

Board Meeting Agenda

Wednesday 25 March 2020

by videoconference from Level 7, 50 Manners Street, Wellington

Est Time	Item	Topic	Objective		Page
B: PUBLIC SESSION					
PBE Items for Consideration					
10.00 am	3	IPSASB Revenue and Expenses	(JS/VSF)		
	3.1	Cover memo	Consider	Paper	
	3.2	Memo: ED 70	Consider	Paper	
	3.3	Memo: ED 71	Consider	Paper	
		IPSASB EDs	Note	Link	
		IPSASB ED 70 At a Glance			
		IPSASB ED 70 Revenue with Performance Obligations			
		IPSASB ED 71 At a Glance			
		IPSASB ED 71 Revenue without Performance Obligations			
		IPSASB ED 72 At a Glance			
		IPSASB ED 72 Transfer Expenses			
10.30 am		<i>Morning tea</i>			
10.45 am		IPSASB Revenue and Expenses (contd)			
11.55 pm	4	PBE Policy Approach	(TC)		
	4.1	Cover memo: Annual review of the application of the PBE Policy Approach	Note	Paper	
	4.2	Memo: <i>Improvements to IPSAS, 2019</i>	Consider	Paper	
	4.3	<i>Improvements to IPSAS, 2019</i>	Note	Link	
	4.4	<i>Policy Approach to Developing the Suite of PBE Standards</i>	Note	Link	
12.15 pm		<i>Lunch</i>			
For-profit Items for Consideration					
12.45 pm	5	General Presentation and Disclosures	(LK)		
	5.1	Cover memo	Consider	Paper	
	5.2	MPMs and disaggregation	Consider	Paper	
	5.3	Amendments to other IFRS Standards	Consider	Paper	

Est Time	Item	Topic	Objective		Page
	5.4	IASB ED/2019/7 <i>General Presentation and Disclosures</i>	Note	Link	
	5.5	IASB ED/2019/7 <i>General Presentation and Disclosures – Basis for Conclusions</i>	Note	Link	
	5.6	IASB ED/2019/7 <i>General Presentation and Disclosures – Illustrative Examples</i>	Note	Link	
	5.7	IASB ED/2019/7 <i>General Presentation and Disclosures – Snapshot</i>	Note	Link	
For-profit Item for Approval					
2.45 pm	6	Classification of Liabilities as Current or Non-current	(TC)		
	6.1	Cover memo	Note	Paper	
	6.2	<i>Classification of Liabilities as Current or Non-current</i>	Approve	Paper	
	6.3	Draft signing memorandum	Approve	Paper	
	6.4	PBE Policy Approach	Consider	Paper	
3.00 pm		<i>Afternoon tea</i>			
Standards for Noting					
3.14 pm	7	Standards Approved	(VSF)		
	7.1	Approval 113 <i>PBE Interest Rate Benchmark Reform</i>	Note	Paper	
	7.2	Approval 114 <i>Withdrawal of PBE FRS 46 (Amendments to PBE FRS 47)</i>	Note	Paper	
	7.3	Approval 115 <i>Revocation of PBE FRS 46</i>	Note	Paper	

Next NZASB meetings:

Wednesday 15 April 2020 (half-day videoconference currently scheduled)

Thursday 7 May 2020



NZ ACCOUNTING
STANDARDS
BOARD

Memorandum

Date: 13 March 2020

To: NZASB Members

From: Joanne Scott and Vanessa Sealy-Fisher

Subject: **Cover memo: IPSASB Revenue and Expenses**

Purpose¹

1. The purpose of this item is to:
 - (a) begin seeking feedback on the proposals in the three IPSASB exposure drafts (see agenda items 3.2 and 3.3); and
 - (b) present a revised plan for Board meetings and decide whether the additional half day meeting in April is still required.

Background

2. The IPSASB issued the following EDs on 21 February 2020:
 - (a) ED 70 *Revenue with Performance Obligations*;
 - (b) ED 71 *Revenue without Performance Obligations*; and
 - (c) ED 72 *Transfer Expenses*.
3. We distributed a combined file containing the three EDs and the At a Glance documents to Board members on 26 February. That combined file has also been made available to Board members alongside these agenda papers.
4. The Board has previously agreed to comment on these EDs. The closing date for comments to the NZASB is 14 August 2019 and to the IPSASB is 15 September 2020. The IPSASB's comment period is slightly longer than we expected. This means we can finalise the comment letter at the Board's meeting in September, rather than in August as originally planned.
5. The Board has already had some discussions about the IPSASB's proposals.
 - (a) October 2019: The Board received an education session on the IPSASB's tentative decisions on revenue with performance obligations (which are dealt with in ED 70).
 - (b) December 2019: The Board discussed the IPSASB's tentative decisions on revenue without performance obligations (which are dealt with in ED 71).

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

- (c) February 2020: The Board received a presentation outlining the proposals in all three EDs.
6. Although we had previously indicated that this meeting would focus on ED 70, we are seeking the Board’s feedback on both ED 70 and ED 71.
- (a) Agenda item 3.2 covers most of the proposals in ED 70 apart from disclosures. At this meeting we are seeking the Board’s views on SMCs 1 to 3. We will also seek feedback on whether the Board wants to comment on SMCs 4 and 5.
 - (b) Agenda item 3.3 focuses on SMC 1 in ED 71. This SMC seeks views on when a transfer recipient has a *present obligation* that meets the definition of a liability (despite there being no *performance obligation* associated with the transaction). We are also seeking feedback on which other ED 71 SMCs the Board wants to comment on.

Plan for Board meetings

7. Table 1 sets out the revised plan for Board meetings between now and September. It does not include the half day meeting scheduled for 15 April. However, this is dependent on how much progress we make on the topics discussed at this meeting and whether the Board agrees that the plan is reasonable. We would like to discuss the plan at the end of this item.

Table 1

25 Mar	ED 70 SMCs 1 to 3 and selected issue ED 71 SMC 1 Present obligation ED 70 and ED 71 decide which SMCs to comment on
15 Apr (half day)	
7 May	ED 71 other issues (apart from disclosure) ED 72 issues ED 72 decide which SMCs to comment on
17 Jun	Any remaining issues (apart from disclosure) Feedback received to date Draft comment letter (apart from disclosure)
13 Aug	Disclosure – all three EDs Draft comment letter
10 Sept	Analysis of submissions and outreach Approve comment letter

Questions for the Board

- Q1. Does the Board agree with the plan for Board meetings?
- Q2. Does the Board agree that the half day meeting on 15 April is NOT required?

Outreach

8. We have already notified constituents about the EDs via an NZASB Update. The EDs, At a Glance documents and links to the IPSASB's webinars are available on the XRB website.
9. We will promote awareness of, and seek feedback on, the proposals at the following meetings:
 - (a) External Reporting Advisory Panel (XRAP) on 21 May in Wellington; and
 - (b) Technical Reference Group (TRG) on 26 May in Auckland (and via teleconference).
10. We have yet to organise the roundtable with representatives from the public sector and not-for-profit (NFP) sector. Given our understanding of workflows in the public sector, we will try to arrange this for late May.
11. We are liaising with Charities Services staff about promoting awareness via the Charities Services' newsletter and website.
12. We will promote awareness of the proposals at various conferences and events.
 - (a) Conferenz NFP and public sector conferences; and
 - (b) New Zealand Society of Local Government Managers' Civic Financial Services Strategic Finance Forum.
13. In addition, we will contact New Zealand respondents who commented on the CP.

Attachments

Agenda item 3.2: Memo: ED 70

Agenda item 3.3: Memo: ED 71

IPSASB EDs See separate file



NZ ACCOUNTING
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Memorandum

Date: 13 March 2020
To: NZASB Members
From: Vanessa Sealy-Fisher
Subject: **IPSASB ED 70**

Purpose and introduction¹

1. ED 70 *Revenue with Performance Obligations* (ED 70) contains five specific matters for comment (SMCs). They cover the following topics.
 - (a) SMC 1: Whether the scope of ED 70, which is based around binding arrangements as defined in the ED, is clear.
 - (b) SMC 2: The IPSASB's decision not to define 'transfer revenue' or 'transfer revenue with performance obligations'.
 - (c) SMC 3: Whether constituents agree with paragraphs AG69 and AG70, which provide guidance about accounting for transactions with components relating to both ED 70 and ED71 *Revenue without Performance Obligations*.
 - (d) SMC 4: Whether the disclosure requirements should be aligned with those in IFRS 15 (because ED 70 is based on, and substantially aligned with, IFRS 15). Disclosures will be discussed at a future Board meeting.
 - (e) SMC 5: An additional disclosure requirement for information on transactions which an entity is compelled to enter into by legislation or other governmental policy decisions (for example, where a public sector entity may be compelled to enter into binding arrangements to provide goods or services to parties who do not have the ability or intention to pay). This disclosure will also be discussed at a future Board meeting.
2. The purpose of this agenda item is to seek feedback on most of the proposals in ED 70, with the aim of identifying the key points for the Board's comment letter on ED 70. The memo includes a summary of the NZASB's comments on the IPSASB's 2017 Consultation Paper (2017 CP),² including how they have been addressed in ED 70.
3. Feedback on the disclosure requirements will be sought at a future Board meeting.

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² Consultation Paper *Accounting for Revenue and Non-Exchange Expenses*

Recommendations

4. We recommend that the Board:
 - (a) PROVIDES FEEDBACK on the matters discussed in this memo; and
 - (b) DECIDES whether to respond to SMCs 4 and 5 in ED 70.

Background

5. ED 70 is based on IFRS 15 *Revenue from Contracts with Customers*. Appendix A to this memo summarises the differences between ED 70 and IFRS 15. The IPSASB has made the following modifications to IFRS 15.
 - (a) Changes to the definitions and terminology in IFRS 15 to ensure consistency with *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*, consistency with definitions and terminology in International Public Sector Accounting Standards (IPSAS), and to reflect the public sector context.
 - (b) Additional application guidance on public sector-specific issues or issues which may be more prevalent in the public sector.
 - (c) Deletion of illustrative examples which have limited or no applicability to the public sector.
 - (d) Modification of the IFRS 15 illustrative examples to reflect the public sector context and the addition of public sector-specific examples.
6. In addition to the modifications outlined above, the IPSASB has extended the scope of revenue transactions with performance obligations to specifically include transactions that involve the transfer of goods or services to third-party beneficiaries.
7. When finalised, the new International Public Sector Accounting Standard (IPSAS) would supersede IPSAS 9 *Revenue from Exchange Transactions* and IPSAS 11 *Construction Contracts*.

Structure of this memo

8. The remaining sections in this memo are:
 - (a) NZASB views on IPSASB 2017 CP;
 - (b) Scope of ED 70;
 - (c) Terminology not defined;
 - (d) Revenue transactions with two components;
 - (e) Control of an asset;
 - (f) Performance obligations;
 - (g) Principal versus agent considerations; and
 - (h) Next steps.

NZASB views on IPSASB 2017 CP

9. In August 2017 the IPSASB issued Consultation Paper *Accounting for Revenue and Non-Exchange Expenses* (the 2017 CP). One of the proposals in the 2017 CP was the development of a revenue standard based on IFRS 15.
10. The IPSASB sought feedback on the following preliminary view.

Preliminary View 1

The IPSASB considers that it is appropriate to replace IPSAS 9 *Revenue from Exchange Transactions*, and IPSAS 11 *Construction Contracts* with an IPSAS primarily based on IFRS 15 *Revenue from Contracts with Customers*. Such an IPSAS will address Category C transactions that:

- (a) Involve the delivery of promised goods or services to customers as defined in IFRS 15; and
- (b) Arise from a contract (or equivalent binding arrangement) with a customer which establishes performance obligations.

Do you agree with the IPSASB’s Preliminary View 1? If not, please give your reason.

11. The Board agreed that the existence or absence of performance obligations in revenue transactions should be the key determinant for revenue recognition in the public sector. However, the Board noted that the scope of the Public Sector Performance Obligation Approach (PSPOA) would depend on how the IPSASB defined key factor such as enforceability and performance obligations.
12. The Board noted that in developing an IPSASB based on IFRS 15, the IPSASB would likely face a number of challenges similar to those experienced by the Australian Accounting Standards Board (AASB), which completed a similar project at the end of 2016.
13. Table 1 outlines the challenges that the Board envisaged the IPSASB would face in developing an IPSAS based on IFRS 15 and how they have been addressed in ED 70.

Table 1: NZASB views on 2017 CP

Challenge identified	How addressed in ED 70
<p>What is <i>enforceability in the public sector</i>?</p> <p>IFRS 15 has no guidance regarding enforceability.</p> <p>The AASB noted that a return obligation is an indicator of enforceability, but not the only indicator. The AASB expanded the enforceability guidance to include a range of factors that could potentially result in an enforceable arrangement. For example, paragraph F12 of AASB 15 <i>Revenue from Contracts with Customers</i> (AASB 15) lists the following examples of terms that could result in enforceable agreements:</p> <ol style="list-style-type: none"> (a) a refund in cash or kind is required when the agreed specific performance has not occurred; 	<p>ED 70 contains application guidance on enforceability (paragraphs AG13–AG24).</p> <p>Instead of a focus on revenue transactions arising from contracts with customers (as in IFRS 15), ED 70 focuses on whether the revenue transaction arises from a binding arrangement as a key determinant for identifying revenue transaction that give rise to enforceable performance obligations.</p> <p>The concept of enforceability proposed in ED 70 is underpinned by the definition of a binding arrangement, being an arrangement that confers both enforceable rights and obligations on both parties to the arrangement. The IPSASB proposes that an arrangement is enforceable when the entity and the purchaser are both able to enforce</p>

Challenge identified	How addressed in ED 70
<p>(b) the customer, or another party acting on its behalf, has a right to enforce specific performance or claim damages;</p> <p>(c) the customer has the right to take a financial interest in assets purchased or constructed by the entity with resources provided under the agreement;</p> <p>(d) the parties to the agreement are required to agree on alternative uses for the resources provided under the agreement; and</p> <p>(e) an administrative process exists to enforce agreements between sovereign States or between a State and another party.</p>	<p>their respective rights and obligations through legal or equivalent means.</p> <p>The guidance in ED 70 is substantively consistent with the guidance in Appendix F of AASB 15. However, ED 70 does not include examples of the terms that result in enforceable agreements as outlined in paragraph F12 of AASB 15.</p>
<p>What is a <i>performance obligation</i> in the public sector?</p> <p>IFRS 15 defines the term performance obligations but does not have any additional guidance on identifying performance obligations.</p> <p>Sometimes resources are provided with no, or minimal, terms and conditions on how the resources must be used. Other resources may have stipulations only in the form of time requirements. For these reasons, it can be difficult to distinguish goods or services provided to meet a general requirement from any of the not-for-profit's (NFP) other goods or services provided.</p> <p>Paragraph F20 of AASB 15 lists the factors to be considered in identifying whether performance obligations are sufficiently specific.</p>	<p>The definition of a performance obligation in ED 70 is identical to the definition in IFRS 15 except for the public sector modification to include the transfer goods or services to the purchaser or a third-party beneficiary. The definition requires the entity to transfer (a) a good or service (or a bundle of goods and services) that is distinct; or (b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the purchaser or third-party beneficiary.</p> <p>ED 70 contains application guidance on identifying performance obligations (paragraph AG32–AG42). The factors in paragraph AG35 to be considered in identifying whether performance obligations are sufficiently specific are identical to the factors listed in paragraph F20 of AASB 15.</p> <p>The guidance in ED 70 and AASB 15 is broadly consistent.</p>
<p><i>Transactions with two components</i> – how and when to account for transactions where there is a performance obligation and another component without a performance obligation. For example, a fundraising dinner where the ticket price could exceed the usual market rate for the dinner, indicating that there are two components: the dinner (for which there is a performance obligation) and a donation.</p> <p>The AASB added guidance in Appendix F of AASB 15 to help NFPs to allocate the transaction price when a customer enters into a contract with an NFP with the dual purpose of obtaining</p>	<p>ED 71 (paragraph 9) deals with transactions with components with performance obligations and components without performance obligations (hybrid transactions) and includes a cross-reference to paragraphs AG69–AG70 of ED 70. ED 71, illustrative example 28, deals with a fundraising dinner.</p> <p>ED 70 contains application guidance for transactions with components within the scope of ED 70 and ED 71 <i>Revenue without Performance Obligations</i> (paragraphs AG69–AG70) and some illustrative examples.³</p>

³ Specific Matter for Comment 3 seeks feedback on whether constituents agree with this guidance.

Challenge identified	How addressed in ED 70
<p>goods or services and to help the NFP achieve its objectives.</p>	<p>The guidance and illustrative examples are consistent with the guidance in Appendix F of AASB 5 (paragraphs F28–F32).</p> <p>There is also some guidance in ED 72 <i>Transfers Expenses</i> (paragraphs 14 and AG53–AG54) about accounting for components of transactions.</p>
<p><i>Licences</i></p> <p>In its comment letter on the 2017 CP, the Board noted that the AASB was considering issues for public sector entity licensors, including the circumstances in which the revenue from granting a licence is, in substance, a tax (and should be accounted for under ED 71) or involves the delivery of goods or services (and should be accounted for under ED 70).</p> <p>Appendix G of AASB 15 contains guidance specifically for not-for-profit public sector licensors.</p>	<p>The requirements and guidance in ED 70 on licencing are identical to the requirements and guidance in IFRS 15. ED 70 does not have any public sector-specific guidance on determining whether the licence revenue is, in substance, a tax or a revenue transaction involving the transfer of services.</p> <p>ED 70 does not contain any of the guidance in Appendix G of AASB 15.</p>
<p>Transactions where the arrangement does not explicitly require the transfer of a good or service but may do so implicitly where there is a <i>direct relationship between the funding and the outputs delivered</i>.</p> <p>Such arrangements have all the criteria to fall within the scope of IFRS 15, except for the lack of an explicit requirement to transfer goods or services. The Board’s view was that, in substance, these transactions are substantially similar to an IFRS 15 transaction – the resource provider is effectively funding the delivery of the outputs (goods or services) to other parties. For example, funding for the salary of an employee who is engaged in providing services to beneficiaries (e.g. a doctor providing health services).</p>	<p>ED 70 applies to revenue arising from binding arrangements with a purchaser that include performance obligations to transfer promised goods or services to the purchaser or a third-party beneficiary.</p> <p>In ED 70, illustrative example 38, a health clinic receives funding from the government to provide free vaccinations. In Case B (paragraphs IE 213 and IE 214), the terms of the binding arrangement specify that the clinic has discretion to spend the funds on expenditures that are directly related to the vaccination program and may include an allocation of salaries of staff who work on vaccination-related activities. The conclusion to this example is that the arrangement is within the scope of ED 71 (rather than ED 70) because the arrangement does not specify that the funding is restricted to fund the provision of vaccines.</p> <p>In addition, page 4 of the ED 71 At a Glance includes an example of the salary for a particular person as an example of eligible expenditure as defined in ED 71.</p>

Scope of ED 70

14. An entity applies ED 70 to revenue arising from binding arrangements with a purchaser that include performance obligations to transfer promised goods or services to the purchaser or to a third-party beneficiary.

15. The modifications made to IFRS 15 for public sector entities are explained in more detail in the IPSASB’s Basis for Conclusions on ED 70 (paragraphs BC16–BC18). In summary, those modifications are as follows.
- (a) ED 70 includes the concept of a binding arrangement (which is broader than a contract) to allow for jurisdictions where government and public sector entities cannot enter into legal contracts but do enter into binding arrangements (which are in substance the same as contracts).
 - (b) ED 70 explains that enforceability of a binding arrangement includes mechanisms that are outside the legal system, such as statutory mechanisms (for example, through legislative or executive authority and/or cabinet or ministerial directives).
 - (c) ED 70 explains that public sector transactions often involve three parties:
 - the purchaser – provides the consideration;
 - the entity – receives the consideration and is responsible for the delivery of the goods or services; and
 - the third-party beneficiary – the individuals or households receiving those goods or services.
16. ED 70 also includes application guidance relating to the definition of a binding arrangement (paragraphs AG7–AG12), the enforceability of a binding arrangement (paragraphs AG13-AG24) and identifying the binding arrangement (paragraphs AG26–AG31). None of this guidance is found in IFRS 15.
17. SMC 1 seeks feedback on whether the scope of ED 70 is clear and, if the scope is not clear, what changes to the scope or the definition of binding arrangements should be made. In order to assist the Board in forming a view on this SMC, the modifications outlined in paragraph 15 above are discussed in more detail below.

Binding arrangements

18. All references to ‘contracts’ in IFRS 15 were replaced with ‘binding arrangements’. This replacement acknowledges that entities in some jurisdictions may not have the power to enter into legal contracts but nevertheless may have the authority to enter into binding arrangements. The IPSASB often makes this type of change to cater for public-specific circumstances. As the concept of a contract may still be applicable in the public sector, the IPSASB retained the definition of contract but specified that a contract is a type of binding arrangement.

19. ED 70 defines a binding arrangement as follows:⁴
- A binding arrangement is an arrangement that confers both enforceable rights and obligations on both parties to the arrangement. A contract is a type of binding arrangement (paragraphs AG7–AG12 provide additional guidance).**⁵
20. In developing ED 70, the IPSASB decided to explicitly specify in the definition that a binding arrangement confers both enforceable rights and obligations on both parties to the arrangement. An arrangement is enforceable when the entity and the purchaser are both able to enforce their respective rights and obligations through legal or equivalent means.
21. The IPSASB agreed that, for the purposes of ED 70, binding arrangements should encompass rights that arise from legislative or executive authority, cabinet or ministerial directives.
22. In determining whether an arrangement is an enforceable binding arrangement, an entity considers the substance rather than the legal form of an arrangement. An arrangement is enforceable by another party through legal or equivalent means if the agreement includes:
- (a) distinct rights and obligations for both purchaser and entity (resource recipient); and
 - (b) remedies for non-performance by the entity which can be enforced by the purchaser through legal or equivalent means.
23. ED 70 contains public sector-specific application guidance relating to the definition of a binding arrangement (paragraphs AG7–AG12) and identifying the binding arrangement (paragraphs AG26–AG31). ED 71 and ED 72 also contain application guidance relating to the definition of a binding arrangement (paragraphs AG10–AG15 and paragraphs AG9–AG14 respectively). The application guidance is consistent across all three EDs.
24. In addition, there are public sector-specific illustrative examples dealing with transactions that arise from an arrangement that is not binding and transactions that arise from a binding arrangement without performance obligations) (Illustrative Examples 1 and 2, paragraphs IE2-IE9).
25. Although the illustrative examples in IFRS 15 that deal with identifying a contract have been modified for the public sector in ED 70, the examples in ED 70 (Illustrative Examples 5–8, paragraphs IE16–IE31) on identifying a binding arrangement deal with the same aspects of identifying a contract as in IFRS 15 (for example, collectability of the consideration and reassessing the criteria for identifying a contract).

⁴ This definition is consistent with the definition of binding arrangement for:

- interests in other entities (an arrangement that confers enforceable rights and obligations on the parties to it as if it were in the form of a contract. It includes rights from contracts or other legal rights) (IPSAS 35, *Consolidated Financial Statements*, IPSAS 36, *Investments in Associates and Joint Ventures*, IPSAS 37, *Joint Arrangements*, and IPSAS 38, *Disclosure of Interests in Other Entities*); and
- service concessions arrangements (describes contracts and other arrangements that confer similar rights and obligations on the parties to it as if they were in the form of a contract) (IPSAS 32, *Service Concession Arrangements: Grantor*).

⁵ ED 70 and IFRS 15 both define a contract as “an agreement between two or more parties that creates enforceable rights and obligations”.

26. The definition of a binding arrangement has the same meaning for the purpose of applying ED 71 and ED 72.

Staff view

27. We agree with the definition of, and application guidance on, binding arrangements in ED 70 (and ED 71 and ED 72).
28. Although there is more application guidance on the definition of a binding arrangement in ED 70 than there is in IPSAS 23 and IPSASs 35–38 dealing with interests in other entities, all the pronouncements include a statement to the effect that binding arrangements can be evidenced in several ways and that they may arise from legal contracts or through equivalent means such as statutory mechanisms.⁶ We also note that the definitions have been tailored to suit the relevant standards: we agree with the variations to the wording.
29. We agree that the inclusion of application guidance for identifying the binding arrangement in ED 70 is important because the existence of a binding arrangement is a necessary element for a transaction to be within the scope of the draft standard. We also agree that the additional guidance is appropriate in an integral appendix to ED 70.

Enforceability

30. A key characteristic of a binding arrangement is the ability of both parties to have and be able to enforce both the rights and obligations conferred on them in the arrangement. That is, the entity receiving the consideration must be able to enforce the promise to receive the funding. Similarly, the entity providing the funding (the purchaser) must be able to enforce the promise to transfer specific goods and services by the entity receiving the consideration. It is the purchaser's ability to compel the delivery of goods and services that creates the basis for the five-step revenue recognition model in ED 70.
31. A binding arrangement is enforceable through legal or equivalent means. Legal enforceability is determined based on the principles set out in the laws of a jurisdiction, which includes legislation, executive authority, cabinet or ministerial directives, as well as judicial rulings and case law precedence. For an arrangement to be enforceable through 'equivalent means', the presence of an enforcement mechanism outside the legal system is required.
32. The IPSASB considered and discussed the following as possible enforcement mechanisms by equivalent means.
- (a) *Cabinet and ministerial decision, including executive authority.* The IPSASB agreed that these are subsets of legislation and may in some circumstances be valid enforcement mechanisms.
 - (b) *Reduction of future funding.* The IPSASB decided that this could only be used to enforce a binding arrangement if the purchaser had a present obligation to provide future funding under another binding arrangement.

