

PUBLIC BENEFIT ENTITIES' CONCEPTUAL FRAMEWORK

This Authoritative Notice was issued on 19 May 2016 by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(c) of the Financial Reporting Act 2013.

This Authoritative Notice is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on 16 June 2016.

Reporting entities that are subject to this Authoritative Notice are required to apply it in accordance with the effective date, which is set out in Part B.

In finalising this Authoritative Notice, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This *Public Benefit Entities' Conceptual Framework* has been issued as a result of a new international public sector conceptual framework.

This Authoritative Notice, when applied, supersedes the *Public Benefit Entities' Framework* issued in September 2014.

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CONTENTS

	From page
Preface.....	4
Chapter 1: Role and Authority of the PBE Conceptual Framework.....	9
Chapter 2: Objectives and Users of General Purpose Financial Reporting	12
Chapter 3: Qualitative Characteristics.....	19
Chapter 4: Reporting Entity	25
Chapter 5: Elements in General Purpose Financial Reports.....	28
Chapter 6: Recognition in Financial Statements.....	35
Chapter 7: Measurement of Assets and Liabilities in Financial Statements	38
Chapter 8: Presentation in General Purpose Financial Reports	51
Basis for Conclusions on PBE Conceptual Framework.....	60
Part B: Effective Date.....	63

The following is available on the XRB website as additional material:

IPSASB Basis for Conclusions

The *Public Benefit Entities' Conceptual Framework* is set out in Chapters 1–8. The *Public Benefit Entities' Conceptual Framework* is based on *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* developed and approved by the International Public Sector Accounting Standards Board.

Preface

Introduction

1. The *Public Benefit Entities' Conceptual Framework* (the PBE Conceptual Framework) establishes the concepts that are to be applied in developing Public Benefit Entity Standards (PBE Standards) applicable to the preparation and presentation of general purpose financial reports (GPFRs) of public benefit entities. Public benefit entities applying PBE SFR- A (NFP) *Public Benefit Entity Simple Format Reporting – Accrual (Not-For-Profit)* or PBE SFR- A (PS) *Public Benefit Entity Simple Format Reporting – Accrual (Public Sector)* may also refer to, and consider the applicability of the definitions and concepts in the PBE Conceptual Framework to the extent that they do not conflict with those Standards.
- 1.1 Public benefit entities are defined as “Reporting entities whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to equity holders.”¹ Although both public sector and not-for-profit public benefit entities share certain characteristics, they also differ in some ways. This Preface therefore has two parts:
 - (a) Part A discusses the characteristics of public sector entities and the public sector as a whole that have influenced the development of the PBE Conceptual Framework and will influence the development of PBE Standards; and
 - (b) Part B discusses the characteristics of not-for-profit entities and the not-for-profit sector as a whole that have influenced the development of the PBE Conceptual Framework and will influence the development of PBE Standards.²

Part A: Public Sector Public Benefit Entities

2. The primary objective of most public sector entities is to deliver services to the public, rather than to make profits and generate a return on equity to investors. Consequently the performance of such entities can be only partially evaluated by examination of financial position, financial performance and cash flows. GPFRs provide information to users for accountability and decision-making purposes. Therefore, users of the GPFRs of public sector entities need information to support assessments of such matters as:
 - Whether the entity provided its services to constituents in an efficient and effective manner;
 - The resources currently available for future expenditures, and to what extent there are restrictions or conditions attached to their use;
 - To what extent the burden on future-year taxpayers³ of paying for current services has changed; and
 - Whether the entity’s ability to provide services has improved or deteriorated compared with the previous year.
3. Governments generally have broad powers, including the ability to establish and enforce legal requirements, and to change those requirements. Globally the public sector varies considerably in both its constitutional arrangements and its methods of operation. However, governance in the public sector generally involves the holding to account of the executive by a legislative body (or equivalent).
4. The following sections highlight characteristics of the public sector that the New Zealand Accounting Standards Board (NZASB) has considered in the development of the PBE Conceptual Framework.

The Volume and Financial Significance of Non-Exchange Transactions

5. In a non-exchange transaction, an entity receives value from another party without directly giving approximately equal value in exchange. Such transactions are common in the public sector. The level and quality of services received by an individual, or group of individuals, is not normally directly related to the level of taxes assessed. An individual or group may have to pay a charge or fee and/or may have had to

¹ External Reporting Board Standard Standard A1 *Application of the Accounting Standards Framework* contains guidance on determining whether an entity is a public benefit entity.

² Unless otherwise stated, references to public sector entities and not-for-profit entities throughout this PBE Conceptual Framework are to public sector public benefit entities and not-for-profit public benefit entities.

³ Where appropriate, references to taxpayers and taxes in this document should be read as encompassing ratepayers and rates.

make specified contributions to access certain services. However, such transactions are, generally, of a non-exchange nature, because the amount that an individual or group of individuals obtains in benefits will not be approximately equal to the amount of any fees paid or contributions made by the individual or group. The nature of non-exchange transactions may have an impact on how they are recognised, measured, and presented to best support assessments of the entity by service recipients and resource providers.

6. Taxation is a legally mandated, compulsory non-exchange transaction between individuals or entities and the government. Tax-raising powers can vary considerably, dependent upon the relationship between the powers of the national government and those of sub-national governments and other public sector entities. International public sector entities are largely funded by transfers from national, regional and state governments. Such funding may be governed by treaties and conventions or may be on a voluntary basis.
7. Governments and other public sector entities are accountable to resource providers, particularly to those that provide resources through taxes and other compulsory transactions. Chapter 2 *Objectives and Users of General Purpose Financial Reporting* discusses the accountability objective of financial reporting.

The Importance of Public Plans and Budgets

8. Many public sector entities in New Zealand are required to prepare and make publicly available their plans for the future, including prospective financial statements. Legislation often defines the contents of that documentation. For example, the Public Finance Act 1989 requires that, as part of the Budget process, the Government present forecast financial statements to the House of Representatives and the Local Government Act 2002 requires that local authorities prepare and adopt an annual plan, which must include forecast financial statements. The planning and budgeting documents that public sector entities are required to make available to Parliament or the public assist Parliament to exercise its oversight function, and assist constituents and their elected representatives to hold the entity's management financially accountable. These planning and budgeting documents outline the projected activities of public sector entities and explain how those activities are expected to be funded. For example, in the case of the Government the forecast financial statements support the appropriation requests.
9. Information that enables users to compare financial results with public plans or budgets facilitates an assessment of the extent to which a public sector entity has met its financial objectives. Such information promotes accountability and informs decision making in subsequent periods. Many public sector entities are therefore required by legislation to report against public plans or budgets. In the case of central government entities there are also requirements to demonstrate compliance with legal requirements relating to the public finances. The needs of users for prospective financial information from public sector entities is discussed in Chapter 2.

The Nature of Public Sector Activities and the Longevity of the Public Sector

10. Many public sector activities are long term and the ability to meet commitments depends upon future taxation and contributions. Many commitments arising from public sector activities and powers to levy future taxation do not meet the definitions of a liability and an asset in Chapter 5 *Elements in General Purpose Financial Reports*. Therefore, such commitments and powers are not recognised in the financial statements.
11. Consequently, the financial statements cannot provide all the information that users need on long-term activities, particularly those delivering social benefits. The financial consequences of many decisions will have an impact many years or even decades into the future, so GPFRs containing prospective financial information on the long-term sustainability of an entity's finances and key areas of spending are necessary for accountability and decision-making purposes as discussed in Chapter 2.
12. Although political control may change regularly, nation states generally have very long existences. While they may encounter severe financial difficulties and may default on sovereign debt obligations, nation states continue to exist. If sub-national entities get into financial difficulties, national governments might act as lenders of last resort or provide large scale guarantees. The main service delivery commitments of sub-national entities may continue to be funded by a higher level of government. In other cases public sector entities that are unable to meet their liabilities as they fall due may continue to exist by restructuring their operations.
13. The going concern principle underpins the preparation of the financial statements. Interpretation of the principle needs to reflect the issues discussed in paragraphs 11 and 12.

The Nature and Purpose of Assets and Liabilities in the Public Sector

14. In the public sector, the primary reason for holding property, plant, and equipment and other assets is for their service potential rather than their ability to generate cash flows⁴. Because of the types of services provided, a significant proportion of assets used by public sector entities is specialised—for example, roads and military assets. There may be a limited market for such assets and, even then, they may need considerable adaptation in order to be used by other operators. These factors have implications for the measurement of such assets. Chapter 7 *Measurement of Assets and Liabilities in Financial Statements* discusses measurement bases for assets.
15. Public sector entities may hold items that contribute to the historical and cultural character of a nation or region—for example, art treasures, historical buildings, and other artefacts. They may also be responsible for national parks and other areas of natural significance with native flora and fauna. Such items and areas are not generally held for sale, even if markets exist. Rather, public sector entities have a responsibility to preserve and maintain them for current and future generations.
16. Governments often have powers over natural and other resources such as mineral reserves, water, fishing grounds, forests and the electromagnetic spectrum. These powers allow governments to grant licenses for the use of such resources or to obtain royalties and taxes from their use. The definition of an asset and recognition criteria are discussed in Chapter 5 and Chapter 6 *Recognition in Financial Statements*.
17. Public sector entities incur liabilities related to their service performance objectives. Many liabilities arise from non-exchange transactions and include those related to the provision of social benefits. Liabilities may also arise from governments' role as a lender of last resort and from any obligations to transfer resources to those affected by disasters. In addition many governments have obligations that arise from monetary activities such as currency in circulation. The definition of a liability and recognition criteria are discussed in Chapters 5 and 6.

The Regulatory Role of Public Sector Entities

18. Public sector entities have powers to regulate entities operating in certain sectors of the economy, either directly or through specifically created agencies. The underlying public policy rationale for regulation is to safeguard the public interest in accordance with specified public policy objectives. Regulatory intervention can also occur where there are market imperfections or market failure for particular services, or to mitigate against factors such as pollution, the impact of which is not transmitted through pricing. Such regulatory activities are carried out in accordance with legal processes.
19. Governments may also regulate themselves and other public sector entities. Judgement may be necessary to determine whether such regulations create rights of, and obligations on, public sector entities that require recognition as assets and liabilities, or whether the public sector entity's ability to amend such regulations has an impact on how such rights and obligations are accounted for. Chapter 5 considers rights and obligations.

Relationship to Statistical Reporting

20. Many governments produce two types of ex-post financial information: (a) government finance statistics (GFS) on the general government sector (GGS) for the purpose of macroeconomic analysis and decision making, and (b) general purpose financial statements (financial statements) for accountability and decision making at an entity level, including financial statements for the whole of government reporting entity.
21. The overarching standards for macro-economic statistics are set out in the *System of National Accounts* (SNA). The SNA is a framework for a systematic and detailed description of the national economy and its components, including the GGS. These standards are then implemented at national or regional level. GFS reporting guidelines include the International Monetary Fund's Government Finance Statistics Manual.
22. General purpose financial statements prepared in accordance with PBE Standards and GFS reports have much in common. Both reporting frameworks are concerned with (a) financial, accrual-based information, (b) a government's assets, liabilities, revenue, and expenses and (c) comprehensive information on cash flows. There is considerable overlap between the two reporting frameworks that underpin this information.

⁴ Many public sector assets will generate cash flows, but this is often not the main reason for holding them.

23. However, PBE Standards and GFS reporting guidelines have different objectives. The objectives of financial reporting by public sector entities are to provide information about the reporting entity that is useful to users of GPFs for accountability purposes and decision-making purposes. GFS reports are used to (a) analyse fiscal policy options, make policy and evaluate the impact of fiscal policies, (b) determine the impact on the economy, and (c) compare fiscal outcomes nationally and internationally. The focus is on evaluating the impact of the GGS and broader public sector on the economy, within the complete macroeconomic statistics framework.
24. The different objectives and focus on different reporting entities lead to the different treatment of some transactions and events. The international accounting profession and statistical bodies are working together with the aim of removing differences between the two accounting frameworks that are not fundamental to their different objectives and reporting entities.

Part B: Not-For-Profit Public Benefit Entities

- 24.1 Consistent with the preceding discussion of public sector public benefit entities, the primary objective of a not-for-profit public benefit entity is to provide goods or services for community or social benefit rather than for a financial return to equity holders.⁵ This primary objective means that their performance can only be partially evaluated by examination of financial position, financial performance and cash flows. GPFs provide information to users for accountability and decision-making purposes. Therefore, users of the GPFs of not-for-profit entities need information to support assessments of such matters as:
- Why the entity has been established and what the entity is seeking to achieve;
 - Whether the entity provided its services to constituents in an efficient and effective manner;
 - The resources currently available for future expenditures, and to what extent there are restrictions or conditions attached to their use;
 - Whether the entity’s ability to provide services has improved or deteriorated compared with the previous year; and
 - The ability of the entity to continue achieving its objectives.
- 24.2 The following sections highlight characteristics of the not-for-profit sector that the NZASB has considered in the development of the PBE Conceptual Framework.

The Sector

- 24.3 The not-for-profit sector is vibrant and diverse. Not-for-profit entities are active in a number of sectors including education, research, health, sport and recreation, social services, culture, environmental protection, professional and business associations, religious activities and more.

Types of Not-For-Profit Entities

- 24.4 Not-for-profit entities are set up with a purpose, or set of purposes, and are often expected to pursue such objectives beyond the lifetime of the founders. This continued existence is achieved using a variety of organisational forms (for example, incorporated societies, unincorporated entities, trusts, charitable trusts, friendly societies, industrial and provident societies and companies). Legislative oversight occurs through a range of statutes, some of which shape the sector’s organisational forms. Although some not-for-profit entities may have formal ownership instruments, this is not common in New Zealand. Not-for-profit entities may plan to generate a financial surplus, but they generally have restrictions on how a surplus may be used.

Reliance on Volunteers

- 24.5 Many not-for-profit entities rely on active participation of volunteers. Members of the governing body are normally not paid for their work, and individuals contribute considerable time and effort in delivering services and providing administrative support. The contribution that volunteers make to the not-for-profit sector is significant, and without that contribution many social services might not be available to the public.

⁵ Subsequent references to “services” in the PBE Conceptual Framework encompass “goods”.

Funding

- 24.6 Not-for-profit entities are often dependent on “third-party” funding – funding from a source other than the recipient of their services. For example, not-for-profit entities may rely on government grants (donations/service contracts), donations from philanthropic organisations, and donations from the public. There may also be restrictions by the provider of the funding on how the funds may be spent.

Non-Exchange Transactions

- 24.7 In a non-exchange transaction, an entity receives value from another party without directly giving approximately equal value in exchange. Such transactions are common in the not-for-profit sector. Service recipients may have to pay a charge or fee and/or may have had to make specified contributions to access certain services. However, such transactions are, generally, of a non-exchange nature, because the amount that service recipients obtain in benefits will not be approximately equal to the amount of any fees paid or contributions made by the recipients. Similarly not-for-profit entities receive non-exchange revenue from resource providers in the form of grants, donations or bequests. The nature of non-exchange transactions may have an impact on how they are recognised, measured and presented to best support assessments of the entity by service recipients and resource providers.

The Nature and Purpose of Assets and Liabilities in the Not-For-Profit Sector

- 24.8 Not-for-profit entities may hold property, plant, and equipment and other assets both for their ability to generate cash flows and for their service potential. For example, not-for-profit entities with environmental aims may hold land in order to achieve their environmental objectives. Not-for-profit entities may also hold items that contribute to the historical and cultural character of a nation or region.

