

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

**Meeting Location:** Washington, D.C., USA

**Meeting Date:** March 14—17, 2023

## Agenda Item 7

For:

- ☐ Approval  
☒ Discussion  
☐ Information

### CONCEPTUAL FRAMEWORK–LIMITED SCOPE UPDATE (CF-LSU) – PHASE TWO: PRUDENCE AND MATERIALITY

<b>Project summary</b>	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.	
<b>Project Staff Lead</b>	John Stanford, Senior Advisor	
<b>Board sponsor</b>	Ian Carruthers, IPSASB Chair (Bord Sponsor)	
<b>Meeting objectives</b>	<b>Topic</b>	<b>Agenda Item</b>
<b>Project management</b>	<a href="#">Conceptual Framework–Limited Scope Update (CF-LSU)–Next Stage: Project Roadmap</a>	<a href="#">7.1.1</a>
	<a href="#">Instructions up to Previous Meeting</a>	<a href="#">7.1.2</a>
	<a href="#">Decisions up to Previous Meeting</a>	<a href="#">7.1.3</a>
<b>Decisions required at this meeting</b>	<a href="#">Prudence</a>	<a href="#">7.2.1</a>
	<a href="#">Obscuring Information as a Factor Relevant to Materiality</a>	<a href="#">7.2.2</a>
<b>Other supporting items</b>	<a href="#">Updated Chapter 3, Qualitative Characteristics</a>	<a href="#">7.3.1</a>

## CONCEPTUAL FRAMEWORK NEXT STAGE: PROJECT ROADMAP

Meeting	Completed Actions or Discussions / Planned Actions or Discussions:
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 of Assets and Liabilities in Financial Statements</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.
February 2022	1. Publication of Exposure Draft 81
March 2022	1. First Review of Responses to Exposure Draft 76 2. Discussion of Issues
June 2022	1. Second Review of Responses to Exposure Draft 76 2. Discussion of Issues 3. Review Revised Chapter 7, <i>Measurement of Assets and Liabilities in Financial Statements</i>
September 2022	1. Third Review of Responses to ED 76: SMCs on Replacement Cost and Value in Use 2. Discussion of Issues 3. Initial Review of Responses to Exposure Draft 81
December 2022	1. Approve Revised Chapter 7, <i>Measurement of Assets and Liabilities in Financial Statements</i> 2. Second Review of Responses to Exposure Draft 81 3. Discussion of Issues
February 2023	1. Third Review of Responses to Exposure Draft 81 2. Discussion of Issues
March 2023	1. Fourth Review of Responses to Exposure Draft 81 2. Discussion of Issues 3. Review Revised Chapter 3, <i>Qualitative Characteristics</i> , 4. Approve Revised Chapter 5, <i>Elements in Financial Statements</i>

## Agenda Item 7.1.1

April 2023	1. Publication of revised Chapter 7, <i>Measurement of Assets and Liabilities in Financial Statements</i>
May 2023	1. Publication of revised Chapter 5, <i>Elements in Financial Statements</i>
June 2023	1. Approve Revised Chapter 3, <i>Qualitative Characteristics</i> , and Chapter 5, <i>Elements in Financial Statements</i>
July 2023	1. Publication of Revised, Chapter 3, <i>Qualitative Characteristics</i> , and Chapter 5, <i>Elements in Financial Statements</i>

**INSTRUCTIONS UP TO PREVIOUS MEETING**

Meeting	Instruction	Actioned
September 2022	1. No Instructions	1. N/A
February 2022	1. All instructions provided up until February 2021 were reflected in ED 81, <i>Conceptual Framework Update: Chapter 3, Qualitative Characteristics Chapter 5, Elements in Financial Statements</i>	1. All instructions provided up until February 2021 were reflected in the ED 81, <i>Conceptual Framework Update: Chapter 3, Qualitative Characteristics Chapter 5, Elements in Financial Statements</i>

**DECISIONS UP TO PREVIOUS MEETING**

Meeting	Decision	BC Reference
September 2022	1. No decisions	1. N/A
February 2022	1. All decisions provided up until February 2022 were reflected in the ED 81, <i>Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements in Financial Statements</i>	1. N/A

## **Prudence**

### **Question**

1. Does the IPSASB approve the recommendation in paragraph 2?

### **Recommendation**

2. Board Sponsor and staff recommend that the approach to prudence in ED 81, *Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements*, is retained in the updated Chapter 3, with some additional explanation of asymmetry.