⁶ See footnote 4

- (c) *Sovereign rights*. The IPSASB agreed that by themselves, sovereign rights do not establish a valid enforcement mechanism. However, if details on how sovereign rights would be used to enforce an agreement were included in the binding arrangement, then this could create a valid enforcement mechanism.
 - (d) *A statement made by government*. The IPSASB decided that a statement made by government to spend money or use assets in a particular way (for example, a general policy statement or announcement following a natural disaster) does not create enforceable rights and obligations on parties as there is no agreement with other parties, and therefore there is no binding arrangement.
33. ED 70 contains application guidance on enforceability (paragraphs AG13–AG24). This guidance includes a discussion of the mechanisms identified in paragraph 29 above. In addition, Illustrative Example 4 (paragraphs IE13–IE15) illustrates enforceability by a mechanism other than legal means.
34. ED 71 and ED 72 also contain application guidance relating to enforceability (paragraphs AG16–AG21 and paragraphs AG15–AG23 respectively). The application guidance is consistent across all three EDs.

Staff view

35. We agree with the additional application guidance and illustrative example regarding the enforceability of a binding arrangement. This guidance is important because the definition of a binding arrangement refers to ‘enforceable rights and obligations’ of both parties to the arrangement.
36. Appendix F of AASB 15 contains Australian implementation guidance for not-for-profit entities, including guidance on enforceable agreements (paragraphs F10–F19). We note that the guidance in ED 70 and Appendix F is consistent but not identical. For example, paragraph F12 includes the following examples of terms in agreements that result in the agreement being enforceable:
- (a) a refund in cash or kind is required when the agreed specific performance has not occurred;
 - (b) the customer, or another party acting on its behalf, has a right to enforce specific performance or claim damages;
 - (c) the customer has the right to take a financial interest in assets purchased or constructed by the entity with resources provided under the agreement;
 - (d) the parties to the agreement are required to agree on alternative uses of the resources provided under the agreement; and
 - (e) an administrative process exists to enforce agreements between sovereign States or between a State and another party.
37. If the Board is of the view that the examples in paragraph F12 are helpful, we can suggest to the IPSASB that they be included in the application guidance in ED 70.

Three-party arrangements

38. Although the IASB's educational materials for IFRS 15 refer to three-party arrangements, they were not explicitly highlighted in IFRS 15. The IPSASB has explicitly referred to three-party arrangements in ED 70 because they are more prevalent in the public sector.
39. The IPSASB replaced the term 'customer' in IFRS 15 with the term 'purchaser' in ED 70 because the use of the term 'purchaser' is widespread in IPSAS and is a broader term more suited to transactions involving the transfer of goods or services to either the purchaser or agreed third-party beneficiary. However, the term 'customer' may still be applicable in some circumstances so the IPSASB retained the definition of a customer but clarified that a customer is a type of purchaser.
40. ED 70 defines a third-party beneficiary as follows:
- A third-party beneficiary is an entity, household or individual who will benefit from a transaction made between two other parties by receiving goods, services or other assets (paragraph AG22 provides additional guidance).**
41. Third-party beneficiary has been defined so that its meaning can be consistently applied to ED 70 as well as ED 71 and ED 72.

Staff view

42. We agree with the inclusion of three-party arrangements within the scope of ED 70 because of the prevalence of these types of arrangements in the public (and not-for-profit) sectors. These transactions give rise to performance obligations when the resource provider can enforce the resource recipient's obligation to transfer distinct goods or services to the third-party beneficiaries.

Questions for the Board

1. Do you agree with the staff views above on identifying revenue transactions within the scope of ED 70, that is, revenue transactions arising from binding arrangements with performance obligations?
2. Do you agree that the examples of terms in agreements that result in the agreements being enforceable (paragraph F12 of AASB 15) are helpful and should be included in ED 70?
3. Do you agree that the scope of this Exposure Draft is clear? If not, what changes to the scope of the Exposure Draft or the definition of binding arrangements would you make?

SMC 1

This Exposure Draft is based on IFRS 15, *Revenue from Contracts with Customers*. Because in some jurisdictions public sector entities may not have the power to enter into legal contracts, the IPSASB decided that the scope of this Exposure Draft would be based around binding arrangements. Binding arrangements have been defined as conferring both enforceable rights and obligations on both parties to the arrangement.

4. Do you have any other comments in response to SMC 1?

Terminology not defined

43. SMC2 seeks feedback on the IPSASB's decision not to define the terms 'transfer revenue' or 'transfer revenue with performance obligations' in ED 70.
44. Even though there is an interaction between ED 70, ED 71 and ED 72, and ED 72 defines transfer expense, the IPSASB decided not to clarify the mirroring relationship between the EDs in this respect.
45. Paragraphs BC21 explains that the IPSASB decided that ED 70 should not include the terms 'transfer revenue' or 'transfer revenue with performance obligations' for the following reasons.
 - (a) The key distinguishing feature for revenue to be within the scope of ED 70 is whether the transaction arises from a transaction with or without performance obligations. A number of IPSASB members were concerned that introducing new definitions relating to revenue may confuse constituents.
 - (b) Transfer revenue with performance obligations would have been a subset of revenue within the scope of ED 70, while transfer revenue would have been a subset of revenue within the scope of ED 71.⁷ Separately defining these terms when their recognition and measurement would have been the same as other types of revenue within their respective standards seems to be adding an unneeded level of complexity.
46. The IPSASB noted that some constituents who provide goods, services and other assets to third-party beneficiaries would like to disclose information in their financial statements regarding their programmes. As a result, the IPSASB decided to include in ED 70 a category for revenue earned from the provision of goods or services to third-party beneficiaries (see ED 70 paragraph AG139).

Staff view

47. Staff agrees with the IPSASB decision not to define the terms 'transfer revenue' and 'transfer revenue with performance obligations' for the reasons explained in the Basis for Conclusions on ED 70.

Questions for the Board

5. Do you agree with the staff views above on not defining the terms 'transfer revenue' and 'transfer revenue with performance obligations'? (SMC 2)
6. Do you have any other comments in response to SMC 2?

⁷ Revenue is defined in ED 70 and IPSAS 1 *Presentation of Financial Statements* as "the gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increased relating to contributions from owners.

Revenue transactions with two components

48. As noted above, the Board identified transactions with two components as a challenge that the IPSASB should consider when developing ED 70.
49. The IPSASB's deliberations on transactions with multiple components are set out in the Basis for Conclusions on ED 70 (paragraphs BC59 and BC60). The IPSASB discussed situations where a purchaser may enter a binding arrangement with an entity with a dual purpose of obtaining goods or services and to help the entity achieve its objectives, for example, providing a donation in addition to obtaining goods or services. The IPSASB noted that there is a rebuttable presumption in ED 70 that all consideration received in a revenue binding arrangement relates entirely to the performance obligations within that arrangement. Because of this underlying presumption, in order to separate a portion of the consideration and account for it outside the scope of ED 70, there must be clear and objective evidence that a portion of the consideration received truly represents amounts that do not relate to performance obligations, which is the case when amounts are provided by a purchaser to help the entity achieve its objectives.
50. The IPSASB decided that to clearly demonstrate that a portion of the consideration is not related to performance obligations, the binding arrangement must state that if the entity does not satisfy its performance obligations to deliver goods or services, it is required to return only a specified portion of the consideration received. The remaining portion which the entity is not required to return would represent consideration received to help the entity achieve its objectives and would fall within the scope of ED 71.
51. Based on the above discussions, the IPSASB decided to provide additional guidance on when and how an entity should separate the consideration from such transactions into a transaction price for goods or services accounted for under ED 70 and amounts to be accounted for under ED 71.
52. Paragraph 9 of ED 71 also deals with transactions with components with performance obligations and components without performance obligations (hybrid transactions) as follows.

Transactions with Components with Performance Obligations and Components without Performance Obligations (Hybrid Transactions)

9. Where revenue transactions include components with performance obligations and components without performance obligations, professional judgment is required to determine whether the different components are identifiable. Where the components are identifiable, the transfer recipient recognizes the revenue from the component with performance obligations according to the principles and requirements of [draft] IPSAS [X] (ED 70). The revenue component without performance obligations is recognized according to the principles and requirements of this [draft] Standard. Where it is not possible to distinguish between the components with performance obligations and the components without performance obligations, the transaction is accounted for in accordance with [draft] IPSAS [X] (ED 70). [Draft] IPSAS [X] (ED 70) paragraphs AG69–AG70 provide additional guidance.

53. ED 70 contains the following two paragraphs to address this matter.

Transactions with Components within the Scope of [draft] IPSAS [X] (ED 71), *Revenue without Performance Obligations*

AG69. This [draft] Standard typically requires an entity to allocate the transaction price to each performance obligation in the binding arrangement so that the allocation depicts the amount of consideration to which the entity expects to be entitled in exchange for transferring the promised goods or services to a purchaser or third-party beneficiary. This is based on the rebuttable presumption that the transaction price is wholly related to the transfer of goods or services.

AG70. In the public sector, a purchaser may enter into a binding arrangement with an entity with a dual purpose of obtaining goods or services and to help the entity achieve its objectives. Such transactions may rebut the presumption that the transaction price is wholly related to the transfer of goods or services, as a portion of the consideration relates to helping the entity achieve its objectives. To demonstrate that this presumption is rebutted, the terms of the binding arrangement must clearly specify that only a portion of the consideration is to be returned to the purchaser in the event the entity does not deliver the promised goods or services, as this indicates that the remaining consideration is intended to help the entity achieve its objectives. When the presumption is rebutted, the entity shall disaggregate the transaction price and account for the component that relates to the transfer of promised goods or services in accordance with this [draft] Standard. The remainder of the transaction price shall be accounted for in accordance with [draft] IPSAS [X] (ED 71), *Revenue without Performance Obligations*.

54. ED 70 also includes an illustrative example of a transaction with one component that is within the scope of ED 70 and one component that is within the scope of ED 71 (Illustrative Example 3, paragraphs IE10–IE12). ED 71 also includes an illustrative example of arrangements that are within the scope of either ED 71 or ED 70 (Illustrative Example 1, paragraphs IE1–IE7).
55. The guidance in ED 70 is consistent with the guidance in Appendix F of AASB 15.

Questions for the Board

7. Do you agree with the staff views above on the proposed accounting for revenue transactions with components relating to both ED 70 and ED 71?
8. Do you agree with the application guidance? If not, why not?

SMC 3

Because the IPSASB decided to develop two revenue standards—this Exposure Draft on revenue with performance obligations and ED 71 on revenue without performance obligations—the IPSASB decided to provide guidance about accounting for transactions with components relating to both exposure drafts. The application guidance is set out in paragraphs AG69 and AG70.

9. Do you have any other comments in response to SMC 3?

Control of an asset

56. In comparing ED 70 with IFRS 15 and with ED 72, we noticed a difference between a paragraph that is common to all three pronouncements.
57. Table 2 includes an extract from ED 70, IFRS 15 and ED 72. The highlighted text in IFRS 15 and ED 72 is *not* in ED 70. The paragraphs relate to the sections of the standards dealing with the satisfaction of performance obligations.

Table 2: Extracts from ED 70, IFRS 15 and ED 72

ED 70	IFRS 15	ED 72
<p>30. An entity shall recognize revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service (i.e., an asset) to a purchaser or third-party beneficiary. An asset is transferred when (or as) the purchaser or third-party beneficiary obtains control of that asset.</p> <p>...</p>	<p>31 An entity shall recognise revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service (ie an asset) to a customer. An asset is transferred when (or as) the customer obtains control of that asset.</p>	<p>33. A transfer provider shall recognize an expense when (or as) the transfer recipient satisfies a performance obligation by transferring a promised good or service (i.e., an asset) to a third-party beneficiary. An asset is transferred when (or as) the third-party beneficiary obtains control of that asset. A transfer provider may determine the point at which the third-party beneficiary obtains control of the asset by reference to the transfer recipient losing control of that asset.</p>
<p>31. ...</p>	<p>32 ...</p>	<p>34. ...</p>
<p>32. Goods and services are assets, even if only momentarily, when they are received and used (as in the case of many services). The economic benefits or service potential embodied in an asset are the potential cash flows (inflows or savings in outflows), or the capacity to provide services that contribute to achieving the entity’s objectives, that can be obtained directly or indirectly in many ways, such as by:</p> <p>...</p>	<p>33 Goods and services are assets, even if only momentarily, when they are received and used (as in the case of many services). Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset. The benefits of an asset are the potential cash flows (inflows or savings in outflows) that can be obtained directly or indirectly in many ways, such as by:</p> <p>...</p>	<p>35. Goods and services are assets, even if only momentarily, when they are received and used by the third-party beneficiary (as in the case of many services). Control of an asset, which is defined in [draft] IPSAS [X] (ED 70), refers to the ability of the third-party beneficiary to direct the use of, and obtain substantially all of the remaining benefits or service potential from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the economic benefits or service potential from, an asset. The economic benefits or service potential embodied in the asset are the potential cash flows (inflows or savings in outflows), or the capacity to provide services that contribute to achieving the third-party beneficiary’s objectives, that can be obtained directly or indirectly in many ways, such as by:</p> <p>...</p>

58. We note that ED 70 defines the term 'control of an asset' as follows:

Control of an asset is the ability to direct the use of and obtain substantially all of the remaining economic benefits or service potential from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the economic benefits or service potential from, the asset.

59. We think the highlighted text in paragraph 33 of IFRS 15 should be included in paragraph 32 of ED 70 as ED 70 is supposed to be aligned with IFRS 15 as closely as possible.

60. We propose to recommend this to the IPSASB in our comment letter.

Question for the Board

10. Do you agree with our proposal to recommend that the sentences about control of an asset in paragraph 33 of IFRS 15 be included in paragraph 32 of ED 70?

Performance Obligations

61. An entity applies ED 70 in accounting for revenue from binding arrangements that include performance obligations as defined. ED 70 defines a performance obligation as follows:

A performance obligation is a promise in a binding arrangement with a purchaser to transfer to the purchaser or third-party beneficiary either:

- (a) **A good or service (or a bundle of goods or services) that is distinct; or**
- (b) **A series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the purchaser or third-party beneficiary.**

62. This definition in ED 70 is the same as the definition in IFRS 15 except for the public sector terminology (performance obligation, purchaser and third-party beneficiary). The definition also applies to ED 71 and ED 72.

63. For a revenue transaction to be within the scope of ED 70, an entity must be able to identify and measure the satisfaction of the performance obligation in the binding arrangement. If a performance obligation is not satisfied over time, the performance obligation is satisfied at a point in time (paragraph 37), and revenue is recognised accordingly.

64. For transfer expenses with performance obligations, ED 72 proposes that the transfer provider would recognise an asset for the right to have goods or services provided to third-party beneficiaries. The transfer provider would control this asset until the transfer recipient met its performance obligations. At this point, the asset would be derecognised, and an expense recognised, as the transfer recipient provided the goods and services to the third-party beneficiaries.

65. ED 70 does not include an SMC dealing with performance obligations. However, as part of our outreach activities, we plan to seek feedback on the following two matters from the perspective of the entity recognising revenue (ED 70) and the transfer provider (ED 72):

- (a) whether an entity is able to identify in a binding arrangement a performance obligation to transfer distinct goods or services to third-party beneficiaries; and

- (b) whether an entity is able to measure the satisfaction of a performance obligation to transfer distinct goods or services to third-party beneficiaries.

66. ED 72 does include SMCs about monitoring the satisfaction of the transfer recipient’s performance obligations throughout the duration of the binding arrangement, the recognition and measurement requirements for transfer expenses with performance obligations, and whether there are any practical difficulties with applying the recognition and measurement requirements for transfer expenses with performance obligations.

Question for the Board

11. Do you agree with our proposals to seek feedback on:
- (a) the ability of an entity to identify a performance obligation in a binding arrangement; and
 - (b) the ability of an entity to measure the satisfaction of a performance obligation identified in a binding arrangement?

Principal versus agent considerations

67. Paragraphs AG77–AG85 of ED 70 contain application guidance for an entity to determine whether the nature of its promise is a performance obligation to provide the specified goods or services itself (i.e. the entity is a principal) or to arrange for those goods or services to be provided by the other party (i.e. the entity is an agent). This guidance is equivalent to the guidance in Appendix B of IFRS 15.
68. Principal versus agent considerations are not new in IPSAS literature. IPSAS 35 *Consolidated Financial Statements* defines a decision-maker as “an entity with decision-making rights that is either a principal or an agent for other parties” and includes guidance for an entity to determine whether it is acting as a principal or an agent (paragraphs AG60–AG74).⁸
69. We are of the view that the guidance in paragraphs AG77–AG85 of ED 70 is appropriate and adequate.
70. We do not propose to seek feedback on this guidance.

Question for the Board

12. Do you agree with our proposal not to seek feedback on the appropriateness and adequacy of the guidance regarding principal versus agent considerations?

Next steps

71. A comparison of the disclosure requirements in all three EDs will be brought to a future meeting for the Board’s consideration.
72. The Board’s feedback will be incorporated into the draft comment letter to the IPSASB. Approval of the comment letter to the IPSASB will be sought at the September Board meeting.

⁸ The discussion is found under the heading of Delegated Power, as part of the Link Between Power and Benefits section of the application guidance.

Appendix A

Differences between ED 70 and IFRS 15

1. ED 70 contains additional application guidance regarding:
 - (a) Objective of the ED (paragraphs AG2–AG4);
 - (b) Scope (paragraphs AG5–AG6);
 - (c) Definition of binding arrangement (paragraphs AG7–AG25);
 - (d) Identifying the binding arrangement (paragraphs AG26–AG31);
 - (e) Identifying performance obligations (paragraphs AG32–AG42);
 - (f) Transactions with components within the scope of ED 71 (paragraphs AG69–AG70);
 - (g) Determination of stand-alone price (paragraph AG91); and
 - (h) Subsequent measurement of non-contractual receivables (paragraphs AG140–AG141).
2. ED 70 includes most of the illustrative examples in IFRS 15, amended as necessary to reflect public sector circumstances. The following table lists:
 - (a) the illustrative examples in IFRS 15 not used in ED 70; and
 - (b) additional illustrative examples in ED 70 for the public sector.

Illustrative examples in IFRS 15 not used in ED 70	Additional illustrative examples in ED 70 for the public sector
Example 23—Price concessions	Example 1—Transaction Arose from an Arrangement that is Not Binding
Example 32—Consideration payable to a customer	Example 2—Transactions Arose from a Binding Arrangement without Performance Obligations
Example 36—Incremental costs of obtaining a contract	Example 3—Transactions with One Component which is Within the Scope of ED 70 <i>Revenue with Performance Obligations</i> and Another Component is Within the Scope of ED 71 <i>Revenue without Performance Obligations</i>
Example 44—Warranties	Example 4—Enforceability by Mechanism other than Legal Means
Example 50—Option that provides the customer with a material right (discount voucher)	Example 38—Provision of Vaccines to Third-Party Beneficiaries
Example 57—Franchise rights	Example 46—Disclosures of Transactions that an Entity was Compelled to Enter by Legislation or Other Governmental Policy Decisions

Appendix B

Comparison of requirements and guidance in IPSASB EDs 70–72

The following table identifies requirements and application guidance (other than disclosures) that are relevant to at least two of the three EDs. The content has been checked for consistency of wording and for equivalency where appropriate (for example, between ED 70 and ED 72 for references to assets/liabilities and the respective treatment of those items).

Topic	ED 70 paras	ED 71 paras	ED 72 para
Identifying the binding arrangement <ul style="list-style-type: none"> ▪ <i>Combination of binding arrangements</i> ▪ <i>Modifications to a binding arrangement</i> <p><u>Application guidance</u></p> <ul style="list-style-type: none"> ▪ <i>Definition of binding arrangement</i> ▪ <i>Enforceability</i> 	8–20		13–23
Identifying the performance obligations <ul style="list-style-type: none"> ▪ <i>Distinct goods or services</i> ▪ <i>Transfer of goods and services</i> 	21–29 AG32–AG42		24–32 AG28–AG38
Satisfaction of performance obligations <ul style="list-style-type: none"> ▪ <i>Performance obligations satisfied over time</i> ▪ <i>Performance obligations satisfied at a point in time</i> ▪ <i>Measuring progress towards complete satisfaction of a performance obligation</i> ▪ <i>Methods for measuring progress</i> ▪ <i>Reasonable measure of progress</i> <p><u>Application guidance also includes</u></p> <ul style="list-style-type: none"> ▪ <i>Simultaneous receipt and consumption of the economic benefits or service potential of the entity performance</i> ▪ <i>Purchaser controls the asset as it is created or enhanced</i> ▪ <i>Entity’s performance does not create an asset with an alternative use</i> ▪ <i>Right to payment for performance completed to date</i> ▪ <i>Output methods</i> ▪ <i>Input methods (only ED 70)</i> 	30–44 AG43–AG60		33–44 AG39–AG52
Measurement	45–89	62–78	47–89
Determining the transaction price <ul style="list-style-type: none"> ▪ <i>Variable consideration</i> ▪ <i>Constraining estimates of variable consideration</i> ▪ <i>Reassessment of variable consideration</i> ▪ <i>The existence of a significant financing component in the binding arrangement</i> ▪ <i>Non-cash consideration</i> ▪ <i>Consideration payable to a purchaser</i> 	46–71		48–71

Topic	ED 70 paras	ED 71 paras	ED 72 para
<u>Application guidance comprises</u> <ul style="list-style-type: none"> ▪ Sale with a right of return (not ED 72) ▪ Transactions with components within the scope of ED 71 	AG61–AG70	AG33	AG53–AG54
Allocating the transaction price to performance obligations <ul style="list-style-type: none"> ▪ Allocation based on stand-alone prices ▪ Allocation of a discount ▪ Allocation of variable consideration 	72–85	80–81	72–85
<u>Application guidance comprises</u> <ul style="list-style-type: none"> ▪ Warranties ▪ Principal versus agent considerations (only ED 70) ▪ Purchaser options for additional goods or services ▪ Purchasers' unexercised rights ▪ Non-refundable upfront fees 	AG71–AG99		AG55–AG69
Changes in the transaction price	86–89		86–89
Presentation	104–108	121–125	121–125
<u>Application guidance: other specific application issues</u> <ul style="list-style-type: none"> ▪ Licensing ▪ Bill-and-hold arrangements 	AG100–AG113 AG129–AG132		AG70–AG83 AG84–AG87



NZ ACCOUNTING
STANDARDS
BOARD

Memorandum

Date: 13 March 2020
To: NZASB Members
From: Joanne Scott
Subject: **IPSASB ED 71**

Purpose and introduction¹

1. ED 71 *Revenue without Performance Obligations* (ED 71) contains seven specific matters for comment (SMCs). They cover the following topics.
 - (a) SMC 1 When a transfer recipient has a present obligation
 - (b) SMC 2 Flowchart in ED 71
 - (c) SMC 3 Guidance on satisfaction of a present obligation
 - (d) SMC 4 Guidance on the allocation of the transaction price to present obligations
 - (e) SMC 5 Subsequent measurement of receivables
 - (f) SMC 6 Disclosure requirements
 - (g) SMC 7 General – approach and principles in ED
2. The purpose of this agenda item is to seek feedback on SMC 1, with the aim of identifying the key points for the NZASB's comment letter on ED 71. The memo includes a summary of the NZASB's comments on the IPSASB's 2017 Consultation Paper,² including why the NZASB did not think that consumption-based and time-based restrictions gave rise to liabilities, and the other options that the NZASB put forward for dealing with such transactions.
3. At the end of the session we will look at the project plan and confirm which of the remaining SMCs in ED 71 the Board wishes to comment on. Because SMCs 3 and 4 flow on from SMC 1 we anticipate also responding to those SMCs.

Recommendations

4. We recommend that the Board:
 - (a) PROVIDES FEEDBACK on the proposals in ED 71 SMC 1; and
 - (b) AGREES to comment on all the SMCs in ED 71.

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

² Consultation Paper *Accounting for Revenue and Non-Exchange Expenses*

Background

5. The proposals in ED 71 aim to address some of the issues encountered in applying IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*, including the difficulty of making the distinctions between exchange and non-exchange transactions, and between conditions and restrictions (with this distinction dependent on whether there is a return obligation), and the lack of guidance on multi-year funding arrangements. When ED 71 is finalised, the new IPSAS will supersede IPSAS 23.
6. Currently IPSASB's revenue standards are based on an exchange/non-exchange distinction. In contrast, ED 70 *Revenue with Performance Obligations* and ED 71 are based on a performance obligation/no performance obligation distinction.
7. The Board has already received presentations and had some preliminary discussions about the proposals in the ED (as noted in agenda item 3.1).

