

Meeting: International Public Sector Accounting
Standards Board

Meeting Location: Zurich, Switzerland

Meeting Date: September 12–15, 2023

Agenda Item 7

For:

- ☒ Approval
☐ Discussion
☐ Information

IMPROVEMENTS

Project summary	To propose improvements to IPSAS and the IPSASB's Policy Paper, <i>Process for Reviewing and Modifying IASB Documents</i> .	
Project staff lead	<ul style="list-style-type: none"> João Fonseca, Principal 	
Meeting objectives	Topic	Agenda Item
Project management	Instructions up to Previous Meeting	7.1.1
	Decisions up to Previous Meeting	7.1.2
	Improvements: Project Roadmap	7.1.3
Decisions required at this meeting	Classification of Liabilities as Current or Non-current and Non-current Liabilities with Covenants (Part 1 of [draft] ED 85)	7.2.1
	Definition of Material (Parts 2, 3, 4, and 5 of [draft] ED 85)	7.2.2
	Interest Rate Benchmark Reform—Phase 2 (Part 6 of [draft] ED 85)	7.2.3
	Lease Liability in a Sale and Leaseback (Part 7 of [draft] ED 85)	7.2.4
	Approval of ED 85, <i>Improvements to IPSAS, 2023</i>	7.2.5
Other supporting items	[Draft] Exposure Draft (ED) 85, <i>Improvements to IPSAS, 2023</i> (page-by-page review)	7.3.1

INSTRUCTIONS UP TO PREVIOUS MEETING

Meeting	Instruction	Actioned
June 2023	<ol style="list-style-type: none"> 1. Assess the impact of the IASB publication Definition of Accounting Estimates (Amendments to IAS 8) on IPSAS 46, Measurement and on phase two of the Measurement project; 2. Add in the introduction section of [draft] ED 85 the criteria that IPSASB applies when analyzing IASB documents that may warrant a departure from those documents; 3. Align the definition of materiality in paragraph 7 of IPSAS 1 with the definition of materiality in the Conceptual Framework; 4. Address the editorials raised by the IPSASB on [draft] ED 85; and 5. Address the editorials raised by the IPSASB on the draft updated Process for Reviewing and Modifying IASB Documents. 	<ol style="list-style-type: none"> 1. See Agenda Item 8.2.8 of the Measurement Application Phase session of the September meeting 2. See page 5 of ED 85 3. See Agenda Item 7.2.2 4. See [draft] ED 85 5. Editorials addressed in the publication.

DECISIONS UP TO PREVIOUS MEETING

Meeting	Decision	ED 85
June 2023	1. Exclude from [draft] ED 85 the International Accounting Standards Board's (IASB's) publications related to Deferred Tax related to Assets and Liabilities arising from a Single Transaction, Initial Application of IFRS 17 and IFRS 9—Comparative Information, and Disclosure of Accounting Policies, (Amendments to IAS 1 and IFRS Practice Statement 2).	See page 5 of ED 85.

IMPROVEMENTS: PROJECT ROADMAP

Meeting	Completed Actions or Discussions / Planned Actions or Discussions:
June 2023	<ol style="list-style-type: none"> 1. Process for Identifying Improvements to IPSAS 2. IFRS Alignment Improvements to IPSAS Included in [draft] ED 85 3. IFRS Amendments <u>not</u> Included in [draft] ED 85
September 2023	<ol style="list-style-type: none"> 1. Classification of Liabilities as Current or Non-current and Non-current Liabilities with Covenants (Part 1 of [draft] ED 85) 2. Definition of Material (Part 2 and Part 3 of [draft] ED 85) 3. Interest Rate Benchmark Reform—<i>Phase 2</i> (Part 4 of [draft] ED 85) 4. Lease Liability in a Sale and Leaseback (Part 5 of [draft] ED 85) 5. Approval of ED 85, <i>Improvements to IPSAS, 2023</i>
Mid-October 2023 – Mid-December 2023	<ol style="list-style-type: none"> 1. Document out for comment
March 2024	<ol style="list-style-type: none"> 1. Review of Responses to ED 85 2. Approval of <i>Improvements to IPSAS, 2023</i>

Classification of Liabilities as Current or Non-current and Non-current Liabilities with Covenants (Part 1 of [draft] ED 85)

Question

1. Does the IPSASB agree to amend IPSAS 1, *Presentation of Financial Statements* to clarify the requirements for the presentation of liabilities in the statement of financial position?

