economic Benefits

BC5.7 The term “service potential” has been used to identify the capability ~~capacity~~ of an asset to provide services in accordance with an entity’s objectives. The term “economic benefits” has been used to reflect the capability ~~ability~~ of an asset to generate net cash inflows. Some argue that economic benefits include service potential. Others argue that service potential includes economic benefits—a further view is that the terms can be used interchangeably. The IPSASB considered whether the explanation of a resource should include a reference to both service potential and the ability to generate economic benefits.

BC5.8 The IPSASB noted that many respondents to the 2010 Consultation Paper and 2012 Exposure Draft, *Elements and Recognition in Financial Statements*, supported inclusion of a specific reference to service potential as a characteristic of an asset, because of the service delivery objectives of most public sector entities. The IPSASB therefore concluded that the explanation of a resource should include both the terms “service potential” and “economic benefits”. This approach acknowledges that the primary objective of most public sector entities is to deliver services, but also that public sector entities may carry out activities with the sole objective of generating net cash inflows.

BC5.8A In the Limited Scope Update the IPSASB reaffirmed the term ‘service potential’ as an attribute of a resource. In the description of service potential in paragraph 5.8 the IPSASB changed the wording ‘the capacity to provide services’ to ‘the capability to provide services’ because of the ambiguity of ‘capacity’. Capacity has the same meaning of ability, but in other usages can mean the adequacy, availability and volume of resources. It is used with this second meaning in ED 77, *Measurement*, such as in guidance on the cost approach. The IPSASB acknowledged that in many languages ‘capacity’ and ‘capability’ will translate similarly. In addition, the IPSASB made a modification to the wording of economic benefits in the description of a resource in paragraph 5.8 and acknowledged that an item can have both service potential and the capability to generate economic benefits. Guidance on the treatment of such assets is provided at standards level.

Control

BC5.9 The IPSASB considered whether control is an essential characteristic of an asset or whether other indicators should be identified as essential characteristics of an asset including:

- Legal ownership;
- The right to access, and to restrict or deny the access of external parties to, the resource;
- The means to ensure that the resources are used to achieve the entity’s objectives; and

- The existence of enforceable rights to service potential or economic benefits arising from a resource.

The IPSASB acknowledges the views of those who argue that control may be difficult to apply in some cases because it requires judgment to assess whether control exists. In addition, control can be erroneously applied to a resource in its entirety and not to the individual benefits that accrue from the resource. However, notwithstanding such difficulties, the IPSASB concluded that control is an essential characteristic of an asset because the presence of control facilitates the association of an asset with a specific entity.

- BC5.10 Legal ownership of a resource, such as a property or item of equipment, is one method of accessing the service potential or economic benefits of an asset. However, rights to service potential or the ability to generate economic benefits may exist without legal ownership of the underlying resource. For example, the rights to service potential or the ability to generate economic benefits through the holding and use of leased property are accessed without legal ownership of the leased asset itself. Therefore, legal ownership of the resource is not an essential characteristic of an asset. Legal ownership is, however, an indicator of control.
- BC5.11 The right to access a resource may give an entity the ability to determine whether to:
- Directly use the resource's service potential to provide services to beneficiaries;
 - Exchange the resource for another asset, such as cash; or
 - Use the asset in any of the other ways that may provide services or generate economic benefits.
- BC5.12 While access to a resource is crucial, there are resources to which an entity has access which do not give rise to assets, such as air. Therefore, the ability to access a resource must be supplemented by the ability to deny or restrict the access of others to that resource—for example, (a) an entity might decide whether to set an entrance fee to a museum and restrict access to those who do not pay the fee, and (b) government may control a natural resource under its land to which it can restrict the access of others. Legally enforceable claims to specific resources, such as a right of access to a road or a right to explore land for mineral deposits, could represent an asset to the holder. However, an entity may be able to access the service potential or ability to generate economic benefits associated with a resource in ways that do not require legal rights. The IPSASB took the view that the factors identified in paragraph BC5.9 are likely to be indicators of the existence of control rather than essential characteristics of the definition of an asset.
- BC5.13 The IPSASB also considered whether the economic ownership approach is a viable alternative to the control approach. The economic ownership approach focuses on an entity's exposure to the underlying economic attributes that contribute to an asset's value to the entity. Some respondents to the Exposure Draft, Elements and Recognition in Financial Statements, in supporting the control approach, commented on the complexity of the economic ownership approach. The IPSASB concluded that the economic ownership approach is subjective and difficult to operate, and therefore rejected this approach.
- BC5.14 The IPSASB considered whether an analysis of exposure to the risks and rewards of ownership is a useful indicator of control. The control approach focuses on the power of the entity to direct how the resource is used in order to benefit from the service potential and/or ability to generate economic benefits embodied in the resource. The risks and rewards approach focuses on an

entity's exposure to the underlying economic attributes that contribute to an asset's value to the entity and the related risks. Consideration of the risks and rewards associated with particular transactions and events, and which party to any transaction or event bears the majority of those risks and rewards, may be relevant and useful in identifying the nature of the asset controlled by parties to the transaction or event. It may also be useful in determining how to quantify and associate the economic rights and obligations with particular parties. However, it is not of itself an indicator of the party that controls an asset. The IPSASB therefore decided not to include the risks and rewards of ownership as an indicator of control.