Structure of this memo

8. The remaining sections in this memo are as follows.
 - (a) IPSAS 23 requirements
 - (b) ED 71 proposals
 - (c) IPSASB's rationale for revenue deferral
 - (d) NZASB views on IPSASB 2017 CP
 - (e) Illustrative examples
 - (f) Australian Accounting Standards
 - (g) GASB project
 - (h) Seeking views on SMC 1
 - (i) Next steps
 - (j) Appendix A: Extracts from AASB 1058 Basis for Conclusions
 - (k) Appendix B: Extracts from GASB project page: Revenue and Expense Recognition
 - (l) Appendix C: Extracts from IPSASB Conceptual Framework Basis for Conclusions

IPSAS 23 requirements

9. IPSAS 23 makes a distinction between two types of stipulations: restrictions and conditions. Restrictions limit or direct the purpose for which a transferred asset may be used. Conditions specify how the resources are to be used by the recipient *and* they require that if the resources are not used in that way then they must be returned to the transferor. Conditions are commonly referred to as use or return requirements. IPSAS 23 states that conditions can give rise to a liability in relation to resources received in a revenue transaction, but restrictions cannot (see Table 1 below for extracts from the Basis for Conclusions on IPSAS 23). IPSAS 23 was issued a number of years before the IPSASB issued its Conceptual Framework and relied on the definition of a liability in IPSAS 1. IPSAS 23 was not amended as a result of the Conceptual Framework.

10. In the case of transactions without use or return conditions, the requirements in IPSAS 23 can lead to large amounts of revenue being recognised at the beginning of a transaction, at the point that the recipient obtains control of the resources. Some feel that the requirements in IPSAS 23 are too restrictive and think that deferral of revenue should be permitted for a wider range of transactions with enforceable obligations.
11. The proposals in ED 70 and ED 71 would address some of the concerns about IPSAS 23.
 - (a) Some transactions (those with performance obligations to provide goods or services to third-party beneficiaries) that currently fall within the scope of IPSAS 23 would fall within the scope of ED 70 (which is based on IFRS 15 *Revenue from Contracts with Customers*) rather than ED 71.
 - (b) ED 71 would require the recognition of liabilities for some transactions with consumption-based stipulations. ED 71 does not actually use the term consumption-based stipulations. It refers to obligations to perform specified activities and obligations to incur eligible expenditure.
12. Table 1 summarises the requirements in IPSAS 23.

Table 1 IPSAS 23

Does transaction fall within the scope of IPSAS 23?
<p>The scope of IPSAS 23 is revenue from non-exchange transactions.</p> <p>IPSAS 23 contains requirements for accounting for taxes and transfers. It distinguishes between transfers with conditions and transfers with restrictions. Both conditions and restrictions are referred to as stipulations.</p> <p><u>Non-exchange transactions</u> are transactions that are not exchange transactions. In a non-exchange transaction an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange. (Defined term, IPSAS 9)</p>
Is there an asset?
<p>Similar to ED 71.</p> <p>An entity recognises an asset in respect of transfers when the transferred resources meet the definition of an asset and satisfy the criteria for recognition. (IPSAS 23 para 76)</p> <p>An entity may, but is not required to, recognise services in-kind. (IPSAS 23 para 98)</p>
If there is an asset, what then?
<p>IPSAS 23's requirements for revenue recognition can be grouped as follows:</p> <ul style="list-style-type: none"> • conditions on transferred assets (commonly referred to as 'use or return' requirements). • restrictions on transferred assets • taxes. <p>Conditions require that the entity either consume the resources received as specified or, in the event that the conditions are breached, return the resources to the resource provider.</p>
Is there a present obligation?
<p>In order for there to be a present obligation associated with the revenue inflow (and for an entity to defer revenue) there must be:</p> <ul style="list-style-type: none"> • A present obligation that meets the definition of a liability

Liabilities are *present obligations* of the entity arising from *past events*, the settlement of which is expected to result in *an outflow* from the entity of resources embodying economic benefits or service potential. (Defined term, IPSAS 1)

A liability is a present obligation of the entity for an outflow of resources that results from a past event. (CF)

- A present obligation that meets the liability recognition criteria
 - probable; and
 - can be reliably estimated. (IPSAS 23 para 50)

Conditions give rise to present obligations and the deferral of revenue. Restrictions do not.

Revenue recognition in IPSAS 23		
Conditions (use or return)	Restrictions	Taxes
Recognise revenue except to the extent that a liability is also recognised (IPSAS 23 para 44). Recognise revenue as the entity satisfies the present obligation(s). (IPSAS 23 para 45) Conditions on a transferred asset give rise to present obligations (IPSAS 23 para 55)	Recognise revenue immediately. Only conditions can give rise to present obligations.	Recognise an asset (and revenue) when the taxable event occurs and the asset recognition criteria are met. (IPSAS 23 para 59) This memo does not address advance taxes.

IPSAS 23 and capital grants

IPSAS 23 does not specifically discuss capital grants. The treatment of capital grants depends on whether the grant has conditions or restrictions. The same goes for transactions with other consumption-based or time-based stipulations. One of the illustrative examples in IPSAS 23 relates to capital grants (paragraphs IG24–IG25).

IPSAS 23 BC extracts

Stipulations—Conditions

BC11. This Standard requires that where the transfer of an asset imposes a condition on the recipient, the recipient should recognize a liability in respect of the transfer on initial recognition of the asset. This is because the recipient is unable to avoid an outflow of resources, as it is required to consume the future economic benefits or service potential embodied in the transferred asset in the delivery of particular goods or services to third parties as specified, or else to return to the transferor future economic benefits or service potential. Depending on the nature of the condition, it may be fulfilled progressively, permitting the entity to reduce the amount of the liability and recognize revenue progressively, or it may only be fulfilled on the occurrence of a particular future event, in which case the entity eliminates the liability and recognizes revenue when that event occurs.

BC12. Some are of the view that a liability should be recognized only when it is probable that conditions attaching to the inflow of resources will not be satisfied, and that future economic benefits or service potential will be required to be returned to the transferor. The IPSASB rejected this proposal, because it could result in entities recognizing revenue prematurely, because the entity would recognize the full fair value of the asset as revenue when it initially gains control of the asset, notwithstanding the outflow of resources necessary to satisfy the condition. The financial statements would not, therefore, recognize the present obligation to fulfill the condition imposed by the transfer or return future economic benefits or service potential to the transferor.

Stipulations—Restrictions

BC13. This Standard does not permit entities to recognize a liability in respect of a restriction when the transferred asset is initially recognized. This is because, as defined in this Standard, restrictions do not of themselves impose a present obligation upon the recipient entity to sacrifice future economic benefits or service potential to satisfy the restriction. A breach of a restriction may ultimately lead to

a penalty, such as a fine, being imposed upon the recipient entity; however, such a penalty is the result of enforcement procedures resulting from the breach, not from the initial recognition of the asset.

ED 71 proposals

13. This section summarises the proposed requirements in ED 71, including the circumstances in which ED 71 proposes the deferral of revenue (see Table 2). The blue shading in Table 2 indicates the focus of this memo.
14. ED 71 contains proposals for accounting for revenue from:
 - (a) transfers with present obligations. Even if a transaction does not give rise to *performance obligations* (as defined in ED 70), ED 71 allows for the possibility that obligations to perform a specified activity or spend money in a certain way could give rise to *present obligations*. An entity would recognise revenue as it satisfies the present obligations in the binding arrangement;
 - (b) transfers without present obligations. An entity would recognise revenue when it obtains control of the resources; and
 - (c) taxes. The proposals carry forward many of the current requirements in IPSAS 23.

Table 2 ED 71 proposals

Does transaction fall within the scope of ED 71?
<p>Scope requirements</p> <ul style="list-style-type: none"> • Inflow arises from a revenue transaction without performance obligations • Not within scope of another standard <p>Examples of transactions that fall within scope:</p> <ul style="list-style-type: none"> • Transfers (whether cash or non-cash), including debt forgiveness, fines, bequests, gifts, donations, goods or services in-kind, and the off-market portion of concessionary loans received. Capital transfers are one form of transfer. • Taxes. <p>Scope</p> <ul style="list-style-type: none"> • Narrower than the scope of IPSAS 23. Some transactions that were previously classified as non-exchange will now be classified as having performance obligations.
Is there an asset? (see paras 32 to 34)
<p>In order for there to be an asset there must be a revenue inflow that:</p> <ul style="list-style-type: none"> • meets the definition of an asset, including being controlled by the transfer recipient; and • meets the asset recognition criteria: <ul style="list-style-type: none"> ○ probable; and ○ can be reliably estimated. <p><u>Assets</u> are resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity. (Defined term, CF and IPSAS 1)</p> <p>Paragraphs 32–44 of ED 71 are mostly about recognition of the asset. However, these paragraphs also cover the possibility that an entity might recognise a liability if it receives an inflow of resources associated with an uncertain arrangement that does not meet the asset recognition criteria.</p>

<p>If there is an asset, what then?</p>
<p>The ED’s requirements for revenue recognition are set out in three sections:</p> <ul style="list-style-type: none"> • transfers with present obligations; • transfers without present obligations; and • taxes. <p>The ED also discusses specific types of transfers, being:</p> <ul style="list-style-type: none"> • capital transfers; • services in-kind; • pledges; and • advance receipts of transfers; and concessionary loans.
<p>Is there a present obligation? (see paras 45 to 52)</p>
<p>In order for there to be a present obligation associated with the revenue inflow (and for an entity to defer revenue) there must be:</p> <ul style="list-style-type: none"> • A binding arrangement. A <u>binding arrangement</u> is an arrangement that confers both enforceable rights and obligations on both parties to the arrangement. A contract is a type of binding arrangement (paragraphs AG7–AG12 provide additional guidance). (Defined term, ED 70) • A present obligation that meets the definition of a liability. The transfer recipient considers whether an obligation to perform a specified activity or incur an eligible expenditure is a present obligation. <ul style="list-style-type: none"> ○ <u>Liabilities</u> are <i>present obligations</i> of the entity arising from <i>past events</i>, the settlement of which is expected to result in <i>an outflow</i> from the entity of resources embodying economic benefits or service potential. (Defined term, IPSAS 1) ○ A present obligation is a binding obligation (legally or by equivalent means), which an entity has little or no realistic alternative to avoid and which results in an outflow of resources (ED 71, para 14) ○ A present obligation is a duty to act or perform in a particular way and may give rise to a liability in respect of any transaction without a performance obligation. Present obligations may be imposed by requirements in binding arrangements establishing the basis of transfers. They may also arise from the normal operating environment, such as the recognition of advance receipts. (ED 71, para 47) ○ A <u>specified activity</u> is an action in a binding arrangement that must be completed by a transfer recipient. (Defined term, ED 71, discussed paras 18 and 19) The ED gives examples of constructing an asset or conducting research. ○ <u>Eligible expenditure</u> is an outflow of resources incurred in accordance with the requirements set out in a binding arrangement. (Defined term ED 71, discussed paras 20 and 21) • There is a past event: <ul style="list-style-type: none"> ○ [in the context of transfers giving rise to present obligations] the past event that gives rise to an unavoidable obligation is the agreement to the terms of the binding arrangement by both parties. (ED 71, para 51) • There is an outflow of resources: <ul style="list-style-type: none"> ○ [in the context of <i>specified activities</i> ED 71 says] The transfer recipient is unable to avoid the outflow of resources as it is required to use the transfer in the delivery of the specified activity or return resources to the transfer provider or incur another form of redress. (ED 71, para 19) ○ [in the context of <i>eligible expenditure</i> ED 71 says] The transfer recipient is unable to avoid the outflow of resources as it is required to use the transfer on eligible expenditure or return resources to the transfer provider or incur another form of penalty. (ED 71, para 21) ○ [more generally in discussing present obligations ED 71, paraphrased, says] This obligation [to use transfers in a particular way or to act or perform in a certain way] results in an outflow of resources because the transfer recipient cannot avoid using those resources either to fulfil the

<p>requirements in the binding arrangement or in the event of a breach of a binding arrangement, by incurring some other form of redress to the transfer provider. (ED 71, para 52)</p> <ul style="list-style-type: none"> • A present obligation that meets the liability recognition criteria. That is: <ul style="list-style-type: none"> ○ probable; and ○ can be reliably estimated. (ED 71, para 46) 		
Revenue recognition		
Transfers with present obligations	Transfers without present obligations	Taxes
<p><i>There must be a binding arrangement</i></p> <p>Recognise revenue except to the extent that a liability is also recognised (para 53).</p> <p>Recognise revenue when (or as) the transfer recipient satisfies the present obligation (para 54).</p> <p>Recognise revenue when (or as) the transfer recipient undertakes the specified activities and has no further enforceable duties or acts to perform. Revenue recognition may be at a point in time or over time (ED 71 paras 57 and 58)</p>	<p><i>There may or may not be a binding arrangement</i></p> <p>Recognise revenue immediately (para 86).</p>	<p><i>No binding arrangement</i></p> <p>Recognise revenue when the taxable event or other event occurs, and the asset recognition criteria are met (para 89).</p> <p>This paper does not address advance taxes.</p>
ED 71 and capital grants		
<p>The treatment of capital transfers (also referred to as capital grants) depends on whether or not the transaction creates present obligations. Capital transfers are treated the same way as other transfers. If there are present obligations the entity recognises revenue as it satisfies the obligations (e.g. over the period of construction). A transaction might have more than one present obligation, such as an obligation to construct an asset and an obligation to use it in a certain way for a period of time. In that case the entity would need to allocate the consideration to the obligations and account for each obligation as appropriate. See ED 71 paragraphs BC19 and BC23.</p>		

IPSASB’s rationale for revenue deferral

15. The IPSASB’s rationale for the revenue deferral requirements in ED 71 is partially explained in Table 2 above. ED 71 outlines what an entity must consider in deciding if it has a present obligation that meets the definition of a liability. ED 71 states that transactions with requirements to carry out *specified activities* or requirements to spend resources on *eligible expenditure* may give rise to present obligations that meet the definition of a liability.
16. In this section we outline the IPSASB’s deliberations on ED 71, which culminated in the publication of ED 71 and the Basis for Conclusions on ED 71. We also consider whether the IPSASB thought about using the concept of other obligations to deal with certain revenue transactions.³ We have focused on the arguments about there being an *outflow of resources* as this may be an aspect where the NZASB disagrees with the IPSASB’s conclusions.

³ The short answer to this question is that because the IPSASB came to the conclusion that some transactions in ED 71 give rise to a liability, there was no need to consider using the concept of other obligations.

17. Extracts from the Basis for Conclusion on ED 71 follow (emphasis added).

Extracts from ED 71 Basis for Conclusions

Enforceable transactions

BC12. The IPSASB considered whether it is possible to have an enforceable transaction with a present obligation that was not a performance obligation, as defined in [draft] IPSAS [X] (ED 70). *The IPSASB concluded that a present obligation that is not a performance obligation can exist.* The present obligation gives rise to a liability because the past event occurs when the transfer provider and transfer recipient enter into a binding arrangement creating enforceable rights and obligations. *Further such an arrangement leads to an outflow of resources because the transfer recipient cannot avoid using those resources either to fulfill the requirements in the binding arrangement or in the event of a breach of a binding arrangement, repaying the resources to the transfer provider or incurring some other form of penalty.*

BC13. The IPSASB decided that the present obligations in enforceable transactions would either be a:

- (a) Specified activity; or
- (b) Requirement to incur eligible expenditure. The transfer recipient would recognize an asset and a liability when it had control of or right to the transfer and the revenue would be recognized (and the liability decreased) when (or as) the present obligation was satisfied.

BC14. The IPSASB noted that a specified activity or the requirement to incur eligible expenditure differs from a performance obligation in [draft] IPSAS [X] (ED 70) because there is no requirement for the transfer recipient to transfer a good or service to either the transfer provider or a third-party beneficiary.

18. Table 3 summarises IPSASB meetings over the period December 2018–December 2019. The comments in Table 3 are drawn from the IPSASB’s minutes and reports by the NZ IPSASB member, but they focus on the aspects of most relevance to this memo. The table is a few pages long but we think it is useful to outline how the IPSASB’s thinking developed.

Table 3: IPSASB’s deliberations leading up to ED 71

Dec 2018	<p>Agenda item 11 Grants and Transfers</p> <p>The IPSASB considered constituents’ comments on the 2017 CP in relation to accounting for transactions with time-based restrictions. The 2017 CP set out three options:</p> <ul style="list-style-type: none"> • Enhanced display/disclosure; • Classifying such transfers as an ‘other obligation’⁴ of the recipient; and • Recognising these transfers in net assets/equity and recycling through the statement of financial performance. <p>The IPSASB decided that enforceability was the key factor in determining the accounting treatment and therefore which standard would be applicable, such that:</p> <ul style="list-style-type: none"> • Enforceable transactions would be accounted for under an IFRS 15-based standard; • Non-enforceable transactions would be accounted for under an updated IPSAS 23:
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⁴ See the end of this section for a discussion of other obligations.

	<ul style="list-style-type: none"> • Transactions that are not enforceable but which have intentions/expectations are to be recognized when the revenue is receivable, the intentions/expectations communicated via enhanced display/disclosure; and • Not to use the term “time requirements”.
<p>March 2019</p>	<p>Agenda item 11 Revenue – IPSAS 23 Update</p> <p>The IPSASB considered which aspects of IPSAS 23 should be retained, amended or deleted. The IPSASB decided that the terms ‘exchange’ and ‘non-exchange’ do not correspond to transactions with performance obligations/no performance obligations. In developing the updated IPSAS 23, staff should consider the appropriate approach/terminology to use in each particular case.</p> <p>Amongst other matters the IPSASB directed staff to:</p> <ul style="list-style-type: none"> • Develop presentational options for transactions not meeting Steps 1 and/or 2 in <i>Revenue from Performance Obligations</i> • Provide examples of transactions that contain binding arrangements but do not have performance obligations as per draft ED 70 and develop possible accounting treatments for such transactions • Prepare a [draft] ED including requirements for <ul style="list-style-type: none"> ○ Capital and Research Grants ○ Enforceable transactions with obligations ○ Taxes ○ Appropriations
<p>June 2019</p>	<p>Agenda item 11 Revenue without Performance Obligations</p> <p>The IPSASB considered an issues paper on revenue recognition. The issues paper set out two approaches for revenue recognition – immediate recognition and a deferral approach. Within the deferral approach there were four options for the timing of revenue recognition.</p> <p>The IPSASB decided that transactions that are not enforceable because there is no binding arrangement will result in revenue being recognized when receivable. This confirmed the tentative decision made in December 2018.</p> <p>The IPSASB instructed staff to:</p> <ul style="list-style-type: none"> • Develop a paper (i) examining the differences and interaction between a present obligation and a performance obligation; (ii) considering the accounting consequences of a breach of ‘terms’; and (iii) presenting different presentation models; • Draft text for enforceable transactions with terms on the basis that revenue is recognised when receivable unless there is a liability at the inception of the arrangement. If a liability arises later, this is a separate event; and • Update an issues paper on capital grants to consider the implications of the present obligation/performance obligation paper.
<p>Sept 2019</p>	<p>Agenda item 8 Revenue without Performance Obligations</p> <p>Staff presented issues papers on (i) the impact of past event on revenue recognition; (ii) outflow of resources; (iii) grants subject to annual appropriations; (iv) capital grants; and (v) initial and subsequent recognition of non-contractual receivables. Staff also presented a draft ED based on IPSAS 23. We have summarised the IPSASB’s overall decisions for agenda item 8, and then look at a couple of the papers in more detail.</p> <p>Overall, the IPSASB decided that:</p>

	<ul style="list-style-type: none"> • The past event for a revenue transaction that arises from a binding arrangement is when the parties enter into that arrangement; • Using resources provided via a binding arrangement to complete enforceable activities, incur eligible expenditure or make repayments in the event of a breach of the arrangement are all considered to be outflows of resources; • For binding arrangements, revenue is recognised as enforceable obligations are satisfied (i.e. specified activities are completed or eligible expenditure is incurred); • Appropriations are one possible indicator of control of an asset but the assessment of control may be jurisdictionally specific; and • Capital transfers are to be accounted for in the same manner as other transfers, and revenue recognition will be dependent on whether the whether the transaction arises from a binding arrangement and the nature of any enforceable obligations. <p>Agenda item 8.2.3 Outflow of resources</p> <p>The IPSASB deliberated on what constitutes an outflow of resources. The IPSASB was asked if it supported the staff view that using resources provided via a binding arrangement to complete ‘enforceable activities’, incur ‘eligible expenditure’, or to reimburse a transfer provider or pay a penalty as a result of a breach of the binding arrangement constitutes an ‘outflow of resources’ in relation to a present obligation.</p> <p>The IPSASB noted what the Conceptual Framework says about outflow of resources (see below), and the fact that there is no other guidance in the Conceptual Framework on this matter.</p> <p><i>IPSASB Conceptual Framework – Paragraphs 5.15 and 5.16</i></p> <p>5.15 Public sector 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.</p> <p>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.</p> <p>Staff outlined a narrow approach to outflow of resources (recognise an outflow only once the return of resources to the transferor becomes likely) and a broader approach (as subsequently reflected in ED 71).</p> <p>The Basis for Conclusions (paragraphs BC12 to BC14, shown earlier in this section) sums up what the IPSASB decided.</p> <p>Agenda Item 8.2.5 Capital Grants</p> <p>The IPSASB noted the treatment of capital grants under various standards.</p> <ul style="list-style-type: none"> • IAS 20 <i>Accounting for Government Grants and Disclosure of Government Assistance</i> – Paragraph 12 of IAS 20 requires government grants to be recognised in profit or loss on a systematic basis over the period in which the entity recognises as expenses the related costs for which the grants are intended to compensate. The grant is recognised as the asset is depreciated. Grants related to assets may be presented as deferred income or deducted from the carrying amount of the asset. • FRS 102, <i>The Financial Reporting Standard applicable in the UK and Republic of Ireland</i> – FRS 102 is based on IFRS for SMEs. It allows the use
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	<p>of a performance model or an accrual model. The performance model requires the grant to be recognized as income as the performance-related conditions are met. If there are no performance-related conditions then the grant is recognised when the entity has control of the resources. The accrual model requires income to be recognised on a systematic basis over the expected life of the asset; and</p> <ul style="list-style-type: none"> • AASB 1058 <i>Income of Not-for-Profit Entities</i>⁵ – AASB 1058 contains requirements about the transfer of a financial asset to enable an entity to acquire or construct a recognisable non-financial asset to be controlled by the recipient entity. AASB 1058 requires an entity to recognise an upfront liability (for the obligation to acquire or construct the asset as well as any other performance obligations) and recognise income in profit or loss when (or as) the entity satisfies the obligations under the transfer. This approach is analogous to the AASB 15 performance obligation approach. <p>Staff expressed the view that the appropriate treatment of capital grants would depend on whether the IPSASB decided that using funds to fulfil a present obligation gives rise to an outflow of resources.</p> <ul style="list-style-type: none"> • If yes, then staff proposed recognising revenue as the recipient completes enforceable activities or incurs eligible expenditure (e.g. over the period of construction). • If no, then staff proposed that transfer recipients should account for the capital grant <i>as if it were</i> a performance obligation. Staff considered that requiring revenue recognition at the point the entity controls the funds would not present representationally faithful or relevant information. <p>The IPSASB agreed that capital grants should be treated the same way as other revenue transactions with present obligations (i.e. revenue is initially deferred and then recognised as enforceable activities are completed or eligible expenditure is incurred).</p>
<p>Dec 2019</p>	<p>Agenda item 8 Revenue without Performance Obligations</p> <p>This meeting involved looking at cross cutting issues such as disclosure requirements and the consistency of requirements across the EDs. There were a number of issues papers, including one on onerous arrangements.</p> <p><i>8.2.7 Onerous binding arrangements</i></p> <p>A Board member had queried whether ED 70 and ED 71 addressed onerous binding arrangements. The staff paper noted that IFRS 15 does not include an onerous test; entities apply the onerous contracts test in IAS 37 <i>Provisions, Contingent Assets and Contingent Liabilities</i>. ED 70 and ED 72 scope out transactions within the scope of IPSAS 19 <i>Provisions, Contingent Assets and Contingent Liabilities</i>. IPSASB staff expressed the view that IPSAS 19, along with the scope exclusions in ED 70 and ED 71, would lead to the application of IPSAS 19 to revenue binding arrangements that become onerous.</p>

⁵ We discuss AASB 1058 in more detail later in this memo. Extracts from the AASB’s Basis for Conclusions on AASB 1058 are set out in Appendix A to this memo.