Non-Financial Information

- 24.9 The most important part of the “story” of a not-for-profit entity is the non-financial information. It is critically important for the user of a GPFR prepared by a not-for-profit entity to be able to understand why the entity has been established, and how it is working towards achieving its financial and service performance objectives.
- 24.10 In the not-for-profit context, the funders of services such as donors are often removed from the delivery transaction because the output is provided to someone other than the funder. In addition, the decision about exactly what services are delivered is usually made by persons other than the funder, for example, the governing body of the delivery entity. In this situation the funders are reliant on GPFRs for information about what services have been delivered with the funding provided and information about the outcomes that entity is seeking to influence.

**CHAPTER 1: ROLE AND AUTHORITY OF THE
PBE CONCEPTUAL FRAMEWORK**

CONTENTS

	Paragraph
Role of the PBE Conceptual Framework.....	1.1–1.1.2
Authority of the PBE Conceptual Framework.....	1.2–1.3
General Purpose Financial Reports.....	1.4–1.7
Applicability of the PBE Conceptual Framework.....	1.8

Role of the PBE Conceptual Framework

- 1.1 The Public Benefit Entities' Conceptual Framework (the PBE Conceptual Framework) establishes the concepts that underpin general purpose financial reporting (financial reporting) by public benefit entities.⁶
- 1.1.1 The role of the PBE Conceptual Framework is to:
- (a) Assist the NZASB in developing PBE Standards applicable to the preparation and presentation of general purpose financial reports (GPFRs) of public benefit entities;
 - (b) Assist the NZASB in its role in commenting on the development of International Public Sector Accounting Standards (IPSASs) by the International Public Sector Accounting Standards Board (IPSASB); and
 - (c) Assist preparers of general purpose financial reports. For example, it may assist preparers in developing consistent accounting policies when dealing with topics that have yet to form the subject of a PBE Standard or when a Standard allows a choice of accounting policy.
- 1.1.2 Public benefit entities applying PBE SFR- A (NFP) *Public Benefit Entity Simple Format Reporting – Accrual (Not-For-Profit)* or PBE SFR- A (PS) *Public Benefit Entity Simple Format Reporting – Accrual (Public Sector)* may also refer to, and consider the applicability of the definitions and concepts in the PBE Conceptual Framework to the extent that they do not conflict with those Standards.

Authority of the PBE Conceptual Framework

- 1.2 The PBE Conceptual Framework does not establish authoritative requirements for financial reporting by public benefit entities that report in accordance with PBE Standards, nor does it override the requirements of PBE Standards. Authoritative requirements relating to the recognition, measurement and presentation of transactions and other events and activities that are reported in GPFRs are specified in PBE Standards.
- 1.3 The PBE Conceptual Framework can provide guidance in dealing with financial reporting issues not dealt with by PBE Standards. In these circumstances, preparers and others can refer to and consider the applicability of the definitions, recognition criteria, measurement principles, and other concepts identified in the PBE Conceptual Framework.

General Purpose Financial Reports

- 1.4 GPFRs are a central component of, and support and enhance, transparent financial reporting by public benefit entities, including public sector entities and not-for-profit entities. GPFRs are financial reports intended to meet the information needs of users who are unable to require the preparation of financial reports tailored to meet their specific information needs.
- 1.5 Some users of financial information may have the authority to require the preparation of reports tailored to meet their specific information needs. While such parties may find the information provided by GPFRs useful for their purposes, GPFRs are not developed to specifically respond to their particular information needs.
- 1.6 GPFRs are likely to comprise multiple reports, each responding more directly to certain aspects of the objectives of financial reporting and matters included within the scope of financial reporting. For example, some entities present prospective financial statements as well as historical financial statements. Entities may also present GPFRs that include both financial statements and service performance information. GPFRs encompass financial statements including their notes (hereafter referred to as financial statements, unless specified otherwise), and the presentation of information that enhances, complements and supplements the financial statements.
- 1.7 The scope of financial reporting establishes the boundary around the transactions, other events and activities that may be reported in GPFRs. The scope of financial reporting is determined by the information needs of the primary users of GPFRs and the objectives of financial reporting. The factors that determine what may be encompassed within the scope of financial reporting are outlined in the next chapter.

⁶ External Reporting Board Standard A1 *Application of the Accounting Standards Framework* identifies the standards to be applied by public benefit entities that have a statutory obligation to prepare general purpose financial reports.

Applicability of the PBE Conceptual Framework

1.8 The PBE Conceptual Framework applies to financial reporting by public benefit entities that apply PBE Standards. Therefore, it applies to a wide range of public sector and not-for-profit reporting entities including:

- Government departments;
- Crown entities;
- Local authorities;
- Trusts;
- Council-controlled organisations (CCOs);
- Charities; and
- Not-for-profit companies.

CHAPTER 2: OBJECTIVES AND USERS OF GENERAL PURPOSE FINANCIAL REPORTING

CONTENTS

	Paragraph
Objectives of Financial Reporting	2.1–2.2
Users of General Purpose Financial Reports	2.3–2.6
Accountability and Decision Making	2.7–2.10
Information Needs of Service Recipients and Resource Providers	2.11–2.13
Information Provided by General Purpose Financial Reports.....	2.14–2.28
Financial Position, Financial Performance, and Cash Flows	2.14–2.17
Plans and Budgets and Compliance with Legislation or Other Authority Governing the Raising and Use of Resources.....	2.18–2.21
Service Performance.....	2.22–2.24
Prospective Financial and Non-Financial Information	2.24.1–2.27
Explanatory Information.....	2.28
Financial Statements and Information that Enhances, Complements and Supplements the Financial Statements	2.29–2.30
Other Sources of Information	2.31

Objectives of Financial Reporting

- 2.1 The objectives of financial reporting by public benefit entities are to provide information about the entity that is useful to users of GPFRs for accountability purposes and for decision-making purposes (hereafter referred to as “useful for accountability and decision-making purposes”).
- 2.2 Financial reporting is not an end in itself. Its purpose is to provide information useful to users of GPFRs. The objectives of financial reporting are therefore determined by reference to the users of GPFRs, and their information needs.

Users of General Purpose Financial Reports

- 2.3 Public benefit entities raise resources from funders or financial supporters, (for example, taxpayers, members and donors), lenders and other resource providers for use in the provision of services to citizens and other service recipients. These entities are accountable for their management and use of resources to those that provide them with resources, and to those that depend on them to use those resources to deliver necessary services. Those that provide the resources and receive, or expect to receive, the services also require information as input for decision-making purposes.
- 2.4 Consequently, GPFRs of public benefit entities are developed primarily to respond to the information needs of service recipients and resource providers who do not possess the authority to require a public benefit entity to disclose the information they need for accountability and decision-making purposes. The legislature (or similar body) and elected or appointed representatives are also primary users of GPFRs, and make extensive and ongoing use of GPFRs when acting in their capacity as representatives of the interests of service recipients and resource providers. Therefore, for the purposes of the PBE Conceptual Framework, the primary users of GPFRs are service recipients and their representatives and resource providers and their representatives (hereafter referred to as “service recipients and resource providers”, unless identified otherwise).
- 2.5 Citizens receive services from, and provide resources to, public benefit entities. Therefore, citizens are primary users of GPFRs. Some service recipients and some resource providers that rely on GPFRs for the information they need for accountability and decision-making purposes may not be citizens—for example, residents who pay taxes and/or receive benefits but are not citizens; multilateral or bilateral donor agencies and many lenders and corporations that provide resources to, and transact with, a public benefit entity; and those that fund, and/or benefit from, the services provided by international governmental organisations. In most cases, public sector entities that provide resources to international governmental organisations are dependent on GPFRs of those organisations for information for accountability and decision-making purposes.
- 2.6 GPFRs prepared to respond to the information needs of service recipients and resource providers for accountability and decision-making purposes may also provide information useful to other parties and for other purposes. For example, statisticians, analysts, the media, financial advisors, public interest and lobby groups and others may find the information provided by GPFRs useful for their own purposes. Organisations that have the authority to require the preparation of financial reports tailored to meet their own specific information needs may also use the information provided by GPFRs for their own purposes—for example, regulatory and oversight bodies, audit institutions, subcommittees of the legislature or other governing body, central agencies and budget controllers, entity management, rating agencies and, in some cases, lending institutions and providers of development and other assistance. While these other parties may find the information provided by GPFRs useful, they are not the primary users of GPFRs. Therefore, GPFRs are not developed to specifically respond to their particular information needs.

Accountability and Decision Making

- 2.7 The primary objective of public benefit entities is to provide goods or services for community or social benefit. Services provided by public sector entities include, for example, welfare, policing, public education, national security and defence services. Services provided by not-for-profit entities and, in some cases public sector entities, include, for example, health, social welfare, housing, research, cultural, sport and recreation, environmental, employment and training, community development and religious services. Although public sector and not-for-profit entities may enter into contracts for the delivery of services, in

many cases, services are provided as a result of a non-exchange transaction⁷ and in a non-competitive environment.

- 2.8 Public benefit entities are accountable to those that provide them with resources, and to those that depend on them to use those resources to deliver services during the reporting period and over the longer term. The discharge of accountability obligations requires the provision of information about the entity’s management of the resources entrusted to it for the delivery of services to constituents and others, and its compliance with legislation, regulation, or other authority that governs its service performance and other operations. Given the way in which the services provided by public benefit entities are funded (primarily by non-exchange transactions) and the dependency of service recipients on the provision of those services over the long term, the discharge of accountability obligations will also require the provision of information about such matters as the entity’s service performance during the reporting period, and its capacity to continue to provide services in future periods.
- 2.9 Service recipients and resource providers will also require information as input for making decisions. For example:
- Lenders, creditors, donors, members and others that provide resources on a voluntary basis, including in an exchange transaction, make decisions about whether to provide resources to support the current and future activities of the entity. In some circumstances, elected or appointed representatives who depend on GPFs for the information they need, can make or influence decisions about the services to be provided and the resources allocated to support the delivery of those services; and
 - Taxpayers do not usually provide funds to public sector entities on a voluntary basis or as a result of an exchange transaction. In addition, in many cases, they do not have the discretion to choose whether or not to accept the services provided by a public sector entity or to choose an alternative service provider. Consequently, they have little direct or immediate capacity to make decisions about whether to provide resources to the government, the resources to be allocated for the provision of services by a particular public sector entity or whether to purchase or consume the services provided. However, service recipients and resource providers can make decisions about their voting preferences, and representations they make to elected officials or other representative bodies—these decisions may have resource allocation consequences for certain public sector entities.
- 2.10 Information provided in GPFs for accountability purposes will contribute to, and inform, decision making. For example, information about the costs, efficiency and effectiveness of past service performance the amount and sources of cost recovery, and the resources available to support future activities will be necessary for the discharge of accountability. This information will also be useful for decision making by users of GPFs, including decisions that donors and other financial supporters make about providing resources to the entity.

Information Needs of Service Recipients and Resource Providers

- 2.11 For accountability and decision-making purposes, service recipients and resource providers will need information that supports the assessments of such matters as:
- The performance of the entity during the reporting period in, for example:
 - Meeting its service performance and other operating and financial objectives;
 - Managing the resources it is responsible for;
 - Complying with relevant budgetary, legislative, and other authority regulating the raising and use of resources;
 - The liquidity (for example, ability to meet current obligations) and solvency (for example, ability to meet obligations over the long term) of the entity;

⁷ Exchange transactions are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equally value to another entity in exchange. Non-exchange transactions are transactions in which an entity receives value from another entity without directly giving approximately equal value in exchange.

- The sustainability of the entity’s service performance and other operations over the long term, and changes therein as a result of the activities of the entity during the reporting period including, for example:
 - The capacity of the entity to continue to fund its activities and to meet its operational objectives in the future (its financial capacity), including the likely sources of funding and the extent to which the entity is dependent on, and therefore vulnerable to, funding or demand pressures outside its control;
 - The physical and other resources currently available to support the provision of services in future periods (its operational capacity); and
- The capacity of the entity to adapt to changing circumstances, whether changes in demographics or changes in domestic or global economic conditions which are likely to impact the nature or composition of the activities it undertakes and the services it provides.

2.12 The information service recipients and resource providers need for these purposes is likely to overlap in many respects. For example, service recipients will require information as input to assessments of such matters as whether:

- The entity is using resources economically, efficiently, effectively and as intended, and whether such use is in their interest;
- The range, volume and cost of services provided during the reporting period are appropriate, and the amounts and sources of their cost recoveries; and
- Current levels of revenue are sufficient to maintain the volume and quality of services currently provided.

Service recipients will also require information about the consequences of decisions made, and activities undertaken, by the entity during the reporting period on the resources available to support the provision of services in future periods, the entity’s anticipated future services and objectives, and the amounts and sources of cost recoveries necessary to support those activities.

2.13 Resource providers will require information as input to assessments of such matters as whether the entity:

- Is achieving the objectives established as the justification for the resources raised during the reporting period;
- Funded current operations from funds raised in the current period or from borrowings or other sources; and
- Is likely to need additional (or less) resources in the future, and the likely sources of those resources.

Lenders and creditors will require information as input to assessments of the liquidity of the entity and, therefore, whether the amount and timing of repayment will be as agreed. Donors will require information to support assessments of whether the entity is using resources economically, efficiently, effectively and as intended. They will also require information about the entity’s anticipated future service performance and resource needs.

Information Provided by General Purpose Financial Reports

Financial Position, Financial Performance, and Cash Flows

2.14 Information about the financial position of a public benefit entity will enable users to identify the resources of the entity and claims to those resources at the reporting date. This will provide information useful as input to assessments of such matters as:

- The extent to which management has discharged its responsibilities for safekeeping and managing the resources of the entity;
- The extent to which resources are available to support future service performance, and changes during the reporting period in the amount and composition of those resources and claims to those resources; and
- The amounts and timing of future cash flows necessary to service and repay existing claims to the entity’s resources.

- 2.15 Information about the financial performance of a public benefit entity will inform assessments of matters such as whether the entity has acquired resources economically, and used them efficiently and effectively to achieve its service performance objectives. Information about the costs of services and the amounts and sources of cost recovery during the reporting period will assist users to determine whether operating costs were recovered from, for example, taxes, user charges, donations, contributions and transfers, or were financed by increasing the level of indebtedness of the entity.
- 2.16 Information about the cash flows of a public benefit entity contributes to assessments of financial performance and the entity's liquidity and solvency. It indicates how the entity raised and used cash during the period, including its borrowing and repayment of borrowing and its acquisition and sale of, for example, property, plant, and equipment. It also identifies the cash received from, for example, taxes, donations, investments and the cash transfers made to, and received from, other public benefit organisations. Information about cash flows can also support assessments of the entity's compliance with spending mandates expressed in cash flow terms, and inform assessments of the likely amounts and sources of cash inflows needed in future periods to support service performance objectives.
- 2.17 Information about financial position, financial performance and cash flows are typically presented in financial statements. To assist users to better understand, interpret and place in context the information presented in the financial statements, GPFRs may also provide financial and non-financial information that enhances, complements and supplements the financial statements, including information about such matters as the entity's:
- Actual financial performance and financial position compared to public plans or budgets, including compliance with any legislative spending controls and other authority governing its operations;
 - Service performance during the reporting period; and
 - Expectations regarding service performance and other activities in future periods, and the long-term consequences of decisions made and activities undertaken during the reporting period, including those that may impact expectations about the future.

Depending upon the level of detail and purpose of this additional information it may be presented in the notes to the financial statements, as a separate part of the GPFR containing the financial statements or in a separate GPFR.