### **Background**

3. Chapter 3, *Qualitative Characteristics*, of the 2014 Conceptual Framework deals with both qualitative characteristics (QCs) and constraints on information in general purpose financial reports. In the context of general purpose financial reporting, prudence is the exercise of caution when making judgments under conditions of uncertainty. The material on individual QCs in the 2014 IPSASB Framework is largely aligned with the IASB's 2010 Conceptual Framework, so that the IPSASB did not see the need for a public sector adaptation. Prudence was not included as a separate QC, and there was no reference to prudence as supporting other QCs in the core text of Chapter 3, *Qualitative Characteristics*.
4. The IPSASB reconsidered the role of prudence in the limited scope update project. The IPSASB concluded that prudence is insufficiently distinct from faithful representation to justify inclusion as an additional qualitative characteristic.
5. However, the IPSASB also decided 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 therefore decided to include two additional paragraphs in the core text of Chapter 3. This approach is consistent with that of the IASB in its 2018 Conceptual Framework (see below paragraph 6), and uses aligned wording with the exception of the deletion of a single sentence and minor differences in terminology. The additional paragraphs and the relevant extract from the Basis for Conclusions are at Appendix A.
6. Specific Matter for Comment 1 highlighted the additional paragraphs, 3.14A and 3.14B, and asked respondents whether they agreed with the approach.

### **Analysis**

#### *Approach to prudence in IASB 2018 Conceptual Framework*

7. The IASB's 2010 Conceptual Framework did not include prudence in its discussion of faithful representation. The IASB revised its approach to prudence in the 2018 Framework. The IASB did not include prudence as a QC, 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'.<sup>1</sup> The IPSASB drew on this revised approach in developing the guidance discussed above.

8. The IASB Framework continues by asserting that the exercise of prudence does not lead to overstatements or understatements of assets, liabilities, income, or expense. Furthermore, the exercise of prudence does not imply the need for asymmetry, although particular standards may contain asymmetric requirements.<sup>2</sup> The IASB gave an example of such asymmetry as the different thresholds for recognizing and disclosing contingent liabilities and contingent assets in IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*. These requirements and guidance are mirrored in IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*.<sup>3</sup>
9. The Basis for Conclusions explains that the IASB noted that different stakeholders have different interpretations of prudence and that this had led to confusion, which perhaps had exacerbated the diversity in use of the term. The IASB concluded that 'it would reduce the confusion by reintroducing the term with a clear explanation that caution works both ways, so that assets and liabilities are neither overstated nor understated.

## Public sector context

10. As discussed above, the material on individual QCs in the 2014 IPSASB Conceptual Framework is aligned with the IASB's 2010 Conceptual Framework, and so prudence is not included as a QC or referred to in the core text. In developing ED 81, the IPSASB did not identify any public sector reason to depart from the IASB's approach, and so the wording in the revised paragraphs is therefore aligned with that in the IASB's 2018 Framework.

## Responses to SMC 1

11. The quantitative summary of the responses on SMC 1 is in Table 1 below.

**Table 1—Responses to SMC 1: Prudence**

Response	Respondents	
	#	%
Agree	17	63
Partially Agree	5	19
Disagree	3	11
<b>Subtotal</b>	<b>25</b>	<b>93</b>
No Comment	2	7
<b>Total</b>	<b>27</b>	<b>100</b>

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<sup>1</sup> Cautious prudence' contrasts with 'asymmetric prudence' under which (a) the threshold for recognizing income and assets is higher than for expenses and liabilities and (b) measurement bases are selected that recognize losses at an earlier stage than gains.

<sup>2</sup> Paragraphs 2.15 & 2.16 of the 2018 IASB Framework.

