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Chief Executive
External Reporting Board
PO Box 11250
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Dear Sir

NZASB Invitation to Comment on Limited Scope Review Draft of PBE FRS XX *Service Performance Reporting*

We are pleased to comment on the revised proposals outlined in the Limited Scope Review Draft of PBE FRS XX *Service Performance Reporting* ("revised ED"). As mentioned in our comment letter on the original *Exposure Draft NZASB 2016-6: Service Performance Reporting* ("original ED"), we are supportive of the NZASB's project to establish a specific standard for reporting service performance. The final standard will provide Public Benefit Entities (PBEs) with a framework for reporting non-financial information, aligning reporting with their primary objective to provide goods or services for a community or social benefit. We believe the proposals will improve PBEs' accountability to users of financial statements, as well as enhancing decision making within an organisation.

Our key concern with the original ED related to the application of its requirements to not-for-profit PBEs (particularly smaller ones in Tier 2) and ensuring there is an appropriate balance between cost of implementation and the benefits. Specifically, we were concerned that smaller PBEs may find it difficult and costly to comply with the original ED's requirements around the disclosure of the impacts that the entity has had on its outcomes. We note that the revised ED no longer requires the disclosure of outputs, outcomes or impacts. This applies to both Tier 1 and Tier 2 PBEs. We also note generally that the revised ED is less prescriptive than the original ED and provides PBEs with greater flexibility around reporting on their service performance. Therefore we believe that our abovementioned key concern is addressed by the revised ED.

In our view, the key risk regarding the revised ED is that the degree of flexibility provided by the less prescriptive and more high-level nature of its requirements may potentially be too high. As such, PBEs' interpretation of the proposed new standard may result in some useful service performance information not being reported. Generally, we believe that the revised ED's requirement to disclose critical judgements should mitigate this risk to some extent. However, we believe it would be useful to include additional requirements or guidance around reporting on the longer-term effects of a PBE's activities on society or a social group (i.e. reporting against what the original ED referred to as "outcomes"), where it is appropriate for an entity to report on this aspect of service performance. Having said this, we understand the challenge around including such requirements/ guidance in a standard that applies to a wide range of PBEs.

We also note that the less prescriptive and more high-level nature of the requirements in the revised ED may result in a lower level of comparability across different entities as compared to the original ED. However, we believe that this is mitigated to some extent by the requirement in the revised ED to disclose critical judgements made in reporting service performance, as well as the requirement to comply with the qualitative characteristics, including comparability.

Other than the matters described above, we do not have significant concerns around the workability of the revised ED or any potential unintended consequences arising from the revised ED.

For a more detailed response, please refer to the attached appendix.

Please do not hesitate to contact us should you have any queries. We also would be happy to meet with you to discuss our comments further.

Yours faithfully
Ernst & Young Limited



Graeme Bennett
Partner

Appendix A - Response to specific Limited Scope Review question

Taking into account the proposals in the 2016 ED, the comments received and the changes made in response to those comments, do you have any comments on the workability of the revised proposals or whether they would have any unintended consequences?

Key changes in the revised ED:

We note that the key changes in the revised ED as compared to the original ED are:

- (1) The requirements of the revised ED are less prescriptive and more high-level than the original ED. For example, unlike the original ED, the revised ED no longer refers to, or requires disclosure of, outputs, outcomes or impacts. Instead, the revised ED requires entities to provide: (a) sufficient contextual information to understand why the entity exists, what it intends to achieve in broad terms over the medium to long term, and how it goes about this, and (b) information about what the entity has done during the reporting period in working towards its broader aims and objectives.
- (2) The revised ED requires entities to disclose critical judgements made when reporting service performance information, i.e. those judgements that have the most significant effect on the selection and aggregation of service performance information, and that are relevant to an understanding of the entity's service performance information.

Workability and potential consequences of the revised ED as a result of the above key changes:

(a) Advantages of revised ED

We believe that the above changes have several advantages in terms of enhancing the workability of the revised ED. For example, the key concern that we had with the original ED related to the application of its requirements to not-for-profit entities, particularly smaller ones in Tier 2, and ensuring there is an appropriate balance between cost of implementation and the benefits. Specifically, we were concerned that smaller entities may find it difficult and costly to comply with the original ED's requirements of having to establish whether there is clear evidence of a link between the entity's outputs and the actual impact on outcomes, and if such evidence existed, to report on the entity's impacts on outcomes. We therefore suggested that Tier 2 PBEs be exempt from the requirement around impacts. As noted above, the revised ED has altogether removed the requirement to report on impacts, as well as outputs and outcomes, for both Tier 1 and Tier 2 PBEs. In addition, although the revised ED has not introduced Tier 2 disclosure concessions, as noted above it is generally much less prescriptive than the original ED. Therefore the proposals in the revised ED should be easier and less costly to apply for all PBEs, including not-for-profit PBEs in Tier 2.