BC5.14A In the Limited Scope Update the IPSASB noted that the IASB 2018 Framework included guidance on the principal-agent relationship. The 2014 IPSASB Framework did not include guidance that in principal-agent relationships custody of a resource controlled by a principal does not give rise to an asset of the agent. While this is implicit in paragraph 5.11, the IPSASB considered that explicit guidance would be useful to underpin standards-level guidance and have therefore inserted a new paragraph 5.12B. This clarifies that in principal-agent relationships custody of a resource controlled by a principal does not give rise to an asset of the agent. The IPSASB included equivalent guidance for liabilities in paragraph 5.16F.

Past Event

- BC5.15 Some respondents to the 2010 Consultation Paper and 2012 Exposure Draft argued that identification of a past transaction or other event which gives rise to the asset should be an essential characteristic of the definition of an asset. Others take the view that the identification of one or more past events is not necessary and should not therefore be an essential characteristic. They consider that such a requirement places undue emphasis on identifying the past event that gave rise to an asset. Such emphasis may be a distraction and lead to debates about which event is the triggering event instead of the more important issue of whether rights to resources exist at the reporting date. Those who take this view consider that the essential characteristic of an asset should be the existence of a resource. Some may accept that one or more a past events provides useful supporting evidence of the existence of an asset, but not that it should be an essential characteristic.
- BC5.16 Many respondents took the view that a past event should be identified as an essential characteristic of the definition of an asset. The IPSASB agrees with these respondents—in particular, that the complex nature of many public sector programs and activities means that there are a number of points at which control of a resource might arise. Therefore, the IPSASB concluded that identification of the appropriate past event is crucial in identifying whether an asset exists.
- BC5.17 The powers and rights of government are particularly significant for the identification of assets. The power to tax and issue licenses, and other powers to access or to deny or restrict access to the benefits embodied in intangible resources like the electromagnetic spectrum, are examples of sovereign powers. It is often difficult to determine when such powers give rise to a right that is a resource and asset of the entity.
- BC5.18 A government's power to establish a right to levy a tax or fee, for example, often begins a sequence of events that ultimately results in the flow of economic benefits to the government. The IPSASB considered two views of when an asset arises from the powers and rights of government to levy a tax or fee. The first view is that the government has an inherent power to tax at every reporting date and, therefore, that the general ability to levy taxes or fees is an asset. Proponents

of this view accept that such an asset is unlikely to be capable of faithfully representative measurement but argue that this should not deflect from an acknowledgement that government has a perpetual asset. The contrary view is that the power to levy taxes and fees must be converted into a right by legal means, and that such a right must be exercised or exercisable in order for an asset to come into existence. Many respondents to the Consultation Paper and Exposure Draft supported this latter view. The IPSASB agrees with these respondents. In particular, the IPSASB concluded that a government's inherent powers do not give rise to assets until these powers are exercised and the rights exist to receive service potential or economic benefits.

Liabilities

BC5.18A The definition of a liability in the 2014 Conceptual Framework was:

A present obligation of the entity for an outflow of resources that results from a past event

BC5.18B The definition of a liability in the IASB's 2018 Conceptual Framework is:

A present obligation of the entity to transfer an economic resource as a result of past events.

BC5.18C As for the asset definition (see above paragraphs BC5.2A–J) both IPSASB and IASB definitions contained the same or similar components—resources/an economic resource; outflow of resources/transfer of resources; and a past event/past events. The differences were:

- (a) As in the asset definitions, the IASB uses the term 'economic resource', whereas the IPSASB uses the term 'resource'. The IPSASB's reason for retaining the term 'resource' is in paragraph 5.2G.
- (b) The IASB definition replaced the term 'outflow of resources' with 'transfer of an economic resource'. This was largely because of the linkage of the term an outflow of resources with the expectation of such an outflow and therefore potential confusion with a recognition threshold.
- (c) As in the asset definition, the IASB uses 'past events' (plural). The IPSASB uses 'past event' (singular). The IPSASB formulation indicates that there need be only one past event in order for the definition to be met.

BC5.18D The IPSASB was persuaded by the adoption of the term transfer of resources and considered the standards-level implications of the adoption of the term "transfer of resources" in the revised definition of a liability at the standards-level.

BC5.18E The IPSASB noted that the term 'transfers' is defined in IPSAS 23, Revenue from Non-Exchange Transactions (Taxes and Transfers). A project to replace IPSAS 23 was underway at the time that the Limited Scope Update took place. The IPSASB concluded that any ambiguities or inconsistencies between conceptual and standards levels could be mitigated by adjustments to new defined terms and the provision of guidance on what a transfer of resources involves. Such guidance is in paragraphs 5.16A-5.16I

BC5.18F Consistent with the analysis for assets at BC5.2H the IPSASB considered that the use of the plural 'past events' rather than the singular 'past event' better conveys that present obligations that give rise to liabilities can accumulate over time due to an initial past event and further past events.

BC5.18G The revised definition of a liability is:

A present obligation of the entity for a transfer of resources that results from past events.

BC5.18H As for assets, the IPSASB considered the sequencing of guidance on liabilities and reconfigured the guidance so that it reflected the components of the definition of a liability more clearly. The revised structure also drew on the approach in the IASB's 2018 Framework in describing the characteristics of an obligation more clearly and linking a present obligation to a past event. This necessitated a relocation of guidance. The revised guidance is in paragraphs 5.14A–5.17D.