<sup>3</sup> Whereas contingent liabilities are disclosed unless the possibility of an outflow of resources embodying economic benefits or service potential is remote. Contingent assets are disclosed where an inflow of economic benefits or service potential is probable.

*Respondents agreeing*

12. Staff has classified 17 respondents as agreeing with the addition of obscuring information as a factor related to materiality (R03, R06, R07, R08, R09, R10, R13, R14, R16, R17, R18, R21, R22, R23, R24, R26 and R27). Table 2 summarizes and analyzes issues raised by these respondents.

**Table 2—Issues Raised by Respondents Agreeing with Proposed Guidance on Prudence**

<b>Respondent(s)</b>	<b>Comment</b>	<b>Analysis</b>
R18 <i>Lack of clarity about what asymmetry is</i>	The only issue is ‘asymmetry’ – it would be helpful to provide additional guidance on what this means in this context.	Paragraph 3.14B provides guidance that ‘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.’ The paragraph then states that ‘Particular standards may contain asymmetric requirements where justified.’  There is no discussion of asymmetry in the Basis for Conclusions. In the development of the proposals the IPSASB decided not to go into detail on cautionary and asymmetric prudence. Staff thinks that an additional paragraph might provide a useful clarification.



R21 <i>Prudence and Resource Accounting</i>	<p>We agree with the revision to introduce prudence into the conceptual framework.</p> <p>A positive consequence of shifting from conservatism to prudence is that it may better support natural resource accounting. Under conservatism natural resources may not have been recognized because there was insufficient certainty they were assets. However, under prudence, natural resources may be necessary to recognize: it may be argued that it is prudent for an entity to recognize natural resources, because recognition would promote sustainability and accountability for their use and protection.</p>	<p>The IPSASB 2014 Conceptual Framework did not adopt or discuss 'conservatism' so there has not been any shift in approach. The question of recognition of Natural Resources is being considered at standards level in that project.</p>
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*Respondents partially agreeing*

13. Staff has classified five respondents as partially agreeing with the revised guidance (R1, R4, R12, R19 and R20). The issues raised by these respondents are summarized and analyzed in Table 3.

**Table 3—Issues Raised by Respondents Partially Agreeing with Proposed Guidance on Prudence**

<b><i>Respondent(s)</i></b>	<b><i>Comment</i></b>	<b><i>Analysis</i></b>
R01/R12 <i>Paragraph 3.14B too cryptic and insufficiently supported in Basis for Conclusions</i>	<p>We fully agree with paragraph 3.14A that well highlights the role of prudence in supporting neutrality and the correct assessment and reporting of assets and liabilities, rather than factoring in consequences of uncertainty in an arbitrary way, especially where liabilities are concerned.</p> <p>Further, we found that we had to look at the IASB's Conceptual Framework for an explanation of what paragraph 3.14B was really about. Paragraph BC2.37(b) of the IASB's Conceptual Framework actually refers to the notion of "asymmetric prudence" and explains that it refers for instance to expenses being recognised at an earlier stage than income would be. Then, paragraph BC2.42 states that asymmetric prudence cannot be systematically required for it may conflict in some instances with relevance and faithful representation. For that reason, the IASB</p>	<p>As noted above, in the development of the proposals the IPSASB decided not to go into detail on cautionary and asymmetric prudence. Staff considers that, without going into a lengthy discussion of cautious and asymmetric prudence, a limited further explanation in the Basis for Conclusions would be useful.</p>