Plans and Budgets and Compliance with Legislation or Other Authority Governing the Raising and Use of Resources

- 2.18 Many public sector entities are required to make plans or budgets publicly available. These plans or budgets provide interested parties with financial information about the entity's operational plans for the forthcoming period, its capital needs and, often, its service performance objectives and expectations. They are used to justify the raising of resources from taxpayers and other resource providers, and may also establish the authority for expenditure of resources.
- 2.19 Although public sector entities may receive resources from donors, lenders or as a result of exchange transactions they are predominantly funded by taxes or revenue from other non-exchange transactions. The expected nature and level of funding from taxes and other non-exchange transactions is generally set out in these public plans or budgets.
- 2.20 GPFRs provide information about the financial results (whether described as "surplus or deficit," "profit or loss," or by other terms), performance and cash flows of the entity during the reporting period, its assets and liabilities at the reporting date and the change therein during the reporting period, and its service performance achievements.
- 2.21 The inclusion within GPFRs of information that assists users in assessing the extent to which revenues, expenses, cash flows and financial results of the entity comply with the estimates reflected in public plans or budgets, and the entity's adherence to relevant legislation or other authority governing the raising and use of resources, is important in determining how well a public sector entity has met its financial objectives. Such information is necessary for the discharge of a public sector entity's accountability to its constituents, enhances the assessment of the financial performance of the entity and will inform decision making.

Service Performance

- 2.22 The primary objective of public benefit entities is to provide services for community or social benefit. Consequently, the financial performance of public benefit entities will not be fully or adequately reflected in any measure of financial results. Therefore, their financial results will need to be assessed in the context of their service performance.
- 2.23 In some cases, quantitative measures of the outputs and outcomes of the entity’s activities during the reporting period will provide relevant information about the entity’s service performance—for example, information about the cost, volume, and frequency of service delivery, and the relationship of services provided to the resource base of the entity. In other cases, information about service performance may need to be communicated by an explanation of the quality of particular services provided or the impact of certain services.
- 2.24 Reporting non-financial as well as financial information about service performance activities, achievements and/or outcomes during the reporting period will provide input to assessments of the economy, efficiency, and effectiveness of the entity’s operations. Reporting such information is necessary for a public benefit entity to discharge its obligation to be accountable—that is, to account for, and justify its use of resources. Decisions that donors make about the allocation of resources to particular entities or purposes are also made, at least in part, in response to information about service performance during the reporting period, and future service performance objectives.

Prospective Financial and Non-Financial Information

- 2.24.1 In planning for the future, entities may prepare prospective financial statements and service performance information that reflect the projected level and mix of services. Many public sector entities are required to make prospective information publicly available. However, not-for-profit entities are not generally subject to requirements to make prospective information publicly available. The following discussion focuses on public sector entities, but aspects of the discussion may also be relevant to not-for-profit entities that make prospective financial information publicly available.
- 2.25 Given the longevity of governments and many government activities, the financial consequences of many decisions made in the reporting period may only become clear many years into the future. Financial statements which present information about financial position at a point in time and financial performance and cash flows over the reporting period will then need to be assessed in the context of the long term.
- 2.26 Decisions made by a public sector entity in a particular period about the provision of services in the future and the funding of those services can have significant consequences for:
- Constituents who will be dependent on those services in the future; and
 - Current and future generations of taxpayers and other involuntary resource providers who will provide the taxes and levies to fund the planned services and related financial commitments.
- 2.27 Information about the entity’s anticipated future services and objectives, their likely impact on the future resource needs of the entity and the likely sources of funding for such resources, will be necessary as input to any assessment of the ability of the public sector entity to meet its service performance objectives and financial commitments in the future. The disclosure of such information in GPFRs will support assessments of the sustainability of the provision of services by a public sector entity, enhance the accountability of the entity and provide additional information useful for decision-making purposes.

Explanatory Information

- 2.28 Information about the major factors underlying the financial and service performance of the entity during the reporting period and the assumptions that underpin expectations about, and factors that are likely to influence, the entity’s future performance may be presented in GPFRs. Such information will assist users to better understand and place in context the financial and non-financial information included in GPFRs, and enhance the role of GPFRs in providing information useful for accountability and decision-making purposes.

Financial Statements and Information that Enhances, Complements and Supplements the Financial Statements

- 2.29 The scope of financial reporting establishes the boundary around the transactions, other events and activities that may be reported in GPFRs. To respond to the information needs of users, the PBE Conceptual Framework reflects a scope for financial reporting that is more comprehensive than that encompassed by financial statements. It provides for the presentation within GPFRs of additional information that enhances, complements, and supplements those statements.
- 2.30 While the PBE Conceptual Framework reflects a scope of financial reporting that is more comprehensive than that encompassed by financial statements, information presented in financial statements remains at the core of financial reporting. How the elements of financial statements are defined, recognised and measured, and forms of presentation and communication that might be adopted for information included within GPFRs, is considered in other chapters of the PBE Conceptual Framework and in the development of individual PBE Standards, as appropriate.

Other Sources of Information

- 2.31 GPFRs play a significant role in communicating the information necessary to demonstrate accountability, as well as providing information useful as input for decision-making purposes. However, it is unlikely that GPFRs will provide all the information users need for accountability and decision-making purposes. For example, while comparison of actual with budget information for the reporting period may be included in the GPFRs of public sector entities, the plans and budgets issued by public sector entities provide more detailed financial and non-financial information. Public benefit entities and independent agencies also issue reports on the need for, and sustainability of, existing services and anticipated economic conditions and changes in the demographics over the medium and longer term that will influence budgets and future service needs. Consequently, service recipients and resource providers may also need to consider information from other sources, including reports on current and anticipated economic conditions, budgets and forecasts, and information about policy initiatives not reported in GPFRs.

CHAPTER 3: QUALITATIVE CHARACTERISTICS

CONTENTS

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

Introduction

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

Relevance

- 3.6 Financial and non-financial information is relevant if it is capable of making a difference in achieving the objectives of financial reporting. Financial and non-financial information is capable of making a difference when it has confirmatory value, predictive value, or both. It may be capable of making a difference, and thus be relevant, even if some users choose not to take advantage of it or are already aware of it.
- 3.7 Financial and non-financial information has confirmatory value if it confirms or changes past (or present) expectations. For example, information will be relevant for accountability and decision-making purposes if it confirms expectations about such matters as the extent to which managers have discharged their responsibilities for the efficient and effective use of resources, the achievement of specified service performance objectives, and compliance with relevant budgetary, legislative and other requirements.
- 3.8 GPFRs may present information about an entity's anticipated future services, objectives and costs, and the amount and sources of the resources that are intended to be allocated to providing services in the future. Such future oriented information will have predictive value and be relevant for accountability and decision-making purposes. Information about economic and other phenomena that exist or have already occurred can also have predictive value in helping form expectations about the future. For example, information that confirms or disproves past expectations can reinforce or change expectations about financial results and service outcomes that may occur in the future.
- 3.9 The confirmatory and predictive roles of information are interrelated—for example, information about the current level and structure of an entity's resources and claims to those resources helps users to confirm the outcome of resource management strategies during the period, and to predict an entity's ability to respond to changing circumstances and anticipated future service needs. The same information helps to confirm or correct users' past expectations and predictions about the entity's ability to respond to such changes. It also helps to confirm or correct prospective financial information included in previous GPFRs.

Faithful Representation

- 3.10 To be useful in financial reporting, information must be a faithful representation of the economic and other phenomena that it purports to represent. Faithful representation is attained when the depiction of the phenomenon is complete, neutral, and free from material error. Information that faithfully represents an economic or other phenomenon depicts the substance of the underlying transaction, other event, activity or circumstance—which is not necessarily always the same as its legal form.

- 3.11 In practice, it may not be possible to know or confirm whether information presented in GPFRs is complete, neutral, and free from material error. However, information should be as complete, neutral, and free from error as is possible.
- 3.12 An omission of some information can cause the representation of an economic or other phenomenon to be false or misleading, and thus not useful to users of GPFRs. For example, a complete depiction of the item “plant and equipment” in GPFRs will include a numeric representation of the aggregate amount of plant and equipment together with other quantitative, descriptive and explanatory information necessary to faithfully represent that class of assets. In some cases, this may include the disclosure of information about such matters as the major classes of plant and equipment, factors that have affected their use in the past or might impact on their use in the future, and the basis and process for determining their numeric representation. Similarly, prospective financial and non-financial information and information about the achievement of service performance objectives and outcomes included in GPFRs will need to be presented with the key assumptions that underlie that information and any explanations that are necessary to ensure that its depiction is complete and useful to users.
- 3.13 Neutrality in financial reporting is the absence of bias. It means that the selection and presentation of financial and non-financial information is not made with the intention of attaining a particular predetermined result—for example, to influence in a particular way users’ assessment of the discharge of accountability by the entity or a decision or judgement that is to be made, or to induce particular behaviour.
- 3.14 Neutral information faithfully represents the economic and other phenomena that it purports to represent. However, to require information included in GPFRs to be neutral does not mean that it is not without purpose or that it will not influence behaviour. Relevance is a qualitative characteristic and, by definition, relevant information is capable of influencing users’ assessments and decisions.
- 3.15 The economic and other phenomena represented in GPFRs generally occur under conditions of uncertainty. Information included in GPFRs will therefore often include estimates that incorporate management’s judgement. To faithfully represent an economic or other phenomenon, an estimate must be based on appropriate inputs, and each input must reflect the best available information. Caution will need to be exercised when dealing with uncertainty. It may sometimes be necessary to explicitly disclose the degree of uncertainty in financial and non-financial information to faithfully represent economic and other phenomena.
- 3.16 Free from material error does not mean complete accuracy in all respects. Free from material error means there are no errors or omissions that are individually or collectively material in the description of the phenomenon, and the process used to produce the reported information has been applied as described. In some cases, it may be possible to determine the accuracy of some information included in GPFRs—for example, the amount of a cash transfer to another entity, the volume of services delivered or the price paid for the acquisition of plant and equipment. However, in other cases it may not—for example, the accuracy of an estimate of the value or cost of an item or the effectiveness of providing particular services may not be able to be determined. In these cases, the estimate will be free from material error if the amount is clearly described as an estimate, the nature and limitations of the estimation process are explained, and no material errors have been identified in selecting and applying an appropriate process for developing the estimate.

Understandability

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

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

Timeliness

- 3.19 Timeliness means having information available for users before it loses its capacity to be useful for accountability and decision-making purposes. Having relevant information available sooner can enhance its usefulness as input to assessments of accountability and its capacity to inform and influence decisions that need to be made. A lack of timeliness can render information less useful.
- 3.20 Some items of information may continue to be useful long after the reporting period or reporting date. For example, for accountability and decision-making purposes, users of GPFRs may need to assess trends in the financial and service performance of the entity and, in the case of public sector entities, an entity's compliance with plans or budgets over a number of reporting periods. In addition, the outcome and effects of some services may not be determinable until future periods—for example, this may occur in respect of services intended to enhance the economic well-being of constituents, reduce the incidence of a particular disease, or increase literacy levels of certain age groups.

Comparability

- 3.21 Comparability is the quality of information that enables users to identify similarities in, and differences between, two sets of phenomena. Comparability is not a quality of an individual item of information, but rather a quality of the relationship between two or more items of information.
- 3.22 Comparability differs from consistency. Consistency refers to the use of the same accounting principles or policies and basis of preparation, either from period to period within an entity or in a single period across more than one entity. Comparability is the goal, and consistency helps in achieving that goal. In some cases, the accounting principles or policies adopted by an entity may be revised to better represent a particular transaction or event in GPFRs. In these cases, the inclusion of additional disclosures or explanation may be necessary to satisfy the characteristics of comparability.
- 3.23 Comparability also differs from uniformity. For information to be comparable, like things must look alike and different things must look different. An over-emphasis on uniformity may reduce comparability by making unlike things look alike. Comparability of information in GPFRs is not enhanced by making unlike things look alike, any more than it is by making like things look different.
- 3.24 Information about the entity's financial position, financial performance, cash flows, compliance with plans or budgets, relevant legislation or other authority governing the raising and use of resources, service performance achievements, and its future plans is necessary for accountability purposes and useful as input for decision-making purposes. The usefulness of such information is enhanced if it can be compared with, for example:
- Prospective financial and non-financial information previously presented for that reporting period or reporting date;
 - Similar information about the same entity for some other period or some other point in time; and
 - Similar information about other entities (for example, public benefit entities providing similar services in different jurisdictions) for the same reporting period.
- 3.25 Consistent application of accounting principles, policies and basis of preparation to prospective financial and non-financial information and actual outcomes will enhance the usefulness of any comparison of projected and actual results. Comparability with other entities may be less significant for explanations of management's perception or opinion of the factors underlying the entity's current performance.

Verifiability

- 3.26 Verifiability is the quality of information that helps assure users that information in GPFRs faithfully represents the economic and other phenomena that it purports to represent. Supportability is sometimes used to describe this quality when applied in respect of explanatory information and prospective financial and non-financial quantitative information disclosed in GPFRs—that is, the quality of information that helps assure users that explanatory or prospective financial and non-financial quantitative information

faithfully represents the economic and other phenomena that it purports to represent. Whether referred to as verifiability or supportability, the characteristic implies that different knowledgeable and independent observers could reach general consensus, although not necessarily complete agreement, that either:

- The information represents the economic and other phenomena that it purports to represent without material error or bias; or
 - An appropriate recognition, measurement, or representation method has been applied without material error or bias.
- 3.27 To be verifiable, information need not be a single point estimate. A range of possible amounts and the related probabilities also can be verified.
- 3.28 Verification may be direct or indirect. With direct verification, an amount or other representation is itself verified, such as by (a) counting cash, (b) observing marketable securities and their quoted prices, or (c) confirming that the factors identified as influencing past service performance were present and operated with the effect identified. With indirect verification, the amount or other representation is verified by checking the inputs and recalculating the outputs using the same accounting convention or methodology. An example is verifying the carrying amount of inventory by checking the inputs (quantities and costs) and recalculating the ending inventory using the same cost flow assumption (for example, average cost or first-in-first-out).
- 3.29 The quality of verifiability (or supportability if such term is used to describe this characteristic) is not an absolute—some information may be more or less capable of verification than other information. However, the more verifiable is the information included in GPFRs, the more it will assure users that the information faithfully represents the economic and other phenomena that it purports to represent.
- 3.30 GPFRs of public benefit entities may include financial and other quantitative information and explanations about (a) key influences on the entity’s performance during the period, (b) the anticipated future effects or outcomes of services undertaken during the reporting period, and (c) prospective financial and non-financial information. It may not be possible to verify the accuracy of all quantitative representations and explanations of such information until a future period, if at all.
- 3.31 To help assure users that prospective financial and non-financial quantitative information and explanations included in GPFRs faithfully represents the economic and other phenomena that they purport to represent, the assumptions that underlie the information disclosed, the methodologies adopted in compiling that information, and the factors and circumstances that support any opinions expressed or disclosures made should be transparent. This will enable users to form judgements about the appropriateness of those assumptions and the method of compilation, measurement, representation and interpretation of the information.

Constraints on Information Included in General Purpose Financial Reports

Materiality

- 3.32 Information is material if its omission or misstatement 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. GPFRs may encompass qualitative and quantitative information about service performance achievements during the reporting period, and expectations about service performance objectives and financial outcomes in the future. Consequently, it is not possible to specify a uniform quantitative threshold 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 PBE Conceptual Framework. In developing PBE Standards, the NZASB 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 PBE Standard, entities preparing GPFRs will also consider the materiality of, for example, the application of a particular accounting policy and the separate disclosure of particular items of information.

Cost-Benefit

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

Balance between the Qualitative Characteristics

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

CHAPTER 4: REPORTING ENTITY

CONTENTS

	Paragraph
Introduction	4.1–4.2
Key Characteristics of a Reporting Entity	4.3–4.11

Introduction

- 4.1 A public benefit reporting entity⁸ is a government or other public sector organisation, not-for-profit entity or identifiable area of activity (hereafter referred to as an entity or public benefit entity) that prepares GPFs.
- 4.2 A public benefit reporting entity may comprise two or more separate entities that present GPFs as if they are a single entity—such a reporting entity is referred to as a group reporting entity.

