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**CANADA**

Submitted to: [www.ifac.org](http://www.ifac.org)

Dear Ross

***ED 81 Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements in Financial Statements***

Thank you for the opportunity to comment on ED 81 *Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements in Financial Statements* (the ED). The ED has been exposed for comment in New Zealand and some New Zealand constituents may comment directly to you.

We support the proposals to update the Conceptual Framework to reflect the latest international conceptual thinking (particularly, the latest updates to the IASB's Conceptual Framework) and to reflect the IPSASB's experience in applying the Conceptual Framework. However, we recommend that the IPSASB consider the following recommendations to further improve these proposals.

- **Materiality:** We recommend not to include in the Conceptual Framework the proposed sentence about display vs disclosure of information, because we are not convinced that it is necessary to discuss this specific matter within the general guidance on materiality, and the wording of the sentence seems unclear.
- **Definition of an asset:** We recommend further simplifying/streamlining the description of a resource, to enhance the understandability of the description.
- **Definition of an asset and definition of a liability:** We recommend clarifying in the core text of the Conceptual Framework that the term 'past events' in the definition of an asset and a liability cover situations where an asset or liability arises from a single past event or multiple past events.

- Definition of a liability: We recommend that the IPSASB considers enhancing the guidance on the recognition of liabilities in its Conceptual Framework – given that the proposed updated guidance on the definition of a liability emphasises that an outflow of resources need not be likely for the definition of a liability to be met. We note that the chapter on recognition of assets and liabilities in the IASB Conceptual Framework contains more detailed guidance as compared to the equivalent chapter in the IPSASB’s Conceptual Framework.
- Binding arrangements that are equally unperformed: The proposed guidance on binding arrangements that are equally unperformed is included in the unit of account section, but it does not seem to relate solely to determining the unit of account. Therefore, we recommend including this guidance in a separate section (like the IASB did) – or else to explain more clearly the decision not to do so.

Our recommendations and responses to the Specific Matters for Comment in the ED are set out in the Appendix to this letter. If you have any queries or require clarification of any matters in this letter, please contact Gali Slyuzberg ([gali.slyuzberg@xrb.govt.nz](mailto:gali.slyuzberg@xrb.govt.nz)) or me.

Yours sincerely



Carolyn Cordery  
**Chair – New Zealand Accounting Standards Board**

## APPENDIX

### Response to Specific Matters for Comment

#### Specific Matter for Comment 1: Prudence

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 BC3.17–BC3.17E explain the reasons for this guidance. Do you agree with this approach? If not, why not? How would you modify these paragraphs?

#### NZASB response

1. We support the proposed amendments to the guidance on prudence. We note that the proposed changes are aligned with the IASB's Conceptual Framework, and we have received feedback from our Accounting Technical Reference Group ('TRG')<sup>1</sup> that such alignment is beneficial.

#### Specific Matter for Comment 2: Obscuring information as a factor relevant to materiality judgement

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?

#### NZASB response

##### *Obscuring information*

2. We support the proposed addition of 'obscuring information' to the factors that should be considered when determining whether an item is material, for the following reasons.
  - (a) We consider materiality to be an important concept in general in the preparation of financial statements, including in the public sector. For example, we note that in our submission on ED 77 *Measurement*, we emphasised the importance of considering materiality when requiring and providing disclosures about inputs into current value measurements of assets and liabilities. Therefore, we welcome the proposed additional guidance on materiality that is aligned with the recent international thinking on this topic (i.e. the IASB's 2018 updates to its Conceptual Framework).

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<sup>1</sup> The Accounting Technical Reference Group (TRG) of the NZASB is an informal consultative group made up of technical partners from Big Four and mid-tier accounting firms and equivalent public sector representatives.

- (b) We have received feedback from our Accounting TRG that the proposed alignment of the guidance on materiality with the guidance in the IASB's Conceptual Framework is beneficial.
  - (c) We also note that in New Zealand, the *Public Benefit Entities Conceptual Framework* – which is based on the IPSASB's Conceptual Framework – is applicable to public benefit entities (PBEs) in both the public and not-for-profit sectors. We have received feedback that in New Zealand, there is a tendency among some not-for-profit entities to provide overly detailed disclosures (such as detailed breakdowns of expenses) – and that the proposal in the ED to refer to 'obscuring information' in the guidance on materiality could help reduce this tendency.
3. In addition, we 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.