Recommendation

2. Staff recommends the IPSASB clarify the criterion in IPSAS 1 for classifying a liability as non-current (i.e., the requirement for an entity to have the right to defer settlement of the liability for at least 12 months after the reporting period).

Background

3. In January 2020 and October 2022, the IASB issued improvements to IAS 1 to clarify the requirements for the classification of a liability as non-current:
 - (a) **January 2020.** *Classification of Liabilities as Current or Non-Current* (Amendments to IAS 1); and
 - (b) **October 2022.** *Non-current Liabilities with Covenants* (Amendments to IAS 1).
4. These clarifications amend paragraphs that exist in IPSAS 1, which are aligned with IAS 1.

Analysis

What is the nature of the amendments?

5. The IASB's amendments to IAS 1 clarify guidance on classifying a liability as non-current (i.e., the requirement for an entity to have the right to defer settlement of the liability for at least 12 months after the reporting period).
6. The IAS 1 amendments clarify the right to defer settlement of a liability for 12-months needs to exist at the end of the reporting period to classify a liability as non-current:
 - (a) This removes an apparent contradiction in IAS 1 between paragraph 69(d)—which required an 'unconditional right' to defer settlement—and paragraph 73—which referred to an entity that 'expects, and has the discretion, to' refinance or roll over an obligation (this clarification also explains how a loan covenant impacts the right to defer settlement); and
 - (b) Clarifies the interpretation of 'settlement' when determining whether the liability is classified as non-current.

Are the amended IAS paragraphs aligned with IPSAS?

7. The January 2020 and October 2022 IASB's amendments to IAS 1 are to paragraphs that exist and are aligned with IPSAS 1. The IPSASB has not omitted or amended the related IAS 1 paragraphs in the past for public sector differences.

Are the amendments applicable to the public sector?

8. The apparent contradiction between 'right' and 'expectation' and the lack of clarity in how to apply 'settlement' noted in paragraph 6 can lead to significant differences in interpretation and result in inconsistent accounting in the public sector.

9. The characteristics of a liability used to determine whether a liability is presented as current or non-current are the same regardless of whether the liability is incurred by a public sector entity or a private sector entity.
10. Incorporating the IAS 1 amendments clarifying the right, as opposed to an expectation, to defer settlement into IPSAS 1 reconciles the apparent contradiction, clarifies application of key terms, and enhances comparability and consistency in accounting across public sector entities.
11. These amendments are applicable and appropriate in the public sector, will maintain alignment with IAS 1, clarify existing guidance, and have been tested through the IASB's due process.

Decision Required

12. Does the IPSASB agree with the staff's [recommendation](#)?

Appendix A – Detailed analysis of IASB’s amendments to IAS 1 and IAS 8 and its applicability to IPSAS 1 and IPSAS 3, respectively

What is the nature of the amendments?

1. The amendments to IAS 1 highlight three application issues in IPSAS 1:

(a) **Contradiction between paragraphs 80(d) and 84** (January 2020).

- (i) Paragraph 80(d) requires an ‘unconditional right’ to defer settlement; and
- (ii) Paragraph 84 refers to an entity that ‘expects, and has the discretion, to’ refinance or roll over an obligation.

This apparent contradiction can lead to diversity in practice. Classification of a liability based on management’s intent can vary significantly from classification based on the existence of a right to defer settlement.

(b) **Unclear use of the term ‘settlement’** (January 2020). It is unclear whether a liability is ‘settled’ when:

- (i) It is rolled over under an existing loan facility; or
- (ii) An entity may settle it by issuing its own equity instruments (converting the liability to equity).

Whether an entity interprets the liability as settled, or a continuation of the existing arrangement, results in different accounting and inconsistent application of the principle in practice.

(c) **Unclear application of the right to defer settlement when covenants exist** (October 2022). It is unclear how to apply the January 2020 improvements in paragraph 1(a) above when an entity may be unable to avoid having to repay a liability within twelve months if the entity’s right to defer settlement of the liability is subject to compliance with covenants during that period.

Application of the January 2020 may not provide useful information when a liability is classified as non-current, but repaid within a year because a breach of a debt covenant.

Are the amendments applicable to the public sector?

2. The improvements to IAS 1 provide solutions that can be applied to IPSAS 1:

(a) **Contradictions between paragraphs 80(d) and 84**. This issue is resolved by amending paragraph 80(d) and the example in paragraph 84 to clarify an entity’s **right** to defer settlement must exist at the end of the reporting period.