	<p>eventually decided that the notion should not be included in the 2018 IASB Conceptual Framework.</p> <p>We would therefore recommend, that should paragraph 3.14B be retained, the IPSASB should envisage clarifying from the outset what asymmetric prudence is (R01)</p> <p>It is not clear what the expression "The exercise of prudence does not imply a need for asymmetry" refers to; therefore, it is considered necessary to provide greater clarity on the relationship between prudence and asymmetry between the accounting guidelines established in IPSASs. (R12)</p>	
<p>R4</p> <p><i>Fundamental and enhancing characteristics</i></p>	<p>There is no distinction between fundamental and enhancing characteristics.</p>	<p>Unlike the 2010 and 2018 IASB Conceptual Frameworks, the 2014 IPSASB Conceptual Framework does not distinguish fundamental characteristics and enhancing characteristics. This issue was not reopened in the limited scope project.</p>
<p>R19</p> <p><i>Prudence as broader than merely a qualitative characteristic</i></p>	<p>Prudence is broader than merely a qualitative characteristic of financial information. Prudence is inherent in the application of professional judgment and is necessary to achieve an appropriate balance amongst the qualitative characteristics while meeting the objectives of financial reporting. The IPSASB is asked to consider this broader view of prudence in finalizing its update to its conceptual framework.</p>	<p>Staff is of the view that the discussion of prudence is appropriate and is aligned with the IASB's 2018 Framework. The issue of appropriate balance between the QCs is addressed in paragraph 3.4 of Chapter 3.</p>

<p>R20 <i>Necessity of new paragraphs</i></p>	<p>Qualitative aspects are important in applying the prudence concept as they would help in cases where judgments have to be made in exercising faithful representation of information.</p> <p>Already addressed in the 2014 Conceptual Framework, with the removal of prudence as an accounting principle, and the fact that IPSASB has returned to it suggests that there still remain those who feel that public sector accounting should apply bias for purposes of prudence. To this extent the two additional paragraphs (3.14 and 3.14B) may provide useful clarification, although otherwise they appear to be already adequately addressed under the Conceptual Framework's definition of Faithful Representation.</p>	<p>Paragraph BC3.17E of the Basis for Conclusions acknowledged the case for retaining the approach in the 2014 Conceptual Framework because 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 therefore decided to include guidance 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 also consistent with the approach of the IASB in its 2018 Conceptual Framework.</p>
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*Respondents disagreeing*

14. Staff has classified three respondents as disagreeing with the revised guidance (R5, R15 and R25). The issues raised by these respondents are summarized and analyzed in Table 4.

**Table 4—Issues Raised by Respondents Disagreeing with Proposed Guidance on Prudence**

<b>Respondent(s)</b>	<b>Comment</b>	<b>Analysis</b>
R05/R025 <i>Dislocation between Framework and standards-level literature</i>	<p>Importantly, asymmetries are not rare: many asymmetric prudence manifestations have been observed in existing IFRS (Barker and McGeachin, 2015) which also apply to IPSAS (Lorson and Haustein, 2019). Therefore, we would suggest that the IPSASB should further reflect on situations where asymmetric prudence could support faithful representation and should provide these situations with a conceptual basis in the Conceptual Framework(R05).</p> <p>We would suggest that the IPSASB gives more prominence to asymmetric prudence in the Conceptual Framework. An analysis of the measurement requirements of IPSASs in relation to asymmetric prudence shows that asymmetric prudence can be found in terms of measurement in a significant number of standards. Annex 1 to this comment letter shows a total of 14 standards where asymmetric prudent requirements have been identified in IPSASs. Against this background, we see a risk that the role of asymmetric prudence is not sufficiently reflected in the CF which may lead to inconsistencies between IPSASB's Conceptual Framework and IPSASs at standards level. We suggest that the IPSASB considers the rationale for standards-level asymmetric requirements in the Conceptual Framework (R25).</p>	<p>Staff acknowledges that current standards-level literature includes various asymmetric requirements. R25's response includes a useful inventory of asymmetric requirements in the current suite of IPSAS. Many IPSAS with asymmetric requirements were developed from IASB literature.</p> <p>The Conceptual Framework establishes high-level principles for the prospective development and maintenance of IPSAS. Where the IPSASB judges that new asymmetric requirements should be introduced, or existing asymmetric requirements retained, explanations will be included in Bases for Conclusions for new or amended standards.</p>