Key Characteristics of a Reporting Entity

- 4.3 Key characteristics of a public sector reporting entity are that:
- It is an entity that raises resources from, or on behalf of, constituents and/or uses resources to undertake activities for the benefit of, or on behalf of, those constituents; and
 - There are service recipients or resource providers dependent on GPFs of the entity for information for accountability or decision-making purposes.
- 4.3.1 Key characteristics of a not-for-profit reporting entity are that:
- It is an entity that receives resources from members, the public and/or funding organisations which it uses to undertake activities for the benefit of, or on behalf of, its members and/or community; and
 - There are service recipients or resource providers dependent on GPFs of the entity for information for accountability or decision-making purposes.
- 4.4 A government may establish and/or operate through administrative units such as ministries or departments. It may also operate through trusts, statutory authorities, government corporations and other entities with a separate legal identity or operational autonomy to undertake or otherwise support the provision of services to constituents. Not-for-profit entities operate through a variety of structures to undertake their activities. Some entities, for example, incorporated societies, charitable trust boards and companies, have a separate legal identity while others are unincorporated. Other public benefit entities may also undertake certain activities through, and may benefit from and be exposed to a financial burden or loss as a result of, the activities of entities with a separate legal identity or operational autonomy.
- 4.5 GPFs are prepared to report information useful to users for accountability and decision-making purposes. Service recipients and resource providers are the primary users of GPFs. Consequently, a key characteristic of a reporting entity, including a group reporting entity, is the existence of service recipients or resource providers who are dependent on GPFs of that entity or group of entities for information for accountability or decision-making purposes.
- 4.6 GPFs encompass financial statements and information that enhances, complements and supplements the financial statements. Financial statements present information about the resources of the reporting entity or group reporting entity and claims to those resources at the reporting date, and changes to those resources and claims and cash flows during the reporting period.
- 4.7 The factors that are likely to signal the existence of users of GPFs of a public benefit entity or group of entities include an entity having the responsibility or capacity to raise or deploy resources, the use of public money or the management of public assets or liabilities, incur liabilities, or undertake activities to achieve service performance objectives. The greater the resources that a public benefit entity raises, manages and/or has the capacity to deploy, the greater the liabilities it incurs and the greater the economic or social impact of its activities, the more likely it is that there will exist service recipients or resource providers who are dependent on GPFs for information about it for accountability and decision-making purposes. In the case of a not-for-profit entity, there is often an additional accountability aspect in relation to the special status granted to the entity (for example, the benefits associated with being a registered charity).

⁸ This definition of a reporting entity differs from that used in the Financial Reporting Act 2013. The Financial Reporting Act 2013 defines a “reporting entity” as an “entity whose financial statements, or group financial statements, reports or other information is required by any enactment to comply, or be prepared in accordance, with generally accepted accounting practice or non-GAAP standards.”

- 4.8 The preparation of GPFs is not a cost-free process. Therefore, if the imposition of financial reporting requirements is to be efficient and effective, it is important that only those public benefit entities for which such users exist are required to prepare GPFs.
- 4.9 In many cases, it will be clear whether or not there exist service recipients or resource providers that are dependent on GPFs of a public benefit entity for information for accountability and decision-making purposes. For example, such users are likely to exist for GPFs of a government at the national or local government level and for international public sector organisations. This is because these governments and organisations generally have the capacity to raise substantial resources from and/or deploy substantial resources on behalf of their constituents, to incur liabilities, and to impact the economic and/or social well-being of the communities that depend on them for the provision of services. Users are likely to exist for GPFs of a not-for-profit entity because these entities receive donations and grants from members, citizens, funders and government for the delivery of services which benefit their members and/or communities.
- 4.10 However, it may not always be clear whether there are service recipients or resource providers that are dependent on GPFs of, for example, individual government departments and agencies or identifiable areas of activity for information for accountability and decision-making purposes. Determining whether these organisations or activities should be identified as reporting entities and, consequently, be required to prepare GPFs will involve the exercise of professional judgement.
- 4.11 The government and some other public benefit entities have a separate identity or standing in law (a legal identity). However, public sector organisations, not-for-profit entities and activities without a separate legal identity may also raise or deploy resources, acquire or manage assets, incur liabilities, undertake activities to achieve service performance objectives or otherwise implement the policy of the government or national or international bodies with which they are affiliated. Service recipients and resource providers may depend on GPFs of these entities and activities for information for accountability and decision-making purposes. Consequently, a public benefit reporting entity may have a separate legal identity or be, for example, an organisation or administrative arrangement without a separate legal identity.

CHAPTER 5: ELEMENTS IN GENERAL PURPOSE FINANCIAL REPORTS**CONTENTS**

	Paragraph
Introduction	5.1–5.5
Purpose of this Chapter.....	5.1
Elements of Service Performance Reporting	5.1.1
Elements of Financial Statements and their Importance.....	5.2–5.4
Elements of Financial Statements Defined	5.5
Assets	5.6–5.13
Definition.....	5.6
A Resource.....	5.7–5.10
Presently Controlled by the Entity	5.11–5.12
Past Event	5.13
Liabilities.....	5.14–5.26
Definition.....	5.14
A Present Obligation	5.15
An Outflow of Resources from the Entity	5.16
Past Event	5.17
Legal and Non-Legally Binding Obligations	5.18–5.26
Equity.....	5.26.1–5.26.2
Definition.....	5.26.1–5.26.2
Net Financial Position, Other Resources, and Other Obligations	5.27–5.28
Revenue and Expense	5.29–5.31
Definitions	5.29–5.31
Surplus or Deficit for the Period.....	5.32
Ownership Contributions and Ownership Distributions.....	5.33–5.37
Definitions	5.33–5.37

Introduction

Purpose of this Chapter

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

Elements of Service Performance Reporting

- 5.1.1 Service performance is the term used to describe an entity's performance in meeting its objectives of supplying goods and services. Service performance is reported in non-financial terms, such as quantities of goods and services provided.⁹ The elements of service performance are inputs, outputs and outcomes.

Elements of Financial Statements and their Importance

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

Elements of Financial Statements Defined

- 5.5 The elements that are defined in this Chapter are:

- Assets;
- Liabilities;
- Equity;
- Revenue;
- Expense;
- Ownership contributions; and
- Ownership distributions.

Assets

Definition

- 5.6 An asset is:

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

⁹ As noted in the Preface, subsequent references to "services" in this PBE Conceptual Framework encompass "goods".

A Resource

- 5.7 A resource is an item with service potential or the ability to generate economic benefits. Physical form is not a necessary condition of a resource. The service potential or ability to generate economic benefits can arise directly from the resource itself or from the rights to use the resource. Some resources embody an entity's rights to a variety of benefits including, for example, the right to:
- Use the resource to provide services;
 - Use an external party's resources to provide services, for example, leases;
 - Convert the resource into cash through its disposal;
 - Benefit from the resource's appreciation in value; or
 - Receive a stream of cash flows.
- 5.8 Service potential is the capacity to provide services that contribute to achieving the entity's objectives. Service potential enables an entity to achieve its objectives without necessarily generating net cash inflows.
- 5.9 Assets that embody service potential may include recreational, heritage, community, defence and other assets which are held by public benefit entities, and which are used to provide services to third parties. Such services may be for collective or individual consumption. Many services may be provided in areas where there is no market competition or limited market competition. The use and disposal of such assets may be restricted as many assets that embody service potential are specialised in nature.
- 5.10 Economic benefits are cash inflows or a reduction in cash outflows. Cash inflows (or reduced cash outflows) may be derived from, for example:
- An asset's use in the production and sale of services; or
 - The direct exchange of an asset for cash or other resources;

Presently Controlled by the Entity

- 5.11 An entity must have control of the resource. Control of the resource entails the ability of the entity to use the resource (or direct other parties on its use) so as to derive the benefit of the service potential or economic benefits embodied in the resource in the achievement of its service performance or other objectives.
- 5.12 In assessing whether it presently controls a resource, an entity assesses whether the following indicators of control exist:
- Legal ownership;
 - Access to the resource, or the ability to deny or restrict access to the resource;
 - The means to ensure that the resource is used to achieve its objectives; and
 - The existence of an enforceable right to service potential or the ability to generate economic benefits arising from a resource.

While these indicators are not conclusive determinants of whether control exists, identification and analysis of them can inform that decision.

Past Event

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

Liabilities

Definition

5.14 A liability is:

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

A Present Obligation

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

An Outflow of Resources from the Entity

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

Past Event

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

Legal and Non-Legally Binding Obligations

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

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

Legal Obligations

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

5.21 Some obligations related to exchange transactions are not strictly enforceable by an external party at the reporting date, but will be enforceable with the passage of time without the external party having to meet further conditions—or having to take any further action—prior to settlement. Claims that are

unconditionally enforceable subject to the passage of time are enforceable obligations in the context of the definition of a liability.

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

Non-Legally Binding Obligations

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

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

- 5.24 In the public sector, obligations may arise at a number of points. For example, in implementing a new policy or service:

- Making a political promise such as an electoral pledge;
- Announcement of a policy;
- Introduction (and approval or adoption) of the plan or budget (which may be two distinct points);
- Obtaining legal authority to take a proposed action; and
- An appropriation becoming effective.

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

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

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

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

Equity

Definition

- 5.26.1 Equity is:

The residual interest in the assets of the entity after deducting all its liabilities.

- 5.26.2 Although equity is defined as a residual, it may be sub-classified in the statement of financial position. For example, funds contributed by owners, accumulated surpluses and reserves relating to revaluations may be shown separately. Such classifications can be relevant to the decision-making needs of the users of financial statements when they indicate legal, regulatory or other restrictions on the ability of the entity to distribute its equity. They may also reflect the fact that parties with ownership interests in an entity have differing rights in relation to the distribution of surpluses or the repayment of capital.

Net Financial Position, Other Resources, and Other Obligations

- 5.27 As explained in paragraph 5.4, in some cases, in developing or revising a PBE Standard, the NZASB may determine that to achieve the objectives of financial reporting a resource or obligation that does not satisfy the definition of an element defined in the PBE Conceptual Framework needs to be recognised in the financial statements. In these cases, the PBE Standard may require or allow these resources or obligations to be recognised as other resources or other obligations, which are items additional to the elements defined in this Framework.
- 5.28 The term net financial position may be used to describe the difference between assets and liabilities after adding other resources and deducting other obligations recognised in the statement of financial position. Net financial position can be a positive or negative residual amount.

Revenue and Expense

Definitions

- 5.29 Revenue is:

Increases in the net financial position of the entity, other than increases arising from ownership contributions.

- 5.30 Expense is:

Decreases in the net financial position of the entity, other than decreases arising from ownership distributions.

- 5.31 Revenue and expense arise from exchange and non-exchange transactions, other events such as unrealised increases and decreases in the value of assets and liabilities, and the consumption of assets through depreciation and erosion of service potential and ability to generate economic benefits through impairments. Revenue and expense may arise from individual transactions or groups of transactions.

Surplus or Deficit for the Period

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

Ownership Contributions and Ownership Distributions

Definitions

5.33 Ownership contributions are:

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

5.34 Ownership distributions are:

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

5.35 It is important to distinguish inflows of resources from owners, including those inflows that initially establish the ownership interest, and outflows of resources to owners in their capacity as owners from revenue and expense. In addition to the injections of resources and the payment of dividends that may occur, in some jurisdictions it is relatively common for assets and liabilities to be transferred between public benefit entities. Where such transfers satisfy the definitions of ownership contributions or ownership distributions they will be accounted for as such.

5.36 Ownership interests may arise on the creation of an entity when another entity contributes resources to provide the new entity with the capacity to commence operational activities. In the public sector, contributions to, and distributions from, entities are sometimes linked to the restructuring of government and will take the form of transfers of assets and liabilities rather than cash transactions. Similarly, a not-for-profit group reporting entity may undertake a restructure which involves the transfer of assets and liabilities among the entities within the group rather than cash transactions. Ownership interests may take different forms, which may not be evidenced by an equity instrument.

5.37 Ownership contributions may take the form of an initial injection of resources at the creation of an entity or a subsequent injection of resources, including those where an entity is restructured. Ownership distributions may be: (a) a return on investment; (b) a full or partial return of investment; or (c) in the event of the entity being wound up or restructured, a return of any residual resources.

CHAPTER 6: RECOGNITION IN FINANCIAL STATEMENTS

CONTENTS

	Paragraph
Recognition Criteria and their Relationship to Disclosure	6.1–6.4
Definition of an Element	6.5–6.6
Measurement Uncertainty	6.7–6.8
Disclosure and Recognition.....	6.9
Derecognition	6.10

Recognition Criteria and their Relationship to Disclosure

- 6.1 This Chapter identifies the criteria that must be satisfied in order for an element to be recognised in the financial statements. Recognition is the process of incorporating and including in amounts displayed on the face of the appropriate financial statement an item that meets the definition of an element and can be measured in a way that achieves the qualitative characteristics and takes account of the constraints on information included in GPFRs.
- 6.2 The recognition criteria are that:
- An item satisfies the definition of an element; and
 - Can be measured in a way that achieves the qualitative characteristics and takes account of constraints on information in GPFRs.
- 6.3 All items that satisfy the recognition criteria are recognised in the financial statements. In some circumstances, a PBE Standard may also specify that, to achieve the objectives of financial reporting, a resource or obligation that does not meet the definition of an element is to be recognised in the financial statements provided it can be measured in a way that meets the qualitative characteristics and constraints. Other resources and other obligations are discussed in Chapter 5 *Elements in General Purpose Financial Reports*.
- 6.4 Recognition involves an assessment of uncertainty related to the existence and measurement of the element. The conditions that give rise to uncertainty, if any, can change. Therefore, it is important that uncertainty is assessed at each reporting date.

Definition of an Element

- 6.5 In order to be recognised as an element in the financial statements an item must meet the definition of one of the elements in Chapter 5. Uncertainty about the existence of an element is addressed by considering the available evidence in order to make a neutral judgement about whether an item satisfies all essential characteristics of the definition of that element, taking into account all available facts and circumstances at the reporting date.
- 6.6 If it is determined that an element exists, uncertainty about the amount of service potential or ability to generate economic benefits represented by that element is taken into account in the measurement of that element (see paragraphs 6.7 and 6.8). Preparers review and assess all available evidence in determining whether an element exists and is recognised, whether that element continues to qualify for recognition (see paragraph 6.9), or whether there has been a change to an existing element.

Measurement Uncertainty

- 6.7 In order to recognise an item in the financial statements, it is necessary to attach a monetary value to the item. This entails choosing an appropriate measurement basis and determining whether the measurement of the item achieves the qualitative characteristics, taking into account the constraints on information in GPFRs, including that the measurement is sufficiently relevant and faithfully representative for the item to be recognised in the financial statements. The selection of an appropriate measurement basis is considered in Chapter 7 *Measurement of Assets and Liabilities in Financial Statements*.
- 6.8 There may be uncertainty associated with the measurement of many amounts presented in the financial statements. The use of estimates is an essential part of the accrual basis of accounting. A decision about the relevance and faithful representativeness of measurement involves the consideration of techniques, such as using ranges of outcomes and point estimates, and whether additional evidence is available about economic circumstances that existed at the reporting date. Disclosures can provide useful information on estimation techniques employed. There may be rare instances in which the level of uncertainty in a single point estimate is so large that the relevance and faithful representativeness of the measure is questionable even if disclosures are provided to explain estimation techniques. Under these circumstances the item is not recognised.