Other obligations

19. Table 3 above notes that the 2017 CP sought views on whether transactions with time-based restrictions should be treated as 'other obligations'. This section looks at what the IPSASB Conceptual Framework says about other obligations and why it mentions them.
20. Although the IPSASB Conceptual Framework does not define 'other resources' or 'other obligations' as elements, it states that in order to achieve the objectives of financial reporting, the IPSASB may determine that a resource or obligation that does not satisfy the definition of an element should be recognised in the financial statements. The IPSASB was concerned that in some circumstances the defined elements (being assets, liabilities, revenue expense, ownership contributions and ownership distributions) may not provide all the information necessary to allow a meaningful assessment of the financial position and financial performance of an entity.
21. In developing the Conceptual Framework the IPSASB's discussions focused on deferred inflows and deferred outflows, where the inflows/outflows relate to a specified future period. The IPSASB said that any requirements to recognise other resources and other obligations would be determined at standards level. The IPSASB's Basis for Conclusions on Chapter 5 of its Conceptual Framework outlines the IPSASB's deliberations on other resources and other obligations. See Appendix C to this memo for relevant extracts from the IPSASB's Conceptual Framework.
22. The discussion of other resources and other obligations is sometimes linked with the IASB's concept of other comprehensive income, as both concepts attempt to deal with the most appropriate way of reporting transactions that span a number of reporting periods. However, in developing the Conceptual Framework the IPSASB rejected the notion of OCI.
23. In developing the PBE Conceptual Framework (which is based on the IPSASB Conceptual Framework) the NZASB kept the reference to other resources and other obligations, but included a statement in the Basis for Conclusions that it would carefully consider any standards-level requirements to recognise an item that did not meet the definition of an element.⁶
24. Asa noted in Table 3 above, in December 2018 the IPSASB considered constituents' comments on the 2017 CP, including whether transactions with time-based restrictions should be treated as an 'other obligation' of the recipient. The IPSASB decided that the accounting for such transactions should hinge on whether the transaction was enforceable.
25. The Basis for Conclusions on ED 71 discusses why the IPSASB concluded certain revenue transactions give rise to a liability. It does not discuss other resources and other obligations because the IPSASB did not consider using these concepts.

⁶ PBE Conceptual Framework, paragraph BC16.

NZASB views on the 2017 CP

26. The purpose of this memo is to seek the NZASB's views on the deferred revenue proposals in ED 71 and the key points that the NZASB wants to make in responding to SMC 1 in ED 71. The NZASB's comments on the IPSASB's 2017 CP are a good starting point.
27. Although the IPSASB has since gone on to develop ED 71 and has firmed up its views in the process, the NZASB's views on the 2017 CP are still relevant. The 2017 CP sought constituents' views about if and when revenue transactions could give rise to liabilities. An extract from the NZASB's submission on the 2017 CP is set out below. We have highlighted the NZASB's view that unfulfilled obligations relating to time-based stipulations and consumption-based stipulations do not give rise to liabilities as defined in the Conceptual Framework.

Extract from NZASB's comment letter on the IPSASB's 2017 CP

In order to develop our responses to the CP and provide our views on the treatment of various types of revenue transactions, we have developed a proposed framework for the recognition of revenue transactions in the public sector. This proposed framework distinguishes between revenue transactions with and without performance obligations,¹ rather than using the exchange or non-exchange distinction.

- We agree that revenue transactions with performance obligations should be accounted for using the Public Sector Performance Obligation Approach (PSPOA) as proposed in the CP, which is based on IFRS 15 *Revenue from Contracts with Customers* adapted for the public sector.
- We agree that revenue transactions with no performance obligations or stipulations should be accounted for under a residual revenue standard (or a residual section of the standard, if there is only one revenue standard). This residual standard would be based on the applicable parts of IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*, updated to address issues relating to these types of transactions.
- We do not agree with the CP's proposal to apply the PSPOA to revenue transactions with no performance obligations but with stipulations over use (including consumption based² and time-based stipulations). In our view, such unfulfilled stipulations do not give rise to a liability as defined in the Conceptual Framework (i.e. they do not require an outflow of resources to an external party) – the only "obligation" is for the entity to use the funds to acquire resources for itself, rather than to transfer goods or services to other parties. In other words, although the stipulations might be regarded as "obligations" in a broader sense, they are not the type of obligation referred to in the definition of a liability.³ Instead the revenue from these transactions should be recognised when the resource recipient has control of the resources transferred.

We have suggested two options for presenting information about revenue arising from these transactions which could highlight the existence of stipulations over the use of resources received and the timing of fulfilment of those stipulations. These options could help to resolve the problem of explaining the resource recipient's performance story, while also faithfully representing the resource recipient's financial position.

We consider that this approach is consistent with the definitions of elements in the Conceptual Framework.

- 1 For the purpose of our proposed recognition framework, the NZASB considers that a revenue or expense transaction with performance obligations is one that involves an enforceable agreement between the resource provider and the resource recipient requiring the resource recipient to deliver goods or services either to the resource provider or to beneficiaries.
- 2 Consumption-based stipulations arise when the resource provider agrees to transfer resources to the resource recipient with the stipulation that the resource recipient must use the resources

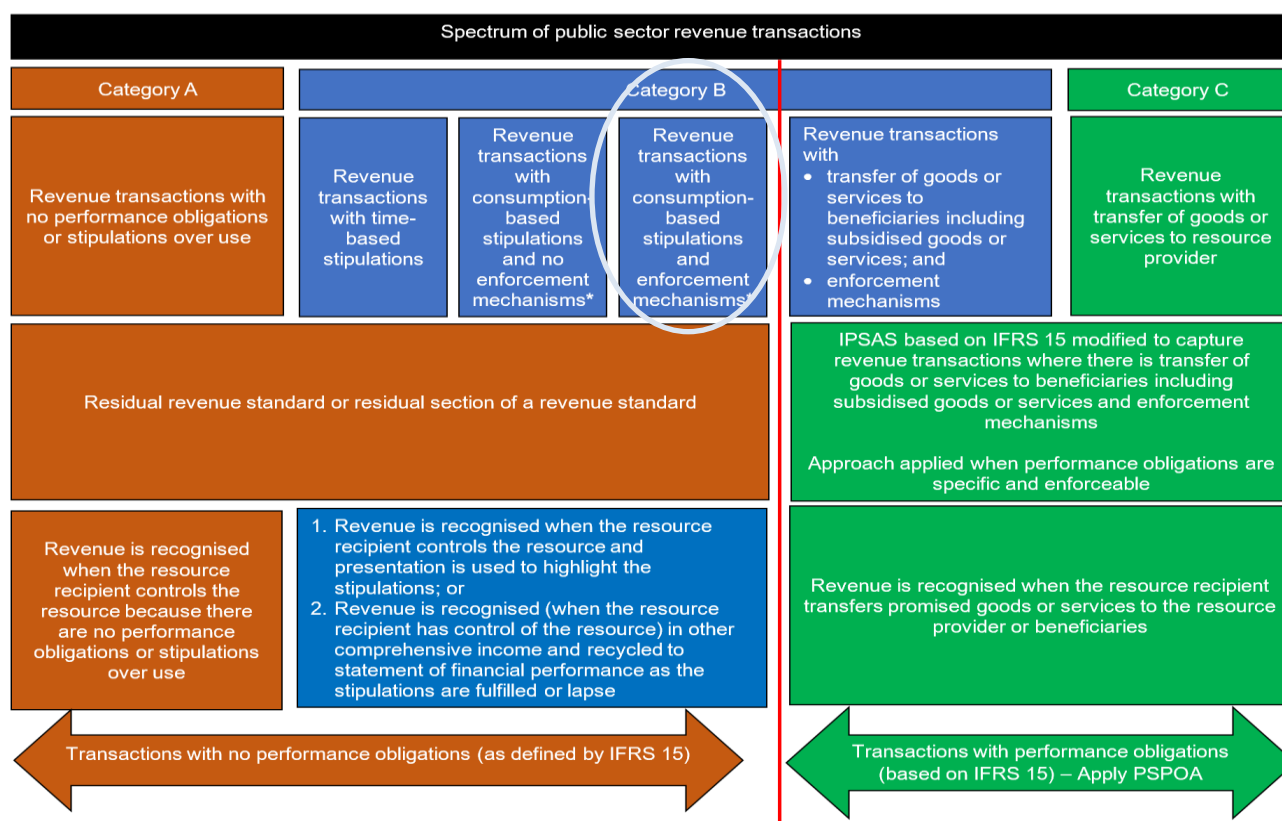
as specified for its own operations, without imposing on the resource recipient an obligation for an outflow of resources to another party.

- 3 The *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (Conceptual Framework), paragraph 5.14, defines a liability as “a present obligation of the entity for an outflow of resources that results from a past event”.

- 28. In relation to the presentation options identified by the NZASB (enhanced disclosure and OCI) the NZASB noted:
 - (a) the need for guidance on determining when stipulations had been satisfied. Stipulations would need to be sufficiently clear to enable the resource recipient to determine when the stipulation has been fulfilled or has lapsed.;
 - (b) the OCI option would be appropriate only for transactions where there are resources with clear stipulations imposed by the resource provider – it would not be appropriate for self-imposed stipulations on the use of funds.

29. The NZASB’s proposed framework in its January 2018 comment letter is shown below.

Diagram 1: NZASB’s proposed framework for revenue recognition



* These categories include capital grants

- 30. The main differences between the NZASB’s proposals in Diagram 1 and the IPSASB’s proposals in ED 71 are in relation to the circled transactions. The next section of this memo looks at some illustrative examples in ED 71 which deal with these types of transactions.

Illustrative examples

31. Table 4 outlines illustrative examples in ED 71 where the IPSASB is proposing that there is a present obligation and deferred revenue. The NZASB’s proposed revenue framework would not have led to deferral of revenue in these examples.

Table 4 ED 71 illustrative examples leading to deferred revenue

<i>Revenue transactions with consumption-based stipulations and enforcement mechanisms</i>	
<p>Example 11 Consumption-based stipulation (capital grant)</p>	<p>Cash transfer to a government housing entity to increase housing stock. The housing entity keeps the completed units. Use or return unspent amount. 5-year period. The example says the binding arrangement meets the requirements for a present obligation (so it must be enforceable). Binding arrangement → present obligation → liability for deferred revenue Recognise revenue (and decrease the liability) as the housing entity satisfies the present obligation (by increasing the housing stock).</p>
<p>Example 13 Consumption-based stipulation (partially capital grant)</p>	<p>Transfer to a provincial government to improve and maintain mass transit systems. There are three separate present obligations in the example.</p> <ul style="list-style-type: none"> • spend CU4 on modernizing the existing railroad and tramway system • spend CU4 for new railroad or tramway systems. • spend CU2 on new rolling stock. <p>Use or return (the example doesn’t say whether this applies to the unspent portion or the whole amount). One-year period. Binding arrangement → present obligation → liability for deferred revenue Recognise revenue (and decrease the liability) as the entity satisfies the present obligations.</p>
<p>Example 19 Consumption-based stipulation</p>	<p>Development assistance (for specified items or expenses). Binding arrangement. Use or return unused portion. 2-year agreement. Binding arrangement → present obligation → liability for deferred revenue Recognise revenue (and decrease the liability) as the recipient government satisfies the present obligation (by spending the money as specified).</p>
<p>Example 20 Consumption-based stipulation</p>	<p>Operational funding (for specified expenses). Binding arrangement. Use or return unused portion for that budget year. The example also illustrates advance receipts and overdue amounts. Binding arrangement → present obligation → liability for deferred revenue Recognise liabilities at various stages:</p> <ul style="list-style-type: none"> • advance receipts – liability on receipt • receipts received on time – liability on receipt. <p>Recognise revenue (and decrease the liability) as the recipient government satisfies the present obligation (by spending the money as specified). Recognise doubtful debt for the amount unlikely to be received.</p>
<p>Example 29 Consumption-based stipulation (capital grant)</p>	<p>Transfer to build a community centre (for general community use). The recipient gets to keep the asset. Use or return unused portion. Regular reporting required.</p>

<i>Revenue transactions with consumption-based stipulations and enforcement mechanisms</i>	
	<p>Binding arrangement → present obligation → liability for deferred revenue</p> <p>The example also illustrates the allocation of an allowance for overheads.</p> <p>Recognise revenue (and decrease the liability) as the recipient government satisfies the present obligation (by spending the money as specified <i>over the period of construction</i>).</p>
<p>Example 30</p> <p>Consumption-based stipulation (capital grant)</p> <p>PLUS</p> <p><i>restrictions on use (possible performance obligation?)</i></p>	<p>This is a variation of Example 29. It now has two components (i) construction of a community centre and (ii) a requirement to use the building as a child-care centre for first 10 years. The recipient keeps the asset.</p> <p>Use or return unused portion. There is a penalty over the first ten years if the centre is not used as a child-care centre. Regular reporting on construction and the use of the centre is required.</p> <p>The example illustrates the allocation of an allowance for overheads and splitting the binding arrangement into components.</p> <p><u>Construction of centre (as per Example 29)</u></p> <p>CU22million.</p> <p>Binding arrangement → present obligation → liability for deferred revenue</p> <p>Recognise revenue (and decrease the liability) as the recipient government satisfies the present obligation (by spending the money as specified).</p> <p><u>Use as a child-care centre for 10 years</u></p> <p>CU3million.</p> <p>No performance obligation. (The binding arrangement specifies certain high level criteria that must be met for the building to qualify as a child-care centre. However it does not specifically require the provision of child-care services to the National Government or third-party beneficiaries.)</p> <p>Although there is an overall binding arrangement, have to assess whether the restrictions over the first ten years' use are enforceable.</p> <ul style="list-style-type: none"> • If enforceable → present obligation → liability for deferred revenue Recognise revenue over ten years. • If not enforceable → NO present obligation Recognise revenue on completion of the centre.
<i>Revenue transactions with time-based stipulations and enforcement mechanisms</i>	
	<p>We have not identified any ED 71 examples that are solely time based.</p>

32. Table 5 identifies two examples with consumption-based stipulations where there would be immediate revenue recognition. These examples are consistent with the NZASB’s proposed revenue framework.

Table 5 ED 71 illustrative examples with immediate revenue recognition

<i>Revenue transactions with consumption-based stipulations and <u>no</u> enforcement mechanisms (or not enforced)</i>	
<p>Example 12</p> <p>Donated asset with consumption-based stipulation</p>	<p>Transfer of land to a university for the establishment of a university campus.</p> <p>No use or return requirement. No other enforcement mechanism.</p> <p>The obligation to establish the university campus is not enforceable.</p> <p>→ No liability</p> <p>Recognise an asset and revenue when the university gains control of the land.</p>

<p>Example 24 Consumption-based stipulation</p>	<p>Cash transfer to rehabilitate deforested area. Binding arrangement. Use or return requirement, but past breaches have not been enforced. Arrangement is enforceable but has not been enforced → No liability Recognise an asset and revenue (assume it is when the National Park gains control of the funds – the example doesn't give any details about when funds are due, versus received).</p>
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33. The NZASB has indicated that it would like some information about how other jurisdictions deal with consumption-based and time-based stipulations. The next two sections look at matters considered by the AASB and the GASB.

Australian Accounting Standards

34. This section gives an overview of Australian Accounting Standards dealing with revenue recognition. It summarises the requirements in relation to capital grants and research grants (with a focus on transactions within the scope of ED 71).
35. In December 2016 the AASB issued AASB 1058 *Income of Not-for-Profit Entities*. At the same time, the AASB added application guidance and illustrative examples for not-for-profit entities to AASB 15 *Revenue from Contracts with Customers*. AASB 1058 superseded the previous income recognition requirements for private sector NFPs, and most of the requirements for public sector NFPs in AASB 1004 *Contributions*.
36. AASB 1058 applies when an NFP entity receives volunteer services or enters into other transactions where the consideration to acquire an asset is significantly less than the fair value of the asset, principally to enable the entity to further its objectives. In the case of assets acquired, the entity recognises and measures the asset at fair value in accordance with the applicable standard. An entity also considers whether it needs to recognise any other 'related amounts' in accordance with the applicable Australian Accounting Standard. Such 'related amounts' include:
- (a) contributions by owners;
 - (b) revenue, or a contract liability arising from a contract with a customer (in accordance with AASB 15);
 - (c) a lease liability;
 - (d) a financial instrument; or
 - (e) a provision.
37. In the same way that the IPSASB is proposing to have two revenue standards, one based on IFRS 15, and the other being a residual revenue standard, the AASB has AASB 15 and AASB 1058. The AASB also issued some Australian-specific application guidance and illustrative examples in AASB 15.
- (a) Appendix F *Australian implementation guidance for not-for-profit entities*. This Appendix explains and illustrates the principles in the Standard from the perspective of not-for-

profit entities in the private and public sectors, particularly to address circumstances where a for-profit perspective does not readily translate to a not-for-profit perspective.

- (b) Appendix G *Australian implementation guidance for not-for-profit public sector licensors* contains explicit application guidance for intellectual property (IP) licences. It applies to public sector NFPs only.
 - (c) *Australian illustrative examples for not-for-profit entities* illustrate how a not-for-profit entity might apply some of the requirements of AASB 15.
38. In order for AASB 15 to apply to an NFP transaction, there are two critical elements that need to be satisfied: (i) the agreement between two or more parties must create ‘enforceable’ rights and obligations; and (ii) the NFP entity’s promise to transfer a good or service needs to be ‘sufficiently specific’. The determination of whether the performance obligation is ‘enforceable’ and ‘sufficiently specific’ is a matter of judgement, having regard to the particular facts and circumstances. AASB 15 Appendix F contains additional guidance to help NFPs make assessments about whether a performance obligation is ‘enforceable’ and ‘sufficiently specific’.
39. AASB 1058 is set up so that an entity looks at the transaction, identifies any liabilities that should be recognised in accordance with other standards (such as AASB 15), and then applies the requirements in AASB 1058 to the remaining amount. Generally, that remaining amount is recognised as income immediately in profit or loss.
40. The IPSASB also uses the concepts of enforceability and sufficiently specific to establish the scope of ED 70 (and ED 71 by default).

Grants for construction or acquisition of non-financial assets

41. AASB 1058 includes specific requirements with respect to grants for construction or acquisition of non-financial assets.
- (a) If the NFP receives a grant to construct a building which it will control, it recognises the cash and a liability (for the obligation to construct the building). The liability is derecognised as it constructs the building.
 - (b) If the NFP receives a grant to acquire specific assets, it recognises income when it acquires those assets.
 - (c) If the NFP receives a grant to develop an asset which does not satisfy the recognition criteria in other accounting standards (e.g. a research grant to develop the NFP’s intellectual property), income is recognised when it receives the grant.
42. The AASB’s Basis for Conclusions on such grants is set out in Appendix A of this memo.

Research grants

43. The illustrative examples that accompany AASB 15 and AASB 1058 consider whether various research transactions fall within the scope of these standards. Depending upon the circumstances a research grant could fall under AASB 15 or AASB 1058.

44. The AASB became aware of different interpretations of how AASB 15 paragraph 35(a) applies in the case of research grants. Paragraph 35(a) addresses whether the customer simultaneously receives and consumes the benefits provided by an entity's performance as the entity performs, as one basis for the entity transferring control of a good or service over time, and therefore satisfying a performance obligation and recognising revenue over time. The AASB recently amended a few of the examples in AASB 15 to clarify the application of paragraph 35(a) and added an example to illustrate other key contract features.⁷ The AASB did not amend AASB 1058, apart from deferring the application of AASB 1058 to research grants for a short period of time.

GASB project

45. The Governmental Accounting Standards Board (GASB) has an active project on Revenue and Expense Recognition. It issued an Invitation to Comment in January 2018 and plans to issue a Preliminary Views document later this year, with the aim of issuing a standard in 2023. The GASB has made a number of tentative decisions but has not yet developed an ED.
46. The GASB project categorises revenue transactions as Category A or Category B. The proposals for Category A transactions appear to be based on ASC Topic 606, *Revenue from Contracts with Customers*, which is very similar to IFRS 15 *Revenue from Contracts with Customers*. We have not attempted to summarise the proposals for Category B transactions. It is difficult to assess what the tentative decisions mean for various transactions without having a good understanding of the project as whole. We have found it difficult to assess what the GASB's tentative decisions mean for certain transactions (for example, both capital grants and in-kind contributions and contributed services appear to be outside the scope of the project). Appendix B of this memo lists the tentative decisions from the GASB project page.

Seeking views on ED 71 SMC 1

47. The key question for the NZASB is whether it agrees that transfer recipients can have present obligations (that meet the definition of a liability) for obligations to perform specified activities or incur eligible expenditure. This section brings together the key points in the memo and contrasts aspects of the IPSASB's Conceptual Framework with the IASB's Conceptual Framework.

48. In its response to the IPSASB's 2017 CP the NZASB said:

We do not agree with the CP's proposal to apply the PSPOA to revenue transactions with no performance obligations but with stipulations over use (including consumption based² and time-based stipulations). In our view, such unfulfilled stipulations do not give rise to a liability as defined in the Conceptual Framework (i.e. they do not require an outflow of resources to an external party) – the only "obligation" is for the entity to use the funds to acquire resources for itself, rather than to transfer goods or services to other parties. In other words, although the stipulations might be regarded as "obligations" in a broader sense, they are not the type of obligation referred to in the definition of a liability.³ Instead the revenue from these transactions should be recognised when the resource recipient has control of the resources transferred.

⁷ AASB 2019-6 *Amendments to Australian Accounting Standards – Research Grants and Not-for-Profit Entities* (December 2019)

49. The IPSASB’s proposals about the recognition of liabilities for deferred revenue in ED 71 are narrower than the proposals in the 2017 CP. The IPSASB is proposing to limit revenue deferral to (i) binding arrangements (which are by definition enforceable) and (ii) to consumption-based stipulations. ED 71 does NOT propose revenue deferral for time-based stipulations. This narrows the areas of disagreement but does not resolve the disagreement.
50. We think that for the purposes of commenting on ED 71 the Board should first form a view on the conceptual arguments. If the Board continues to disagree with the IPSASB’s proposals on conceptual grounds it can consider how to present those arguments, whether it would support the same proposals with a different rationale, or whether it would prefer the IPSASB to address user needs via presentation options.
51. The IPSASB’s rationale for the proposals in ED 71 were set out in an earlier section of this memo. The key argument is set out in paragraph BC12 from ED 71.

BC12. The IPSASB considered whether it is possible to have an enforceable transaction with a present obligation that was not a performance obligation, as defined in [draft] IPSAS [X] (ED 70). *The IPSASB concluded that a present obligation that is not a performance obligation can exist.* The present obligation gives rise to a liability because the past event occurs when the transfer provider and transfer recipient enter into a binding arrangement creating enforceable rights and obligations. *Further such an arrangement leads to an outflow of resources because the transfer recipient cannot avoid using those resources either to fulfill the requirements in the binding arrangement or in the event of a breach of a binding arrangement, repaying the resources to the transfer provider or incurring some other form of penalty.*

52. Because the definition of a liability and views about whether there is a present obligation go to the heart of this matter, in Table 6 we have contrasted the IPSASB’s and IASB’s definitions of a liability and other comments about the nature of the obligations giving rise to liabilities. The IPSASB completed its Conceptual Framework in 2014.⁸

Table 6 Liabilities and present obligations

IPSASB liabilities and present obligations	
<u>IPSAS 1 Presentation of Financial Statements</u>	
<u>Liabilities</u> are <i>present obligations</i> of the entity arising from <i>past events</i> , the settlement of which is expected to <i>result in an outflow</i> from the entity of resources embodying economic benefits or service potential.	
<u>IPSASB Conceptual Framework</u>	
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 sector 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.

⁸ The Table does not show complete extracts.

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.

ED 71

A present obligation is a binding obligation (legally or by equivalent means), which an entity has little or no realistic alternative to avoid and which results in an outflow of resources. (ED 71, para 14)

A present obligation is a duty to act or perform in a particular way and may give rise to a liability in respect of any transaction without a performance obligation. (ED 71, para 47)

IASB liabilities and present obligationsIASB Conceptual Framework

A **liability** is a *present obligation* of the entity to *transfer an economic resource* as a result of *past events*. (CF 4.26, emphasis added)

For a liability to exist, three criteria must all be satisfied:

- (a) the entity has an obligation;
- (b) the obligation is to transfer an economic resource; and
- (c) the obligation is a present obligation that exists as a result of past events. (CF 4.27)

An obligation is a duty or responsibility that an entity has no practical ability to avoid. An obligation is always owed to another party (or parties). The other party (or parties) could be a person or another entity, a group of people or other entities, or society at large. It is not necessary to know the identity of the party (or parties) to whom the obligation is owed. (CF 4.29)

If one party has an obligation to transfer an economic resource, it follows that another party (or parties) has a right to receive that economic resource. (CF 4.30)

The second criterion for a liability is that the obligation is to transfer an economic resource.

To satisfy this criterion, the obligation must have the potential to require the entity to transfer an economic resource to another party (or parties). (CF 4.36 and 4.37)

A present obligation exists as a result of past events only if:

- (a) the entity has already obtained economic benefits or taken an action; and
- (b) as a consequence, the entity will or may have to transfer an economic resource that it would not otherwise have had to transfer. (CF 4.33)

An entity does not yet have a present obligation to transfer an economic resource if it has not yet satisfied the criteria in paragraph 4.43, that is, if it has not yet obtained economic benefits, or taken an action, that would or could require the entity to transfer an economic resource that it would not otherwise have had to transfer. For example, if an entity has entered into a contract to pay an employee a salary in exchange for receiving the employee's services, the entity does not have a present obligation to pay the salary until it has received the employee's services. Before then the contract is executory—the entity has a combined right and obligation to exchange future salary for future employee services. (CF 4.47)

53. When the IASB was developing working on its most recent Conceptual Framework, it received feedback from some Australian and New Zealand constituents about present claims.