Amending paragraph 84 to emphasize the need for the **right** to exist at the end of the reporting period is consistent with accounting for the substance of transactions, as opposed to management’s intent, and was already illustrated in the examples in paragraphs 85 and 86. This improvement enhances the consistency within the literature.

In addition to enhancing consistency, amending paragraph 80(d) to remove the emphasis of an ‘unconditional’ right, results in guidance in line with the anticipated terms of a loan arrangement. This is because the right to defer settlement of a loan is rarely unconditional—they are often conditional on compliance with covenants. If an entity’s right to defer settlement

of a liability is subject to the entity complying with specified conditions, the entity has a right to defer settlement of the liability at the end of the reporting period if it complies with those conditions at that date.

- (b) **Clarification of the term ‘settlement’.** A liability rolled over under an existing loan facility does not involve a transfer of economic resources or service potential. Since a liability is defined as an obligation to transfer an economic resource or service potential¹, a settlement has not occurred. Adding paragraph 87A clarifies aspects of the meaning of ‘settlement’ to enhance consistent accounting.

A liability settled by issuing the entity’s own equity instruments at the option of the bondholder is already addressed in paragraph 80(d). Paragraph 80(d) is clear a bond that the holder may convert to equity before maturity is classified as current or non-current according to the terms of the bond, without considering the possibility of earlier settlement by conversion to equity. Paragraph 80(d) applies only to liabilities that include a counterparty conversion option that meets the definition of an equity instrument and, applying IPSAS 28 *Financial Instruments: Presentation*, is recognized separately from the host liability as the equity component of a compound financial instrument.

In other cases, that is, if an obligation to transfer equity instruments is classified applying IPSAS 28 as a liability or part of a liability—the transfer of equity instruments would constitute settlement of the liability for the purpose of classifying it as current or non-current. Moving the statement about counterparty conversion options from paragraph 80(d) to new paragraph 87C clarified its scope.

- (c) **Clarification of the right to defer settlement.** The January 2020 amendments removed the emphasis on ‘unconditional’ right to entity’s right to so that where the entity has the ability to defer settlement of a liability that is subject complying with specified conditions, it is clear the entity has a right to defer settlement if it complies with those conditions at that reporting date.

In practice the information provided by the 2020 amendment – i.e., a binary classification model – does not meet user information needs in situations where an entity may be unable to avoid having to repay a liability within twelve months if the entity’s right to defer settlement of the liability is subject to compliance with covenants during that period. In such situations, the related liability could be repayable either within or after twelve months, depending on whether the entity complies with those covenants after the reporting date.

This issue is resolved by:

- (i) Adding paragraph 83B clarifying only covenants with which an entity is required to comply on or before the reporting date should affect the classification of a liability as current or non-current; and

¹ Paragraph 7 of IPSAS 1 defines a liability as present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.

Paragraph 5.14 of the Conceptual Framework defines a liability as a present obligation of the entity to transfer resources as a result of past events.

- (ii) Adding disclosure information that enables users of financial statements to understand the risk that non-current liabilities with covenants could become repayable within twelve months. See paragraph 87B.
- 3. These amendments to IPSAS 1 will help constituents apply the liability classification principles consistency and support the comparability of financial information across entities and jurisdictions. In addition, these amendments will maintain alignment with IAS 1, for which staff see no public sector reason to depart given the nature of the improvements.

Definition of Material (Parts 2, 3, 4, and 5 of [draft] ED 85)

Question

1. Does the IPSASB agree to amend IPSAS 1, *Presentation of Financial Statements* to clarify the definition of material and delete the description of materiality in IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors*?

Recommendation

2. Staff recommends the IPSASB:
 - (a) Clarify the definition of material in IPSAS 1; and
 - (b) Delete the description of materiality in IPSAS 3.

Background

3. In October 2018, the IASB published *Definition of Material* (Amendments to IAS 1 and IAS 8) to provide guidance to help entities make materiality judgements.
4. This guidance amends paragraphs that exist in IPSAS 1 and IPSAS 3, which are aligned with IAS 1, *Presentation of Financial Statements* and IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, respectively.

Analysis

What is the nature of the amendments?