Disclosure and Recognition

- 6.9 The failure to recognise 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. However, disclosure can provide information about items that meet many, but not all the characteristics of the definition of an element. Disclosure can also provide information on items that meet the definition of an element but cannot be measured in a manner that achieves the qualitative characteristics sufficiently to meet the objectives of financial reporting. Disclosure is appropriate when knowledge of the item is considered to be relevant to the evaluation of the net financial position of the entity and therefore meets the objectives of financial reporting.

Derecognition

- 6.10 Derecognition is the process of evaluating whether changes have occurred since the previous reporting date that warrant removing an element that has been previously recognised from the financial statements, and removing the item if such changes have occurred. In evaluating uncertainty about the existence of an element the same criteria are used for derecognition as at initial recognition.

CHAPTER 7: MEASUREMENT OF ASSETS AND LIABILITIES IN FINANCIAL STATEMENTS

CONTENTS

	Paragraph
Introduction	7.1
The Objective of Measurement.....	7.2–7.12
Measurement Bases and their Selection	7.5–7.7
Entry and Exit Values	7.8–7.9
Observable and Unobservable Measures	7.10
Entity-Specific and Non-Entity Specific Measures	7.11
Level of Aggregation or Disaggregation for Measurement.....	7.12
Measurement Bases for Assets.....	7.13–7.68
Historical Cost	7.13–7.21
Current Value Measurements	7.22–7.23
Market Value.....	7.24–7.36
Replacement Cost.....	7.37–7.48
Net Selling Price	7.49–7.57
Value in Use.....	7.58–7.68
Measurement Bases for Liabilities.....	7.69–7.91
Historical Cost	7.70–7.73
Cost of Fulfilment	7.74–7.79
Market Value.....	7.80–7.81
Cost of Release	7.82–7.86
Assumption Price	7.87–7.91

Introduction

- 7.1 This Chapter identifies the measurement concepts that guide the NZASB in the selection of measurement bases for PBE Standards and by preparers of financial statements in selecting measurement bases for assets and liabilities where there are no requirements in PBE Standards.

The Objective of Measurement

- 7.2 The objective of measurement is:

To select those measurement bases that most fairly reflect the cost of services, operational capacity and financial capacity of the entity in a manner that is useful in holding the entity to account, and for decision-making purposes.

- 7.3 The selection of a measurement basis for assets and liabilities contributes to meeting the objectives of financial reporting by providing information that enables users to assess:
- The cost of services provided in the period in historical or current terms;
 - Operational capacity—the capacity of the entity to support the provision of services in future periods through physical and other resources; and
 - Financial capacity—the capacity of the entity to fund its activities.
- 7.4 The selection of a measurement basis also includes an evaluation of the extent to which the information provided achieves the qualitative characteristics while taking into account the constraints on information in financial reports.

Measurement Bases and their Selection

- 7.5 It is not possible to identify a single measurement basis that best meets the measurement objective at a Conceptual Framework level. Therefore, the PBE Conceptual Framework does not propose a single measurement basis (or combination of bases) for all transactions, events and conditions. It provides guidance on the selection of a measurement basis for assets and liabilities in order to meet the measurement objective.
- 7.6 The following measurement bases for assets are identified and discussed in terms of the information they provide about the cost of services delivered by an entity, the operating capacity of an entity, the financial capacity of an entity, and the extent to which they provide information that meets the qualitative characteristics:
- Historical cost;
 - Market value;
 - Replacement cost;
 - Net selling price; and
 - Value in use.

Table 1 summarises these measurement bases in terms of whether they (a) provide entry or exit values; (b) are observable in a market; and (c) whether or not they are entity-specific.¹⁰

¹⁰ In some cases a judgement has been made in classifying a particular measurement basis as observable or unobservable in a market and/or as entity or non-entity specific.

Table 1: Summary of Measurement Bases for Assets

Measurement Basis	Entry or Exit	Observable or Unobservable in a Market	Entity or Non-Entity Specific
Historical cost	Entry	Generally observable	Entity-specific
Market value in open, active and orderly market	Entry and exit	Observable	Non-entity-specific
Market value in inactive market	Exit	Dependent on valuation technique	Dependent on valuation technique
Replacement cost	Entry	Observable	Entity-specific
Net selling price	Exit	Observable	Entity-specific
Value in use	Exit ¹¹	Unobservable	Entity-specific

7.7 The following measurement bases for liabilities are identified and discussed in terms of (a) the information they provide about the cost of services delivered by an entity, the operating capacity of an entity and the financial capacity of an entity; and (b) the extent to which they provide information that meets the qualitative characteristics:

- Historical cost;
- Cost of fulfilment;
- Market value;
- Cost of release; and
- Assumption price.

Table 2 summarises these measurement bases in terms of whether they (a) provide entry or exit values; (b) are observable in a market; and (c) whether or not they are entity-specific.

Table 2: Summary of Measurement Bases for Liabilities

Measurement Basis	Entry or Exit	Observable or Unobservable in a Market	Entity or Non-Entity Specific
Historical cost	Entry	Generally observable	Entity-specific
Cost of fulfilment	Exit	Unobservable	Entity-specific
Market value in open, active and orderly market	Entry and exit	Observable	Non-entity specific
Market value in inactive market	Exit	Dependent on valuation technique	Dependent on valuation technique
Cost of release	Exit	Observable	Entity-specific
Assumption price	Entry	Observable	Entity-specific

¹¹ As pointed out in paragraph 7.66, for non-cash-generating assets the calculation of value in use may require the use of replacement cost as a surrogate.

Entry and Exit Values

- 7.8 Measurement bases may provide either entry or exit values. For assets, entry values reflect the cost of purchase. Historical cost and replacement cost are entry values. Exit values reflect the economic benefits from sale. An exit value also reflects the amount that will be derived from use of the asset. In a diversified economy entry and exit prices differ as entities typically:
- Acquire assets tailored to the entity’s particular operating requirements for which other market participants would be unwilling to pay a similar price; and
 - Incur transaction costs on acquisition.
- 7.9 Measurement bases for liabilities may also be classified in terms of whether they are entry or exit values. Entry values relate to the transaction under which an obligation is received or the amount that an entity would accept to assume a liability. Exit values reflect the amount required to fulfil an obligation or the amount required to release the entity from an obligation.

Observable and Unobservable Measures

- 7.10 Certain measures may be classified according to whether they are observable in an open, active and orderly market.¹² Measures that are observable in a market are likely to be more understandable and verifiable than measures that are not observable. They may also be more faithfully representative of the phenomena they are measuring.

Entity-Specific and Non-Entity Specific Measures

- 7.11 Measures may also be classified according to whether they are “entity-specific” or “non-entity-specific”. Measurement bases that are entity-specific reflect the economic and current policy constraints that affect the possible uses of an asset and the settlement of a liability by an entity. Entity-specific measures may reflect economic opportunities that are not available to other entities and risks that are not experienced by other entities. Non-entity-specific measures reflect general market opportunities and risks. The decision on whether to use an entity-specific or non-entity-specific measure is taken by reference to the measurement objective and the qualitative characteristics.

Level of Aggregation or Disaggregation for Measurement

- 7.12 In order to present assets and liabilities in the financial statements in a way that provides information that best meets the measurement objective and achieves the qualitative characteristics it may be necessary to aggregate or disaggregate them for measurement purposes. In assessing whether such an aggregation or disaggregation is appropriate the costs are compared with the benefits.

Measurement Bases for Assets

Historical Cost

- 7.13 Historical cost for an asset is:

The consideration given to acquire or develop an asset, which is the cash or cash equivalents or the value of the other consideration given, at the time of its acquisition or development.

- 7.14 Historical cost is an entry, entity-specific value.¹³ Under the historical cost model assets are initially reported at the cost incurred on their acquisition. Subsequent to initial recognition, this cost may be allocated as an expense to reporting periods in the form of depreciation or amortisation for certain assets, as the service potential or ability to generate economic benefits provided by such assets are consumed over their useful lives. Following initial recognition, the measurement of an asset is not changed to reflect changes in prices or increases in the value of the asset.
- 7.15 Under the historical cost model the amount of an asset may be reduced by recognising impairments. Impairment is the extent to which the service potential or ability to generate economic benefits provided by an asset have diminished due to changes in economic or other conditions, as distinct to their

¹² The term “open, active and orderly markets” was developed by Dr. J. Alex Milburn. For example, see *Toward a Measurement Framework for Profit-oriented Entities*, published by the Canadian Institute of Chartered Accountants in 2012.

¹³ The term “historical cost” may also be referred to as the “cost model” or generically as “cost-based measures.”

consumption. This involves assessments of recoverability. Conversely, the amount of an asset may be increased to reflect the cost of additions and enhancements (excluding price increases for unimproved assets) or other events, such as the accrual of interest on a financial asset.

Costs of Services

7.16 Where historical cost is used, the cost of services reflects the amount of the resources expended to acquire or develop assets consumed in the provision of services. Historical cost generally provides a direct link to the transactions actually undertaken by the entity. Because the costs used are those carried forward from an earlier period without adjustment for price changes, they do not reflect the cost of assets when the assets are consumed. As the cost of services is reported using past prices, historical cost information will not facilitate the assessment of the future cost of providing services if cumulative price changes since acquisition are significant. Where plans or budgets are prepared on the historical cost basis, historical cost information demonstrates the extent to which the plan or budget has been executed.

Operational Capacity

7.17 If an asset has been acquired in an exchange transaction, historical cost provides information on the resources available to provide services in future periods, based on their acquisition cost. At the time an asset is purchased or developed, it can be assumed that the value to the entity of its service potential is at least as great as the cost of purchase.¹⁴ When depreciation or amortisation is recognised it reflects the extent to which the service potential of an asset has been consumed. Historical cost information shows that the resources available for future services are at least as great as the amount at which they are stated. Increases in the value of an asset are not reflected under the historical cost model. If an asset has been acquired in a non-exchange transaction the transaction price will not provide information on operating capacity.

Financial Capacity

7.18 The amount at which assets are stated in financial statements assists in an assessment of financial capacity. Historical cost can provide information on the amount of assets that may be used as effective security for borrowings. An assessment of financial capacity also requires information on the amount that could be received on sale of an asset, and reinvested in assets to provide different services. Historical cost does not provide this information when significantly different from current exit values.

Application of the Qualitative Characteristics

7.19 Paragraphs 7.16–7.18 explain the areas where historical cost provides relevant information in terms of its confirmatory or predictive value. Application of historical cost is often straightforward, because transaction information is usually readily available. As a result amounts derived from the historical cost model are generally representationally faithful in that they represent what they purport to represent—that is, the cost to acquire or develop an asset based on actual transactions. Estimates of depreciation and impairment used in the historical cost model, particularly for non-cash-generating assets, can affect representational faithfulness. Because application of historical cost generally reflects resources consumed by reference to actual transactions, historical cost measures are verifiable, understandable and can be prepared on a timely basis.

7.20 Historical cost information is comparable to the extent that assets have the same or similar acquisition dates. Because historical cost does not reflect the impact of price changes, it is not possible to compare the amounts of assets that were acquired at different times when prices differed in a meaningful way.

7.21 In certain circumstances the application of historical cost necessitates the use of allocations—for example where:

- Several assets are acquired in a single transaction;
- Assets are constructed by the entity itself and overheads and other costs have to be attributed; and
- The use of a flow assumption, such as first-in-first-out, is necessary when many similar assets are held. To the extent such allocations are arbitrary they reduce the extent to which the resulting measurement achieves the qualitative characteristics.

¹⁴ Where this is not the case the initial historical cost measurement will be reduced by the amount of the impairment.

Current Value Measurements

7.22 Current value measurements reflect the economic environment prevailing at the reporting date.

7.23 There are four current value measurement bases for assets:

- Market value;
- Replacement cost;
- Net selling price; and
- Value in use.

Market Value

7.24 Market value for assets is:

The amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

7.25 At acquisition market value and historical cost will be the same, if transaction costs are ignored and the transaction is an exchange transaction. The extent to which market value meets the objectives of financial reporting and the information needs of users partially depends on the quality of the market evidence. Market evidence, in turn, depends upon the characteristics of the market in which the asset is traded. Market value is particularly appropriate where it is judged that the difference between entry and exit values is unlikely to be significant or the asset is being held with a view to sale.

7.26 In principle, market values provide useful information because they fairly reflect the value of the asset to the entity. In an open, active and orderly market (see paragraph 7.28), the asset cannot be worth less than market value as the entity can obtain that amount by selling the asset, and cannot be worth more than market value, as the entity can obtain equivalent service potential or the ability to generate economic benefits by purchasing the same asset.

7.27 The usefulness of market values is more questionable when the assumption that markets are open, active and orderly does not hold. In such circumstances it cannot be assumed that the asset may be sold for the same price as that at which it can be acquired and it is necessary to determine whether an exit price or an entry price is the more useful measure. Exit-based market values are useful for assets that are held for trading, such as certain financial instruments, but may not be useful for specialised operational assets. Furthermore, while the purchase of an asset provides evidence that the value of the asset to the entity is at least as great as its purchase price, operational factors may mean that the value to the entity may be greater. Hence market values may not reflect the value to the entity of the asset, represented by its operational capacity.

Market Values in Open, Active and Orderly Markets

7.28 Open, active and orderly markets have the following characteristics:

- There are no barriers that prevent the entity from transacting in the market;
- They are active so there is sufficient frequency and volume of transactions to provide price information; and
- They are orderly, with many well-informed buyers and sellers acting without compulsion, so there is assurance of “fairness” in determining current prices—including that prices do not represent distress sales.

An orderly market is one that is run in a reliable, secure, accurate and efficient manner. Such markets deal in assets that are identical and therefore mutually interchangeable, such as commodities, currencies and securities where prices are publicly available. In practice few, if any, markets fully exhibit all of these characteristics, but some may approach an orderly market as described.

Market Values where it cannot be assumed that Markets are Open, Active and Orderly

7.29 Markets for assets that are unique and rarely traded are not open, active and orderly: any purchases and sales are individually negotiated, and there may be a large range of prices at which a transaction might be agreed. Therefore, participants will incur significant costs to purchase or to sell an asset. In such

circumstances it is necessary to use an estimation technique to estimate the price at which an orderly transaction to sell the asset would take place between market participants at the measurement date under current market conditions.

Costs of Services

- 7.30 Revenue from services reported in financial statements is measured on the basis of prices current in the reporting period. If assets used to provide services are measured at market value, the allocation of the cost of assets to reflect their consumption in the current reporting period is based on the current market value of the asset.
- 7.31 The use of market values permits a return on assets to be determined. However, public benefit entities do not generally carry out activities with the primary objective of generating profits, and services are often provided in non-exchange transactions or on subsidised terms. Consequently there may be limited relevance in a reported return derived from exit-based market prices.
- 7.32 As noted above, revenue from providing services reported in financial statements is measured on the basis of prices current in the reporting period. Thus the surplus or deficit for a period includes price movements that take place over the period during which assets and liabilities are held, and no profit or loss is reported on the sale of an asset. Where the asset is traded on an open, active and orderly market, the existence of the market provides assurance that the entity would be able to realise the market value (and no more) at the reporting date: it is therefore unnecessary to postpone recognition of changes in value until a surplus is realised on sale. However, where assets used to provide services are not traded on open, active and orderly markets, or a close approximation to such markets, the relevance of revenue and expense related to changes in market value is more questionable.

Operational Capacity

- 7.33 Information on the market value of assets held to provide services in future periods is useful if it reflects the value that the entity is capable of deriving from assets by using them in providing or delivering services. However, if an exit-based market value is significantly lower than historical cost, market value is likely to be less relevant than the historical cost of such assets in providing information on operational capacity—such a market value is also likely to be less relevant than entry value-based current measures.