A Present Obligation

BC5.19 In considering when obligations are present obligations, the IPSASB accepts that a legal obligation gives rise to a present obligation. In some jurisdictions, public sector entities are not permitted to enter into certain legal arrangements, but there are equivalent mechanisms that give rise to a present obligation. Such mechanisms are considered legally binding. The IPSASB then considered how to classify obligations that are not legal obligations. The IPSASB noted that “constructive obligation” is a term embedded in standard-setting literature globally and has been used in IPSASs. However, it has proved difficult to interpret and apply in a public sector context. Therefore, the IPSASB considered alternative terminology, for example the term “a social or moral duty or requirement.” The IPSASB has concerns that the term “social” might be confused with political values and that the term “moral obligations” risks a perception that standard setters and preparers are arbiters of morality. Therefore, the IPSASB decided that making a distinction between “legally binding” and “non-legally binding obligations” is the most straightforward and understandable approach. The IPSASB considered and rejected the view that the term “non-legally binding obligations” might be interpreted as referring to obligations, the legality of which is questionable. Paragraphs BC5.30–BC5.34 discuss non-legally binding obligations and explain their meaning for the purposes of the Conceptual Framework.

A Transfer of Resources

BC5.19A The guidance on ‘an outflow of resources from the entity’ in the 2014 Conceptual Framework was limited to statements that ‘a liability must involve an outflow of resources from the entity for it to be settled and that an obligation that can be settled without an outflow of resources from the entity is not a liability.’

BC5.19B In IPSASB’s Revenue project some constituents indicated that ED 71, *Revenue without Performance Obligations*, was not clear on what gives rise to a liability in a binding arrangement. It became evident that this lack of clarity was partly attributable to uncertainty over what constitutes an outflow of resources from the entity.

BC5.19C The IPSASB noted that the IASB 2018 Framework includes guidance on the application of a transfer of resources. With appropriate changes for public sector terminology this guidance has been added in paragraphs 5.16A–5.16E of Chapter 5:

- (a) Paragraph 5.16A (states that the obligation must have the potential to require the entity to transfer a resource to another party. The transfer does not have to be certain or even likely and might be dependent on a specified uncertain future event occurring.
- (b) Paragraph 5.16B states that an obligation can meet the definition of a liability even if the probability of a transfer of a resource is low.

- (c) Paragraph 5.16C provides examples of obligations to transfer a resource.
- (d) Paragraph 5.16D indicates that rather than fulfill an obligation to transfer a resource to another party, entities may sometimes negotiate release, transfer the obligation to a third party or replace the obligation with another obligation by entering into a new transaction. This paragraph reflects that in the public sector an entity's ability to extinguish or reduce a present obligation other than by fulfillment may be limited.
- (e) Paragraph 5.16E states that in the situations described in paragraph 5.16D an entity has an obligation to transfer a resource until it has negotiated release, transferred or replaced the obligation.

BC5.19D The IPSASB emphasized that the ability to extinguish or reduce a present obligation by methods other than fulfillment does not mean that an entity has a realistic alternative of avoiding a transfer of resources and therefore a rationale for non-recognition of a present obligation as a liability, which otherwise meets recognition criteria.

Conditional and Unconditional Obligations

- BC5.20 In the context of a present obligation, the IPSASB considered whether “conditional” and “unconditional” obligations, “stand-ready obligations” and “performance obligations” might be present obligations.
- BC5.21 An unconditional obligation is one that stands on its own, independent of future events. Unconditional obligations give rise to liabilities if the definition of a liability is satisfied. A conditional obligation involves the possible occurrence of a future event, which may or may not be under the control of the reporting entity. The IPSASB concluded that it is possible for conditional obligations to give rise to liabilities as defined in the Conceptual Framework. Determining whether a conditional obligation satisfies the definition of a liability will involve consideration of the nature of the obligation and the circumstances in which it has arisen. Given the complexity of public sector programs and activities, identifying the past event (or events), which has (have) resulted in the entity having little or no realistic alternative to avoid an outflow of resources, often may not be straightforward. Guidance on whether conditional obligations that exist in particular arrangements or circumstances may give rise to liabilities consistent with the definitions identified in the Conceptual Framework is a standards-level issue.
- BC5.22 A variety of terms are used to describe present obligations that may arise from, or exist in conjunction with, conditional obligations in particular circumstances. Amongst these are stand ready-obligations and performance obligations. The characteristics of these obligations and the conclusions reached by the IPSASB in the context of the Conceptual Framework are outlined below.

Stand-Ready Obligations

- BC5.23 Stand-ready obligations are a type of conditional obligation. Stand-ready obligations require an entity to be prepared to fulfill an obligation if a specified uncertain future event outside the entity's control occurs (or fails to occur). The term stand-ready obligation is used to describe a liability that may arise in certain contractual circumstances, such as those related to insurance, certain financial instruments such as a derivative contract in a loss position, and for warranties where the entity has an obligation to transfer resources if a specified future event occurs (or does not occur). In such circumstances, there may be an identifiable past event and an outflow of

resources from the entity, although the exact identity of the party to whom settlement will be made will not generally be known.