<p>R05</p> <p><i>Asymmetric prudence more conducive to intergenerational equity</i></p>	<p>Cautious prudence would better contribute to the robustness of net assets measurement. However, the period in which prudence-induced revenues and expenses are recorded might not be the period in which the relevant risks originate – e.g., when an expense is initially classified as possible and only in later periods is it reclassified as probable. Moreover, strong incentives exist also in the public sector to overstate financial position and performance and to shift costs and deficits to future generations, especially for entities that are struggling to achieve break-even and when financial statements are used as instruments to enforce financial sustainability measures. From this perspective, asymmetric prudence (as defined for example in German standards) could better serve the pursuit of intergenerational equity and could be usefully retained as a distinct qualitative characteristic – as is currently the case both in the proposed EPSAS conceptual framework<sup>6</sup> and in German standards.</p>	<p>Staff is of the view that the general purpose financial statements should provide information that meets the objectives of financial reporting. They do this by reflecting financial position at the reporting date and financial performance in the reporting period in a way that meets the qualitative characteristics while bearing in mind the constraints of financial reporting. If risks change and necessitate a modification of accounting estimates this will be reflected in the accounting period in which the changes are identified.</p>
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<p>R15</p> <p><i>Prudence should be a standalone qualitative characteristic</i></p>	<p>We do not agree with this approach. Whilst we acknowledge that faithful representation would cover prudence, we are of the view that prudence should be regarded as a standalone qualitative characteristic. The exercise of caution in preparing financial statements is now more needed more than ever. The reason for this is because:</p> <ul style="list-style-type: none"> <li>• There is increasing need for judgement and estimation in presenting items in the financial statements and the fact that this is happening in environments of extreme uncertainty where change is also very rapid. For example, we have seen due to changes in technology natural monopolies for public sector entities going away overnight and sometimes rendering significant investments worthless. This requires more caution in presenting items in financial statements.</li> <li>• Increasingly public sector entities are now subject to scrutiny and expectation of performances by the different constituencies that they serve. We have seen increasingly jurisdictions where executives in those entities are given performance contracts and thus there is high risk for non-conservative approach in depicting items in the balance sheet especially where judgement and estimation is required.</li> </ul> <p>Due to the above, we are of the view that prudence which requires the exercise of caution should be regarded as a standalone qualitative characteristic.</p>	<p>Staff acknowledges these environmental factors, but in line with previous Board decisions does not see a clear public sector reason to depart from the IASB's approach.</p>
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**Way Forward**

15. Board Sponsor and staff do not think that the respondents who disagreed or partially disagreed with the approach to prudence in ED 81 made a sufficiently persuasive case for changing the approach. Staff does acknowledge that a number of IPSAS include asymmetrical requirements. Many of these requirements preceded the approval of the 2014 Conceptual Framework and have been used successfully in practice for many years. The Conceptual Framework establishes high-level principles for the prospective development and maintenance of IPSAS. Where the IPSASB judges that new asymmetric requirements should be introduced, or existing asymmetric requirements retained, explanations will be included in Bases for Conclusions for new or amended standards.
16. As the term 'asymmetry' is used in the core text in paragraph 3.14B staff believes that there is a case for insertion of a paragraph in the Basis for Conclusions to explain the term better. If members support this approach such a paragraph will be brought to the April 2023 check-in meeting or the June 2023 meeting.

**Decision Required**

17. Does the IPSASB agree with the Board Sponsor and staff [recommendation in paragraph 2](#) that the approach to prudence in ED 81, is retained in the updated Chapter 3, with some additional explanation of asymmetry?

**Appendix A**

**PROPOSED ADDITIONAL PARAGRAPHS ON PRUDENCE IN ED 81**

**Core Text**

- 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 where this is a consequence of decisions intended to select the most relevant information that faithfully represents what it purports to represent.

**Basis for Conclusions**

- BC3.17A The International Accounting Standards Board (IASB) revised its approach to prudence in the *Conceptual Framework for Financial Reporting*, published in 2018 (the IASB 2018 Conceptual 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 Conceptual 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 2014 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 Conceptual 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 Conceptual 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 Conceptual Framework.

## **Obscuring Information as a Factor Related to Materiality Judgments**

### **Question**

1. Does the IPSASB approve the recommendation in paragraph 2?

### **Recommendation**

2. Board Sponsor and staff recommend that guidance on obscuring information as a factor related to materiality judgments exposed in ED 81, *Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements*, should be included in revised Chapter 5, subject to deletion of the final sentence of paragraph 3.32A on the disclosure of material items that are not separately displayed or displayed sufficiently prominently on the face of a financial statement.