Financial Capacity

- 7.34 An assessment of financial capacity requires information on the amount that would be received on sale of an asset. This information is provided by market value.

Application of the Qualitative Characteristics

- 7.35 Values determined in open, active and orderly markets can be readily used for financial reporting purposes. The information will meet the qualitative characteristics—that is it will be relevant, representationally faithful, understandable, comparable, and verifiable. Under such market conditions entry and exit values can be assumed to be the same or very similar. Because it can be prepared quickly, such information is also likely to be timely.
- 7.36 The extent to which market values meet the qualitative characteristics will decrease as the quality of market evidence diminishes and the determination of such values relies on estimation techniques. As indicated above, exit-based market values are only likely to be relevant to assessments of financial capacity and not to assessments of the cost of services and operational capacity.

Replacement Cost

- 7.37 Replacement cost¹⁵ is:

The most economic cost required for the entity to replace the service potential of an asset (including the amount that the entity will receive from its disposal at the end of its useful life) at the reporting date.

¹⁵ The full term is “optimised depreciated replacement cost” to denote that it refers to the replacement of the service potential embodied in an asset and not the asset itself (see paragraph 7.41). The term “replacement cost” is used for economy of expression in the PBE Conceptual Framework.

- 7.38 Replacement cost differs from market value because:
- In a public benefit entity context it is explicitly an entry value that reflects the cost of replacing the service potential of an asset;
 - It includes all the costs that would necessarily be incurred in the replacement of the service potential of an asset; and
 - It is entity-specific and therefore reflects the economic position of the entity, rather than the position prevailing in a hypothetical market. For example, the replacement cost of a vehicle is less for an entity that usually acquires a large number of vehicles in a single transaction and is regularly able to negotiate discounts than for an entity that purchases vehicles individually.
- 7.39 Because entities usually acquire their assets by the most economic means available, replacement cost reflects the procurement or construction process that an entity generally follows. Replacement cost reflects the replacement of service potential in the normal course of operations, and not the costs that might be incurred if an urgent necessity arose as a result of some unforeseeable event, such as a fire.
- 7.40 Replacement cost is the cost of replacing an asset's service potential. Replacement cost adopts an optimised approach and differs from reproduction cost, which is the cost of acquiring an identical asset.¹⁶ Although in many cases the most economic replacement of the service potential will be by purchasing an asset that is similar to that which is controlled, replacement cost is based on an alternative asset if that alternative would provide the same service potential more cheaply. For financial reporting purposes, it is therefore necessary to reflect the difference in service potential between the existing and replacement asset.
- 7.41 The appropriate service potential is that which the entity is capable of using or expects to use, having regard to the need to hold sufficient service capacity to deal with contingencies. Therefore, the replacement cost of an asset reflects reductions in required service capacity. For example, if an entity owns a school that accommodates 500 pupils but, because of demographic changes since its construction, a school for 100 pupils would be adequate for current and reasonably foreseeable requirements, the replacement cost of the asset is that of a school for 100 pupils.
- 7.42 In some cases the value that will be derived from an asset will be greater than its replacement cost. However, it would not be appropriate to measure the asset at that value, as it includes benefits from future activities, rather than service potential at the reporting date. Replacement cost represents the highest potential value of an asset, as, by definition, the entity is able to secure equivalent service potential by incurring replacement cost.

Costs of Services

- 7.43 Replacement cost provides a relevant measure of the cost of the provision of services. The cost of consuming an asset is equivalent to the amount of the sacrifice of service potential incurred by that use. That amount is its replacement cost—the entity is able to restore its position to that prevailing immediately before the consumption of the asset by an outlay equal to replacement cost.
- 7.44 The costs of services are reported in current terms when based on replacement cost. Thus the amount of assets consumed is stated at the value of the assets at the time they are consumed—and not, as with historical cost, at the time they were acquired. This provides a valid basis for a comparison between the cost of services and the revenue received in the period—which are generally transactions of the current period and measured in current prices—and for assessing whether resources have been used economically and efficiently. It also provides a useful basis for comparison with other entities that report on the same basis, as asset values will not be affected by different acquisition dates, and for assessing the cost of providing services in the future and future resource needs, as future costs are more likely to resemble current costs than those incurred in the past, when prices were different (see also paragraph 7.48).

Operational Capacity

- 7.45 In principle, replacement cost provides a useful measure of the resources available to provide services in future periods, as it is focused on the current value of assets and their service potential to the entity.

¹⁶ There may be cases where replacement cost equates to reproduction cost. This is where the most economic way of replacing service potential is to reproduce the asset.

Financial Capacity

- 7.46 Replacement cost does not provide information on the amounts that would be received on the sale of assets. It therefore does not facilitate an assessment of financial capacity.

Application of the Qualitative Characteristics

- 7.47 As noted above, replacement cost is relevant to assessments of the cost of services and operational capacity. It is not relevant to assessments of financial capacity. In some circumstances calculation of replacement cost is complex, and subjective judgements are required. These factors may reduce the representational faithfulness of replacement cost. In these circumstances the timeliness, comparability and verifiability of information prepared on a replacement cost basis may be affected, and replacement cost may be more costly than some alternatives. Replacement cost information may also not be straightforward to understand, particularly when that information reflects a reduction in required service capacity (see paragraph 7.41).
- 7.48 Replacement cost information is comparable within an entity as assets that provide equivalent service potential are stated at similar amounts, regardless of when those assets were acquired. In principle different entities may report similar assets at different amounts, because replacement cost is an entity-specific measure that reflects the opportunities for replacement that are available to the entity. The opportunities for replacement may be the same or similar for different public benefit entities. Where they are different, the economic advantage of an entity that is able to acquire assets more cheaply is reported in financial statements through lower asset values and a lower cost of services in order to be representationally faithful.

Net Selling Price

- 7.49 Net selling price is:
The amount that the entity can obtain from sale of the asset, after deducting the costs of sale.
- 7.50 Net selling price differs from market value in that it does not require an open, active and orderly market or the estimation of a price in such a market and that it includes the entity's costs of sale. Net selling price therefore reflects constraints on sale. It is entity-specific.
- 7.51 The potential usefulness of measuring assets at net selling price is that an asset cannot be worth less to the entity than the amount it could obtain on sale of the asset. However, it is not appropriate as a measurement basis if the entity is able to use its resources more efficiently by employing the asset in another way, for example by using it in the delivery of services.
- 7.52 Net selling price is therefore useful where the most resource-efficient course available to the entity is to sell the asset. This is the case where the asset cannot provide service potential or the ability to generate economic benefits at least as valuable as net selling price. Net selling price may provide useful information where an entity is contractually obligated to sell an asset at below market value. There may be cases where net selling price can indicate a development opportunity.

Costs of Services

- 7.53 It is not appropriate to quantify the cost of the provision of services at net selling prices. Such an approach would involve the use of an exit value as the basis of the expense reported.

Operational Capacity

- 7.54 Stating assets held for use in the provision of services at net selling price does not provide information useful to an assessment of operating capacity. Net selling price shows the amount that could be derived from an asset's sale, rather than the value of the service potential that could be derived from that asset.

Financial Capacity

- 7.55 As noted above, an assessment of financial capacity requires information on the amount that would be received on sale of an asset. Such information is provided by the use of net selling price. However, such a measure is not relevant for assets that may yield more valuable service potential by continuing to use them to deliver services.

Application of the Qualitative Characteristics

- 7.56 As indicated in paragraph 7.52 net selling price provides relevant information only where the most resource-efficient course available to the entity is to sell the asset. Assessments of net selling price may be made by reference to active markets where they exist. For major assets it may be possible and cost-effective to obtain professional appraisals. Net selling price will generally provide understandable information.
- 7.57 In most cases where net selling price is relevant, it will achieve the qualitative characteristics of faithful representation, verifiability, and timeliness.

Value in Use

- 7.58 Value in use is:

The present value to the entity of the asset's remaining service potential or ability to generate economic benefits if it continues to be used, and of the net amount that the entity will receive from its disposal at the end of its useful life.

Suitability of Value in Use

- 7.59 Value in use is an entity-specific value that reflects the amount that can be derived from an asset through its operation and its disposal at the end of its useful life. As noted in paragraph 7.42 above, the value that will be derived from an asset is often greater than its replacement cost—it is also usually greater than its historical cost. Where this is the case, reporting an asset at its value in use is of limited usefulness, as by definition, the entity is able to secure equivalent service potential at replacement cost.
- 7.60 Value in use is also not an appropriate measurement basis when net selling price is greater than value in use, as in this case the most resource-efficient use of the asset is to sell it, rather than continue to use it.
- 7.61 Therefore, value in use is appropriate where it is less than replacement cost and greater than net selling price. This occurs where an asset is not worth replacing, but the value of its service potential or ability to generate economic benefits is greater than its net selling price. In such circumstances value in use represents the value of the asset to the entity.
- 7.62 Value in use is an appropriate measurement basis for the assessment of certain impairments, because it is used in the determination of the recoverable amount for an asset or group of assets.

Costs of Services, Operational Capacity, Financial Capacity

- 7.63 Because of its potential complexity¹⁷, its limited applicability and the fact that its operationalisation in a public benefit entity context for non-cash-generating assets involves the use of replacement cost as a surrogate, value in use is generally inappropriate for determining the cost of services. Its usefulness to assessments of operational capacity is limited, and is only likely to be significant in the atypical circumstances where entities have a large number of assets that are not worth replacing, but their value in use is greater than their net selling price. This may be the case if, for example, an entity will discontinue provision of a service in the future, but the proceeds of immediate sale are less than the service potential embodied in the assets. Value in use does involve an estimate of the net amount that an entity will receive from disposal of the asset. However, its limited applicability reduces its relevance for assessments of financial capacity.

Application of the Qualitative Characteristics

- 7.64 While value in use may be used in assessments of certain impairments its relevance for financial reporting purposes is limited to the circumstances outlined in paragraph 7.61.
- 7.65 The extent to which value in use meets the other qualitative characteristics depends on how it is determined. In some cases, an asset's value in use can be quantified by calculating the value that the entity will derive from the asset assuming its continued use. This may be based on the future cash inflows related to the asset, or on cost savings that will accrue to the entity through its control of the asset. The calculation of value in use takes into account the time value of money and, in principle, the risk of variations in the amount and timing of cash flows.

¹⁷ See below paragraph 7.66

- 7.66 The calculation of value in use can be complex. Assets that are employed in cash-generating activities often provide cash flows jointly with other assets. In such cases value in use can be estimated only by calculating the present value of the cash flows of a group of assets and then making an allocation to individual assets.
- 7.67 Most assets held by public benefit entities are held with the primary objective of contributing to the provision of services, rather than to the generation of a commercial return: such assets are referred to as “non-cash-generating assets.” Because value in use is usually derived from expected cash flows, its operationalisation in such a context can be difficult. It may be inappropriate to calculate value in use on the basis of expected cash flows, because such a measure would not be faithfully representative of the value in use of such an asset to the entity. Therefore, it would be necessary to use replacement cost as a surrogate for financial reporting purposes.
- 7.68 The method of determining value in use reduces its representational faithfulness in many cases. It also affects the timeliness, comparability, understandability and verifiability of information prepared on a value in use basis.

Measurement Bases for Liabilities

- 7.69 This section discusses the measurement bases for liabilities. This section does not repeat all the discussion in the section on assets. It considers the following measurement bases:
- Historical Cost;
 - Cost of Fulfilment;
 - Market Value;
 - Cost of Release; and
 - Assumption Price.

Historical Cost

- 7.70 Historical cost for a liability is:
- The consideration received to assume an obligation, which is the cash or cash equivalents, or the value of the other consideration received at the time the liability is incurred.*
- 7.71 Under the historical cost model initial measures may be adjusted to reflect factors such as the accrual of interest, the accretion of discount or amortisation of a premium.
- 7.72 Where the time value of a liability is material—for example, where the length of time before settlement falls due is significant—the amount of the future payment is discounted so that, at the time a liability is first recognised, it represents the value of the amount received. The difference between the amount of the future payment and the present value of the liability is amortised over the life of the liability, so that the liability is stated at the amount of the required payment when it falls due.
- 7.73 The advantages and drawbacks of using the historical cost basis for liabilities are similar to those that apply in relation to assets. Historical cost is appropriate where liabilities are likely to be settled at stated terms. However, historical cost cannot be applied for liabilities that do not arise from a transaction, such as a liability to pay damages for a tort or civil damages. It is also unlikely to provide relevant information where the liability has been incurred in a non-exchange transaction, because it does not provide a faithful representation of the claims against the resources of the entity. It is also difficult to apply historical cost to liabilities that may vary in amount, such as those related to defined benefit pension liabilities.

Cost of Fulfilment

- 7.74 Cost of fulfilment is:
- The costs that the entity will incur in fulfilling the obligations represented by the liability, assuming that it does so in the least costly manner.*
- 7.75 Where the cost of fulfilment depends on uncertain future events, all possible outcomes are taken into account in the estimated cost of fulfilment, which aims to reflect all those possible outcomes in an unbiased manner.

- 7.76 Where fulfilment requires work to be done—for example, where the liability is to rectify environmental damage—the relevant costs are those that the entity will incur. This may be the cost to the entity of doing the remedial work itself, or of contracting with an external party to carry out the work. However, the costs of contracting with an external party are only relevant where employing a contractor is the least costly means of fulfilling the obligation.
- 7.77 Where fulfilment will be made by the entity itself, the fulfilment cost does not include any surplus, because any such surplus does not represent a use of the entity’s resources. Where fulfilment amount is based on the cost of employing a contractor, the amount will implicitly include the profit required by the contractor, as the total amount charged by the contractor will be a claim on the entity’s resources—this is consistent with the approach for assets, where replacement cost would include the profit required by a supplier, but no profit would be included in the replacement cost for assets that the entity would replace through self-construction.
- 7.78 Where fulfilment will not take place for an extended period, the cash flows need to be discounted to reflect the value of the liability at the reporting date.
- 7.79 Cost of fulfilment is generally relevant for measuring liabilities except in the following circumstances:
- Where the entity can obtain release from an obligation at a lower amount than cost of fulfilment, then cost of release is a more relevant measure of the current burden of a liability, just as, for an asset, net selling price is more relevant when it is higher than value in use; and
 - In the case of liabilities assumed for a consideration, assumption price (see paragraphs 7.87–7.91) is more relevant when assumption price is higher than both cost of fulfilment and cost of release.

Market Value

- 7.80 Market value for liabilities is:

The amount for which a liability could be settled between knowledgeable, willing parties in an arm’s length transaction.

- 7.81 The advantages and disadvantages of market value for liabilities are the same as those for assets. Such a measurement basis may be appropriate, for example, where the liability is attributable to changes in a specified rate, price or index quoted in an open, active and orderly market. However, in cases where the ability to transfer a liability is restricted and the terms on which such a transfer might be made are unclear the case for market values, even if they exist, is significantly weaker. This is particularly the case for liabilities arising from obligations in non-exchange transactions, because it is unlikely that there will be an open, active and orderly market for such liabilities.

Cost of Release

- 7.82 “Cost of release” is the term used in the context of liabilities to refer to the same concept as “net selling price” in the context of assets. Cost of release refers to the amount of an immediate exit from the obligation. Cost of release is the amount that either the creditor will accept in settlement of its claim, or a third party would charge to accept the transfer of the liability from the obligor. Where there is more than one way of securing release from the liability, the cost of release is that of the lowest amount—this is consistent with the approach for assets, where net selling price would not reflect the amount that would be received on sale to a scrap dealer, if a higher price could be obtained from sale to a purchaser who would use the asset.
- 7.83 For some liabilities, transfer of a liability is not practically possible and cost of release will therefore be the amount that the creditor will accept in settlement of its claim. This amount will be known if it is specified in the agreement with the creditor—for example, where a contract includes a specific cancellation clause.
- 7.84 In some cases there may be evidence of the price at which a liability may be transferred—for example, in the case of some pension liabilities. Transferring a liability may be distinguished from entering into an agreement with another party that will fulfil the entity’s obligation or bear all the costs stemming from a liability. For a liability to be transferred it is necessary that all of the creditor’s rights against the entity are extinguished. If this is not the effect of an arrangement, the liability remains a liability of the entity.