- BC5.24 The 2010 Consultation Paper included a discussion of stand-ready obligations. Many respondents found the distinction between a stand-ready obligation and other conditional obligations ambiguous. The 2012 Exposure Draft explained that the term stand-ready obligation is not widely used in the public sector, and does not work well in certain public sector circumstances, and suggested that whether a stand-ready obligation gave rise to a liability is a standards-level issue. Some respondents did not agree with the explanation in the 2012 Exposure Draft, and expressed a view that the Conceptual Framework should provide guidance for use at the standards level on whether stand-ready obligations can give rise to liabilities in certain circumstances.
- BC5.25 A public sector entity's obligation to transfer resources to another entity in particular circumstances that may occur in the future includes, for example, as a potential lender of last resort and in support of programs that provide a wide range of social benefits. The existence of an obligation to transfer resources to another party in these circumstances may be dependent on ongoing satisfaction of a number of conditions of differing significance and nature that are subject to change by the government or public sector entity. The IPSASB is of the view that the circumstances in which liabilities arise as a consequence of the obligation of a public sector entity to transfer resources to other parties consistent with the terms of programs, and how such liabilities should be described and accounted for, should be considered at the standards level consistent with the principles established in the Conceptual Framework. The IPSASB decided that the Conceptual Framework should not resolve whether all obligations that might be classified as stand-ready meet the definition of a liability. The IPSASB also decided not to use the term "stand-ready obligation" in the Conceptual Framework.

Performance Obligations

- BC5.26 A performance obligation is an obligation in a contract or other binding arrangement between an entity and an external party to transfer a resource to that other party. Performance obligations are often explicitly stated in a contract or other arrangement. Not all performance obligations are explicit. For example, a statutory requirement may give rise to an implicit performance obligation of a public sector entity that is additional to the terms of an agreement or contract.
- BC5.27 A performance obligation also arises when an entity enters into an arrangement whereby it receives a fee and, in return, provides an external party with access to an asset of the government. The IPSASB concluded that it is not necessary to identify a specific external party for a performance obligation to arise, but it is important to analyze such obligations in order to determine whether they include a requirement to provide an outflow for a transfer of resources. Obligations that require an entity to provide access to a resource, but do not entail an outflow a transfer of resources do not give rise to liabilities. However, obligations that require an entity to forgo future resources may be liabilities. Performance obligations are often conditional obligations. Determining whether such obligations give rise to liabilities is dependent upon the terms of particular binding agreements and may vary between jurisdictions. The IPSASB concluded that the circumstances under which performance obligations give rise to liabilities should be considered at standards level.

Past Event

BC5.28 The IPSASB considered whether the definition of a liability should require the existence of a past transaction or other event. Some take the view that identification of a past event is not an essential characteristic of a liability, and that, consequently, there is no need for the definition of a liability to include a reference to a past event. These commentators argue that there may be many possible past events and that establishing the key past event is likely to be arbitrary. They suggest that the identification of a past event is not a primary factor in determining whether a liability exists at the reporting date. This view mirrors the opposition to the inclusion of a past event in the definition of an asset, which is discussed in paragraphs BC5.15–BC5.18.

BC5.29 The IPSASB acknowledges this view, but also noted that many respondents to the 2010 Consultation Paper and 2012 Exposure Draft consider that a past event is a characteristic of a liability. The IPSASB agrees with the view that the complexity of many public sector programs and activities and the number of potential points at which a present obligation might arise means that, although challenging, identification of the past event that gives rise to a liability is critical in determining when public sector liabilities should be recognized.

An incremental sacrifice of resources as a result of past events

BC5.29A In developing proposals on revenue the IPSASB acknowledged that the transfer of resources arising from a binding arrangement must be incremental in order to give rise to a liability. Paragraph 4.43 of the IASB 2018 Framework provides guidance that the concept 'as a result of past events' means that:

- (a) An entity has already obtained economic benefits or taken an action; and
- (b) As a consequence, the entity will or may have to transfer an economic resource that it would not otherwise have had to transfer. The activity increases the magnitude of the economic resources that the entity will or may have to transfer.

BC5.29B This guidance establishes a principle that, in order to meet the definition of a liability, the past events must give rise to an incremental sacrifice of resources. An obligation, which can be fulfilled without an incremental sacrifice of resources does not meet the definition of a liability.

Little or No Realistic Alternative to Avoid.

BC5.30 Some respondents to the 2012 Exposure Draft expressed concerns that the phrase “little or no realistic alternative to avoid” in the description of a present obligation is open to different interpretations. They proposed removal of the words “little or” from this phrase in order to reduce the potential for misinterpretation. The IPSASB considered this proposal. The IPSASB was concerned that such a change might be interpreted as establishing a threshold test of virtual certainty in determining whether a present obligation exists. The IPSASB considers such a threshold too high. Consequently, the IPSASB confirmed that a present obligation is a legally binding or non-legally binding requirement that an entity has little or no realistic alternative to avoid.

BC5.31 Determining when a present obligation arises in a public sector context is complex and, in some cases, might be considered arbitrary. This is particularly so when considering whether liabilities can arise from obligations that are not enforceable by legal or equivalent means. In the context of programs to deliver social benefits there are a number of stages at which a present obligation can arise and there can be significant differences between jurisdictions, even where programs

are similar, and also over time within the same jurisdiction—for example, different age cohorts may have different expectations about the likelihood of receiving benefits under a social assistance program. Assessing whether a government cannot ignore such expectations and therefore has little or no realistic alternative to transfer resources may be subjective. This gives rise to concerns that such subjectivity undermines consistency in the reporting of liabilities, and can also impact adversely on understandability. Some therefore take the view that an essential characteristic of a liability should be that it is enforceable at the reporting date by legal or equivalent means.