*Additional comment relating to materiality: Display and disclosure of information*

4. While SMC 2 focuses on the proposed reference to 'obscuring information', we note that the ED also proposes to add the following sentence to paragraph 3.32 of the IPSASB Conceptual Framework:
- "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".*
5. We recommend not to add this proposed sentence to the Conceptual Framework, for the following reasons.
- (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. We note that the individual standard IPSAS 1 *Presentation of Financial Statements* discusses separate presentation of items in the primary financial statements and disclosures in the notes – including the presentation of additional items that are not specified in IPSAS 1, and disclosure of items that are not presented in the financial statements.
  - (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. Presumably, the intent of this sentence was to explain that if an entity decides that an item is not material enough to be displayed separately or prominently on the face of the financial statements, the entity should consider whether the item is sufficiently material to be disclosed in the notes. However, 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.

6. As noted above, we do not recommend including the sentence on ‘display and disclosure’ in the Conceptual Framework. However, if the IPSASB decides to retain this proposed sentence, we think that:
  - (a) this sentence should be moved to a separate paragraph and amended as follows for greater clarity: “Where an entity judges that a material item need not be separately (or prominently) displayed ~~is not separately displayed~~ on the face of a financial statement ~~(or displayed sufficiently prominently)~~, an entity considers disclosure”; and
  - (b) the Basis for Conclusions should explain why the sentence was added.

**Specific Matter for Comment 3: Rights-based approach to resources**

Paragraphs 5.7A-5.7G reflects a rights-based approach to the description of resources in the context of an asset. The reasons for this approach are in paragraphs BC5.3A-5.3F.

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

NZASB response

*General comment: rights-based approach to describing a resource*

7. We support the proposal to describe a resource as a right – instead of the current description, which distinguishes between ‘items’ and ‘rights’. We agree with the IPSASB that service potential or economic benefit associated with the ownership of an item arises from the rights conferred by such ownership. Therefore, for the purpose of describing a resource in the context of the definition of an asset, we agree that it is not useful to distinguish between owned items and rights to use an item.
8. However, we have a suggestion for further improving the wording of the proposed new description of a resource.

*Recommendation to simplify the description of a resource*

9. We think the proposed description of a resource could be further streamlined and simplified, to enhance the clarity of the description, as explained below.
  - (a) The proposed description of a resource in paragraph 5.6A of the ED is: “a right to either service potential or the capability to generate economic benefits, or a right to both”.
  - (b) The part of the description relating to economic benefits refers to a “right to [...] the capability to generate economic benefits”. We think this part of the description could be streamlined.
  - (c) We note that the IASB’s description of a resource is: “a right that has the potential to produce economic benefits”.
  - (d) Considering the IASB’s description, as well as the need to also refer to service potential to reflect the public sector context, we would recommend that the IPSASB considers the following alternative description of a resource:
 

*“A resource is a right that has the capability to generate economic benefits or service potential or both.”*

*Definition of an asset and definition of a liability: reference to 'past events'*

10. While SMC 3 focuses on the description of a resource, we also have a comment on the proposed change to the definition of an asset (this comment also relates to the definition of a liability).
11. Similar to the IASB's Conceptual Framework, the ED proposes to amend both the definition of an asset and the definition of a liability by replacing the term 'a past event' (singular) with 'past events' (plural).
12. The Basis for Conclusions in the ED explains that the term 'past events' also includes scenarios where an asset or liability arises as a result of a single past event. However, we would recommend clarifying this point in the core text of the IPSASB Conceptual Framework, for the reasons explained below.
13. We have received feedback from our Accounting TRG that the proposed change from 'past event' to 'past events' seems to imply that a single event is no longer sufficient for an asset or a liability to arise.
14. We note that the following points may justify the feedback we received and may warrant further clarification of this matter for users of the IPSASB Conceptual Framework.
  - (a) The IASB's Conceptual Framework has been referring to 'past events' for many years, since before the IPSASB issued its Conceptual Framework in 2014. We understand that when first publishing its Conceptual Framework, the IPSASB will have deliberately decided to use the term 'past event', rather than 'past events' as per the IASB's Conceptual Framework. The IPSASB is now proposing to change this decision.
  - (b) Users of the IPSASB Conceptual Framework would have become accustomed to the reference to 'past event' in the definition of assets and liabilities. Like our Accounting TRG, such users might question whether the proposed change from 'past event' to 'past events' implies that a single event is no longer sufficient for a liability to arise – despite the explanation in the Basis for Conclusions.
15. We also note that when an asset or a liability arises from an accumulation of multiple events, it may be possible to identify a single event after which the definition of an asset/liability is met (and before which the definition was not met). However, this single event may not always be sufficient on its own to cause the definition of an asset/liability to be met. We acknowledge that the reference to 'events' as proposed in the ED would cover such situations. Nevertheless, there could also be situations where an asset or an asset/liability arises from a single event.
16. Therefore, we recommend clarifying in the core text of the IPSASB Conceptual Framework that the term 'past events' includes a single past event or multiple past events. This could be added as a new paragraph, or as a footnote next to the term 'past events'. We acknowledge that the IASB Conceptual Framework does not include such additional explanation. However, in light of the feedback we have received and our considerations above, we think this explanation would be useful for users of the IPSASB Conceptual Framework.