### **Background**

3. Chapter 3, *Qualitative Characteristics*, of the 2014 Conceptual Framework addressed both qualitative characteristics of information in general purpose financial reports (GPFRs) and constraints on information included in GPFRs.
4. Specific Matter for Comment (SMC) 2 asked whether respondents agreed with the addition of obscuring information to misstating and omitting information as a factor relevant to materiality judgments and if not, why not?

### **Analysis**

#### *Approach to obscuring information in International Accounting Standards Board (IASB) Conceptual Framework*

5. In its 2010 Conceptual Framework, the International Accounting Standards Board (IASB) treated materiality as an entity-specific aspect of relevance, whereas the IPSASB considered materiality a constraint on information included in general purpose financial reports (GPFRs).
6. The IASB made amendments to its 2018 Conceptual Framework to add obscuring information as a factor in influencing materiality. The IPSASB drew on these amendments in amending the 2014 guidance on materiality.

#### *Public Sector Issues*

7. Paragraphs 3.32-3.34 of Chapter 3 of the 2014 Conceptual Framework provides guidance on materiality. Paragraph 3.32 described information as material 'if its omission or misstatement 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.'
8. ED 81 proposed amending paragraph 3.32 to include obscuring information to the factors that can affect materiality. A further amendment to this paragraph proposed softening the threshold for determining if information is material, to 'could reasonably be expected to influence' rather than the more blunt 'could influence.' The IPSASB considered that obscuring information is a persistently difficult area in the public sector.
9. The IPSASB made minor modifications in paragraph 3.32A from the IASB amendments to reflect the broader scope of Chapter 3, which provides guidance on GPFRs rather than just the financial statements. The IPSASB added a final sentence (not in the IASB amendments) that '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.'

10. Paragraph 3.32A stated that it is not possible to specify a uniform quantitative characteristic or a uniform set of characteristics at which a particular type of information becomes material. The use of the word 'characteristic', rather than 'threshold' as in the IASB amendment also reflected the broader scope of the IPSASB guidance.
11. The proposed amendments and the Basis for Conclusions in ED 81 are at Appendix A.

## Responses to SMC 2

12. The quantitative summary of the responses on SMC 2 is in Table 1 below.

**Table 2—Responses to SMC 2: Obscuring Information as a Factor Related to Materiality Judgments**

Response	Respondents	
	#	%
Agree	23	85
Partially Agree	0	0
Disagree	2	8
<b>Subtotal</b>	<b>25</b>	<b>93</b>
No Comment	2	7
<b>Total</b>	<b>27</b>	<b>100</b>

## Respondents agreeing

13. Staff has classified 23 respondents as agreeing with the addition of obscuring information as a factor related to materiality (R01, R03, R04, R05, R06, R07, R08, R09, R10, R13, R15, R16, R17, R18, R19, R20, R21, R22, R23, R24, R25, R26, and R27). However, while agreeing to the main proposal, a number of these respondents expressed reservations about other aspects of the amendments. Table 2 summarizes and analyzes issues raised by these respondents.

**Table 2—Issues Raised by Respondents Agreeing with Proposed Guidance on Obscuring Information as a Factor Related to Materiality Judgments**

<i>Respondent(s)</i>	<i>Comment</i>	<i>Analysis</i>
R03, R10, R13 <i>Need for further clarification on what obscuring information is</i>	Notes that the determination of whether information has been obscured or not allow for a significant amount of judgement. Proposes that the Board include additional guidance on what constitutes "obscuring of information". This will ensure that minimal judgement is utilized. "Obscuring information" should include the following (as articulated in the IASB Conceptual framework):	Neither the current IASB Conceptual Framework nor the Basis for Conclusions include supporting examples. The examples highlighted in R03's response are in IAS 1, <i>Presentation of Financial Statement</i> ,  Staff thinks that the proposal of R10 and R13 has merit. However, on balance, staff