- BC5.32 A converse view is that where a government has a record of honoring obligations, failing to recognize them as liabilities leads to an overstatement of that government's net financial position. According to this view, if a government has a consistent record of raising citizen expectations through publicly-announced obligations to provide financial support—for example to the victims of natural disasters—and has met such obligations in the past, a failure to treat such obligations as liabilities is not in accordance with the objectives of financial reporting, and leads to the provision of information that does not meet the qualitative characteristics of faithful representation and relevance.
- BC5.33 On balance, the IPSASB agrees with those who argue that, in the public sector, liabilities can arise from binding obligations that the entity has little or no realistic alternative to avoid, even if they are not enforceable in law. The IPSASB decided to use the term “non-legally binding obligations” for such obligations in the Conceptual Framework. However, the IPSASB acknowledges the views of those who are skeptical that liabilities can arise from obligations that are not legally enforceable. Consequently, paragraph 5.23 5.15F of this Chapter identifies the attributes that a non-legally binding obligation is to possess for it to give rise to a liability.
- BC5.34 The wide variation in the nature of public sector programs and operations, and the different political and economic circumstances of jurisdictions globally, means that categorical assertions of the circumstances under which obligations not enforceable in law become binding and give rise to present obligations are inappropriate. However, the IPSASB is of the view that present obligations are extremely unlikely to arise from election pledges. This is because electoral pledges will very rarely, (a) create a valid expectation on the part of external parties that the entity will honor the pledge, and (b) create an obligation which the entity has no realistic alternative but to settle. Therefore, the Framework includes a presumption that liabilities do not arise from electoral pledges. However, it is accepted that in practice a government with a large majority will be better placed to enact intended legislation than a minority government, and that there may be infrequent circumstances where a government announcement in such circumstances might give rise to a liability. In assessing whether, in these circumstances, a non-legally binding obligation gives rise to a liability the availability of funding to settle the obligation may be an indicator. This is discussed in paragraph 5.25.

Sovereign Power to Avoid Obligations

- BC5.35 The sovereign power to make, amend and repeal legal provisions is a key characteristic of governments. Sovereign power potentially allows governments to repudiate obligations arising from both exchange and non-exchange transactions. Although in a global environment such a power may be constrained by practical considerations, there are a large number of examples of governments defaulting on financial obligations over the last century. The IPSASB considered the impact of sovereign power on the definition of a liability. The IPSASB concluded that failing

to recognize obligations that otherwise meet the definition of a liability on the grounds that sovereign power enables a government to walk away from such obligations would be contrary to the objectives of financial reporting and, in particular, may conflict with the qualitative characteristics of relevance and faithful representation. Many respondents to the Consultation Paper and the Exposure Draft supported this position. The IPSASB therefore concluded that the determination of the existence of a liability should be by reference to the legal position at the reporting date.

Commitments

BC5.36 Commitment accounting procedures are a central component of budgetary control for public sector entities in many jurisdictions. They are intended to assure that budgetary funds are available to meet the government's or other public sector entity's responsibility for a possible future liability, including intended or outstanding purchase orders and contracts, or where the conditions for future transfers of funds have not yet been satisfied. Commitments which satisfy the definition of a liability and the recognition criteria are recognized in financial statements, in other cases information about them may be communicated in notes to the financial statements or other reports included in GPFRs. The IPSASB concluded that commitment accounting might be addressed in the future when dealing with elements for the more comprehensive areas of general purpose financial reporting outside the financial statements.

Unit of Account and Executory Contracts

Unit of Account

BC5.36A The IASB 2018 Framework describes unit of account as 'the right or the group of rights, the obligation or the group of obligations, or the group of rights and obligations, to which recognition criteria and management concepts apply.'

BC5.36B The IPSASB took the view that unit of account was a standards-level issue during the development of the IPSASB Framework and there was no guidance on unit of account. Since 2014 the importance of decisions on the unit of account has been highlighted in a number of projects and led the IPSASB to reevaluate the case for high-level guidance.

BC5.36C The IPSASB decided that guidance in the Conceptual Framework would be beneficial in informing standards-level requirements and guidance on unit of account. The IPSASB drew on the IASB 2018 Framework for this guidance, which is in paragraphs 5.26A-5.26I. The term 'obligations' includes 'present obligations.' The guidance on consideration of how the selection of a unit of account provides useful information in the IASB 2018 Framework is in the context of the qualitative characteristics of relevance and faithful representation. Other QCs may need to be taken into account in assessing whether information is useful in determining the unit of account.

Executory Contracts

BC5.36D The IPSASB 2014 Framework does not include guidance on executory contracts. In the Limited Scope Update, the IPSASB evaluated whether guidance should be added to the Framework.

BC5.36E The IASB 2018 Framework describes an executory contract as 'a contract or a portion of a contract, that is equally unperformed—neither party has fulfilled any of its obligations, or both parties have partially fulfilled their obligations to an equal extent.'

BC5.36F The IPSASB noted that the term 'contract' has been problematic in some jurisdictions. This is because some public sector entities may not have powers to enter into contracts, although they may be able to enter into other binding arrangements. Consequently, the term 'contract' has not been used widely in the Conceptual Framework. At the standards level the term 'binding arrangement' has been generally used. The IPSASB concluded that the principles of executory contract accounting could be incorporated in the section on Unit of Account and that a separate section on Executory Contracts is unnecessary. This guidance is in paragraphs 5.26G–5.26I.

Net Financial Position, Other Resources and Other Obligations

BC5.37 This section of the Basis for Conclusions outlines the IPSASB's approach to models of financial performance to be reported in the financial statements, and specifically the treatment of deferred inflows and deferred outflows.