In addition, the move towards more general service performance reporting requirements gives PBEs greater freedom and flexibility to "tell their story" in a way that is tailored - and therefore most relevant and meaningful - to the specific PBE and its users. At the same time, the revised ED still specifically requires PBEs to provide disclosures on what they intend to achieve in the longer term and what they have provided during the year in terms of service performance, thereby still aligning PBEs' reporting requirements with their primary objective to provide goods or services for a community or social benefit.

We also note that the more general requirements of the revised ED will help avoid potential inconsistencies between the proposed standard and the terminology and requirements contained within the various pieces of legislation that require public sector PBEs to report on their service performance.

In terms of the requirement to disclose critical judgements, we believe that it will enhance the transparency of PBEs' service performance reports. Furthermore, we agree with the NZASB's comment in the Basis of Conclusion of the revised ED that the requirement to disclose critical judgement is a "necessary counterbalance" to the less prescriptive requirements of the revised ED. Specifically, we believe that the

requirement to disclose critical judgements will to some extent mitigate certain concerns that arise from the move to more high-level requirements, as explained below.

(b) Discussion of potential risks arising from the revised ED

While we acknowledge the benefit of flexibility around service performance reporting requirements, we believe that there is a risk that the degree of flexibility provided by the less prescriptive and more high-level nature of the requirements in the revised ED may potentially be too high. As such, there is a potential risk that some useful service performance information, which would have been required under the original ED, may not be disclosed by PBEs under the revised ED. In general, the revised ED provides requirements that mitigates these risks. For example, we note that the original ED included an explicit requirement to explain the link between a PBE's outputs and expected outcomes. Such an explanation arguably enhances the understandability and therefore usefulness of service performance information, as without it there is a risk that PBEs will report on their service performance by disclosing their wider service performance objectives and providing a list of goods/service produced during the year, but there may be a "disconnect" between the two elements. We note that the requirement to explain the link between outputs and expected outcomes was removed in the revised ED. However, we believe that this is mitigated by the revised ED's requirement to disclose critical judgements, as paragraph 46(a) of the revised ED requires PBEs to consider "*the extent to which the entity's service performance information is consistent with and clearly linked to the entity's overall purpose and strategies*", and states that "*[i]f it is not, users may need to understand why not*". Thus the revised ED still ensures that it is clear to users how the goods, services or other aspects of service performance reported on by a PBE are connected to the PBE's wider service performance goals.

However, in other cases, while the risk around useful information not being disclosed is mitigated to a certain extent, we believe that more detailed requirements or additional guidance could be beneficial. For example, it could be argued that the requirements in the original ED to report on outputs, outcomes and impacts, and to disclose performance measures with regards to outputs and impacts on outcomes, will have helped ensure a certain minimum level of information and structure in service performance reports, which would have been useful for users. These requirements arguably would have been useful to the reporting entity, in terms of providing a degree of clarity as to what it is expected to include in its service performance report. While the revised ED no longer requires PBEs to report on outputs, outcomes or impacts, it still specifically requires PBEs to provide contextual information on their broad service performance objectives and methods (which needs to draw on the entity's performance framework, theory of change or intervention logic, if used, and explain the main ways in which the PBE carries out service performance activities (paragraph 17-18)), and to report what they have provided during the year in terms of service performance (by providing an appropriate mix of service performance measures and/or descriptions). Further, the revised ED includes some guidance around performance measures, such as general examples of performance measures and descriptions (paragraph 20) and specific examples of possible performance measures and descriptions for reporting on goods and services provided (paragraphs 27-28). Therefore, while less prescriptive and more flexible, the revised ED still contains certain specific requirements and guidance around information to be disclosed. In addition, the requirement in the revised ED to disclose critical judgements should ensure that the reason for including or excluding certain service performance information is clear to users, and the overarching requirement to provide service performance information that is appropriate and meaningful for users, should help ensure that the service performance information provided to users is sufficient and useful.