5. The IASB's amendments to IAS 1 align the definition of materiality between IAS 1, IAS 8 and the Conceptual Framework and clarify several interpretation challenges identified by stakeholders:
 - (a) The materiality threshold of 'could influence decisions of users' may be understood as requiring too much information to be provided, because almost anything 'could' influence the decisions of some users;
 - (b) 'Information is material if omitting it or misstating it' focuses only on information that cannot be omitted (material information) and does not consider the effect of including immaterial information; and
 - (c) The term 'users' is too broad and implies an entity is required to consider all possible users of its financial statements when deciding what information to disclose.

Are the amended IAS paragraphs aligned with IPSAS?

6. The IASB's amendments to IAS 1 and IAS 8 are to paragraphs that exist and are aligned with IPSAS 1 and IPSAS 3, respectively. The IPSASB has not omitted or amended the related IAS 1 and IAS 8 paragraphs in the past for public sector differences.

Are the amendments applicable to the public sector?

7. Public sector entities make materiality judgements just like in the private sector. As the inconsistencies between IPSAS 1, IPSAS 3 and the updated IPSASB Conceptual Framework, and issues identified in paragraph 5 are also applicable in the public sector, the different application of the definition of material can lead to significant inconsistent accounting in the public sector.

8. Incorporating the IAS 1 amendments into IPSAS 1 address these inconsistencies and ensure materiality is applied more consistently across the public sector.
9. The proposed new definition of materiality in IPSAS 1.7 is consistent with the approved definition of materiality at the June 2023 meeting in the Chapter 3 of the Conceptual Framework (paragraph 3.32), which includes the guidance on obscuring information emphasizing that obscuring information can affect the decisions of users just as omitting or misstating that information can. In this way, it prevents confusion and different meanings because of different wording and can be applied consistently in practice.
10. The proposed new guidance in paragraph 12A(e) of IPSAS 1 also clarifies that including immaterial information in the financial statements should also be considered in the context of obscuring information in addition to 'misstating' and 'omitting'.
11. With the updated definition of materiality in IPSAS 1.13 a description in IPSAS 3.8 is unnecessary and can create confusion when applying both IPSAS in practice. Deleting the description from IPSAS 3 improves the understandability of the definition of material.
12. These amendments are applicable and appropriate in the public sector, will maintain alignment with IAS 1, clarify existing guidance, and have been tested through the IASB's due process.

Decision Required

13. Does the IPSASB agree with the staff's [recommendation](#)?

Interest Rate Benchmark Reform—Phase 2 (Part 6 of [draft] ED 85)

Question

1. Does the IPSASB agree to amend IPSAS 43, *Leases* to clarify that entities apply the practical expedient in paragraph 43 when a lease contract is modified because of a change in terms related to Interest Rate Benchmark Reform?

Recommendation

2. Staff recommends amend IPSAS 43, *Leases* to clarify that entities apply the practical expedient in paragraph 43 to account for a lease modification as a result of the Interest Rate Benchmark Reform.

Background

3. In August 2020, the IASB published *Interest Rate Benchmark Reform—Phase 2* (Amendments to IFRS 9, IAS 39, IFRS 7 and IFRS 16) to provide guidance on how to account for a contractual modification resulting from the replacement of an interest rate benchmark with an alternative benchmark rate.
4. This Agenda Item addresses the incorporation of the IASB's *Interest Rate Benchmark Reform—Phase 2* into IPSAS 43 (amendments to the financial instruments suite of IPSAS [IPSAS 28, IPSAS 29, and IPSAS 41] were addressed as part of the 2021 Improvements to IPSAS).

Analysis

What is the nature of the amendments?

5. The IASB's amendments to IFRS 16 introduce a practical expedient for lessees to account for a lease modification as a result of the interest rate benchmark reform.
6. This was necessary because of circumstances outside of the control of entities - global interest rate benchmark reform - entities that had entered into lease arrangements would have modifications to the contractual terms of the lease contract. Practical relief was provided to ease the burden of the financial reporting specifically related to these circumstances.

Are the amended IFRS paragraphs aligned with IPSAS?

7. The IASB's amendments to IFRS 16 relate to a paragraph that also exists in IPSAS 43 and is aligned. The IPSASB has not omitted or amended the related IFRS 16 paragraphs in the past for public sector differences.

Are the amendments applicable to the public sector?

8. The practical expedient allows entities with leases amended by a change in interest rate (as a result of interest rate benchmark reform) to continue to account for the existing lease. This eliminates onerous analysis for lease modifications that are otherwise outside of the control of the entity and allows the entity to focus resources on more pressing financial reporting matters.
9. Including the practical expedient in IPSAS 43 has the added benefit of enhancing comparability between public and private sector entities and provide the same cost-relief to public sector preparers in applying the changes from the Interest Rate Benchmark Reform.
10. These amendments are applicable and appropriate in the public sector, will maintain alignment with IFRS 16, provide cost-relief to preparers, and have been tested through the IASB's due process.