	<ul style="list-style-type: none"> <li>Utilization of unclear or vague language</li> <li>Disaggregation of similar information</li> <li>Aggregation of similar items (IPSASB Staff note: should be dissimilar items) (R03)</li> </ul> <p>Recommend that the IPSASB considers further clarifying what is meant by 'obscuring information'. This clarification could be provided in paragraph 3.32 or in a footnote to that paragraph. The clarification could explain that if financial statements include excessive amounts of detailed information, this could negatively affect a user's ability to find the information that the user needs to be able to make decisions, or to confirm that the entity has discharged its accountability. Therefore, for financial statements to provide useful information to users, it is important to ensure that material information is not obscured by immaterial information. (R10)</p> <p>Recommend that an explanation is included to assist stakeholders to understand the meaning of "obscuring" information, and guidance on assessing whether or when information would obscure other information in the financial statements. Preparers found the brief explanation in the basis for conclusions insufficient to fully understand the concept. If not included in the Conceptual Framework, such guidance may be suitable for the materiality practice statement. (R13)</p>	<p>considers that examples should be provided at the standards level or in guidance, rather than in the Conceptual Framework. The IPSASB has a project on presentation of financial statements.</p>
<p>R10/R17/R19/R25 <i>Appropriateness of final sentence of 3.32 on display and disclosure/Clarification of the circumstances in which an entity</i></p>	<p>Notes that the ED also proposes to add a final sentence to paragraph 3.32 of the IPSASB Conceptual Framework:</p> <p>Recommend not to add this proposed sentence to the Conceptual Framework, for the following reasons.</p>	<p>Staff agrees with the points made by R10, R17 and R19. In particular, staff accepts that there is a risk that the guidance, as drafted, might be misinterpreted and inadvertently undermine the</p>

<p><i>judges that a material item shall not be separately displayed.</i></p>	<p>(a) Firstly, we are not convinced that it is necessary to discuss the specific matter of display vs disclosures in the general materiality guidance in the Conceptual Framework.</p> <p>(b) Secondly, we think the wording of the proposed sentence on 'display and disclosure' is unclear and may not reflect the intent behind the sentence. The current drafting of the sentence seems to imply that when an entity did not display a material item with sufficient prominence (which implies an omission), the entity should remedy this by considering disclosure in the notes. (R10)</p> <p>Inconsistent with IASB's approach. IFRS requires that if items in the financial statements are material, such items shall first be disaggregated and separately presented. This is inconsistent with the procedure (of considering disclosure where a material item is not separately displayed. Do not believe this matter requires additional considerations specific to public sector entities.</p> <p>It is inappropriate to provide guidance on presentation in chapters other than Chapter 8.</p> <p>We believe the guidance given in the current Chapter 8 provides sufficient information. I the guidance on presentation needs to be amended in terms of materiality, such amendments should be made in Chapter 8 rather than in paragraph 3.32. (R17)</p> <p>While we recognize that the Conceptual Framework is to be read as a whole, as the sentence in paragraph 3.32 currently reads, the IPSASB's intent is not clear (R19)</p> <p>It might be worth clarifying the circumstances in which an entity judges</p>	<p>principle in paragraph 6.9 of the IPSASB 2014 Conceptual Framework that 'the failure to recognize items that meet the definition of an element and the recognition criteria is not rectified by the disclosure of accounting policies, notes or other explanatory detail.'</p> <p>In the view of staff R25's comment highlights the risk of this sentence.</p> <p>Staff therefore proposes that the final sentence of paragraph 3.32 is deleted.</p>
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	that a material item shall not be separately displayed. For instance, one possibility would be to refer to those cases in which the information is not relevant to an understanding of the entity's financial position or financial performance (please refer to IPSAS 1 paras. 89 and 104), as situations in which a material item does not require separate presentation. (R25)	
R15 <i>Basis for Conclusions focuses too much on obscuring material information by including immaterial information</i>	Think that there needs to be a bit more explanation on what obscuring information entails. As it looks, based on the text in paragraph BC3.32B it would seem as obscuring information is inclusion of immaterial information. We believe that obscuring is broader than that. By definition, obscuring means "make unclear or difficult to understand" We propose that this definition be added in the text.	Staff agrees and proposes that paragraph BC3.32B is amended to remove the reference to "the inclusion of immaterial disclosures", as this reference potentially risks giving insufficient emphasis to other ways in which information might be obscured.
R16 <i>More work required at the standards level</i>	Think that more work is still required at the Standards-level. (In response to IASB) we mentioned that one issue we presently are dealing with by having general, overarching objectives, as is currently the case with IAS 1 Presentation of Financial Statements (and more specifically IAS 1.9), without also having individual Standards-level disclosure objectives, is that there is not currently a strong basis to support the exclusion of less important disclosures that are specifically required by an IFRS standard.  Think this same issue exists in IPSAS and thus simply changing the definition of materiality will not be sufficient to lead to any meaningful change without also addressing this matter at the Standards-level. On that basis, we would encourage the IPSASB to articulate its plan to address similar disclosure issues under IPSAS standards.	Noted. The purpose of the Conceptual Framework is to provide the high-level principles with detailed implementation at the standards level. The Conceptual Framework alone will not lead to beneficial change.