However, it is possible that PBEs may need additional guidance when applying these less prescriptive requirements. We believe that this applies particularly to PBEs that report on the longer-term effects of their activities on society (similarly to what the original ED referred to as "outcomes"). We do not expect all PBEs within the scope of the proposed standard to be required to report on their performance against such social outcomes. For example, as noted in paragraph 19(a) of the proposed ED, a not-for-profit PBE that is responsible for providing certain goods or services to a group in the community, it would be appropriate to focus on goods or services produced during the year in its service performance report. However, for certain PBEs, especially in the public sector, reporting on longer-term social effects would provide useful information for users and help discharge the entity's accountability. We note that some guidance exists in

the revised ED regarding reporting on performance against longer-term social effects of a PBE's activities (for example, paragraph 25 says that performance measures "may be used to inform assessments of the broad or longer-term effects of a project or an entity's work" on recipients of goods/services or a group of society - such as changes in educational achievements or poverty levels). However, generally, the revised ED seems to have a greater focus, or at least more guidance, on reporting on what has been produced during the year. Therefore, while we do not argue that the proposed standard should require all PBEs in Tier 1 and 2 to report on the long-term effect of their activities on society, we believe that additional requirements or guidance in this area would be useful. Such guidance will give PBEs that report on the longer-term social effects of their activities greater clarity as to how they are expected to report on this, and will help ensure that useful information is provided to users. Having said this, we understand the challenge around including such requirements/guidance, given that the proposed standard will apply to a wide range of different PBEs, i.e. both Tier 1 and Tier 2 PBEs across both the public and not-for-profit sectors.

Another potential concern with the less prescriptive approach of the revised ED is a possible lack of comparability in service performance reports across different PBEs. In our comment letter on the original ED, we noted that the proposals as originally drafted will improve consistency in service performance reporting between entities with similar activities and between reporting periods. Given the less prescriptive and more high-level nature of the requirements in the revised ED, it is possible that service performance reporting may be less consistent across entities as compared to the consistency that will have been achieved by the original ED. This applies especially to PBEs in the not-for-profit sector, where - unlike in the public sector - there is no legislation that requires service performance reporting. However, we believe that the requirement in the revised ED to disclose critical judgements will help mitigate this concern to some extent. For example, paragraph 44 of the revised ED acknowledges that entities need to apply judgement when deciding on an appropriate and meaningful mix of performance measures (as per paragraphs 21-22), and requires entities to disclose the critical judgements applied in this regard. In addition, the revised ED still requires service performance information to comply with the qualitative characteristics, including comparability.

Finally, it could be argued that the benefits of the more prescriptive requirements in the original ED may have outweighed the cost of complying with these requirements for Tier 1 PBEs, therefore there would have been merit in retaining the more prescriptive requirements of the original ED and providing Tier 2 disclosure concessions. However, it is not clear that the merits of such an approach would be greater than the abovementioned benefits of the NZASB's chosen approach, namely the benefits of greater flexibility, more tailored information and lower compliance costs to both Tier 1 and Tier 2 PBEs, as well as lack of conflict with legislative requirements for public sector PBEs. In addition, as noted above, the requirements in the revised ED to disclose critical judgements, comply with the qualitative characteristic of comparability and provide information that is appropriate and meaningful to users should help mitigate the potential concern around comparability and ensure that PBEs provide service performance information that is useful to users. However, please note the abovementioned discussion around the potential risk associated with a high degree of flexibility in the revised ED, which could be mitigated by additional guidance.

Other comments on the revised ED:

Additionally, we note the following with regards to the revised ED:

- The revised ED has added an emphasis on neutrality when requiring service performance information to be faithfully representative. We believe that this will help ensure that both good and poor service performance is reported, which will enhance PBEs' accountability and the usefulness of service performance information for users.
- The revised ED increases the implementation period of the proposed requirements from 2 years to 3 years. We believe that this enhances the workability of the proposed standard, as it will allow PBEs, particularly not-for-profit PBEs, sufficient time to update their systems and processes and ensure that the new standard is properly implemented.

- We note that under the standards *PBE Simple Format Reporting - Accrual*, Tier 3 public sector PBEs whose legislation requires service performance reporting and all Tier 3 not-for profit PBEs are required to report on their outputs and outcomes in a statement of service performance. By contrast the revised ED, which will apply to Tier 1 and Tier 2 PBEs, does not specifically refer to outputs and outcomes. We suggest that the NZASB considers whether *PBE Simple Format Reporting - Accrual* should be amended in this respect to be consistent with the revised ED.