Decision Required

11. Does the IPSASB agree with the staff's [recommendation](#)?

Lease Liability in a Sale and Leaseback (Part 7 of [draft] ED 85)

Questions

1. Does the IPSASB agree to amend IPSAS 43, *Leases* to clarify that seller-lessees subsequently measure lease liabilities arising from a leaseback in a way that it does not recognize any amount of the gain or loss that relates to the right of use it retains?

Recommendation

2. Staff recommends the IPSASB clarify that the seller-lessees subsequently measure lease liabilities arising from a leaseback in a way that it does not recognize any amount of the gain or loss that relates to the right of use it retains.

Analysis

What is the nature of the amendments?

3. The IASB's amendments to IFRS 16 clarify that seller-lessees should not recognize any amount of the gain or loss that relates to the right of use it retains when subsequently measuring lease liabilities arising from a leaseback.
4. The IASB made the amendments to IFRS 16, *Leases* because without the amendments, a seller-lessee could recognize a gain on the right of use it retains in a sale and leaseback transaction solely because of a remeasurement (for example, following a lease modification or change in the lease term) if it had applied the subsequent measurement requirements for lease liabilities unrelated to a sale and leaseback transaction. This could have been the case, in particular, in a leaseback that includes variable lease payments that do not depend on an index or rate—because these payments are excluded from 'lease payments' as defined in IFRS 16. The seller-lessee might therefore have recognized a gain, even though no transaction or event would have occurred to give rise to that gain.

Are the amended IFRS paragraphs aligned with IPSAS?

5. The IASB's amendments to IFRS 16 relate to paragraphs that also exist in IPSAS 43 and are aligned. The IPSASB has not omitted or amended the related IFRS 16 paragraphs in the past for public sector differences.

Are the amendments applicable to the public sector?

6. Public sector entities also enter into sale and leaseback transactions like in the private sector. By incorporating the same amendment in IPSAS 43, it more appropriately reflects the substance of the transaction and does not permit a gain on day two because of the subsequent measurement methodology.
7. These amendments are applicable and appropriate in the public sector, will maintain alignment with IFRS 16, and have been tested through the IASB's due process.

Decision Required

8. Does the IPSASB agree with staff's [recommendation](#)?

Approval of ED 85, *Improvements to IPSAS, 2023*

Questions

1. Does the IPSASB agree to:
 - (a) Approve ED 85, *Improvements to IPSAS, 2023* for exposure; and
 - (b) A 60-day consultation period.

Recommendation

2. Staff recommends ED 85 be approved for exposure with a 60-day consultation period.

Analysis

Structure and content of ED 85

3. The structure and content of ED 85 has been developed according to previous editions of improvements to IPSAS and consistent with staff's recommendations in Agenda Items [6.2.1](#), [6.2.2](#), [6.2.3](#), and [6.2.4](#).

Consultation Period

4. The normal consultation period for the *Improvements to IPSAS* projects is 60 days.² Staff expects to publish ED 85 by mid-October 2023 with a consultation period end date of mid-December 2023. This would allow staff to bring back to the March 2024 meeting the analysis of the responses to ED 85 and for the IPSASB to approve the final *Improvements to IPSAS, 2023*.

Decision Required

5. Does the IPSASB agree with staff's [recommendation](#)?

² The IPSASB's [Due Process and Working Procedures](#) states that Improvement's exposure drafts generally have a 60-day exposure period as a result of the consequential nature of the changes.

Supporting Document 1 – [draft] Exposure Draft 85, *Improvements to IPSAS, 2023*

1. The [draft] Exposure Draft 85 is posted separately for easier readability.
2. Compared to the version presented to the IPSASB at the June 2023 meeting, the IASB's publication *Definition of Accounting Estimates* (Amendments to IAS 8) was removed from [draft] Exposure Draft 85 because it will be addressed in the IPSASB's project on Measurement Application Phase (see [Agenda Item 8.2.8](#) of the September 2023 meeting), Parts 3 and 4 were added as consequential amendments from the IASB's publication *Definition of Material* (Amendments to IAS 1 and IAS 8), and all editorial suggestions were addressed.