**Specific Matter for Comment 4: Definition of a liability**

The revised definition of a liability is in paragraph 5.14:

*A present obligation of the entity to transfer resources as a result of past events.*

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

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

NZASB response

17. We support the proposal to refer to the transfer of resources in the definition of a liability. However, please refer to our comments under SMC 3 concerning the proposal to replace the term ‘past event’ with ‘past events’ in the definition. We also have some comments on the guidance accompanying the proposed new definition. Please refer to the next SMC.

**Specific Matter for Comment 5: Guidance on the transfer of resources**

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 paragraphs BC5.19A-BC5.19D.

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

NZASB response

*General comment*

18. We support including guidance on the transfer of a resource, to support the proposed new definition of a liability. However, we recommend that the IPSASB also considers enhancing the guidance on the *recognition* of liabilities (and assets) in light of these proposals. This is explained in the paragraphs that follow.

*Guidance on the recognition of liabilities (and assets)*

19. The proposed amendments to the guidance on liabilities in the ED emphasise that an obligation may meet the definition of a liability even if the probability of having to transfer resources is low. For example:
- (a) the proposed new paragraph 5.16A says: “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 [...]”; and
  - (b) the proposed new paragraph 5.16B says: “An obligation can meet the definition of a liability even if the probability of a transfer of a resource is low. [...]”.
20. We understand the rationale for these proposals, i.e. to avoid conflating the principles of the *definition* of a liability with the *recognition* principles. We also note that the IASB made similar amendments to the guidance of the definition of a liability in its Conceptual Framework in 2018.
21. We note that the guidance on the recognition of liabilities in the IASB’s Conceptual Framework appears to be more detailed and robust than the IPSASB’s existing guidance on the

recognition of liabilities. The chapter on recognition in the IPSASB Conceptual Framework includes some references to considering the qualitative characteristics. However, the chapter on recognition in the IASB's Conceptual Framework includes specific sections on considering relevance and faithful representation when determining whether a liability (or an asset) is recognised. These sections include a specific discussion on low probability of outflow (and inflow) of economic resources, as well as a discussion on existence uncertainty and measurement uncertainty.

22. We recommend enhancing the guidance on the recognition of liabilities (and assets) in the IPSASB Conceptual Framework in a similar vein to the abovementioned IASB guidance. Such enhancements would help clarify that when the likelihood of a transfer of resources is low, an item may meet the definition of a liability but might not meet the criteria for recognition.
23. An example of where the abovementioned enhanced guidance could be useful is when a preparer considers whether an obligation is a contingent liability – which is disclosed but is not recognised in the statement of financial position – or whether it is a liability that needs to be recognised in the statement of financial position.

**Specific Matter for Comment 6: Revised structure of guidance on liabilities**

In addition to including guidance on the transfer of resources, the IPSASB has restructured the guidance on liabilities so that it aligns better with the revised 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?

NZASB response

*General comment*

24. We agree with the restructure of the guidance on liabilities, to match the order in which terms are described in the revised definition of a liability. However, we make the recommendations below with respect to restructured paragraphs 5.15A and 5.17C.

*Recommendation to amend paragraphs 5.15A*

25. Paragraphs 5.15A and 5.17C both refer to public communication of intentions in the context of a liability. We note that there is a possible inconsistency between these references, as explained below.
  - (a) Paragraph 5.15A states that an obligation must be to an external party to give rise to a liability, and that an entity “cannot be obligated to itself, *even where it has publicly communicated an intention to behave in a particular way*” [italics added for emphasis].
  - (b) Paragraph 5.17C then discusses the point at which a liability arises. This paragraph states that a promise made in an election is unlikely to give rise to a present obligation that meets the definition of a liability, but an announcement might have “such political support that the government has little option to withdraw”. This implies that public communication could give rise to a liability – and there is no qualification in this paragraph that the liability must be to an external party. Therefore, this paragraph

could be read as being inconsistent with what paragraph 5.15A says about public communication of intentions.