<p>R22 <i>Importance of transparency</i></p>	<p>Agree with the addition of obscuring information as factor relevant to materiality judgements.</p> <p>However, we wish to highlight that as transparency is an important expression of the overarching qualities that financial reporting is to achieve or aspire to (as expressed in BC3.6), we believe that information is only obscured when there are limitations imposed by rules and regulations as well as due to national interest.</p>	<p>Staff accept that regulators and auditors have an important role to play in reducing the risk of material information being obscured.</p>
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## *Respondents disagreeing*

14. Staff has classified R11 and R12 as disagreeing with the addition of obscuring information as factor relevant to materiality. R11 considered that the proposals lacked clear instructions on the calculation and application of the concept of materiality, leading to an over-reliance on professional judgment.
15. R12 considered the proposal unclear since a new term is being added without a definition and full development. In the view of R12 the modification adds to confusion on the concept of materiality.

## **Way Forward**

16. Most respondents supported the proposal to add obscuring information to omitting and misstating information as factors that can adversely affect the judgments of the users of financial statements. Those who expressed reservations considered that the term 'obscuring' is unclear. Board Sponsor and staff consider that the purpose of the Conceptual Framework is to establish high-level principles not to go into detail and there is a risk if one aspect of obscuring information is emphasized. Board Sponsor and Staff does not think that the respondents who disagreed with the addition of obscuring information made a persuasive case for departing from the approach proposed in ED 81. They therefore do not recommend a change.
17. Board Sponsor and staff agrees with those who expressed reservations about the additional sentence on separate display and disclosure in paragraph 3.32. They agree with those respondents who considered that the sentence might be misinterpreted in light of the existing principle that disclosure is not an alternative to recognition in Chapter 6, Recognition in Financial Statements.

## **Decision Required**

18. Does the IPSASB agree with the Board Sponsor and staff recommendation in paragraph 2 that guidance on obscuring information as a factor related to materiality judgments should be included in revised Chapter 5, subject to deletion of the final sentence of paragraph 3.32A on the disclosure of material items that are not separately displayed or displayed sufficiently prominently on the face of a financial statement?

**Appendix A**

**GUIDANCE ON OBSCURING INFORMATION AS A FACTOR AFFECTING  
MATERIALITY IN ED 81 AND BASIS FOR CONCLUSIONS**

**CORE TEXT (Proposed changes are underlined or struck out)**

**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 ~~could~~ to 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 quantitative threshold 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.



## **Basis for Conclusions**

BC3.32A In 2018 the IASB amended IAS 1, *Presentation of Financial Statements*, and IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*. The amendments clarified 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 it suggests that, amongst other practices, 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 Conceptual 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 Conceptual Framework. In the Limited Scope Update the IPSASB did not reassess this classification. The IPSASB acknowledged that materiality can impact a number of qualitative characteristics.

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 BC3.32, the IPSASB concluded that additional guidance is not justified.