Consultation Paper, Elements and Recognition in Financial Statements

BC5.38 The 2010 Consultation Paper discussed two contrasting approaches to financial performance:

- An approach that measures financial performance as the net result of all changes in the entity's resources and obligations during the period. This was described as the asset and liability-led approach; and
- An approach that measures financial performance as the result of the revenue inflows and expense outflows more closely associated with the operations of the current period. This was described as the revenue and expense-led approach.

BC5.39 The 2010 Consultation Paper noted that the two different approaches could lead to different definitions of the elements related to financial performance and financial position. The revenue and expense-led approach is strongly linked to the notion of inter-period equity. Inter-period equity refers to the extent to which the cost of programs and providing services in the reporting period is borne by current taxpayers and current resource providers. The asset and liability-led approach is linked to the notion of changes in resources available to provide services in the future and claims on these resources as a result of period activity

BC5.40 A further section of the 2010 Consultation Paper discussed Other Potential Elements and pointed out that, if IPSASB adopted the revenue and expense-led approach, IPSASB would need to address deferred flows. Under this approach, deferred flows are items that do not meet the proposed definitions of revenue and expense, but which are nevertheless considered to affect the financial performance of the period. The Consultation Paper identified three options for dealing with such flows:

- Defining deferred inflows and deferred outflow as elements on the statement of financial position;
- Broadening the asset and liability definitions to include items that are deferrals; or
- Describing deferred flows as sub-classifications of net assets/net liabilities (subsequently referred to as the residual amount).

BC5.41 The 2010 Consultation Paper had two specific matters for comment on these areas. The first asked constituents to indicate whether they preferred the asset and liability-led approach or revenue and expense-led approach and to indicate their reasons. The second asked whether deferred inflows and deferred outflows need to be identified on the statement of financial position.

If respondents supported identification on the statement of financial position they were asked to indicate which of the three approaches in paragraph BC5.40 they supported.

- BC5.42 The responses to these specific matters for comment were inconclusive. A small majority of respondents expressing a view favored the asset and liability-led approach. However, a number of respondents who supported the asset and liability-led approach also indicated that they favored identifying deferrals on the statement of financial position. The IPSASB took these views into account in the development of the at 2012 Exposure Draft stage.

Exposure Draft, Elements and Recognition in Financial Statements

- BC5.43 The 2012 Exposure Draft expressed a view that it is important to be able to distinguish flows that relate to the current reporting period from those that relate to specified future reporting periods. The 2012 Exposure Draft therefore proposed the following definitions of a deferred inflow and a deferred outflow:

- *A deferred inflow is an inflow of service potential or economic benefits provided to the entity for use in a specified future reporting period that results from a non-exchange transaction and increases net assets; and*
- *A deferred outflow is an outflow of service potential or economic benefits provided to another entity or party for use in a specified future reporting period that results from a non-exchange transaction and decreases net assets.*

- BC5.44 The two key features of these definitions were:

- The proposed elements were restricted to non-exchange transactions; and
- The flows had to be related to a specified future period.

- BC5.45 The IPSASB's rationale for including these characteristics were as risk-avoidance measures to reduce the possibility of deferred inflows and deferred outflows being used widely as smoothing devices, and to ensure that deferred inflows and deferred outflows are not presented on the statement of financial position indefinitely. The Exposure Draft included two Alternative Views. The first Alternative View considered the meaning of net financial position to be unclear in light of the combined impact of deferred inflows and deferred outflows. The second Alternative View disagreed with the view that deferred inflows and deferred outflows should be identified and recognized as separate elements and expressed a view that these flows meet the definitions of revenue and expense.

- BC5.46 Many respondents disagreed with defining deferred inflows and deferred outflows as elements. Some expressed reservations about the implications for alignment with the International Accounting Standards Board's Conceptual Framework, and International Financial Reporting Standards more generally. A number of respondents considered that the proposed approach did not reflect economic reality and that it would be more difficult to determine an objective basis for deferring revenue and expense under the revenue and expense-led approach. Nevertheless, a number of respondents also expressed the view that information on flows relating to particular reporting periods has information value.

- BC5.47 The rationale for restricting the definitions to non-exchange transactions was challenged as conceptually weak both by respondents who favored defining deferred inflows and deferred outflows as elements and those opposed to these proposed elements. Respondents also

disagreed with the restriction to specified time periods, because it would potentially lead to the different accounting treatment of very similar transactions dependent upon whether a specific period was identified—a grant without conditions receivable by an entity to finance its general activities for a five year period would have met the definition of a deferred inflow, whereas a similar grant for a future unspecified period would have met the definition of revenue.

Finalizing the Elements Chapter

BC5.48 The IPSASB considered that it needed to balance the limited support for the proposals on deferred flows in the 2012 Exposure Draft, and the perceived needs of users for information about flows relating to particular reporting periods.

BC5.49 The IPSASB therefore considered five options (A–E below) in responding to input from the due process and its perception of users' information needs:

- A. Defining deferred inflows and deferred outflows as elements in a more principles-based manner and not specifying the financial statements in which the elements are to be recognized. As such, the Conceptual Framework would not predetermine the presentation of the elements
- B. Deriving the definitions of revenue and expense from the asset and liability definitions;
- C. Broadening the asset and liability definitions;
- D. Accepting that certain economic phenomena that do not meet the definition of any element may need to be recognized in financial statements in order to meet the objectives of financial reporting; and
- E. Reporting inflows and outflows that provide service potential or economic benefits, but do not affect assets and liabilities as defined in the Framework and reporting inflows and outflows that do not affect revenue and expense

BC5.50 The IPSASB ~~does~~ did not consider that defining deferred inflows and deferred outflows as elements in Option A is justified in light of the objections that respondents had made to the proposals in the 2012 Exposure Draft. The IPSASB therefore rejected Option A.