- 7.85 In assessing whether cost of release is appropriate for measuring liabilities it is necessary to consider whether release in the envisaged manner is an option that is open to the entity in practice, having regard to any consequences of obtaining release, such as damage to the entity’s reputation.
- 7.86 Just as net selling price is relevant only when the most resource-efficient course available to the entity is to sell the asset, so cost of release is relevant only when the most resource-efficient course is to seek immediate release from an obligation. In particular, where cost of fulfilment is lower than cost of release, cost of fulfilment provides more relevant information than cost of release, even if it is feasible to negotiate a release from the obligation in accordance with the methods for transferring a liability in paragraph 7.84.

Assumption Price

- 7.87 “Assumption price” is the term used in the context of liabilities to refer to the same concept as replacement cost for assets. Just as replacement cost represents the amount that an entity would rationally pay to acquire an asset, so assumption price is the amount which the entity would rationally be willing to accept in exchange for assuming an existing liability. Exchange transactions carried out on arms-length terms will provide evidence of assumption price—this is not the case for non-exchange transactions.
- 7.88 In the context of an activity that is carried out with a view to profit, an entity will assume a liability only if the amount it is paid to assume the liability is greater than the cost of fulfilment or release— i.e., the settlement amount. Once that assumption price has been received by the entity, the entity has an obligation to its creditor.
- 7.89 At the time a liability is first incurred in an exchange transaction, assumption price represents the amount that was accepted by the entity for assuming the liability—it is therefore usually reasonable to assume that assumption price is the price that the entity would rationally accept for assuming a similar liability. It would charge a higher amount, if competitive pressures allowed it to do so, but it might be unwilling to accept a lower price. Just as replacement cost is a current value so, conceptually, is assumption price. There are, however, practical problems in reflecting changes in prices in obligations that are stated at assumption price.
- 7.90 A consequence of stating performance obligations at the assumption price is that no surplus is reported at the time the obligation is taken on. A surplus or deficit is reported in the financial statements in the period when fulfilment (or release) takes place, as it is the difference between the revenue arising from satisfaction of the liability and the cost of settlement.
- 7.91 An entity may have a potential obligation that is larger than assumption price. If the entity has to seek release from a contract, the other party to the contract may be able to claim recompense for losses that it will sustain, as well as the return of any amounts paid. However, provided that the entity can settle the obligation by fulfilment, it can avoid such additional obligations and it is representationally faithful to report the obligation at no more than assumption price—this is analogous to the position where an asset will yield greater benefits than replacement cost. Under such circumstances, as explained in paragraph 7.42, replacement cost rather than value in use is the most relevant measurement basis.

CHAPTER 8: PRESENTATION IN GENERAL PURPOSE FINANCIAL REPORTS

CONTENTS

	Paragraph
Introduction	8.1–8.8
Presentation	8.4–8.8
Information Selection.....	8.9–8.35
Information Selection—Nature of Information.....	8.11–8.14
Information Selected for Display or Disclosure	8.15–8.24
Principles Applicable to Information Selection.....	8.25–8.35
Information Location	8.36–8.44
Principles for Allocation of Information between Different Reports.....	8.38–8.40
Principles for Location of Information within a Report.....	8.41–8.44
Information Organisation	8.45–8.64
Nature of Information Relevant to Organisation	8.47–8.53
Principles Applicable to Information Organisation	8.54–8.64

Introduction

- 8.1 This Chapter sets out the concepts applicable to the presentation of information in GPFRs.
- 8.2 Presentation is linked to Chapters 1 to 4—the objectives of financial reporting, users’ needs, the qualitative characteristics, constraints on information included in GPFRs and the reporting entity all influence presentation decisions. For information reported in the financial statements, presentation is also linked to the definitions of the elements, recognition criteria and measurement bases identified in Chapters 5 to 7—for example:
- The definitions of the elements affect the items that can be presented in the financial statements;
 - Application of the recognition criteria affects the location of information; and
 - The selection of measurement bases impacts the information presented on measurement methodologies.

Language in which Financial Statement and Other GPFRs are Issued

- 8.3 The language (or languages) in which financial statements and other GPFRs are issued supports achievement of the objectives of financial reporting and the qualitative characteristics. All translated versions need to be faithful to the original language version. The translated version is made available to meet the needs of users with reference to:
- Legal requirements in the entity’s jurisdiction; and
 - Translation costs and benefits.

Presentation

- 8.4 Presentation is the selection, location and organisation of information that is reported in the GPFRs.
- 8.5 Presentation aims to provide information that contributes towards the objectives of financial reporting and achieves the qualitative characteristics while taking into account the constraints on information included in GPFRs. Decisions on selection, location and organisation of information are made in response to the needs of users for information about economic or other phenomena.
- 8.6 Chapter 1 explains that GPFRs are likely to comprise multiple reports, each responding more directly to certain aspects of the objectives of financial reporting and matters included within the scope of financial reporting. In addition to the financial statements, GPFRs provide information relevant to, for example, assessments of an entity’s service performance and the sustainability of its finances. The objectives of financial reporting, applied to the area covered by a particular report, guide presentation decisions for that report.
- 8.7 Presentation decisions may:
- Result in the development of a new GPFR, the movement of information between reports, or the amalgamation of existing reports; or
 - Be detailed decisions on information selection, location and organisation within a GPFR.

Presentation Decisions are Interlinked

- 8.8 Decisions on information selection, location and organisation are interlinked and, in practice, are likely to be considered together. The amount or type of information selected could have implications on whether it is included in a separate report or organised into tables or separate schedules. The following three sections separately focus on each presentation decision.

Information Selection

- 8.9 Decisions on information selection address what information is reported:
- In the financial statements; and
 - In GPFRs outside the financial statements (other GPFRs).

- 8.10 As Chapter 2 *Objectives and Users of General Purpose Financial Reporting* explains, the objectives of financial reporting are to provide information about the entity that is useful to users of GPFs for accountability and decision-making purposes. Chapter 2 describes the types of information that users need to meet the objectives of financial reporting. That description guides decisions on whether particular types of reports are needed. This Chapter focuses on the selection of information to be presented in GPFs, including financial statements and other reports.

Information Selection—Nature of Information

Nature of Information in Financial Statements

- 8.11 Users' information needs identified in Chapter 2 underpin information selection for the financial statements. Those needs include information about the financial position, financial performance and cash flows of an entity in order to:
- Enable users to identify the resources of the entity and claims on those resources at the reporting date;
 - Inform assessments of matters such as whether the entity has acquired resources economically, and used them efficiently and effectively to achieve its service performance objectives; and
 - Inform assessments of financial performance and the entity's liquidity and solvency.
- 8.12 The financial statements may also provide information that assists users in assessing the extent to which:
- An entity has met its financial objectives;
 - Revenues, expenses, cash flows and financial results of the entity comply with public plans or budgets; and
 - A public sector entity or, where relevant, another entity has adhered to relevant legislation or other authority governing the raising and use of public monies.
- 8.13 The financial statements do not report comprehensively on an entity's service performance. However information in the financial statements may provide information relevant to the financial aspects of service performance such as information about:
- Revenue, expenses and cash flows related to services; and
 - The assets and liabilities that inform users' evaluations of, for example, an entity's operational capacity or financial risks that could impact on service provision.
- 8.14 Other reports in GPFs present information additional to the financial statements. Such information could, for example, include:
- Information on the sustainability of an entity's public finances, where relevant;
 - Financial statement discussion and analysis; or
 - Service performance information.

Information Selected for Display or Disclosure

- 8.15 Information is selected for display or disclosure in GPFs. Information selected for display communicates key messages in a GPF, while information selected for disclosure makes displayed information more useful by providing detail that will help users to understand the displayed information. Disclosure is not a substitute for display.
- 8.16 Repetition of information in a GPF needs to generally be avoided. However, the same information may be both displayed and disclosed. For example, a total displayed on the face of the financial statements may be repeated in the notes, where the notes provide a disaggregation of the displayed total. Similarly the same information may be presented in different GPFs in order to address their different aims.

Information Selected for Display

- 8.17 Every GPF contains key messages that are communicated, so every GPF contains displayed information. Displayed information is kept to a concise, understandable level, so that users can focus on the key messages presented and not be distracted by detail that could otherwise obscure those messages.

Displayed information is presented prominently, using appropriate presentation techniques such as clear labelling, borders, tables and graphs.

- 8.18 The items displayed on the face of the financial statements provide information about such matters as the reporting entity's financial position, financial performance and cash flows.
- 8.19 Assessment of whether an item satisfies the recognition criteria is one of the key mechanisms in determining whether information is displayed on the face of the statement of financial position or statement of financial performance and/or disclosed either in the notes or elsewhere in the GPFs. In other cases, for example a statement of cash flows, displayed information will also support achievement of the objectives of financial reporting.
- 8.20 Developing requirements for the display of line items and totals involves balancing the standardisation of displayed information, which facilitates understandability, with information that is tailored for entity-specific factors. The aim of both standardised display requirements and entity-specific information is to ensure that information necessary to meet the objectives of financial reporting is available for all entities, while allowing information to be displayed in a manner that reflects the nature and operations of specific entities.

Information Selected for Disclosure

- 8.21 Disclosed information is likely to include:
- The basis for the displayed information, such as applicable policies or methodologies;
 - Disaggregations of displayed information; and
 - Items that share some but not all of the aspects of displayed information—for example disclosures on items that meet some, but not all, of the characteristics of the definition of an element¹⁸ or disclosures on items that meet the definition of an element, but not the recognition criterion.
- 8.22 The level of detail provided by disclosed information contributes to achievement of the objectives of financial reporting, without being excessive. Disclosed information, like displayed information, is necessary for achievement of the objectives of financial reporting.
- 8.23 Information disclosed in the notes to the financial statements:
- Is necessary to a user's understanding of the financial statements;
 - Provides information that presents the financial statements in the context of the entity and its operating environment; and
 - Generally will have a clear and demonstrable relationship to information displayed on the face of the financial statement(s) to which it pertains.
- 8.24 Information disclosed in the notes may also include:
- Entity-related factors that could influence judgements about reported information (for example, information about related parties and controlled entities or interests in other entities);
 - The basis for what is displayed (for example, information on accounting policies and measurement, including measurement methods and measurement uncertainties where applicable);
 - Disaggregations of amounts displayed on the face of the statements (for example, a break-down of property, plant and equipment into different classes);
 - Items that do not meet the definition of an element or the recognition criteria, but are important to an understanding of the entity's finances and ability to deliver services—for example, information about events and conditions, that might affect future cash flows or service potential, including their natures, possible effects on cash flows or service potential, probabilities of occurrence, and sensitivities to changes in conditions; and
 - Information that may explain underlying trends affecting displayed totals.

¹⁸ Chapter 5 *Elements in General Purpose Financial Reports*, explains that other resources and other obligations that do not meet the definition of elements may be recognised in order to contribute to the objectives of financial reporting.

Principles Applicable to Information Selection

- 8.25 Decisions about what information needs to be displayed and disclosed involve consideration of:
- The objectives of financial reporting;
 - The qualitative characteristics and constraints on information included in GPFRs; and
 - The relevant economic or other phenomena about which information may be necessary.
- 8.26 Information selection results in information that contributes to meeting the objectives of financial reporting, as applied to the area covered by a particular report, and provides the appropriate level of detail. Decisions on information selection involve information prioritisation and summarisation. Information selection avoids information overload that reduces understandability. Too much information may make it difficult for users to understand the key messages, and, consequently undermines achievement of the objectives of financial reporting.
- 8.27 Preparers, applying pronouncements and their professional judgement, are responsible for ensuring that information that meets the objectives of financial reporting and achieves the qualitative characteristics is provided in the GPFRs that they prepare.
- 8.28 Decisions on information selection require continuing and critical review. Information identified for possible selection is reviewed as it is developed and considered for presentation, with particular reference to its relevance, materiality and cost-benefit, although all the qualitative characteristics and constraints are applied to decisions on information selection. Past decisions may require reconsideration because new information may make existing information requirements redundant with the result that those items no longer achieve the qualitative characteristics and/or the constraints.
- 8.29 All material transactions, events, and other items reported are presented in a manner that conveys their substance rather than their legal or other form so that the qualitative characteristics of relevance and representational faithfulness are achieved.
- 8.30 The benefits to users of receiving information need to justify the costs to entities of collecting and presenting that information. In making this assessment it is important to consider how individual items impact on the overall view presented and the nature of the information presented. Items that may appear to have little benefit when viewed in isolation could have much greater benefit in contributing to the complete set of information presented.
- 8.31 Information needs to be presented on a sufficiently timely basis to enable users to hold management or the governing body accountable and to inform users' decisions.
- 8.32 GPFRs may include additional information derived from sources other than the financial information system. The qualitative characteristics apply to such information. The date of delivery of any such additional information needs to be as close as possible to the financial statements' reporting date, so that reported information will be timely.

Principles for Selection of Information for Display and Disclosure

- 8.33 Decisions about display or disclosure apply to both the financial statements and other GPFRs. The objectives of financial reporting are applied to the area covered by a particular report to guide the identification of information for display or disclosure. The identification of information for display and disclosure in a particular GPFR may involve the development of:
- Classification principles;
 - A list of broad types of information that are displayed and a similar list of broad types of information that are disclosed; and/or
 - Lists of specific information that preparers must display or disclose.
- 8.34 Decisions about selection of information to be displayed and disclosed are made:
- With reference to each other rather than in isolation; and
 - To effectively communicate an integrated set of information.

- 8.35 Selection decisions with respect to information in other GPFRs are made after carefully considering the relationship of the other GPFRs to the financial statements.

Information Location

- 8.36 Decisions on information location are made about which:
- Report information is located within; and
 - Component of a report information is located.
- 8.37 The location of information has an impact on information's contribution to achievement of the objectives of financial reporting and the qualitative characteristics. Location may affect the way that users interpret information and the comparability of information. Location may be used to:
- Convey the relative importance of information and its connections with other items of information;
 - Convey the nature of information;
 - Link different items of information that combine to meet a particular user need; and
 - Distinguish between information selected for display and information selected for disclosure.

Principles for Allocation of Information between Different Reports

- 8.38 Factors relevant to decisions about allocating information between the financial statements and another GPFR include:
- *Nature*: Whether the nature of the information, for example historical versus prospective, supports including the information either in the same or a different GPFR, because of considerations related to, for example, comparability and/or understandability;
 - *Jurisdiction-Specific*: Whether jurisdiction-specific factors, such as legal provisions, specify requirements on information location; and
 - *Linkage*: Whether or not the additional information envisaged needs to link very closely to information already included in an existing report. The linkages between all information need to be assessed, not only linkages between new and existing information.
- 8.39 The factors above, which are expressed from the perspective of adding information to an existing set of information, also apply to considerations of whether the grouping of existing information could be improved, which is discussed in the section on information organisation.
- 8.40 A separate GPFR may be necessary when:
- Additional user information needs, not satisfied by an existing report, are identified; and
 - A separate GPFR to meet those needs is more likely to achieve the objectives of financial reporting and the qualitative characteristics than including information in an existing report.