... some respondents from Australia and New Zealand (including two standard setters, a preparer of financial statements and an accountancy body), observed that liabilities must be *present claims against the entity's assets*, ie that there must be another party or parties (which could be the public at large) that is or are entitled to receive, or benefit from, the future transfer of economic resources, and that would suffer harm if the entity failed to meet its obligations

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54. In considering these comments about present claims we find it hard to see how obligations to perform specified activities or incur eligible expenditure could represent *present claims against an entity's assets*. We accept that it may not be appropriate to apply arguments made in relation to one conceptual framework to another conceptual framework. The two conceptual frameworks were developed at different points in time for different types of entities. Due to the two international boards completing their projects four years apart the IPSASB never had the opportunity to debate some of the issues raised with the IASB.⁹ Therefore we do not know the IPSASB's views about these arguments. We have, however, included this point in the memo, because the argument might resonate with some Board members.
55. We note that the IPSASB's definition of a liability refers to *outflows of resources*, rather than *transfers of economic resources* but we are not aware whether this difference in wording was intended to mean anything different from the IASB's wording.

Questions for the Board

Q1. Do you agree with the IPSASB's proposals that, for the purposes of ED 71 *Revenue without Performance Obligations*, a specified activity and eligible expenditure give rise to present obligations? Are there other examples of present obligations that would be useful to include in the [draft] Standard?

We would like to work through:

- (a) whether the Board agrees or disagrees with ED 71 on conceptual grounds;
- (b) if the Board disagrees with ED 71 on conceptual grounds, does it nevertheless support the proposed accounting outcomes from a user information needs or decision-making perspective; and
- (c) does the Board have a view on the possible use of 'other obligations' to bring about the deferral of revenue?

Q2. Is there any other work the Board would like us to do to help it form a view on ED 71 SMC 1?

Next steps

56. We will begin drafting the response to SMC 1. The plan for future Board meetings is set out in agenda item 3.1. The topics for future meetings will be influenced by which SMCs the Board wants to comment on. As a starting position we propose that the Board comment on all SMCs in ED 71 (shown below), although we are not sure what SMC 7 is trying to elicit.

Question for the Board

Q3. Does the Board agree to comment on all SMCs in ED 71?
(All the SMCs are shown below).

⁹ The IASB completed its most recent Conceptual Framework in 2018 and reflects debates that took place or continued after 2014.

Specific Matter for Comment 1: (Paragraphs 14–21)

The ED proposes that a present obligation is a binding obligation (legally or by equivalent means), which an entity has little or no realistic alternative to avoid and which results in an outflow of resources. The IPSASB decided that to help ascertain whether a transfer recipient has a present obligation, consideration is given to whether the transfer recipient has an obligation to perform a specified activity or incur eligible expenditure.

Do you agree with the IPSASB's proposals that for the purposes of this [draft] Standard, *Revenue without Performance Obligations*, a specified activity and eligible expenditure give rise to present obligations? Are there other examples of present obligations that would be useful to include in the [draft] Standard?

Specific Matter for Comment 2: (Paragraph 31)

The flowchart that follows paragraph 31 of this [draft] Standard illustrates the process a transfer recipient undertakes to determine whether revenue arises and, if so, the relevant paragraphs to apply for such revenue recognition. Do you agree that the flowchart clearly illustrates the process? If not, what clarification is necessary?

Specific Matter for Comment 3: (Paragraphs 57–58)

The IPSASB decided that a transfer recipient recognizes revenue without performance obligations but with present obligations when (or as) the transfer recipient satisfies the present obligation.

Do you agree that sufficient guidance exists in this [draft] Standard to determine when a present obligation is satisfied and when revenue should be recognized? For example, point in time or over time. If not, what further guidance is necessary to enhance clarity of the principle?

Specific Matter for Comment 4: (Paragraphs 80–81)

The IPSASB decided that the objective when allocating the transaction price is for a transfer recipient to allocate the transaction price to each present obligation in the arrangement so that it depicts the amount to which the transfer recipient expects to be entitled in satisfying the present obligation. The amount of revenue recognized is a proportionate amount of the resource inflow recognized as an asset, based on the estimated percentage of the total enforceable obligations satisfied.

Do you agree sufficient guidance exists in this [draft] Standard to identify and determine how to allocate the transaction price between different present obligations? If not, what further guidance is necessary to enhance clarity of the principle?

Specific Matter for Comment 5: (Paragraphs 84–85)

Do you agree with the IPSASB's proposals that receivables within the scope of this [draft] Standard should be subsequently measured in accordance with the requirements of IPSAS 41, *Financial Instruments*? If not, how do you propose receivables be accounted for?

Specific Matter for Comment 6: (Paragraphs 126–154)

The disclosure requirements proposed by the IPSASB for revenue transactions without performance obligations are intended to provide users with information useful for decision making, and to demonstrate the accountability of the transfer recipient for the resources entrusted to it.

Do you agree the disclosure requirements in this [draft] Standard provide users with sufficient, reliable and relevant information about revenue transactions without performance obligations? In particular, (i) what disclosures are relevant; (ii) what disclosures are not relevant; and (iii) what other disclosures, if any, should be required?

Specific Matter for Comment 7: (Paragraphs N/A)

Although much of the material in this [draft] Standard has been taken from IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*, the IPSASB decided that the ED should establish broad principles for the recognition of revenue from transactions without performance obligations, and provide guidance on the application of those principles to the major sources of revenue for governments and other public sector entities. The way in which these broad principles and guidance have been set out in the ED are consistent with that of [draft] IPSAS [X] (ED 72), *Transfer Expenses*.

Do you agree with the approach taken in the ED and that the structure and broad principles and guidance are logically set out? If not, what improvements can be made?

Appendix A

Extracts from AASB 1058 Basis for Conclusions

Transfers for the purpose of enabling an entity to acquire or construct a recognisable non-financial asset to be controlled by the entity

- BC95 Some respondents to ED 260 sought clarification on whether a transfer made for the purposes of enabling an BC95 entity to acquire or construct a recognisable non-financial asset for its own use would be recognised as income immediately, or whether a contract liability determined in accordance with AASB 15 arises. The Board noted that these concerns specifically related to whether a transfer of financial assets to enable an entity to acquire or construct a non-financial asset would result in a transfer of goods or services to the transferor or another party. If such a transfer does not result in the transfer of goods or services to the transferor or another party it will be outside the scope of AASB 15 and no contract liability is recognisable; and consequently, under the proposals, the transfer recognised as income on receipt.
- BC96 The Board heard feedback from constituents from the university sector that universities presently recognise a cash grant received to build an educational facility at the time of receiving the grant (that is, on gaining control). Some constituents hold the view that this accounting treatment does not appropriately reflect the relationship of the grant and its related expenditure as the related expenditure is recognised over a number of reporting periods as the educational facility is built.
- BC97 The Board discussed whether such transfers were within the scope of AASB 15, as had been suggested by ED 260. The Board considered that in the absence of guidance, diverse practice may arise in this regard, for example, some may consider that:
- (a) the construction or acquisition of a recognisable non-financial asset on behalf of the grantor is an activity representing services being transferred to the grantor, similar to research activities undertaken on behalf of the grantor but benefiting the community at large. Under this view, an entity would conclude there had been a transfer of goods or services to the transferor or another party;
 - (b) the construction or acquisition of the recognisable non-financial asset is not an activity representing services being transferred to the grantor as the asset remains with the not-for-profit entity. Under this view, an entity would conclude that the transfer is not a contract with a customer within the scope of AASB 15; and
 - (c) AASB 15 applies, but does not require any originally transferred cash and an associated contract liability to be recognised. Instead, the underlying recognisable non-financial asset and income is recognised as the asset is constructed, akin to treating the transaction as an in-substance transfer of the underlying asset as consideration for the construction or acquisition service.
- BC98 For avoidance of doubt, the Board decided to identify the accounting that applies to such transfers. In its redeliberations, the Board observed that in such arrangements, in substance, the transferor had intended to transfer a recognisable non-financial asset to the not-for-profit entity. The Board considered that an in-substance transfer of a good for use by the entity itself should not result in income until the recipient has satisfied its obligation to construct or acquire the asset. That is, the timing of income recognition should reflect the entity receiving the asset directly, rather than the cash to construct or acquire the asset. Accordingly, the Board decided that the accounting for such transactions should reflect that of the approach in AASB 15. However, given the diverse views as to whether AASB 15 applies, the Board decided to specify instead requirements in AASB 1058 to mirror, to the extent appropriate, the accounting that would be achieved had the transaction been accounted for had it been incontestably a contract with a customer within the scope of AASB 15.
- BC99 The Board sought feedback on its proposals in this regard as part of the public 'fatal flaw' review of the draft Standard. Respondents to the draft Standard were generally supportive of the proposal to include specific requirements for such arrangements.

- BC100 The Board discussed the following concerns about the proposal:
- (a) what is meant by 'own use';
 - (b) whether the specified accounting could apply also in instances where the non-financial asset acquired is a resource controlled that meets the definition of an asset but that is not permitted to be recognised by an Accounting Standard; and
 - (c) whether the specified accounting should be extended to apply also in instances where a non-financial asset (for example, construction materials) are made available to the entity, instead of cash or another financial asset.
- BC101 The Board discussed feedback seeking clarification whether the specified accounting could apply to instances where an asset is constructed as directed but used by others as part of furthering the not-for-profit entity's objectives. For example, a not-for-profit entity whose mission is to provide housing services may receive a grant to construct public housing, however, the not-for-profit entity would not itself occupy the building when constructed. The Board observed its intention was for the scope of the accounting specified to include such transfers. In finalising AASB 1058, the Board decided to refer instead to "a recognisable non-financial asset to be controlled by the entity" and to add guidance to clarify the types of arrangements that could be within scope.
- BC102 The Board also discussed whether the specified accounting could apply also in instances where the non-financial asset acquired is a resource controlled that meets the definition of an asset but that is not permitted to be recognised by an Accounting Standard. For example, a not-for-profit entity may be provided a grant to conduct research services with any detailed research data collected and rights to any commercial use of the data retained by the not-for-profit entity. AASB 138 Intangible Assets does not permit research activity to be recognised as an asset.
- BC103 The Board considered whether to:
- (a) limit the application of paragraphs 15–17 of the Standard to only grants (and other transfers) to develop a non-financial asset that qualifies for recognition under another Australian Accounting Standard; or
 - (b) clearly articulate that the application of paragraphs 15–17 of the Standard includes grants (and other transfers) to develop a non-financial asset for which recognition is prohibited by another Australian Accounting Standard.
- BC104 The Board discussed the scope of these paragraphs having regard to grants received to conduct specified research activity; the related intellectual property of which may or may not be controlled by the not-for-profit entity recipient. The Board observed that extending the application of paragraphs 15-17 of the Standard to include grants (and other transfers) to develop a non-financial asset for which recognition is prohibited by another Australian Accounting Standard would be consistent with the underlying principle being that the grantor intended to transfer a good (rather than a financial asset) to the not-for-profit recipient. However, the Board was concerned that extending the paragraphs in this manner would:
- (a) create ambiguity in the distinction between a service and a good, and lack of clarity as to whether an implicit good component in a contract needs to be separately identified from the service. The Board observed that many service contracts in both the not-for-profit and for-profit sector arguably give rise to (unrecognised) knowledge or expertise to the service renderer;
 - (b) result in a lack of comparability, as some constituents may contend that all the value in such a contract is attributable to the unrecognised good acquired; while others contend that the value remains with the service rendered (i.e. the good is an incidental product that the customer does not value in entering the contract). Yet others may contend that some apportionment is appropriate;
 - (c) be seen as being inconsistent with the Board's decision not to extend the accounting specified by AASB 15 to all transactions of not-for-profit entities, regardless of whether a contract with a customer exists. The Board could not see a clear distinction why the accounting should differ between transactions that through the conduct of an activity result in incidentally gaining

control of intellectual property assets, and an arrangement to deliver services for which income may be recognised immediately in accordance with this Standard; and

- (d) create confusion as to whether this Standard would allow certain intangible assets to be recognised, where their recognition is otherwise prohibited.

Consequently, the Board decided that the accounting set out in paragraphs 15–17 of the Standard should be limited to transactions that will result in a recognisable non-financial asset controlled by the entity.

BC105 The Board observed that universities (and other not-for-profit recipients of grants to perform research) would need to determine whether the accounting for a grant to perform research is specified by AASB 15 or AASB 1058. The Board considered its decision to limit the scope of paragraphs 15–17 of the Standard will not result in significant additional costs to affected entities, as the entity would already be required to assess a funding arrangement within the scope of AASB 15 for whether revenue is recognised over time, or at a point in time.

BC106 However, given the significance of grants to conduct research to universities and other not-for-profit recipients, the Board decided to develop several implementation examples to AASB 15 to set out the accounting in this regard. The examples illustrate scenarios where income would be recognised immediately on gaining control of the financial asset in accordance with this Standard, or recognised over time, or at the end of the agreement, in accordance with AASB 15. The Board’s considerations in this regard are set out in its Basis for Conclusions to AASB 2016-8.

Appendix B

Extracts from GASB project page: Revenue and Expense Recognition¹⁰

Background

This project was prompted by three factors (i) common exchange transactions that are not specifically addressed in existing GASB literature; (ii) the results of the Financial Accounting Foundation's (FAF) Post-Implementation Review (PIR) of GASB Statements No. 33, *Accounting and Financial Reporting for Nonexchange Transactions* and No. 36, *Recipient Reporting for Certain Shared Nonexchange Revenues*; and (iii) the development of the GASB's conceptual framework.

Exchange Transactions that are Not Specifically Addressed in Existing Literature

GASB standards provide guidance for revenue recognition for nonexchange transactions in Statements 33 and 36. However, GASB standards provide limited guidance for exchange and exchange-like transactions and that guidance is based on pre-November 30, 1989 Financial Accounting Standard Board (FASB) and the American Institute of Certified Public Accountants (AICPA) pronouncements incorporated through Statement 62. That guidance has not been reexamined and generally has been applied through custom and practice.

Additionally, the FASB recently issued FASB Accounting Standards Codification® (ASC) Topic 606, *Revenue from Contracts with Customers*. These major changes in the FASB standards offer an opportunity to consider a performance obligation approach to the GASB's standards. Therefore, the project is considering developing guidance or improving existing guidance on revenue recognition related to:

- Exchange and exchange-like transactions having single elements
- Exchange and exchange-like transactions having multiple elements
- The differentiation between exchange-like and nonexchange transactions.

Post-Implementation Review of Statements 33 and 36

The FAF conducted a PIR of Statements 33 and 36 and published its findings in November 2015. Among those findings, the PIR report showed that Statements 33 and 36: (1) resolved the issues underlying their stated needs, (2) produced decision-useful information for users of financial statements, and (3) could be applied as intended. However, there were areas that could be considered in this project, including:

- Distinguishing between eligibility requirements and purpose restrictions
- Determining when a transaction is an exchange or nonexchange transaction
- Using the availability period concept consistently across governments
- Applying time and contingency requirements.

Conceptual Framework

Statements 33 and 36 were issued in the 1990s, prior to the completion of key parts of the conceptual framework through the issuance of Concepts Statement No. 4, *Elements of Financial Statements*, in 2007. Concepts Statement 4 includes the definition of two additional elements in financial statements, deferred inflows and deferred outflows of resources. Therefore, an evaluation of the recognition of nonexchange transactions against the conceptual framework would be necessary.

....

¹⁰ [GASB project page](#)

Current Developments

Since August 2019, the Board has deliberated categorization of various transactions in the scope of this project. The Board also considered issues related to moral and constructive obligations, portfolio considerations, and recognition unit of account.

....

Tentative GASB Decisions to Date

Model Assumptions

The Board tentatively decided to propose the following model assumptions:

1. Inflows and outflows are of equal importance in resource flows statements.
2. Inflows and outflows should be classified independently, and not in relationship to each other.
3. The government is an economic entity and not an agent of the citizenry.
4. Symmetrical considerations, to the extent possible, should be included in revenue and expense recognition.
5. A consistent viewpoint, from the resource provider perspective, will be applied in the revenue and expense analysis.

The AB Model

The Board tentatively agreed to the following model development proposals related to categorization:

1. To develop a model in which revenue and expense transactions would be organized into two categories: Category A and Category B (the AB Model). While the concepts included in the tentative descriptions of Category A and Category B are foundational to the model development, the concepts require further refinement.
 - a. Category A transactions should be considered as comprised of two flows, an acquisition coupled with a sacrifice (or a sacrifice coupled with an acquisition). The acquisition coupled with the sacrifice can be identified as rights and obligations that articulate in equivalent terms; that is, the rights and obligations are dependent on the existence of each other, such that there is a remedy for failure of either party to meet the terms of the arrangement. While the right represents the right to receive consideration in a transaction, the obligation represents the requirement to perform via action or inaction. Category A transactions may include reciprocal and nonreciprocal transactions. Binding arrangements in Category A transactions include contracts, grant agreements, memorandums of understanding, interlocal agreements, and legally enforceable purchase orders.
 - b. Category B transactions should be considered as comprised of a single flow, that is an acquisition without a sacrifice or a sacrifice without an acquisition. The obligation would represent the requirement to provide resources. The right would represent the ability to receive or collect resources. Binding arrangements associated with Category B transactions include enabling legislation and purpose-restricted grants.
 - c. To refine these descriptions, the Board should rely on two characteristics identified in the exploratory work: (1) the binding arrangement and (2) rights and obligations that articulate in equivalent terms.
 - i. The binding arrangement should:
 - Have a rebuttable presumption of enforceability
 - Have economic substance.
 - d. Category A binding arrangements should include:
 - i. Mutual assent between the parties of capacity in the transaction
 - ii. Identification of rights and obligations, which are substantive, by the parties to the transaction

- iii. Dependency of the rights and obligations in the binding arrangement on the existence of each other.
 - e. Category B binding arrangements should be identified as those that fail any of the Category A characteristics.
 - f. The terms government and counterparty should be used to describe parties to a transaction, rather than developing terms for specific identification of the parties.
 - g. Forbearance, as an obligation to perform, should be described as a promise to forgo exercising a right in exchange for consideration, such that a dependent relationship exists between the forbearance and the consideration, and remedies exist in the case of breach.
 - h. The term *binding arrangement* should be retained to describe arrangements in the scope of this project.
 - i. Economic substance should be described as an expected change in the risk, amount, or timing of the government's cash flows or an impact on the government's service potential.
 - j. The rebuttable presumption of enforceability and recourse available beyond a court of law allow for moral and constructive obligations to be within the scope of the project.
2. The structure of the categorization component of the model should be proposed as having the following four steps:
 - a. Identification of a binding arrangement, as evidenced by both a rebuttable presumption of enforceability and economic substance, in order for the binding arrangement to be in the scope of the project
 - b. Mutual assent between the parties of capacity, as evidenced by mutual approval of the terms and conditions of the arrangement between parties that have authority to enter into the transaction on behalf of the government or its counterparty
 - c. Identification of the parties' substantive rights and obligations, which are in the form of a right to consideration or an obligation to perform, including action or inaction (forbearance), and are identifiable for both the government and the counterparty to the transaction
 - d. Interdependency between those rights and obligations, such that the obligations are dependent on the rights, the rights are dependent on the obligations, and a remedy exists in case of noncompliance by one of the parties.
3. The following transactions should be identified as Category A transactions:
 - a. Fees for specific services, such as water fees, tuition fees, transit fares, and lottery tickets
 - b. Eligibility-driven grants
 - c. Research grants
 - d. Revolving loans
 - e. Medicaid fee-for-service programs
 - f. Labor costs
 - g. Purchase orders and contracts
4. The following transactions should be identified as Category B transactions:
 - a. Taxes
 - b. Special assessments
 - c. Regulatory fees, such as professional licenses, building permits, or drivers' licenses
 - d. Punitive fees, such as fines, penalties, and forfeitures
 - e. Donations
 - f. Purpose-restricted grants
 - g. Medicaid supplementary payments
 - h. Capital fees, such as passenger facility charges, developer fees, or wastewater impact fees
 - i. Individual assistance.
 - j. Payment in lieu of taxes (PILOT) programs, in general (each program should be independently assessed to ensure proper categorization)

- k. Escheat revenues
 - l. Government-mandated transactions.
5. The categorization assessment should be applied at the binding arrangement level, except for circumstances in which there is potential for multiple transactions in the binding arrangement to be categorized in different categories.
 6. Categorization should be reassessed when the terms and conditions of a binding arrangement have changed significantly.
 7. Categorization may be applied to a portfolio of binding arrangements with similar characteristics, if a government reasonably expects that the effects of the portfolio assessment would not differ from those of the categorization application to the individual binding arrangements.
 8. Right of refund should not be considered in the categorization assessment.
 9. To move away from the following characteristics identified during the exploratory work. The Board tentatively agreed not to rely on:
 - a. Service relatable or distinct goods or services in any categorization definition
 - b. Specific beneficiary in any categorization definition
 - c. The characteristic of cost recovery as a distinguishing characteristic of revenue and expense transactions
 - d. The characteristic of benefit as a distinguishing characteristic of revenue and expense transactions
 - e. Value to develop categorization definitions
 - f. Consideration as a means to categorize revenue and expense transactions.
 - g. The characteristic of voluntary in the categorization component of the model
 - h. Collectibility in the categorization component of the model
 - i. The type of remedy available for a breach of an agreement in the categorization component of the model.
 10. The earnings recognition approach should no longer be considered in this project.

The Board tentatively agreed to the following model development proposals related to recognition:

1. Revenue recognition is broadly comprised of the following four steps:
 - a. First, identify whether there is an increase in assets (increase in net assets)
 - b. Second, identify whether the assets meet the definition of a liability
 - c. Third, identify whether the assets meet the definition of a deferred inflow of resources
 - d. Fourth, recognize revenue.
2. Expense recognition is broadly comprised of the following four steps:
 - a. First, identify whether there is an incurrence of a liability (decrease in net assets)
 - b. Second, identify whether the liability meets the definition of an asset
 - c. Third, identify whether the asset meets the definition of a deferred outflow of resources
 - d. Fourth, recognize expense.
3. With those four recognition steps:
 - a. Guidance should require that analysis follows the specific hierarchical path and that, therefore, the elements should be assessed in the prescribed sequential order.
 - b. A definition for advances should be developed to describe the circumstance in which a government receives resources before a government has a legally enforceable claim in both revenue categories, with the intent to clarify that those resources should always be recognized as liabilities.
 - c. Guidance permitting netting of assets and liabilities for transactions and events in the scope of this project should not be permitted.

- d. Guidance permitting netting of revenues and expenses for transactions and events in the scope of this project should not be permitted.
- e. The recognition unit of account in Category A binding arrangements should be a performance obligation for both revenues and expenses.
 - i. A performance obligation should be described as distinct goods or services, which include:
 - 1. Distinct goods, such as the purchase of supplies
 - 2. Distinct services, such as the provision of transportation
 - 3. Bundles of goods or services, such as physician care and prescription drugs in patient care
 - 4. A series of distinct goods or services, such as the provision or consumption of water or electricity, or the incurrence of allowable costs in expenditure-driven grants.
 - ii. The recognition unit of account for Category A grants should be explicitly described as “allowable costs incurred in compliance with all grant requirements.”
- f. Recognition guidance for a series of distinct goods or services in Category A revenue transaction should be developed at a later date in conjunction with consideration or allocation of consideration.
- g. The fulfillment of a performance obligation for both revenue and expense recognition should be described as the point at which there is a transfer of control over a resource.
- h. Eligibility requirements, as provided in paragraph 20 of Statement 33, should be adjusted to reflect the needs of Category B transactions as follows:
 - i. Required characteristics of recipients should not be considered for any recognition guidance.
 - ii. Time requirements
 - 1. Should be retained to address recognition of deferrals and revenue and expense
 - 2. Should not be considered in asset recognition
 - 3. Do not impose a present obligation and, therefore, are not liabilities.
 - iii. Reimbursement requirements are not applicable to Category B transactions, as all expenditure-driven grants have been tentatively identified as Category A transactions.
 - iv. Contingencies are retained to address recognition of voluntary Category B revenues.
- i. In circumstances in which it is probable that a provider will not provide the resources or will require a return of resources because eligibility requirements are no longer met or it becomes apparent that a recipient will not comply with purpose restrictions within the specified time limit, the provider should recognize a receivable and the recipient should recognize a liability.
- j. Probability of compliance with grant requirements should not be a revenue recognition attribute.
- k. Applicability to a reporting period, for transactions in the scope of this project, should be defined based on time requirements and fulfillment of a performance obligation.
 - i. Applicability to a reporting period should not be used to analyze assets or liabilities.
- l. A practical portfolio consideration should be provided for recognition in both binding arrangements and performance obligations if the government reasonably expects that the effects on the financial statements of applying this guidance to the portfolio would not differ significantly from applying this guidance to each binding arrangement and to each performance obligation.
- m. The primary criterion for the recognition of revenue or expense in Category B transactions should be the time requirements, as defined in Statement 33 and specified in the binding arrangement for the transaction.