BC5.51 The IPSASB considered two variants of Option B. In the first variant deferred flows would be taken directly to surplus/deficit, while in the second variant deferred flows would initially be taken to residual amount and then recycled to surplus/deficit in the period that time stipulations occur.

BC5.52 The IPSASB considers that taking deferred flows directly to surplus/deficit under the first variant of Option B may not produce information that is representationally faithful of an entity's sustainable performance and therefore does not meet the objectives of financial reporting. The second variant of Option B relies on recycling and, in the view of some IPSASB members would have implicitly introduced the notion of "other comprehensive income" into the Framework. The IPSASB has strong reservations about such a development. For these reasons the IPSASB rejected Option B.

BC5.53 The IPSASB noted that Option C would require changes to the definitions of an asset and a liability so that:

- The definition of an asset would include resources that an entity does not control; and
- The definition of a liability would include obligations that are not present obligations.

The IPSASB considers that such changes would distort the essential characteristic of an asset—that an entity controls rights to resources—and the essential characteristic of a liability—that an entity has a present obligation for an outflow of resources. In the view of the IPSASB this would make assets and liabilities less easily understandable. Adoption of such an option would also be a departure from globally understood definitions of an asset and a liability. For these reasons the IPSASB rejected Option C

- BC5.54 Option E was a hybrid approach that involved components of the other four options. It would allow reporting of inflows and outflows that provide service potential or economic benefits, but would not affect the definitions of an asset and liability and the reporting of inflows and outflows that do not affect revenue and expense as defined in the Framework. The idea of this approach was to acknowledge that further conceptual thinking on financial performance is necessary.
- BC5.55 Option D is broader than Option E because it is not necessarily restricted to deferred flows, but could encompass broader economic phenomena—for example obligations that are not present obligations, because, although they contain performance obligations, it is not clear that they require an outflow of resources. Option D acknowledges that there may be circumstances under which the six elements defined in the Conceptual Framework may not provide all the information in the financial statements that is necessary to meet users' needs. In the view of the IPSASB it is transparent to acknowledge that other items may be recognized. Unlike Option A, Option D does not involve defining additional elements, and, unlike Option C, Option D does not involve modification of generally understood definitions of an asset and a liability.
- BC5.56 The IPSASB concluded that Option D provides the most transparent approach. The terms “other obligations” and “other resources” are used to describe these economic phenomena in the Conceptual Framework. Option D also enhances the accountability of the IPSASB because the circumstances under which other obligations and other resources will be recognized will be determined at standards level and explained in the Bases for Conclusions of specific standards.

Financial Statements

- BC5.57 Net financial position is the aggregate of an entity's net assets (assets minus liabilities) and other resources and other obligations recognized in the statement of financial position at the reporting date. Where resources and obligations other than those that meet the definition of the elements are recognized in the financial statements, the amounts reported as net assets and net financial position will differ. In these circumstances, the interpretation of net financial position will be determined by reference to the nature of the other resources and other obligations recognized in the financial statements under the relevant IPSAS.
- BC5.58 The IPSASB considered whether it should use both the terms “net assets” and “net financial position” in the Conceptual Framework. The IPSASB acknowledges a view that net assets is a generally understood term. However, the IPSASB considered that using both terms could be confusing and therefore decided to use the term “net financial position” to indicate the residual amount of an entity.

Revenue and Expense

Gross or Net Increase in “Net Financial Position” in Definition of Revenue

BC5.59 The IPSASB considered whether the definition of revenue should specify that the increase in net financial position is “gross” or “net”. The IPSASB acknowledges that a gross approach might not be appropriate in areas such as the disposal of property, plant, and equipment where such an approach would require the full disposal proceeds to be recognized as revenue, rather than the difference between the disposal proceeds and the carrying amount. Conversely, a net approach might be similarly inappropriate in certain circumstances—for example, the sale of inventory. The IPSASB concluded that whether the increase in net financial position represented by revenue is presented gross or net should be determined at standards level, dependent on which treatment better meets the objectives of financial reporting.

Distinguishing Ordinary Activities from Activities outside the Ordinary Course of Operations

BC5.60 Some standard setters structure their definitions of elements so that, for example, inflows and outflows arising from transactions and events relating to activities in the ordinary course of operations are distinguished from inflows and outflows that relate to activities outside the ordinary course of operations. An example of this approach is to define revenue and expense as elements that relate to an entity’s “ongoing major or central operations,” and to define gains and losses as elements that relate to all other transactions, events and circumstances giving rise to increases or decreases in net assets.²

BC5.61 The IPSASB acknowledges that distinguishing transactions and events related to the ordinary course of operations from transactions and events outside the ordinary course of operations can provide useful information for users of the financial statements. Therefore, it may be useful to adopt the terms “gains and losses” to reflect inflows and outflows from transactions and events outside the ordinary course of operations. However, the IPSASB is of the view that, conceptually, gains and losses do not differ from other forms of revenue and expense, because they both involve net increases or decreases of assets and/or liabilities. The IPSASB also noted that many respondents to the 2010 Consultation Paper and 2012 Exposure Draft shared this view. Therefore, the IPSASB decided not to define gains and losses as separate elements.