Principles for Location of Information within a Report

- 8.41 Paragraph 8.17 of this Chapter states that displayed information is presented prominently, using appropriate presentation techniques—location is one way to achieve this. Information location within a report ensures that displayed information is given appropriate prominence and is not obscured by more detailed and extensive disclosed information.
- 8.42 The location of information in the financial statements contributes to communicating a comprehensive financial picture of an entity.
- 8.43 For the financial statements, displayed information is shown on the face of the appropriate statement, while disclosures are in the notes. Distinguishing displayed information and disclosed information through location ensures that those items that directly relate to communicating matters, such as an entity's financial position, financial performance and cash flows, can be highlighted, with further more detailed information provided through disclosure in the notes.

- 8.44 For other GPFRs, displayed information may either be located separately from disclosed information or located in the same area, but distinguished from disclosed information and given prominence through the use of another presentation technique.

Information Organisation

- 8.45 Information organisation addresses the arrangement, grouping and ordering of information, which includes decisions on:
- How information is arranged within a GPFR; and
 - The overall structure of a GPFR.
- 8.46 Information organisation involves a range of decisions including decisions on the use of cross-referencing, tables, graphs, headings, numbering, and the arrangement of items within a particular component of a report, including decisions on item order. How information is organised can affect its interpretation by users.

Nature of Information Relevant to Organisation

- 8.47 Decisions about the organisation of information take into account:
- Important relationships between information; and
 - Whether information is for display or disclosure.

Types of Relationships

- 8.48 Important relationships include, but are not restricted to:
- Enhancement;
 - Similarity; and
 - Shared purpose.
- 8.49 *Enhancement*: Information in one place in a GPFR may be enhanced through information provided elsewhere. For example, budget, prospective and service performance information enhances information in the financial statements. Tables and graphs may be used to enhance the understanding of narrative information. Links to information reported outside the GPFRs may enhance the understandability of information reported in GPFRs.
- 8.50 *Similarity*: A relationship of similarity exists where information reported in one place is based on information reported elsewhere in the GPFRs, and the information either has not been adjusted or has had relatively minor adjustments. For example, if service performance information includes the cost of services, or the value of assets used in different services, then it may be helpful to show how those totals relate to expense and assets reported in the financial statements. Another example is the relationship between the total expense reported against budget and total expense reported in the statement of financial performance. A reconciliation between the two different amounts can enhance users' understanding of an entity's finances.
- 8.51 *Shared purpose*: A relationship of shared purpose exists where information reported in different places contributes to the same purpose. An example is where different statements and disclosures provide information needed for assessments of accountability for services delivered. Information about (a) the actual and budgeted cost of different services, (b) financial and non-financial resources used in the provision of different services, and (c) future provision of different services may be included in different places. To make the relationship between the information in different places clear, it may be appropriate to organise the information by using techniques such as common headings and referencing.
- 8.52 Relationships may exist between information in different:
- GPFRs;
 - Components within a GPFR; and
 - Parts of a single component.

Grouping of Information

8.53 The three factors noted in the section on information selection as being applicable to decisions on information location—linkage, nature of information and jurisdiction-specific considerations—also apply to considerations of whether the grouping of existing information could be improved. Decisions on effective grouping of information consider linkages between information sets, the nature of the different information sets, and, to the extent appropriate, jurisdiction-specific factors.

Principles Applicable to Information Organisation

8.54 Information organisation:

- Supports achievement of the objectives of financial reporting; and
- Helps reported information meet the qualitative characteristics.

8.55 Information organisation:

- Helps to ensure that key messages are understandable;
- Clearly identifies important relationships;
- Gives appropriate prominence to information that conveys key messages; and
- Facilitates comparisons.

8.56 Related information is linked through the use of consistent headings, presentation order, and/or other methods appropriate to the relationship and type of information. Where links are to information reported outside the GPFRs it is important that:

- Links to information from other sources do not undermine a GPFR's achievement of the qualitative characteristics; and
- The issuance date of any such linked information is as close as possible to the financial statements' reporting date so that reported information will be timely.

Comparability

8.57 Information organisation takes into account the benefits of consistent presentation over time. Consistent presentation supports users' ability to understand information and facilitates their access to information. It helps to achieve the qualitative characteristic of comparability.

Principles for Information Organisation within the Financial Statements

8.58 Information displayed on the face of the financial statements is usually organised into numeric totals and sub-totals. Its organisation provides a structured overview of such matters as the reporting entity's financial position, financial performance and cash flows.

8.59 For the financial statements, relationships may exist between:

- Subsets of displayed amounts or changes in displayed amounts and their impact on an entity's financial position, financial performance and/or cash flows;
- Different displayed amounts in different financial statements, which all reflect the impact of a common external event, or contribute together towards an understanding of an aspect of the entity's financial position or financial performance; and
- Displayed amounts and related note disclosures that provide information that explains or could otherwise support users' understanding of displayed items.

8.60 The organisation of information in financial statements includes decisions on:

- The type and number of statements;
- Disaggregation of totals into meaningful subcategories;
- Ordering and grouping of items displayed within each statement;
- Identification of aggregates (additive and subtractive); and
- Identification of other information for inclusion on the face of the statement.

- 8.61 Information disclosed in the notes to the financial statements is organised so that relationships to items reported on the face of the financial statements are clear. The notes are an integral part of the financial statements.

Principles for Organisation of Information within Other GPFRs

- 8.62 As is the case for the financial statements, information organisation in other GPFRs helps to ensure that key messages conveyed by displayed information are understandable. Presentation that clearly identifies important relationships is likely to enhance the extent to which a report:
- Meets the objectives of financial reporting; and
 - Achieves the qualitative characteristics.
- 8.63 Linking related information helps users to find important information. Some information is more understandable when organised into graphs, charts, tables, ratios or key performance indicators. Other information may be presented more effectively in narrative form. Information organisation supports users' understanding of linkages between information within the same GPFR.
- 8.64 Information organisation facilitates comparisons such as making clear when items are similar or dissimilar. Inter-period comparability is facilitated by avoiding changes to the way that information is organised for the same entity from year to year unless such changes enhance relevance and understandability. Inter-entity comparisons are facilitated when different reporting entities organise the information they present in similar ways.

Basis for Conclusions

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

Preface

Introduction

- BC1. Consistent with the Accounting Standards Framework, the PBE Conceptual Framework is based on *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (the Conceptual Framework) developed and approved by the International Public Sector Accounting Standards Board (IPSASB). The New Zealand Accounting Standards Board (NZASB) has considered the appropriateness of the IPSASB's Conceptual Framework for application by Tier 1, Tier 2 and Tier 3 public benefit entities in New Zealand and has made some modifications, as discussed in this Basis for Conclusions. For example, the language has been generalised to refer to all public benefit entities and references to not-for-profit entities have been included. The NZASB considers that the IPSASB's Conceptual Framework is generally appropriate for public benefit entities in New Zealand, except as discussed in this Basis for Conclusions.
- BC2. The NZASB noted that the IPSASB's Basis for Conclusions on each chapter of the Conceptual Framework would be useful for entities applying the PBE Conceptual Framework and agreed to make the IPSASB's Basis for Conclusions available as additional material on the XRB website at www.xrb.govt.nz.

Addition of Part B: Not-for-Profit Entities

- BC3. The IPSASB develops standards for public sector entities. The IPSASB included a Preface in its Conceptual Framework to provide context for readers about the key characteristics of public sector entities that the IPSASB considered in developing the Conceptual Framework. The NZASB develops standards for public benefit entities, which include both public sector public benefit entities and not-for-profit public benefit entities. Because the characteristics of public sector entities can differ from those of not-for-profit entities, the NZASB decided to discuss the key characteristics of public sector entities and not-for-profit entities in separate sections of the Preface.

Approved Budget

- BC4. The Preface to the IPSASB's Conceptual Framework included a discussion of the "approved budget" and the IPSASB made a number of references to the approved budget throughout the Conceptual Framework. The NZASB noted that, in a New Zealand context, many public sector entities have a requirement to make plans or budgets publicly available and subject to various forms of public scrutiny, but these plans or budgets are not normally referred to as an approved budget. The NZASB therefore modified this discussion, and subsequent references to the approved budget in other Chapters, to reflect the New Zealand context.

Explanatory Guides

- BC5. The IPSASB Conceptual Framework refers to the concepts in the Conceptual Framework being applied in developing IPSASs and Recommended Practice Guides (RPGs) and states that the concepts in the Conceptual Framework do not override the requirements in IPSASs and RPGs. The NZASB noted that PBE Standards and the PBE Conceptual Framework, when issued, have legal status under the Financial Reporting Act 2013. However, explanatory guides issued by the NZASB do not have legal status. The NZASB therefore decided not to refer to explanatory guides when discussing the application of the PBE Conceptual Framework.

Chapter 1 Role and Authority of the PBE Conceptual Framework

- BC6. The NZASB's discussion of the role of the PBE Conceptual Framework is broader than the discussion in the IPSASB's Conceptual Framework. The NZASB has also acknowledged the role of the PBE Conceptual Framework in assisting it to comment on the IPSASB's proposals and in assisting preparers of general purpose financial reports.
- BC7. The NZASB has replaced the IPSASB's examples of entities that might use the Conceptual Framework with New Zealand examples.

Chapter 2 Objectives and Users of General Purpose Financial Reporting

- BC8. Chapter 2 of the IPSASB’s Conceptual Framework included a discussion of “service delivery achievements” and the IPSASB made a number of references to service delivery throughout the Conceptual Framework. The NZASB noted that, in a New Zealand context, the term service performance is widely used and understood. The NZASB therefore modified this discussion, and subsequent references to service delivery to reflect the New Zealand context.
- BC9. Chapter 2 of the IPSASB’s Conceptual Framework included a discussion on prospective financial and non-financial information. The NZASB noted that, in planning for the future, both public sector and not-for-profit entities are likely to use prospective financial statements. However, not-for-profit entities are less likely to make that information publicly available in a GPFR. The NZASB acknowledged this difference in the discussion on prospective financial and non-financial information.

Chapter 3 Qualitative Characteristics

- BC10. The NZASB did not make any significant modifications to Chapter 3 of the IPSASB’s Conceptual Framework.

Chapter 4 Reporting Entity

- BC11. The NZASB made two modifications to Chapter 4 of the IPSASB’s Conceptual Framework:
- (a) Although some activities may be regarded as separate reporting entities in New Zealand, they are not commonly referred to as ‘programmes’. The IPSASB’s references to ‘programmes’ as potential reporting entities have therefore been omitted.
 - (b) Paragraph 4.7 explains that there is often an additional accountability aspect for not-for-profit entities in relation to the special status granted to them, for example, the benefits associated with being a registered charity.

Chapter 5 Elements in General Purpose Financial Reports

Elements of Service Performance Reporting

- BC12. Chapters 5 to 7 of the IPSASB’s Conceptual Framework focus only on the definition, recognition and measurement of the elements of financial statements. The IPSASB decided to focus on the elements of financial statements in these chapters because it had not yet issued standards-level guidance on service performance reporting. The NZASB noted that the previous PBE Framework had referred to the elements of service performance reporting and agreed that the PBE Conceptual Framework should specify the elements of service performance reporting.

Revenue

- BC13. Respondents to the NZASB’s Exposure Draft noted that the IPSASB’s Conceptual Framework and the PBE Conceptual Framework define and describe ‘revenue’ as an element. Respondents also noted that the equivalent element in the New Zealand Equivalent to the IASB Conceptual Framework for Financial Reporting 2010 (NZ Framework) is ‘income’. The definition of income in that framework encompasses both revenue (which arises in the course of the ordinary activities of an entity) and gains (being other items that meet the definition of income and which may, or may not, arise in the ordinary course of the ordinary activities of an entity). Respondents expressed concern regarding the difference in terminology used by the two international standard setting bodies and the potential for this to be confusing. The NZASB acknowledged this concern but noted that the difference is longstanding and the decision to base PBE Standards on IPSASs required the adoption of the IPSASB’s defined term

Equity

- BC14. The IPSASB did not define equity as an element of financial statements. It defined revenue, expense, assets, liabilities, contributions by owners and distributions to owners. It also used the term “net financial position” to describe the residual of assets less liabilities, adjusted for any other resources or obligations recognised in the statement of financial position. The IPSASB’s reasons for not establishing an element equivalent to net financial position are set out in paragraphs BC5.66 to BC5.68 in its Basis for Conclusions on Chapter 5. One reason was that the IPSASB was concerned that the terms “residual interest” and “ownership interest” can be misunderstood or misinterpreted. That led it to the conclusion

that net financial position is a residual amount that should not be defined. However, the IPSASB acknowledged that the terms “residual interest” and “ownership interest” have been used in some jurisdictions.

- BC15. The NZASB considered that a definition of equity is required for completeness. The NZASB noted that the previous Conceptual Frameworks used in New Zealand had included a definition of equity, the definition of a PBE refers to equity, and that the term has wide acceptance in New Zealand. The NZASB noted that PBE Standards currently use the term “net assets/equity” and considered whether this should be the defined term. Given that the term equity was the defined term used in the previous PBE Framework, the NZASB considered that it was appropriate for New Zealand PBEs. This led to using the term equity, rather than net financial position, in the definitions of ownership contributions and ownership distributions.

Other Resources and Other Obligations

- BC16. The NZASB noted that the IPSASB’s Conceptual Framework left open the possibility of the IPSASB issuing IPSASs that require or allow the recognition of resources or obligations that do not satisfy the definition of an element. The IPSASB indicated that the recognition of such items would be limited to circumstances where it was considered necessary to ensure that the financial statements provide information that is useful for a meaningful assessment of the financial performance and financial position of an entity. The NZASB had concerns about the possibility of recognising an item that does not meet the definition of an element. However, at the point that the NZASB was approving the PBE Conceptual Framework, the IPSASB had not applied this concept at a standards level. The NZASB agreed to retain reference to other resources and other obligations in paragraph 5.4 in the PBE Conceptual Framework, but to note that it would carefully consider any future requirements in IPSASs to recognise an item that did not meet the definition of an element.

Statement of Financial Performance

- BC17. The IPSASB’s Conceptual Framework refers to revenue and expense being reported in the statement of financial performance. The NZASB considered whether the PBE Conceptual Framework should instead refer to the statement of comprehensive revenue and expense, which is the statement referred to throughout PBE Standards. The NZASB decided not to change the titles of statements used in the IPSASB’s Conceptual Framework on the grounds that it would be appropriate to wait until the IPSASB considers the presentation of revenue and expenses in the financial statements in the context of a review of IPSAS 1 *Presentation of Financial Statements*. The NZASB will continue to monitor projects of both the IPSASB and the IASB which may have implications for the PBE Conceptual Framework. In particular, the NZASB will continue to monitor any conceptual work developments in relation to the meaning of financial performance.

Chapter 6 Recognition in Financial Statements

- BC18. The NZASB did not make any significant modifications to Chapter 6 of the IPSASB’s Conceptual Framework.

Chapter 7 Measurement of Assets and Liabilities in Financial Statements

- BC19. The NZASB did not make any significant modifications to Chapter 7 of the IPSASB’s Conceptual Framework. The NZASB acknowledged that some of the discussion in the Chapter (for example, the section on replacement cost) might be used more in a public sector context but considered that it could also be useful for not-for-profit entities.

Chapter 8 Presentation in General Purpose Financial Reports

- BC20. The NZASB did not make any significant modifications to Chapter 8 of the IPSASB’s Conceptual Framework.

Part B

Effective Date

This Authoritative Notice is effective for financial statements covering periods beginning on or after 1 January 2017. Earlier application is permitted provided an entity has applied, or is applying, PBE Standards, PBE SFR- A (NFP) *Public Benefit Entity Simple Format Reporting – Accrual (Not-For-Profit)* or PBE SFR- A (PS) *Public Benefit Entity Simple Format Reporting – Accrual (Public Sector)*.