- i. In the absence of time requirements in the binding arrangement related to a Category B transaction, revenue and expense should be recognized when the corresponding asset and liability are recognized.
4. Category A revenue recognition:
 - a. Assets should be recognized when the government has a right to receive by performing an obligation through either action (transfer of goods or services) or forbearance, or when resources are received prior to performance.
 - b. Assets should not be recognized solely based on the payment terms of the binding arrangement.
 - c. For expenditure-driven grants, a receivable should be recognized when the government has incurred allowable costs pursuant to all applicable compliance requirements established by an executed grant agreement.
 - d. A liability should not be recognized in a wholly unperformed binding arrangement; that is, a performance obligation is not a present obligation.
 - e. A liability should be recognized for resources received by the government prior to satisfying its performance obligation (advances) in a binding arrangement. Those resource represent a present obligation to perform or are refundable.
 - i. Nonrefundable advances are also liabilities.
 - f. Deferred inflows of resources should not be recognized in Category A revenue transactions, in the scope of this project, in either the economic resources measurement focus or the short-term resources measurement focus.
 - g. Revenue should be recognized over time in Category A revenue transactions in the circumstances in which one of the three proposed criteria below are met:
 - i. The customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs.
 - ii. The entity's performance creates or enhances an asset (for example, work in process) that the customer controls as the asset is created or enhanced.
 - iii. The entity's performance does not create an asset with an alternative use to the entity, and the entity has an enforceable right to payment for performance completed to date.
 - h. Revenue should be recognized at the point in time at which control of resources is transferred in Category A revenue transactions in the circumstances in which none of the three proposed criteria above are met.
5. Category B revenue recognition:
 - a. Subcategories identified in Statement 33 should be retained for recognition purposes of Category B transactions.
 - i. Asset recognition provisions in Statement 33 generally should be retained; that is, based on the existence of a legally enforceable claim, with an expanded rationale for the existence of an asset.
 - ii. Deferred inflows and outflows of resources should be recognized based on the existence of time requirements.
 - b. Derived Category B revenue
 - i. Assets should be recognized for derived Category B revenues when the underlying transaction or activity on which the tax or fee is imposed occurs or when the resources are received, whichever occurs first.
 - ii. Capital fees such as passenger facility charges and impact fees have been tentatively identified as derived Category B transactions.
 - iii. Resources received before the underlying transaction occurring should be recognized as liabilities.
 - iv. Revenue should be recognized for derived Category B transactions when the underlying transaction or activity on which the tax or fee is imposed occurs.

- c. Imposed Category B revenue
 - i. Asset recognition for property taxes should occur when the governing body approves the imposition of the tax; that point should be identified as the "imposition date." The terms lien, levy, and assessment should not be used to describe when a legally enforceable claim arises in a property tax revenue transaction.
 - ii. Asset recognition for imposed Category B revenues should occur when the individual or entity engages in, or applies for a permit to engage in, the activity upon which the government has imposed a fee.
 - iii. Regulatory fees and special assessments should be considered imposed Category B revenue transactions.
 - iv. Resources received before the government has a legally enforceable claim should be recognized as a liability.
 - v. Revenue recognition for imposed Category B property tax transactions should occur in the period for which the tax is imposed.
 - vi. Revenue recognition for imposed Category B regulatory fee transactions should occur when the individual or entity commits the act of applying and qualifies for a permit to engage in a regulated activity.
 - vii. Revenue recognition for imposed Category B punitive fee transactions should occur when the individual or entity has committed or omitted an act that is a violation of a law for which a punitive fee is prescribed by the governing body's legislation.
- d. Voluntary Category B revenue
 - i. Asset recognition for voluntary Category B revenue transactions should occur either when the government receives the resources or when a promise is made that is verifiable, measurable, and probable of collection, whichever occurs first. A promise that is probable of collection should have to comply with any pre-established conditions.
 - 1. Pledges should be recognized as assets whether pledged to an endowment or for other purposes.
 - ii. A liability should be recognized for assets received as advances in voluntary Category B revenue transactions, which infrequently occurs in certain PILOT programs when a not-for-profit provides resources to a government before a binding arrangement is established.
 - iii. Pledges for endowments should be recognized as deferred inflows of resources when the promise is established; revenue should be recognized when resources are received and the government can begin to comply with time requirements.
- e. Government mandated Category B revenue
 - i. Asset recognition for government-mandated Category B revenue transactions should occur when the resource provider has appropriated the resources and the corresponding fiscal period has begun.
 - ii. A liability should not be recognized in government-mandated and voluntary Category B revenue transactions for purpose restrictions placed on assets received to which the government already has established a legally enforceable claim.
 - iii. The provisions in Statement 33 should be modified to acknowledge the existence of unrestricted government-mandated revenue transactions.

Appendix C

Extracts from IPSASB Conceptual Framework Basis for Conclusions – Chapter 5

Net Financial Position, Other Resources and Other Obligations

BC5.37 This section of the Basis for Conclusions outlines the IPSASB's approach to models of financial performance to be reported in the financial statements, and specifically the treatment of deferred inflows and deferred outflows.

Consultation Paper, Elements and Recognition in Financial Statements

BC5.38 The Consultation Paper discussed two contrasting approaches to financial performance:

- An approach that measures financial performance as the net result of all changes in the entity's resources and obligations during the period. This was described as the asset and liability-led approach; and
- An approach that measures financial performance as the result of the revenue inflows and expense outflows more closely associated with the operations of the current period. This was described as the revenue and expense-led approach.

BC5.39 The Consultation Paper noted that the two different approaches could lead to different definitions of the elements related to financial performance and financial position. The revenue and expense-led approach is strongly linked to the notion of inter-period equity. Inter-period equity refers to the extent to which the cost of programs and providing services in the reporting period is borne by current taxpayers and current resource providers. The asset and liability-led approach is linked to the notion of changes in resources available to provide services in the future and claims on these resources as a result of period activity.

BC5.40 A further section of the Consultation Paper discussed Other Potential Elements and pointed out that, if IPSASB adopted the revenue and expense-led approach, IPSASB would need to address deferred flows. Under this approach, deferred flows are items that do not meet the proposed definitions of revenue and expense, but which are nevertheless considered to affect the financial performance of the period. The Consultation Paper identified three options for dealing with such flows:

- Defining deferred inflows and deferred outflow as elements on the statement of financial position;
- Broadening the asset and liability definitions to include items that are deferrals; or
- Describing deferred flows as sub-classifications of net assets/net liabilities (subsequently referred to as the residual amount).

BC5.41 The Consultation Paper had two specific matters for comment on these areas. The first asked constituents to indicate whether they preferred the asset and liability-led approach or revenue and expense-led approach and to indicate their reasons. The second asked whether deferred inflows and deferred outflows need to be identified on the statement of financial position. If respondents supported identification on the statement of financial position they were asked to indicate which of the three approaches in paragraph BC5.40 they supported.

BC5.42 The responses to these specific matters for comment were inconclusive. A small majority of respondents expressing a view favored the asset and liability-led approach. However, a number of respondents who supported the asset and liability-led approach also indicated that they favored identifying deferrals on the statement of financial position. The IPSASB took these views into account at Exposure Draft stage.

Exposure Draft, Elements and Recognition in Financial Statements

BC5.43 The Exposure Draft expressed a view that it is important to be able to distinguish flows that relate to the current reporting period from those that relate to specified future reporting periods. The Exposure Draft therefore proposed the following definitions of a deferred inflow and a deferred outflow:

- *A deferred inflow is an inflow of service potential or economic benefits provided to the entity for use in a specified future reporting period that results from a non-exchange transaction and increases net assets; and*
- *A deferred outflow is an outflow of service potential or economic benefits provided to another entity or party for use in a specified future reporting period that results from a non-exchange transaction and decreases net assets.*

BC5.44 The two key features of these definitions were:

- The proposed elements were restricted to non-exchange transactions; and
- The flows had to be related to a specified future period.

BC5.45 The IPSASB's rationale for including these characteristics were as risk-avoidance measures to reduce the possibility of deferred inflows and deferred outflows being used widely as smoothing devices, and to ensure that deferred inflows and deferred outflows are not presented on the statement of financial position indefinitely. The Exposure Draft included two Alternative Views. The first Alternative View considered the meaning of net financial position to be unclear in light of the combined impact of deferred inflows and deferred outflows. The second Alternative View disagreed with the view that deferred inflows and deferred outflows should be identified and recognized as separate elements and expressed a view that these flows meet the definitions of revenue and expense.

BC5.46 Many respondents disagreed with defining deferred inflows and deferred outflows as elements. Some expressed reservations about the implications for alignment with the International Accounting Standards Board's Conceptual Framework, and International Financial Reporting Standards more generally. A number of respondents considered that the proposed approach did not reflect economic reality and that it would be more difficult to determine an objective basis for deferring revenue and expense under the revenue and expense-led approach. Nevertheless, a number of respondents also expressed the view that information on flows relating to particular reporting periods has information value.

BC5.47 The rationale for restricting the definitions to non-exchange transactions was challenged as conceptually weak both by respondents who favored defining deferred inflows and deferred outflows as elements and those opposed to these proposed elements. Respondents also disagreed with the restriction to specified time periods, because it would potentially lead to the different accounting treatment of very similar transactions dependent upon whether a specific period was identified—a grant without conditions receivable by an entity to finance its general activities for a five year period would have met the definition of a deferred inflow, whereas a similar grant for a future unspecified period would have met the definition of revenue.

Finalizing the Elements Chapter

BC5.48 The IPSASB considered that it needed to balance the limited support for the proposals on deferred flows in the Exposure Draft, and the perceived needs of users for information about flows relating to particular reporting periods.

BC5.49 The IPSASB therefore considered five options (A–E below) in responding to input from the due process and its perception of users' information needs:

- A. Defining deferred inflows and deferred outflows as elements in a more principles-based manner and not specifying the financial statements in which the elements are to be recognized. As such, the Conceptual Framework would not predetermine the presentation of the elements;
- B. Deriving the definitions of revenue and expense from the asset and liability definitions;
- C. Broadening the asset and liability definitions;
- D. Accepting that certain economic phenomena that do not meet the definition of any element may need to be recognized in financial statements in order to meet the objectives of financial reporting; and
- E. Reporting inflows and outflows that provide service potential or economic benefits, but do not affect assets and liabilities as defined in the Framework and reporting inflows and outflows that do not affect revenue and expense.

BC5.50 The IPSASB does not consider that defining deferred inflows and deferred outflows as elements in Option A is justified in light of the objections that respondents had made to the proposals in the Exposure Draft. The IPSASB therefore rejected Option A.

BC5.51 The IPSASB considered two variants of Option B. In the first variant deferred flows would be taken directly to surplus/deficit, while in the second variant deferred flows would initially be taken to residual amount and then recycled to surplus/deficit in the period that time stipulations occur.

BC5.52 The IPSASB considers that taking deferred flows directly to surplus/deficit under the first variant of Option B may not produce information that is representationally faithful of an entity's sustainable performance and therefore does not meet the objectives of financial reporting. The second variant of Option B relies on recycling and, in the view of some IPSASB members would have implicitly introduced the notion of "other comprehensive income" into the Framework. The IPSASB has strong reservations about such a development. For these reasons the IPSASB rejected Option B.

BC5.53 The IPSASB noted that Option C would require changes to the definitions of an asset and a liability so that:

- The definition of an asset would include resources that an entity does not control; and
- The definition of a liability would include obligations that are not present obligations.

The IPSASB considers that such changes would distort the essential characteristic of an asset—that an entity controls rights to resources—and the essential characteristic of a liability—that an entity has a present obligation for an outflow of resources. In the view of the IPSASB this would make assets and liabilities less easily understandable. Adoption of such an option would also be a departure from globally understood definitions of an asset and a liability. For these reasons the IPSASB rejected Option C.

BC5.54 Option E was a hybrid approach that involved components of the other four options. It would allow reporting of inflows and outflows that provide service potential or economic benefits, but would not affect the definitions of an asset and liability and the reporting of inflows and outflows that do not affect revenue and expense as defined in the Framework. The idea of this approach was to acknowledge that further conceptual thinking on financial performance is necessary.

BC5.55 Option D is broader than Option E because it is not necessarily restricted to deferred flows, but could encompass broader economic phenomena—for example obligations that are not present obligations, because, although they contain performance obligations, it is not clear that they require an outflow of resources. Option D acknowledges that there may be circumstances under which the six elements defined in the Conceptual Framework may not provide all the information in the financial statements that is necessary to meet users' needs. In the view of the IPSASB it is transparent to acknowledge that other items may be recognized. Unlike Option A, Option D does not involve defining additional elements, and, unlike Option C, Option D does not involve modification of generally understood definitions of an asset and a liability.

BC5.56 The IPSASB concluded that Option D provides the most transparent approach. The terms "other obligations" and "other resources" are used to describe these economic phenomena in the Conceptual Framework. Option D also enhances the accountability of the IPSASB because the circumstances under which other obligations and other resources will be recognized will be determined at standards level and explained in the Bases for Conclusions of specific standards.

Financial Statements

BC5.57 Net financial position is the aggregate of an entity's net assets (assets minus liabilities) and other resources and other obligations recognized in the statement of financial position at the reporting date. Where resources and obligations other than those that meet the definition of the elements are recognized in the financial statements, the amounts reported as net assets and net financial position will differ. In these circumstances, the interpretation of net financial position will be determined by reference to the nature of the other resources and other obligations recognized in the financial statements under the relevant IPSAS.

BC5.58 The IPSASB considered whether it should use both the terms "net assets" and "net financial position" in the Conceptual Framework. The IPSASB acknowledges a view that net assets is a generally understood term. However, the IPSASB considered that using both terms could be confusing and therefore decided to use the term "net financial position" to indicate the residual amount of an entity.



NZ ACCOUNTING
STANDARDS
BOARD

Memorandum

Date: 13 March 2020

To: NZASB Members

From: Tracey Crookston

Subject: Annual Review of Application of the PBE Policy Approach

Purpose and Introduction¹

1. The purpose of this agenda item is to give the Board the opportunity to review and confirm its previous decisions regarding the application of the [Policy Approach to Developing the Suite of PBE Standards](#) (PBE Policy Approach).²
2. The Board applies the PBE Policy Approach to:
 - (a) new or amending IFRS Standards and decides whether to incorporate the new standard or amendment into the PBE Standards or wait for the IPSASB to consider the pronouncement. The PBE Policy Approach is applied when the new or amending IFRS Standard is approved by the Board for issue in New Zealand; and
 - (b) new or amending IPSASs. There is a rebuttable assumption that these will be incorporated into the PBE Standards. The PBE Policy Approach is applied when the IPSASB issues the new or amending IPSAS.
3. The agenda provides an annual update, at a point in time, of which pronouncements issued by the IASB or the IPSASB are yet to be incorporated into the PBE Standards. The update includes a summary of the current status of applying the PBE Policy Approach together with staff recommendations.

Recommendations

4. The Board is asked to:
 - (a) REVIEW the application of the PBE Policy Approach; and
 - (b) AGREE the recommendations set out in the table below.

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

² The PBE Policy Approach was last updated by the XRB Board in December 2018. The PBE Policy Approach may be amended pending future XRB Board decisions as a result of the *Targeted Review of the New Zealand Accounting Standards Framework*.

IASB pronouncements not included in PBE Standards	We recommend that the Board:
Revenue	
IFRS 15 <i>Revenue from Contracts with Customers</i>	AGREES to wait for the IPSASB to complete its revenue projects and then apply the PBE Policy Approach to the IPSASB's new and revised revenue standards.
<i>Clarifications to NZ IFRS 15 Revenue from Contracts with Customers</i>	
Leases	
IFRS 16 <i>Leases</i>	AGREES to wait for the IPSASB's decision on leases at its March 2020 meeting.
Interests in Other Entities	
<i>Sale or Contribution of Assets Between an Investor and its Associate or Joint Venture</i> (Amendments to IFRS 10 and IAS 28)	AGREES to continue to MONITOR the IASB's research project on the equity method of accounting.
<i>Effective Date of Amendments to IFRS 10 and IAS 28</i>	
Insurance Contracts	
IFRS 17 <i>Insurance Contracts</i>	NOTES that PBE IFRS 17 <i>Insurance Contracts</i> has been issued (with a scope modification to limit its application to Tier 1 and Tier 2 not-for-profit PBEs) and that a public sector specific PBE insurance project is on the workplan.
Other	
Other IASB pronouncements	NOTES the status of the other IASB pronouncements that have not yet been incorporated into PBE Standards (see paragraph 31).
IPSASB pronouncements not included in PBE Standards	We recommend that the Board:
Social Benefits	
IPSAS 42 <i>Social Benefits</i>	NOTES that it has AGREED to DEFER its decision to develop a PBE Standard based on IPSAS 42 <i>Social Benefits</i> until the IPSASB has issued a standard on transfer expenses.
Collective and Individual Services	
<i>Collective and Individual Services</i> (Amendments to IPSAS 19)	NOTES that it has AGREED to DEFER making a decision about incorporating <i>Collective and Individual Services</i> (Amendments to IPSAS 19) into PBE Standards until the IPSASB has issued a standard on transfer expenses.
Other	
Other IPSASB pronouncements	NOTES the status of the other IPSASB pronouncements that have not yet been incorporated into the PBE Standards (see paragraphs 39–42).

Background

Applying the PBE Policy Approach and monitoring

5. Since 1 October 2013 the Board has applied the PBE Policy Approach to pronouncements that have been issued by both the IASB and the IPSASB. The pronouncement may be a new IFRS Standard or IPSAS or a change to an existing IFRS Standard or IPSAS.
6. For pronouncements issued by the IASB, the Board must decide whether to make a change to the PBE Standards, or whether to wait for the IPSASB to consider the IASB pronouncement for inclusion in the respective IPSASs.
7. The Board monitors pronouncements issued by the IASB but not yet considered by the IPSASB. We track these pronouncements and bring a summary to the Board at regular intervals so the Board can review its earlier decisions and monitor ongoing projects.

Staff tracking tables

8. Staff maintain tracking tables to ensure that the PBE Policy Approach has been applied to all pronouncements issued by the IASB and the IPSASB since 1 October 2013.
9. The staff tracking tables have not been included in the agenda papers as they are quite large and detailed. They are available on request from staff.

Structure of this memo

10. The remainder of this memo provides further information about firstly IASB pronouncements and secondly IPSASB pronouncements that are yet to be incorporated into the PBE Standards, together with recommendations for the Board (as summarised on page 2).

A. IASB pronouncements

Revenue

11. In the table below we have summarised the IASB pronouncements issued as NZ IFRSs that relate to revenue that have not been incorporated into the PBE Standards.

NZASB Approval and Date	IASB Pronouncement
Approval 44 – June 2014	IFRS 15 <i>Revenue from Contracts with Customers</i>
Approval 71 – May 2016	<i>Clarifications to IFRS 15 Revenue from Contracts with Customers</i>

12. In June 2014, the NZASB issued NZ IFRS 15 *Revenue from Contracts with Customers*. In August 2014, the Board agreed that IFRS 15 should not be incorporated into the PBE Standards at that time.
13. On 21 February 2020 the IPSASB issued ED 70 *Revenue with Performance Obligations (ED 70)*. ED 70 is aligned with IFRS 15 *Revenue from Contracts with Customers (IFRS 15)* and includes *Clarifications to IFRS 15 Revenue from Contracts with Customers*.

14. The Board is considering ED 70 at agenda item 3.2.

Recommendation

We recommend that the Board AGREES to wait for the IPSASB to complete its revenue projects and then apply the PBE Policy Approach to the IPSASB's new and revised revenue standards.

Leases

15. In the table below we have summarised the IASB pronouncement issued as an NZ IFRS that relates to leases that has not been incorporated into the PBE Standards.

NZASB Approval and Date	IASB Pronouncement
Approval 68 – February 2016	IFRS 16 <i>Leases</i>

16. The IASB issued IFRS 16 *Leases* in January 2016. The Board approved and issued NZ IFRS 16 *Leases* in February 2016.
17. A timeline of the Board's deliberations on leases in the PBE sector is set out in Appendix A.
18. At this meeting the Board will receive a verbal update on the March IPSASB meeting discussion on leases.

Recommendation

We recommend the Board AGREES to wait for the IPSASB's decision on leases at its March 2020 meeting.

Interests in other entities

19. In December 2016, the Board approved for issue five PBE Standards dealing with interests in other entities, including PBE IPSAS 35 *Consolidated Financial Statements* and PBE IPSAS 36 *Investments in Associates and Joint Ventures*. These new PBE Standards incorporated most of the IASB's narrow scope amendments on these topics.
20. In the table below we have summarised the IASB pronouncements issued as NZ IFRSs that relate to interests in other entities that have not been incorporated in the PBE Standards.

NZASB Approval and Date	IASB Pronouncement
Approval 54 – October 2014	<i>Sale or Contribution of Assets Between an Investor and its Associate or Joint Venture</i> (Amendments to IFRS 10 and IAS 28)
Approval 67 – February 2016	<i>Effective Date of Amendments to IFRS 10 and IAS 28</i>

21. The narrow scope amendments to NZ IFRS 10 and NZ IAS 28 established the requirements for the recognition of a partial gain or loss for transactions between an investor and its associate or joint venture dependent on whether the sale or contribution of assets constitutes a business as defined in NZ IFRS 3 *Business Combinations*.

22. In December 2015, the IASB deferred the effective date of these amendments indefinitely, pending further research in this area as part of its research project on the equity method.³ The IASB did not want to force entities to change their accounting twice in a short period. The amendments remained available for early adoption. In New Zealand, in the for-profit sector, the Board deferred the effective date of these amendments until 1 January 2020 (and subsequently extended this to 1 January 2025).
23. The IPSASB issued IPSAS 40 *Public Sector Combinations* in January 2017 and incorporated equivalent amendments to IPSAS 35 and IPSAS 36 (via consequential amendments in IPSAS 40). These amendments are to be applied from a date to be determined by the IPSASB.
24. In developing PBE IPSAS 40 *PBE Combinations* the Board reconsidered incorporating the amendments into PBE IPSAS 35 and PBE IPSAS 36. However, given the IASB’s 2016 decision to defer work on its equity method research project until it has undertaken post-implementation reviews of certain standards, the Board decided not to incorporate these amendments.
25. In 2019, the Board issued *2019 Amendments to NZ IFRS* which included amendments to NZ IFRS 10 and NZ IAS 28 to defer the effective date of *Sale or Contribution of Assets between and Investor and its Associate or Joint Venture* (amendments to NZ IFRS 10 and NZ IAS 28) from annual periods beginning on or after 1 January 2020 to annual periods beginning on or after 1 January 2025.

Recommendation

We recommend that the Board AGREES to continue to MONITOR the IASB’s research project on the equity method.

Insurance contracts

26. IFRS 17 *Insurance Contracts* was issued in May 2017.

NZASB Approval and Date	IASB Pronouncement
Approval 90 – August 2017	IFRS 17 <i>Insurance Contracts</i>

27. At its August 2017 meeting, the Board approved for issue NZ IFRS 17 *Insurance Contracts*. NZ IFRS 17 supersedes NZ IFRS 4 *Insurance Contracts* which is the basis for PBE IFRS 4 *Insurance Contracts*.
28. At this point, the IPSASB does not have an equivalent standard on insurance and has no plans to develop a standard.
29. The Board considered the application of the PBE Policy Approach to NZ IFRS 17 at its February 2018 meeting. The Board agreed to develop a PBE Standard based on IFRS 17.

³ In May 2016 the IASB deferred further work on the equity method project until the Post-implementation Reviews (PiR) of IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities* are undertaken. As part of the PiR for these standards, the IASB has decided to seek feedback on investors’ information needs regarding investments accounted for using the equity method. The PiR is currently in the first phase, during which the IASB will identify the issues to examine in greater detail.

30. PBE IFRS 17 *Insurance Contracts*, which applies only to Tier 1 and Tier 2 not-for-profit PBEs, was issued in July 2019.

Recommendation

We recommend that the Board NOTES that PBE IFRS 17 *Insurance Contracts* has been issued (with a scope modification to limit its application to Tier 1 and Tier 2 not-for-profit PBEs) and that a public sector specific PBE insurance project is on the workplan.

Other IASB pronouncements

31. The following table summarises other IASB pronouncements that have not yet been incorporated into the PBE Standards, and which we are continuing to monitor.

NZASB Approval and Date	IASB Pronouncement	Status
Approval 103 – [December 2018]	<i>Definition of a Business</i> (Amendments to IFRS 3)	<p>In December 2018, the Board considered this and noted that the IPSASB plans to include this project in its workplan for 2019–2023.</p> <p>The Board agreed to wait for the IPSASB to consider the amendments to IFRS 3 before deciding whether to incorporate them into the PBE Standards.</p> <p>At its June 2019 meeting the IPSASB considered a draft ED 68 <i>Improvements</i>. IPSASB staff had proposed to include the amendments set out in <i>Definition of a Business</i>. The IPSASB did not agree with that proposal. The IPSASB decided to consider these amendments as part of a narrow scope update of IPSAS 40 <i>Public Sector Combinations</i> (no date set).</p> <p>When considering, at its August 2019 meeting, whether to comment on ED 68 the Board agreed to continue to wait for the IPSASB to consider this pronouncement.</p>
Approval 104 – [December 2018]	<i>Definition of Material</i> (Amendments to IAS 1 and IAS 8)	<p>At its December 2018 meeting, the Board also considered these pronouncements. The Board agreed to wait for the IPSASB to consider these amendments before deciding whether to incorporate them into PBE Standards.</p>
Approval 105 – [December 2018]	<i>Definition of Material</i> (Amendments to Conceptual Frameworks)	<p>At its June 2019 meeting the IPSASB considered a draft ED 68 <i>Improvements</i>. IPSASB staff had proposed to include the amendments set out in <i>Definition of Material</i>. The IPSASB did not agree with that proposal. The IPSASB decided to consider these amendments as part of the <i>Limited Scope Review of the Conceptual Framework</i> (2020–2021).</p> <p>When considering, at its August 2019 meeting, whether to comment on ED 68 the Board agreed to continue to wait for the IPSASB to consider these pronouncements.</p>
	<i>Classification of Liabilities as</i>	<p>Issued by the IASB in January 2020, amends IAS 1 <i>Presentation of Financial Statements</i></p>

NZASB Approval and Date	IASB Pronouncement	Status
	<i>Current or Non-current</i>	Approval to issue this pronouncement is sought at agenda item 6.2. The PBE Policy Approach is applied to this pronouncement at agenda item 6.4.