Ownership Interests in the Public Sector

BC5.62 As discussed in more detail in BC5.66–BC5.70, the IPSASB considered whether, and, if so, under what circumstances, ownership interests exist in the public sector and whether transactions related to ownership interests should be excluded from the definitions of revenue and expense. Because transactions with owners, in their role as owners, are different in substance to other inflows and outflows of resources the IPSASB concluded that it is necessary to distinguish flows relating to owners from revenue and expense. Therefore, ownership contributions and ownership distributions are defined as elements and excluded from the definitions of revenue and expense.

² See, for example, Financial Accounting Standards Board, Statement of Financial Accounting Concepts No. 6, *Elements of Financial Statements*.

Surplus or Deficit in the Reporting Period

BC5.63 This chapter states that the difference between revenue and expense is the entity's surplus or deficit for the period. The IPSASB considered whether it should provide explanatory guidance on the interpretation of surplus or deficit. The IPSASB discussed a view that public sector entities have operating and funding models. According to this view a surplus provides an indicator of the ability of the entity to:

- Reduce demands for resources from resource providers;
- Increase either the volume and/or quality of services to recipients;
- Reduce debt (where an entity has debt-raising powers); or
- A combination of these factors.

BC5.64 Conversely a deficit provides an indicator of:

- The need to increase demands on resources from resource providers;
- Reduce either the volume and/or quality of services to recipients;
- Increase debt (where an entity has debt-raising powers); or
- A combination of these factors.

BC5.65 The IPSASB acknowledges that there is a need for greater clarity on the meaning of surplus or deficit in the public sector, and therefore that aspects of the above approach might be developed further in the future. However, the IPSASB considered the concept of an operating and funding model or business model is not well developed in the public sector, and that developing an operating and funding model appropriate for all public sector entities is problematic. Therefore, the IPSASB decided not to include guidance on the interpretation of surplus or deficit in the Conceptual Framework.

Ownership Contributions, and Ownership Distributions

BC5.66 The IPSASB considered whether net financial position is a residual amount, a residual interest or an ownership interest. The IPSASB acknowledges the view that the interest of resource providers and service recipients in the long-term efficiency of the entity, its capacity to deliver services in the future and in the resources that may be available for redirection, restructuring or alternative disposition is similar to an ownership interest. The IPSASB also accepts that the terms "residual interest" and "ownership interest" have been used in some jurisdictions to characterize third parties' interests in net assets. The term "residual interest" indicates that service recipients and resource providers have an interest in the capability of the entity to finance itself and to resource future operations. The term "ownership interest" is analogous to the ownership interest in a private sector entity and, for some, indicates that the citizens own the resources of the public sector entity and that government is responsible to the citizens for the use of those resources. Some supporters of this approach argue that it emphasizes the democratic accountability of governments.

BC5.67 The IPSASB is of the view that the term "residual interest" may also suggest that service recipients and resource providers have a financial interest in the public sector entity. Similarly, the term "ownership interest" may suggest that citizens are entitled to distributions from the public sector entity and to distributions of resources in the event of the entity being wound up. The

IPSASB therefore concluded that the terms “residual interest” and “ownership interest” can be misunderstood or misinterpreted, and that net financial position is a residual amount that should not be defined.

- BC5.68 However, the IPSASB acknowledges that part of net financial position can in certain circumstances be an ownership interest. Such instances may be evidenced by the entity having a formal equity structure. However, there may be instances where an entity is established without a formal equity structure, with a view to sale for operation as a commercial enterprise or by a private sector not-for-profit entity. An ownership interest can also arise from the restructuring of government or public sector entities, such as when a new government department is created. The IPSASB therefore considered whether ownership interests should be defined as an element. The IPSASB acknowledges the view that identifying the resources (or claims on future resources) attributable to owners provides information useful for accountability and decision-making purposes. The IPSASB concluded that such interests can be identified through the sub-classification of net financial position. However, the IPSASB also concluded that it is important to distinguish inflows of resources from owners and outflows of resources to owners, in their role as owners, from revenue, expense, other resources and other obligations. Therefore, ownership contributions and ownership distributions are defined as elements. Detailed guidance to support the assessment of whether certain inflows and outflows of resources satisfy the definitions of ownership contributions and ownership distributions will be developed at standards level, as appropriate.

International Public Sector Accounting Standards, Exposure Drafts, Consultation Papers, Recommended Practice Guidelines, and other IPSASB publications are published by, and copyright of, IFAC.

The IPSASB and IFAC do not accept responsibility for loss caused to any person who acts or refrains from acting in reliance on the material in this publication, whether such loss is caused by negligence or otherwise.

The 'International Public Sector Accounting Standards Board', 'International Public Sector Accounting Standards', 'Recommended Practice Guidelines', 'International Federation of Accountants', 'IPSASB', 'IPSAS', 'RPG', 'IFAC', the IPSASB logo, and IFAC logo are trademarks of IFAC, or registered trademarks and service marks of IFAC in the US and other countries.

Copyright © January 2022 by the International Federation of Accountants (IFAC). All rights reserved. Permission is granted to make copies of this work to achieve maximum exposure and feedback provided that each copy bears the following credit line: *"Copyright © January 2022 by the International Federation of Accountants (IFAC). All rights reserved. Used with permission of IFAC. Permission is granted to make copies of this work to achieve maximum exposure and feedback."*