26. We acknowledge that paragraph 5.15A and 5.17C discuss public communication of intentions in different contexts. Nevertheless, to avoid confusion that could result from the perceived inconsistency between these two paragraphs, we recommend deleting the reference to public communication in paragraph 5.15A. That is, we recommend deleting from paragraph 5.15A the words “even where it has publicly communicated an intention to behave in a particular way”. We think that deleting these words would not detract from the usefulness of paragraph 5.15A.

*Recommendation to clarify the reason for amending paragraph 5.17C*

27. The relocated paragraph 5.17C lists factors that are likely to impact judgement around the point at which a liability arises. The factor discussed in the second bullet point of paragraph 5.17C is the entity’s ability to modify or change the obligation before it crystallises. We note that in the ED, the last sentence in this bullet point is marked for deletion. The deleted sentence says: “Similarly, if an obligation is contingent on future events occurring, there may be discretion to avoid an outflow of resources before these events occur”.
28. We recommend clarifying the reason for the deletion of this sentence in the Basis for Conclusions. We have received feedback that such clarification would be useful.
29. We think that a possible reason for the proposed deletion may have been to avoid a possible inconsistency with the new paragraph 5.16A. Paragraph 5.16A states: “For that potential [to require a transfer of resources] to exist, it does not need to be certain, or even likely, that the entity will be required to transfer resources—the transfer may, for example, be required only if a specified uncertain future event occurs”. If that is indeed the reason for deleting the abovementioned sentence in the second bullet point of paragraph 5.17C, we recommend stating this in the Basis for Conclusions.

**Specific Matter for Comment 7: Unit of account**

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

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?

NZASB response

30. We support the proposal to add a section with guidance on the unit of account. However, we think that the guidance on accounting principles for binding arrangements that are equally unperformed should be relocated to a separate section, rather than being part of the unit of account section. Please refer to the next SMC.

**Specific Matter for Comment 8: Accounting principles for binding arrangements that are equally unperformed**

The IPSASB took the view that guidance on accounting principles for binding arrangements that are equally unperformed should be included in the Conceptual Framework, but that a separate section on accounting principles for such binding arrangements is unnecessary. These principles are included in paragraphs 5.26G-5.26H of the section on Unit of Account. The explanation is at paragraphs BC5.36D-BC5.36F. Do you agree that:

- (a) Guidance on principles for binding arrangements that are equally unperformed is necessary; and if so
- (b) Such guidance should be included in the Unit of Account section, rather than in a separate section?

If you do not agree, please give your reasons.

NZASB response

*Inclusion of guidance on binding arrangements that are equally unperformed*

31. We support the proposal to include guidance on principles for binding arrangements that are equally unperformed in the IPSASB Conceptual Framework. However, we recommend relocating this guidance into a separate section. Further information is included below.

*Location of guidance on binding arrangements that are equally unperformed*

32. Our Accounting TRG questioned the rationale for including the guidance on binding arrangements that are equally unperformed within the section on 'unit of account' – noting that in the IASB Conceptual Framework, the equivalent guidance on executory contracts is included in a separate section. The Basis for Conclusions explains that the IPSASB decided that a separate section on this topic is 'unnecessary', but the reason for this decision is not provided.
33. We are concerned that including the guidance on 'binding arrangements that are equally unperformed' within the section on 'unit of account' would imply to readers of the Conceptual Framework that the concepts in this guidance are confined solely to the determination of the unit of account. We do not think that this implication is correct. For example, we note the following.
- (a) Paragraph 5.26G states that "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". Arguably, this guidance relates to meeting the definition of an asset or a liability.
  - (b) Paragraph 5.26H states "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". Arguably, this guidance relates to meeting the definition of an asset or a liability, as well as the timing of recognition of an asset or a liability.

34. Therefore, we would recommend including the guidance on 'binding arrangements that are equally unperformed' in a separate section in Chapter 5, rather than within the 'unit of account' section (similarly to the IASB).
35. If the IPSASB does not relocate the guidance on binding arrangements that are equally unperformed to a separate section, then we think it would be important to clarify in the Basis for Conclusions that the principles in this guidance have broader application than just the 'unit of account' topic, and the reason why it is not necessary to have a separate section for this guidance.