Recommendation

We recommend that the Board NOTES the status of the other IASB pronouncements that have not yet been incorporated into PBE Standards

B. IPSASB pronouncements

Social Benefits

- 32. At its February 2019 meeting, the Board noted that the IPSASB has issued IPSAS 42 *Social Benefits*.
- 33. Staff recommended that the most efficient approach would be to seek feedback from PBEs on all proposals for non-exchange expenses at the same time and then finalise all the relevant requirements together.
- 34. The Board agreed to defer its decision to develop a PBE Standard based on IPSAS 42 until the IPSASB has completed other related projects dealing with non-exchange expenses (now referred to by the IPSASB as transfer expenses).
- 35. The IPSASB issued ED 72 *Transfer Expenses* in February 2020.

Recommendation

We recommend that the Board NOTES that it has AGREED to DEFER its decision to develop a PBE Standard based on IPSAS 42 *Social Benefits* until the IPSASB has issued a standard on transfer expenses.

Collective and Individual Services

- 36. *Collective and Individual Services* (Amendments to IPSAS 19) was issued in January 2020.
- 37. At its December 2019 meeting, the Board agreed to defer making a decision about incorporating the amendments to IPSAS 19 into the PBE Standards until the IPSASB has issued its standard on transfer expenses.
- 38. As noted in paragraph 35, the IPSASB issued ED 72 *Transfer Expenses* in February 2020.

Recommendation

We recommend that the Board NOTES that it has AGREED to DEFER making a decision about incorporating *Collective and Individual Services* (Amendments to IPSAS 19) into the PBE Standards until the IPSASB has issued a standard on transfer expenses.

Other IPSASB pronouncements

39. The IPSASB issued *Improvements to IPSAS, 2018* in October 2018. We sought feedback on the proposals concurrently with the IPSASB and in nearly all cases we proposed to incorporate equivalent amendments into the PBE Standards. The only IPSASB proposals not incorporated in the *2018 Omnibus Amendments to PBE Standards* were in relation to certain amendments to IPSAS 16 *Investment Property*.
40. At its 31 October 2018 meeting the Board agreed to consider the IPSASB's amendments to IPSAS 16 in a future omnibus ED.
41. We have subsequently contacted IASB staff to see if the IASB plans to incorporate these amendments into IAS 40 *Investment Property*. IASB staff have indicated that at this stage they do not propose to include these amendments in IAS 40.

Recommendation

We recommend that the Board NOTES that it AGREED to consider the amendments to IPSAS 16 as part of a future PBE Omnibus ED.

42. The IPSASB issued *Improvements to IPSAS, 2019* in January 2020. We have applied the PBE Policy Approach to this pronouncement at agenda item 4.2.

Related links

[PBE Policy Approach \(December 2018\)](#)

Appendix A: Timeline of the Board's deliberation on leases in the PBE sector

Date	Comment
2016	
March, August, November	At each of these meetings, the Board considered whether to develop a PBE Standard based on IFRS 16 ahead of the IPSASB. Outreach was also undertaken during this time to assist the Board with its considerations. On balance, the Board agreed not to develop a PBE Standard based on IFRS 16. However, the Board agreed to continue to closely monitor the IPSASB's project on leases.
2018	
January	The IPSASB issued ED 64 <i>Leases</i> (ED 64) with a comment period ending 30 June 2018. The IPSASB developed a public sector specific approach in ED 64, to address: <u>Lessor Accounting</u> – ED 64 proposed a single right-of-use model for lessors. IFRS 16 <i>Leases</i> requires a right-of-use model for lessees, and a risks and rewards model for lessors; <u>Concessionary Leases</u> – ED 64 proposed guidance for concessionary leases because of the prevalence in the public sector of leases at below market terms. IFRS 16 does not include guidance for leases at below market terms.
June	The Board submitted its comment letter to the IPSASB.
2019	
March – IPSASB	Constituents were divided on the ED 64 proposed approaches for public sector specific issues. There were strong views that IPSASB should develop a standard aligned with IFRS 16 and equally strong views that public sector specific proposals in ED 64 should be taken forward. The IPSASB decided to extend the project timeline to better understand respondents' views on both IFRS 16 and ED 64.
March – NZASB	The Board noted that it had previously decided not to develop a PBE standard ahead of the IPSASB but acknowledged that given the delay, it may need to reconsider this decision. The Board requested further information from staff in order to make this decision.
June	At its June 2019 meeting the Board received feedback on the outreach undertaken by staff and agreed to defer the decision on whether to develop a PBE Standard ahead of the IPSASB until after the September IPSASB meeting. It was anticipated that there would then be more information regarding the IPSASB's planned approach for lessor accounting. The Board also agreed to investigate the types of leases/arrangements entered into by PBEs to determine whether additional guidance is needed in relation to the definition of a lease for PBEs. To date, some limited outreach has been undertaken by staff.
	During 2019, the IPSASB formed a Leases Task Force whose primary focus was to address the departure or non-departure from IFRS 16 for lessor accounting. The IPSASB also invited stakeholders (including national standard setters, preparers, auditors, the GFS community) to share their different perspectives on lease accounting. These initiatives highlighted that constituents are divided on the issue of lease accounting (for lessors and concessionary leases).
December	Lease accounting was discussed at the December 2019 IPSASB meeting, but no further decisions were reached.

Date	Comment
2020	
March	<p>The IPSASB staff paper for the March 2020 meeting recommends that the IPSASB makes a strategic decision on the future direction of the Leases project.</p> <p>The IPSASB staff recommend a phased approach going forward:</p> <p><u>Phase 1</u></p> <ul style="list-style-type: none"> • prioritise developing the accounting model(s) for lessors and lessees (issuing another ED). <p><u>Phase 2</u></p> <ul style="list-style-type: none"> • developing concessionary lease requirements based on the models developed in phase 1 (issuing a request for information potentially alongside a further ED). <p>IPSASB staff are recommending that the accounting model(s) for both <u>lessors</u> and <u>lessees</u> be aligned with IFRS 16.</p>



Memorandum

Date: 13 March 2019

To: NZASB Members

From: Tracey Crookston

Subject: **PBE Policy Approach: *Improvements to IPSAS, 2019***

Recommendations

1. The Board is asked to:
 - (a) CONSIDER the application of the [Policy Approach to the Development of PBE Standards](#) (the PBE Policy Approach) to *Improvements to IPSAS, 2019*; and
 - (b) AGREE, in the next omnibus amendments to PBE Standards, to consider aligning the following paragraphs in PBE Standards with the amendments in *Improvements to IPSAS, 2019*.

PBE Standard	<i>Improvements to IPSAS, 2019 – Amendments</i>
PBE IPSAS 30 <i>Financial Instruments: Disclosures</i>	<i>Implementation Guidance</i> <ul style="list-style-type: none"> • paragraphs IG22A–IG22D and IG23 – on credit risk. <i>Application Guidance</i> <ul style="list-style-type: none"> • paragraph AG5(h) – disclosures about financial guarantee contracts issued through a non-exchange transaction.
PBE IPSAS 13 <i>Leases</i>	<ul style="list-style-type: none"> • paragraph 76 – correct cross reference to other IPSAS
PBE IPSAS 21 <i>Impairment of Non-Cash-Generating Assets</i> and PBE IPSAS 26 <i>Impairment of Cash-Generating Assets</i>	Clarifying the requirements in relation to impairment of revalued assets: <ul style="list-style-type: none"> • paragraphs 54A and 69A of IPSAS 21; and • paragraphs 73A and 108A of IPSAS 26.

Background

2. In July 2019 the IPSASB issued Exposure Draft 68 *Improvements to IPSAS, 2019* which proposed narrow scope amendments to several IPSASs. In August 2019 the Board NOTED the proposals in ED 68 and AGREED not to comment on the ED. We analysed the proposals and recommended that we consider a few of the proposals once they had been finalised.¹

¹ The analysis of ED 68 was included in agenda item 2.7, August 2019.

3. *Improvements to IPSAS, 2019* was issued in January 2020. Apart from a few minor changes the proposals are the same as those in ED 68.
4. The next step is to consider whether *Improvements to IPSAS, 2019* should be incorporated into the PBE Standards, and if so, when. The PBE Policy approach contains a rebuttable presumption that the NZASB will adopt a new or amended IPSAS.

Application of the PBE Policy Approach

5. We have analysed the amendments in *Improvements to IPSAS, 2019* in the table below and recommend that a few of the amendments be considered as part of the next omnibus amendments to PBE Standards.

IPSAS	Summary	Staff comments
<i>Amendments to Other IPSAS resulting from IPSAS 41, Financial Instruments</i>		
IPSAS 5 <i>Borrowing Costs</i>	The amendments update the guidance related to the components of borrowing costs. The amendments to IPSAS 5 were inadvertently omitted when IPSAS 41 was issued.	N/A We included equivalent amendments to PBE IPSAS 5 <i>Borrowing Costs</i> when we issued PBE IPSAS 41.
IPSAS 30 <i>Financial Instruments: Disclosures</i>	The amendments add implementation guidance on hedge accounting and credit risk (paragraphs IG13A–IG13C and IG22A–IG22D are added and paragraph IG23 is amended). These amendments to IPSAS 30 were inadvertently omitted when IPSAS 41 was issued.	Consider in next PBE Omnibus. We included similar implementation guidance in PBE IPSAS 30 <i>Financial Instruments: Disclosures</i> when we issued PBE IPSAS 41. The implementation guidance we included in PBE IPSAS 30 was based on IFRS 9 <i>Financial Instruments</i> . There is one difference – the IPSASB has modified the types of entities and instruments in the credit risk implementation guidance to make them more public sector specific. <u>We recommend considering aligning PBE IPSAS 30 paragraphs IG22A–IG22D and IG23 with the amendments made by <i>Improvements to IPSAS, 2019</i>.</u>
IPSAS 30 <i>Financial Instruments: Disclosures</i>	An amendment to update the guidance for the disclosure of financial guarantee contracts issued through a non-exchange transaction. This amendment to IPSAS 30 was inadvertently omitted when IPSAS 41 was issued.	Consider in next PBE Omnibus We included a similar amendment to PBE IPSAS 30 when we issued PBE IPSAS 41. However, the IPSASB’s amendments to paragraph AG5(h) of IPSAS 30 differ from our amendments to PBE IPSAS 30. The IPSASB’s amendment refers to disclosing the circumstances that result in fair value not being determinable. PBE IPSAS 30

IPSAS	Summary	Staff comments
		<p>paragraph AG5(h) is more generic and suggests disclosing the nature of the financial guarantee contracts whose fair value on initial recognition could not be determined. <u>We recommend considering aligning paragraph AG5(h) of PBE IPSAS 30 with the amendment made by Improvements to IPSAS, 2019.</u></p>
<p>IPSAS 33 <i>First-time Adoption of Accrual Basis International Public Sector Accounting Standards (IPSASs)</i></p>	<p>Amendments to update the guidance on classifying financial instruments on initial adoption of accrual basis IPSAS. This amendment to IPSAS 33 was inadvertently omitted when IPSAS 41 was issued.</p>	<p>N/A There is no PBE Standard based on IPSAS 33. We included similar amendments to PBE FRS 47 <i>First-time Adoption of PBE Standards</i> when we issued PBE IPSAS 41.</p>
<p><i>Other Improvements to IPSAS</i></p>		
<p>IPSAS 13 <i>Leases</i></p>	<p>Amendments to paragraphs 67 and 76 of IPSAS 13 to replace the current references to other international and/or national accounting standards with references to the IPSASs on impairment (being IPSAS 21 <i>Impairment of Non-Cash-Generating Assets</i> and IPSAS 6 <i>Impairment of Cash-Generating Assets</i>).</p>	<p>N/A Paragraph 67 of PBE IPSAS 13 is already aligned with the IPSASB's changes. No further action needed. Consider in next PBE Omnibus <u>Staff recommend that we consider making equivalent amendments to paragraph 76 of PBE IPSAS 13 in the next omnibus amendments to PBE Standards.</u></p>
<p>IPSAS 13 <i>Leases</i>; IPSAS 17 <i>Property, Plant, and Equipment</i></p>	<p>Amendments to remove transitional provisions which should have been deleted when IPSAS 33 was issued.</p>	<p>N/A There is no PBE Standard based on IPSAS 33.</p>
<p>IPSAS 21 <i>Impairment of Non-Cash-Generating Assets</i>; IPSAS 26 <i>Impairment of Cash-Generating Assets</i></p>	<p>Amendments to clarify the requirements for the impairment of revalued assets in the scope of IPSAS 17 and IPSAS 31 <i>Intangible Assets</i>.</p>	<p>Consider in next PBE Omnibus When <i>Impairment of Revalued Assets</i> (Amendments to PBE IPSAS 21 and PBE IPSAS 26) was issued in April 2017, the NZASB included amendments to PBE IPSAS 21 <i>Impairment of Non-Cash-Generating Assets</i> and PBE IPSAS 26 <i>Impairment of Cash-Generating Assets</i> to clarify that revaluations of assets are accounted for in accordance with the relevant standard (that is, on a class of assets basis for property, plant and equipment and on an individual asset basis for intangible assets). At the time, NZASB staff discussed this issue with IPSASB staff and it was</p>

IPSAS	Summary	Staff comments
		<p>agreed that the IPSASB would make equivalent amendments to IPSAS 21 and IPSAS 26.</p> <p>The amendments are the same in principle, but the wording is slightly different.</p> <p><u>We are of the view that the IPSASB's amendments are more clearly expressed and recommend that we consider making equivalent amendments to PBE IPSAS 21 and PBE IPSAS 26 in the next omnibus amendments to PBE Standards.</u></p>
<p>IPSAS 33, <i>First-time Adoption of Accrual Basis International Public Sector Accounting Standards (IPSASs)</i></p>	<p>Amendments to clarify the implementation guidance on deemed cost to make it consistent with the core principles in the Standard.</p>	<p>N/A</p> <p>There is no PBE Standard based on IPSAS 33.</p>
<p>IPSAS 40 <i>Public Sector Combinations</i></p>	<p>Amendments to add an effective date paragraph for when an entity adopts IPSAS 33. This was inadvertently omitted when IPSAS 40 was issued.</p>	<p>N/A</p> <p>We have not used the transitional provisions in IPSAS 40 in PBE IPSAS 40 <i>PBE Combinations</i>.</p>

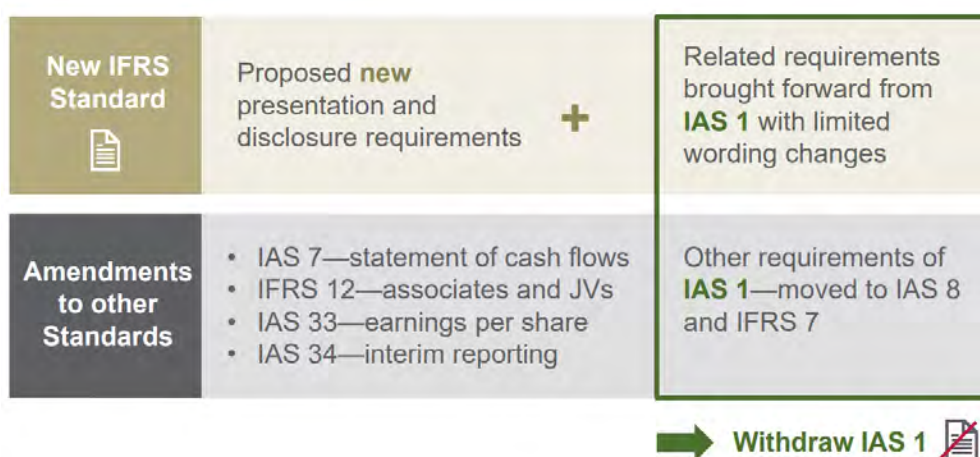
Next steps

6. We will develop an exposure draft of omnibus amendments to PBE Standards later in the year.

Date: 13 March 2020
To: NZASB Members
From: Lisa Kelsey
Subject: General Presentation and Disclosures

Purpose and introduction¹

- In December 2019 the IASB issued Exposure Draft ED/2019/7 *General Presentation and Disclosures* (the ED) under its *Primary Financial Statements* project. The ED proposes to introduce a new IFRS Standard that sets out general presentation and disclosure requirements. The proposed new standard will replace IAS 1 *Presentation of Financial Statements*. The structure of the ED is shown in the diagram below.



- Because the ED contains several new proposals, we grouped the proposals for consideration over two NZASB meetings (February and March 2020).
- At its February 2020 meeting the Board provided feedback on:
 - Objective and roles of the primary financial statements and the notes;
 - Structure of the statement of profit or loss:
 - Subtotals and categories;
 - Operating category and operating profit or loss;

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

- (iii) Integral associates and joint ventures category, and operating profit or loss and income and expenses from integral associates and joint ventures;
 - (iv) Investing category;
 - (v) Financing category and profit or loss before financing and income tax; and
 - (vi) Classification of foreign exchange differences and fair value gains and losses on derivatives and non-derivative financial instruments; and
 - (c) Statement of financial position:
 - (i) Integral and non-integral associates and joint ventures; and
 - (ii) Goodwill.
- 4. Under this agenda item we have prepared two memos for the Board's consideration. Agenda item 5.2 seeks feedback on the following proposals:
 - (a) Management performance measures (MPMs);
 - (b) EBITDA;
 - (c) Unusual income and expenses;
 - (d) Aggregation and disaggregation;
 - (e) Analysis of operating expenses;
 - (f) Statement presenting comprehensive income; and
 - (g) Effective date and transition.
- 5. Agenda item 5.3 seeks feedback on the proposed amendments to other IFRS Standards:
 - (a) IAS 7 *Statement of Cash Flows*;
 - (b) IFRS 12 *Disclosure of Interests in Other Entities*;
 - (c) IAS 33 *Earnings per Share*;
 - (d) IAS 34 *Interim Financial Reporting*;
 - (e) IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; and
 - (f) IFRS 7 *Financial Instruments: Disclosures*.
- 6. Agenda item 5.3 also seeks feedback from the Board on going concern.
- 7. In each of these memos we have a number of questions for the Board. To assist the Board in considering the questions we have provided a summary of feedback received from our outreach to date and also preliminary staff views.

Recommendations

- 8. We recommend that the Board:
 - (a) CONSIDERS the proposals outlined in agenda items 5.2 and 5.3; and
 - (b) PROVIDES feedback on the questions contained in agenda items 5.2 and 5.3.

Next steps

9. We will continue to undertake outreach activities on the ED.
10. We will bring a draft comment letter to the May Board meeting.

Attachments

- | | |
|------------------|---|
| Agenda item 5.2: | MPMs and disaggregation |
| Agenda item 5.3: | Amendments to other IFRS Standards |
| Agenda item 5.4: | IASB ED/2019/7 <i>General Presentation and Disclosures</i> (in supporting papers) |
| Agenda item 5.5: | IASB ED/2019/7 <i>General Presentation and Disclosures</i> – Basis for Conclusions (in supporting papers) |
| Agenda item 5.6 | IASB ED/2019/7 <i>General Presentation and Disclosures</i> – Illustrative Examples (in supporting papers) |
| Agenda item 5.7 | IASB ED/2019/7 <i>General Presentation and Disclosures</i> – Snapshot (in supporting papers) |



NZ ACCOUNTING
STANDARDS
BOARD

Memorandum

Date: 13 March 2020

To: NZASB Members

From: Lisa Kelsey

Subject: **MPMs and disaggregation**

Introduction¹

1. This memo sets out the information that Board members need to provide feedback on the proposals in Exposure Draft ED/2019/7 *General Presentation and Disclosures* (the ED) relating to management performance measures (MPMs) and disaggregation. Therefore, it is **not** expected that Board members have read the ED.

Recommendations

2. We recommend that the Board:
 - (a) CONSIDERS the proposals outlined in this memo; and
 - (b) PROVIDES feedback on the questions in this memo.

Structure of this memo

3. The remaining sections in this memo are as follows.
 - (a) Non-GAAP performance measures
 - (i) New Zealand
 - (ii) Internationally
 - (iii) Regulators
 - (iv) FMA Guidance
 - (b) Management Performance Measures (MPMs)
 - (c) EBITDA
 - (d) Unusual income and expenses
 - (e) Aggregation and disaggregation
 - (f) Analysis of operating expenses
 - (g) Statement presenting comprehensive income
 - (h) Effective date and transition

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

4. In each section of the memo we have summarised the proposals in the ED. The section headings include references to the relevant paragraphs from the ED and the Basis for Conclusions should Board members wish to refer to the proposals in the ED or read the IASB's considerations in developing the ED.

Non-GAAP performance measures

New Zealand

5. The XRB conducted a survey *Alternative Performance Measures (APMs): A New Zealand user-needs survey*² via an online questionnaire between November 2016 and January 2017. The aim of the survey was to better understand how APMs are viewed and whether they are effective in meeting the information needs of users of financial reports in New Zealand.
6. Some of the results are as follows.
- (a) 88.5% of respondents found APMs useful or sometimes useful.
 - (b) Respondents use APMs to clarify, understand and assess a company's business, underlying performance and future prospects.
 - (c) APMs are widely used, but also subject to a few caveats, with respondents wanting to understand why they are being used and how they have been calculated.
 - (d) Respondents felt APMs should be reconciled or explained against GAAP measures.
 - (e) 74.7% of respondents think APMs should be assured.
7. In June 2017, PwC published a research paper *An alternative picture to performance*.³ PwC set out to explore how widely APMs are used and what is being adjusted by the NZX 50 companies. PwC summarised the findings as follows.
- (a) 92% of the NZX 50 presented an adjusted GAAP profit number.
 - (b) Adjustments almost always have a favourable impact on profit.
 - (c) Companies commonly adjust for fair value movements, asset impairment and depreciation, amortisation, interest and tax.
 - (d) Descriptions of reconciling items are often too broad to understand what they relate to.
 - (e) Companies use inconsistent approaches as to where and how reconciliations are presented.

² <https://www.xrb.govt.nz/information-hub/current-research-reports/>

³ <https://www.pwc.co.nz/pdfs/an-alternative-picture-of-performance.pdf>

Internationally

8. The IASB has published on its website an academic overview of the PFS project.⁴ The article was written by IASB members Ann Tarca and Tom Scott. The article notes:

Users support enhancing the quality of adjusted earnings measures, while at the same time limiting opportunistic behaviour. A recent survey of CFA⁵ Institute members reported that the majority of respondents (63%) held the view that management's alternative performance measures should be regulated; 59% of respondents expected that standard-setters should set standards for such measures. CFA Institute members also strongly support reporting such additional performance measures in financial statements where they would be subject to audit, which should also result in enhanced internal controls.

9. The IASB is aware that many entities disclose non-GAAP/management-defined performance measures outside the financial statements – it has received feedback that users find such information useful because it provides insight into:
- (a) how management views the entity's financial performance;
 - (b) how a business is managed; and
 - (c) the persistence or sustainability of an entity's financial performance.

However, the IASB notes that users have expressed concerns about the quality of the disclosures provided about these measures. In some cases, the disclosures:

- (a) lack transparency in how the management performance measures are calculated;
- (b) lack clarity regarding why these measures provide management's view of the entity's performance;
- (c) create difficulties for users trying to reconcile the measures to the related measures included in IFRS Standards; and
- (d) are reported inconsistently from period to period.

Regulators

10. At present, in many jurisdictions the national securities regulator has provided guidance or requirements for entities that report non-GAAP measures. However, the guidance/requirements can vary across jurisdictions and the measures, along with any related disclosures (such as reconciliations back to IFRS/GAAP totals), are not normally presented within the financial statements are therefore not subject to audit.
11. In June 2016, the International Organisation of Securities Commissions (IOSCO) released a statement on non-GAAP financial measures.⁶ Many security regulators in those jurisdictions that are members of IOSCO, including the FMA, sought to align their guidance/requirements with the principles in the IOSCO statement.

⁴ <https://www.ifrs.org/academics/academic-overview-of-the-primary-financial-statements-project/>

⁵ Chartered Financial Analyst

⁶ <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD532.pdf>

FMA guidance

12. The FMA issued its guide *Disclosing non-GAAP financial information* in July 2017. The guidance replaced the *2012 Guidance note: Disclosing non-GAAP financial information* to reflect the requirements of the Financial Markets Conduct Act 2013 (FMC Act) and the FMA's findings from the review of non-GAAP financial information since 2012.
13. The 2017 guidance sets out the FMA's expectations on the use of financial information outside of the financial statements, where that information is not prepared and presented in accordance with generally accepted accounting practice (GAAP) or is presented as an alternative to statutory profit.
14. The FMA's guidance is aligned with the principles in the IOSCO statement, except where those principles were inappropriate (or inadequate) for the New Zealand market.
15. The FMA's guidance is broadly aligned with the IASB's proposals. For those Board members interested, we have provided a comparison between the IASB's proposed requirements and the FMA's guidance in [Appendix 2](#) of this memo.

Management Performance Measures (paragraphs 103–110, B76–B85, BC145–BC180)

16. The IASB is of the view that MPMs can complement measures required by IFRS Standards, providing users of financial statements with useful insight into management's view of performance and its management of the business. Requiring the disclosure of information about these measures in the financial statements would:
 - (a) ensure they are subject to the requirements in IFRS Standards regardless of the entity's jurisdiction and thus improve the discipline with which they are prepared and improve their transparency; and
 - (b) subject the disclosures, which may have previously been provided outside of the financial statements, to audit – for entities with audit requirements.
17. The IASB has heard the following concerns about including MPMs in financial statements:
 - (a) MPMs may be incomplete or biased;
 - (b) MPMs may be given undue prominence or legitimacy by including them in financial statements; and
 - (c) some adjustments made in arriving at MPMs may be difficult to audit—for example, adjustments made when an entity uses a tailormade accounting policy.
18. In response to the concerns above, the IASB noted that MPMs included in the financial statements:
 - (a) would be subject to the general requirement for information to faithfully represent what it purports to represent, which would not be met if measures were misleading;
 - (b) would rarely be presented on the face of the statement of profit or loss; and

- (c) are similar to segment measures of profit or loss in that they are based on management’s view. Segment measures of performance are included in the financial statements and are audited.

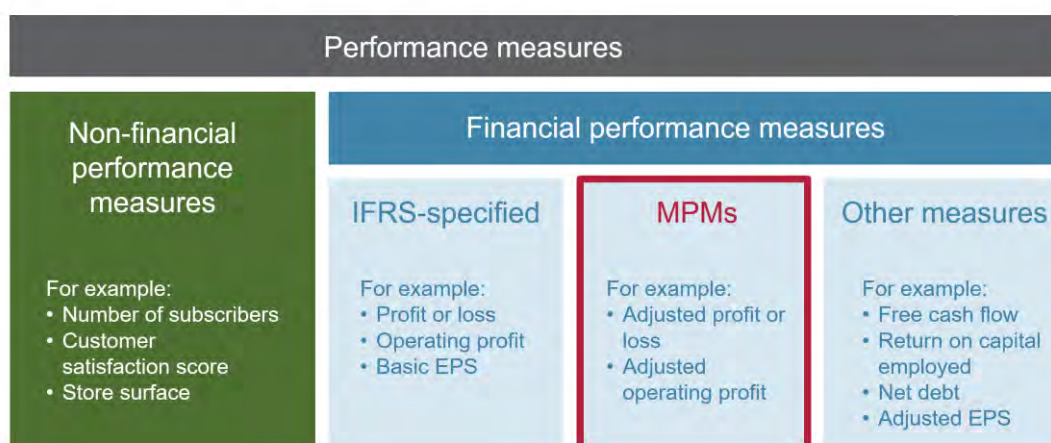
19. The IASB’s proposed definition of MPMs is shown below.

103 *Management performance measures* are subtotals of income and expenses that (see paragraphs B76–B81):

- (a) are used in public communications outside financial statements;
- (b) complement totals or subtotals specified by IFRS Standards; and
- (c) communicate to users of financial statements management’s view of an aspect of an entity’s financial performance.

- 20. The phrase ‘public communications outside financial statements’ includes the use of MPMs in management commentary, press releases or in investor presentations.
- 21. The ED does not explain when subtotals of income and expenses would or would not complement totals or subtotals specified by IFRS Standards.
- 22. Not all non-GAAP measures will be MPMs. In [Appendix 1](#) we have provided a summary of the proposed requirements and guidance from the ED on what is an MPM and what is not an MPM.
- 23. Examples of measures that can be MPMs are shown in the red box below. Non-financial performance measures (for example, customer retention rate), IFRS-specified measures and other measures (for example, currency adjusted revenue or return on capital employed) are not MPMs. The IASB has noted in the Basis for Conclusions of the ED that EBITDA measures may meet the definition of an MPM.

Which measures can be MPMs?



24. The IASB considered but rejected requiring MPMs to be based on amounts recognised and measured in accordance with IFRS Standards. The IASB noted that because MPMs will be company-specific measures, the IASB does not expect them to be comparable across companies. However, investors would be able to understand differences in how companies have calculated their measures using the proposed disclosures.

25. The IASB proposes that an entity disclose MPMs and all related information in a **single note** to the financial statements. Disclosing MPMs and the related information in a single location improves the transparency of those measures by:
- (a) providing management performance measures together with the information needed to understand those measures; and
 - (b) helping users of financial statements to identify and locate the related information.
26. The table below summarises the proposed disclosure requirements.

MPMs—proposed disclosures in the notes

<p>A description of why the MPM provides management's view of performance, including explanation of:</p> <ul style="list-style-type: none"> • how the MPM has been calculated; and • how the measure provides useful information about an entity's financial performance. 	
<p>A reconciliation of the MPM(s) to the most directly comparable subtotal or total specified by IFRS Standards</p>	<p>A statement that the MPM provides management's view of an aspect of the entity's financial performance and is not necessarily comparable with measures with a similar description provided by other entities</p>
<p>The effect of tax and non-controlling interests separately for each of the differences between the MPM and the most directly comparable subtotal or total specified by IFRS Standards.</p>	<p>If there is a change in how the MPM is calculated, explanation should be provided to help users understand the reasons for and effect of the change</p>

27. For the purposes of the required reconciliation, 'subtotal or total specified by IFRS Standards' would include:
- (a) the three new subtotals;⁷
 - (b) operating profit before depreciation and amortisation;
 - (c) gross profit and similar subtotals, such as net interest income;
 - (d) profit before tax; and
 - (e) profit from continuing operations.
- Consequently, these subtotals would not be MPMs.
28. We would like to draw the Board's attention to the following.
- (a) The proposed definition of MPMs means:
 - (i) MPMs are a subset of APMs reported by entities – MPMs are limited to subtotals of income and expenses;

⁷ The ED proposes to introduce three new defined subtotals into the statement of profit or loss. The proposed new subtotals are:

- (a) operating profit or loss;
- (b) operating profit or loss and income and expenses from integral associates and joint ventures; and
- (c) profit or loss before financing and income tax.

- (ii) only subtotals of income and expenses that management use in public communications for example, in management commentary, press releases or in investor presentations outside the financial statements will meet the definition of MPMs.
 - (iii) APMs that do not meet the definition of an MPM would still be subject to the FMA’s Guidance on presenting non-GAAP information. As noted above we have included a comparison of the FMA’s Guidance with the IASB MPM proposals (see Appendix 2).
- (b) The proposals include a requirement that MPMs shall faithfully represent aspects of the financial performance of the entity to users of the financial statements. Therefore, a management-defined performance measure that does not faithfully represent an aspect of an entity’s performance should not be included in the financial statements as an MPM. The IASB acknowledges that including information about such measures in the financial statements may increase transparency about these measures. However, the IASB believes that all information included in the financial statements should provide a faithful representation of what it purports to represent.

Relevant extracts from the ED and Basis for Conclusions are shown below.

105	<p>Management performance measures shall:</p> <ul style="list-style-type: none"> (a) faithfully represent aspects of the financial performance of the entity to users of financial statements; and (b) be described in a clear and understandable manner that does not mislead users. <p>...</p>
BC159	<p>Some stakeholders argue that there should be no restriction on when an entity can disclose information about its management performance measures. In their view, one of the main objectives of the management performance measure proposals is to provide users of financial statements with enough information to prevent them from being misled by these measures. They argue that restricting the disclosure of information about management performance measures to situations when those measures faithfully represent an aspect of an entity’s performance is inconsistent with that objective because:</p> <ul style="list-style-type: none"> (a) the requirements of IFRS Standards cannot prevent disclosure of potentially misleading measures outside the financial statements. While in some jurisdictions local law or regulation may prevent the disclosure of such measures, this is not always the case. (b) the requirement that a management performance measure must faithfully represent an aspect of an entity’s performance would prevent the disclosure of useful information about such measures in circumstances when users are most likely to be misled. (c) entities wishing to avoid the proposed disclosure requirements could do so by disclosing performance measures outside the financial statements that they believe would be assessed by their auditors or regulators as not providing a faithful representation.
BC160	<p>These stakeholders also note that IFRS 8 does not place a similar explicit restriction on the disclosure of segment information which reflects the views of management.</p>
BC161	<p>The Board acknowledges that including information about such measures in the financial statements may increase transparency about these measures. However, the Board thinks that all information included in the financial statements should provide a faithful representation of what it purports to represent. A management-defined performance measure that does not faithfully represent an aspect of an entity’s performance should not be included in the financial statements as a management performance measure.</p>

BC162 The Board also considered whether it should specifically state that management performance measures should not be misleading. The Board rejected such a proposal as unnecessary because misleading measures would not provide a faithful representation of the financial performance of the entity.

- (c) The IASB is not proposing to prohibit entities from presenting MPMs as subtotals on the face of the statement of financial performance. The IASB noted that prohibiting an entity from presenting MPMs in the statement of financial performance may prevent an entity from complying with the requirement in IFRS Standards – to present additional line items, headings and subtotals when that information is relevant to an understanding of the entity’s financial statements. However, the IASB expects that few MPMs would meet the requirements for presentation as a subtotal in the statement(s) of financial performance. To meet the requirements subtotals must:
- (i) fit into the structure of the proposed categories;
 - (ii) not disrupt the presentation of an analysis of operating expenses by nature or by function; and
 - (iii) be comprised of amounts recognised and measured applying IFRS Standards.
- (d) The IASB is proposing to prohibit entities from using columns to present MPMs on the face of the statement(s) of financial performance. This further restricts the circumstances in which such measures may be presented on the face of the statement(s) of financial performance.
- (e) An entity can have more than one MPM or may have no MPMs.
- (f) The IASB is proposing that the income tax effect and the effect on non-controlling interests is disclosed for each item disclosed in the reconciliation (between each MPM and the most directly comparable subtotal or total specified by IFRS Standards). The IASB is proposing a simplified approach for calculating the tax effect. An entity shall determine the income tax effect on the basis of a reasonable pro rata allocation of the current and deferred tax of the entity in the tax jurisdiction(s) concerned or by another method that achieves a more appropriate allocation in the circumstances.
- (g) The FMA guidance on presenting non-GAAP information notes that entities should clearly explain the reasons for presenting the non-GAAP financial information, including: (i) why the information is useful to investors; and (ii) how it is used internally by management. The proposed disclosure requirements for MPMs in the ED do not explicitly require an entity to disclose how an MPM is used internally by management. Additionally, the FMA guidance contains the following note for for-profit FMC reporting entities:
- NZ IFRS 8 *Operating Segments* (NZ IFRS 8) requires disclosure of profit or loss for segments based on the measure reported internally to management. This may be different to the profit calculated in accordance with statutory financial reporting requirements. In most cases, we expect that any non-GAAP profit information disclosed will not differ from the segment reporting disclosures in the financial statements. If non-GAAP profit information is disclosed and it differs from the segment reporting disclosures in the financial statements, an explanation should be included justifying this

difference. No explanation is required if the differences comprise only normal inter-segment eliminations or corporate expense allocations.

Feedback from outreach to date

Investors

- Requirements that provides a greater level of scrutiny and rigour around management disclosures are welcomed. However, we will still make our own decisions about how we want to treat some of this information. If there is a reconciliation back to accepted numbers (that is, IFRS figures) this is a good health check to understand what management may or may not be including. This will allow us to consider whether it is intuitively right.
- We consider MPMs communicated in our analysis. In some cases, agree with adjustments companies make, but in other cases may not. For example, may disagree that an adjusted “one-off” item is in fact one-off.
- If MPMs are presented they should be audited.
- Some investors supported having requirements that MPMs presented in the financial statements must be faithfully representative, noting concerns that the use of ‘underlying earnings’ in the retirement village industry is not a faithful representation.
- Although the reconciliation is helpful, unless there is some consistency in the adjustments between entities there will not be comparability. However, requiring this would probably be a step too far for an accounting standard.
- The proposals are unlikely to prevent companies from making adjustments that show a better outcome.
- Agree information about MPMs should be disclosed in notes to financial statements.
- Agree MPMs provide useful information.
- Noted that some retirement villages already include their “industry standard” MPM in the notes to the financial statements.
- Would like a five-year history of MPMs in the financial statements.
- The entity must clearly state what the adjustments are for.

XRAP

- Agree with bringing MPMs into the financial statements, will improve consistency and transparency.
- Referring to the definition of an MPM – Is it clear what the IASB mean by “are used in public communications” – does this include posts on social media?
- Concerns raised with auditing the requirement that MPMs presented in the financial statements must faithfully represent aspects of financial performance.

Feedback NZAuASB at February 2020 meeting

- Agree there is a demand for information about MPMs.
- Agree information about MPMs is useful.
- Noted that some entities are already providing some of the proposed information in the notes to the financial statements.
- Concerns that MPMs will be given more prominence if included on face of financial statements.
- Concerns that [the use of] MPMs may proliferate if they are included in the financial statements.

- Need to acknowledge there will be an increase in audit costs/fees to audit these proposed additional disclosures.
- Concerns that entities are just adjusting for one off negative items that have not been budgeted for.
- We can audit what is there, we can opine on consistency, i.e. entities making same adjustments year on year.
- There is currently an audit expectation gap – users think because information is included in an entity’s annual report it is audited. Bringing MPMs into the financial statements will make it clear they have been subject to audit.
- This is an area of public interest, liked the proposals. Just need to ensure there are clear criteria to audit against.
- The challenge is the restriction of MPMs to those measures that faithfully represent an aspect of an entity’s performance – how do you audit “faithfully represent”? Will this lead to disagreements on what meets the test to be allowed in the financial statements?
- If users are looking in the financial statements for MPMs, the provision outside the financial statements of non-GAAP financial performance measures may decrease.
- Neutrality may be a concern – “a justified bias”.
- The accounting standard needs to be clear it is referring to financial performance measures.
- Completeness of information – some non-GAAP measures in financial statements and some outside.
- Maybe any non-GAAP measure can come into financial statements? For example, subscriber churn or internal rate of return very important measures depending on the industry?
- Concern that an entity may have to provide disclosures within the financial statements for MPMs and disclosures outside of the financial statements for Non-GAAP (non-MPM) measures used to meet the FMA guidance. Essentially reporting/disclosing information about alternative performance measures in different places.
- A NZAuASB staff member questioned if there could be a conflict between an MPM providing ‘management’s view’ and being ‘faithful representative’.

IFRS Masterclass (Preparers)

- There was general agreement that information about MPMs should be included in the financial statements.
- No comments were made on the proposed disclosure requirements.

TRG feedback received via email in lieu of November TRG meeting

- Auditing the MPM disclosures under the proposals could be tricky. Particularly auditing disclosures that explain why an MPM provides management’s view of performance. Furthermore, there are concerns that the definition of what is meant by MPMs is not ‘tight’ enough.

TRG feedback received at 3 March meeting

For the purposes of this memo we have summarised the feedback received from TRG members on the MPM proposals. Detailed feedback can be found at agenda item 8.6 Update on TRG March 2020 meeting.

Information about MPMs as defined by the IASB should be included in the financial statements?

- Overall, TRG members agreed it made sense to include MPMs in the financial statements and subject them to audit.

- However, the following concerns were raised.
 - The requirement that “MPMs shall faithfully represent aspects of the financial performance of the entity to users of financial statements” would present challenges from an audit perspective.
 - Bringing MPMs into the financial statements would give legitimacy to those performance measures.
 - The MPM proposals may undermine the usefulness of the statement of profit or loss.
 - The requirements were not very clear (especially for an unsophisticated preparer) on what would meet the definition of an MPM

Proposed disclosure requirements for MPMs

- TRG members broadly agreed with the proposed disclosures.
- However, the following concerns were raised.
 - The cost may exceed the benefits of requiring entities to disclose the tax effect and the effect on non-controlling interests for each reconciling item.
 - The interaction of the MPM disclosure requirements with the segment reporting disclosure requirements – they wondered whether an entity that provides information about MPMs in its segment reporting note would need to repeat this information in a separate MPM note.
 - Increased costs for auditors to audit the new disclosures.

Questions for Board members

1. Management Performance Measures (ED question 11)

- (a) Do you agree that information about MPMs as defined by the IASB should be included in the financial statements? Why or why not?
- (b) Do you agree with the proposed disclosure requirements for MPMs? Why or why not? If not, what alternative disclosures would you suggest and why?
- (c) Do you have any other comments on the proposals relating to MPMs?

Preliminary staff view*Overall*

- *We agree that APMs/Non-GAAP measures can provide useful information to users of financial statements.*
- *We agree information about MPMs should be included in the financial statements and subject to audit. We agree that that the proposals will bring more transparency and discipline to the reporting of these financial performance measures.*

Definition of an MPM

- *We believe that the IASB needs to provide guidance to clarify the intended scope of ‘public communications outside the financial statement’ used in the definition of MPMs.*
 - *We note that the proposed guidance provides examples of public communications (management commentary, press releases and investor presentations). However, the guidance does not specially limited public communications to these forms of communication.*
 - *Some constituents have questioned if public communications outside the financial statement would include posts on social media made by the company.*
 - *Other constituents have raised concerns from an audit perspective, noting challenges of having to review all of an entity’s public communications for possible MPMs.*
 - *We also have concerns that the IASB has not provided guidance on the timeframe of public communications. It is not clear from the proposed definition of an MPM or associated guidance, whether an entity would need to consider all public communications during the year (such as quarterly investor communications) or only those communications relating to the interim/annual reporting period.*
- *We are unclear as to the purpose of paragraph 103(b) of the proposed definition of MPMs. This sub paragraph states that MPMs are subtotals of income and expenses that “complement totals or subtotals specified by IFRS Standards”. We question whether the IASB intended this sub paragraph to restrict MPMs to those that are subtotals of income and expense that cover the same reporting period as the financial statements (see previous comment on the scope of ‘public communications’). We recommend that the IASB consider whether paragraph 103(b) is necessary. If paragraph 103(b) is retained, then we recommend the IASB provide more guidance to clarify when a total or subtotal would and would not complement an IFRS total or subtotal.*
- *We have concerns with paragraph 105(a) which specifically restricts the disclosure of MPMs in the financial statements to those MPMs that “faithfully represent aspects of the financial performance of the entity to users of the financial statements”.*
 - *We acknowledge there is a general requirement in IFRS Standards that financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of information.*
 - *Paragraph 2.13 of the Conceptual Framework for Financial Reporting states “To be a perfectly faithful representation, a depiction would have three characteristics. It would be complete, neutral and free from error. Of course, perfection is seldom, if ever, achievable. The Board’s objective is to maximise those qualities to the extent possible.”*
 - *In our view there can be tension between:*
 - *communicating to users of financial statements management’s view of an aspect of an entity’s financial performance; and*

- *the restriction that MPMs must faithfully represent an aspect of an entity's financial performance.*
- *We note that IFRS 8 does not place a similar explicit restriction on the disclosure of segment information which reflect the views of management.*
- *The restriction in paragraph 105(a) does not prevent entities from using such MPMs outside of the financial statements.*
- *We believe that where entities are reporting such MPMs outside the financial statement, information about these MPMs is still useful to users of the financial statements and should be disclosed in the financial statements and subject to audit.*
- *Additionally, we have heard concerns from auditors and preparers about how to interpret 'faithfully represents' in the context of MPMs and subsequently how this will be audited.*
- *Therefore, we recommend that the IASB remove this restriction. We consider that paragraph 105(b) which requires MPMs to be described in a clear and understandable manner that does not mislead users will be sufficient.*
- *We acknowledge that removing paragraph 105(a) will allow MPMs that might not faithfully represent an aspect of an entity's financial performance to be included in the financial statements. However, we believe that such MPMs should not be restricted from being included in the financial statements. Information about such MPMs would provide useful information to users. For example, why the MPM presents management's view of performance and a reconciliation back to a comparable total or subtotal specified by IFRS Standards.*
- *If the IASB retains the restriction in paragraph 105(a), then we believe that further guidance is needed to clarify when an MPM faithfully represents aspects of the financial performance of the entity to users of the financial statements.*

Proposed disclosures

- *Generally, agree with the proposed disclosure requirements.*
- *However, we need to seek feedback from NZ constituents on the cost/benefit of providing the tax and non-controlling interest effects of reconciling items between an MPM and total or subtotal specified by IFRS Standards.*
- *In addition to explaining how an MPM has been calculated and how the MPM provides useful information about an entity's financial performance, we recommend that the IASB also require disclosure of how an MPM is used internally by management.*

EBITDA (paragraphs BC172–BC173)

29. At its February meeting the Board considered proposals in the ED to introduce requirements for entities to present three new defined subtotals into the statement of profit or loss. Some Board members questioned whether the IASB had considered earnings before interest, tax, depreciation and amortisation (EBITDA) as a required subtotal.
30. The IASB has not propose to define EBITDA. The IASB considered, but rejected, describing operating profit or loss before depreciation and amortisation as EBITDA. The table below includes the IASB's rationale for this decision.

Extract from Basis for Conclusions on the ED

...

BC172 The Board also considered whether to define earnings before interest, tax, depreciation and amortisation (EBITDA). However, the Board noted that, although EBITDA is one of the most commonly used measures in communications with users of financial statements, it is not used in some industries such as finance. Furthermore, users have no consensus about what EBITDA represents, other than it being a useful starting point for various analyses. Its calculation is diverse in practice. Consequently, EBITDA measures may meet the definition of management performance measures.

BC173 The Board also considered whether a measure calculated as operating profit or loss before depreciation and amortisation would provide similar information to many of the EBITDA measures that are currently provided. However, the Board concluded it should not describe operating profit or loss before depreciation and amortisation as EBITDA. To do so would imply that operating profit or loss is the same as earnings before interest and tax which is not the case because operating profit or loss does not include, for example, income from investments or from equity-accounted associates and joint ventures. In other words, the Board was concerned about the difference between what the measure represents and the meaning of the EBITDA acronym. However, as discussed in paragraph BC171, the Board has included operating profit or loss before depreciation and amortisation in the list of IFRS specified subtotals. Consequently, an EBITDA measure equal to that amount would not be a management performance measure.

...

31. We would like to draw the Board's attention to the following.
- (a) EBITDA is a commonly used measure in communications with users of financial statements.
 - (b) EBITDA is also used for other purposes, for example in sale and purchase agreements, or company valuations.
 - (c) The calculation of EBITDA is diverse in practice, particularly in relation to the interest component.
 - (d) An EBITDA measure used in public communications outside of the financial statements could meet the definition of an MPM.
 - (e) In certain circumstance, albeit rare, it may still be possible for entities to present an EBITDA subtotal in the statement of profit or loss. Any such subtotal would also need to comply with the other proposed requirements including classifying income and expenses in the required categories and presenting an analysis of operating expenses by nature.
 - (f) Operating profit or loss before depreciation and amortisation is included in the list of IFRS specified subtotals (i.e. not an MPM).

Feedback from outreach to date*Investors*

- Would like an EBITDA subtotal to be included – in theory could possibly be able to calculate but would like for the subtotal to be readily available.

TRG feedback received via email in lieu of November TRG meeting

- Support, in principle, introducing some common sub-totals, as alternatives to EBIT and EBITDA, particularly given the lack of consistency in calculation of these in relation to interest (i.e. sometimes included, sometimes not). Despite the apparent inconsistency in calculation of EBIT/DA these terms are widely used by many and the market will need some time to adjust to new measures.

- Agree not to define EBITDA as it has no conceptual basis.
- Understand the IASB's rationale for not defining EBITDA. However, note that this is a number that users always want, so wouldn't it be preferable to define it for comparability purposes for users?

TRG feedback received at 3 March meeting

- TRG members agreed that the IASB would not be able to come up with a definition of EBITDA that would be satisfactory to everyone.
- TRG members noted that the proposals allowed for the subtotal operating profit before depreciation and amortisation – this may become the new EBITDA.

Question for Board members

2. EBITDA (ED question 12)

The IASB has not proposed requirements relating to EBITDA.

Do you agree? Why or why not? If not, what alternative approach would you suggest and why?

Preliminary staff view


- *We agree with not proposing requirements relating to EBITDA. In our view the calculation of EBITDA is diverse in practice, particularly in relation to the interest component. It would be difficult for the IASB to come up with a globally accepted definition of EBITDA.*
- *However, as EBITDA is such a commonly used measure, we would suggest that the IASB provides guidance to clarify when EBITDA would be able to be presented in the statement of profit and loss.*
- *We support the IASB's proposal that operating profit before depreciation and amortisation is not an MPM.*

Unusual income and expenses (paragraphs 100–102, B67–B75, BC122–BC144)

32. The IASB has observed that many entities disclose unusual or similarly described expenses (and a few disclose unusual income). However, the way entities disclose this information varies significantly and it is often not clear how or why items have been identified as unusual.
33. From a recent desktop review of a sample of NZX 50 entities, we observed the use of the following terms when describing expenses: non-recurring items, abnormal items, significant items and one-off items.

34. In 2017 the IASB issued a Discussion paper *Disclosure Initiative—Principles of Disclosure*. The Discussion paper explored how to improve the communication effectiveness of disclosures. The IASB received the following feedback in relation to the disclosure of unusual items.
- (a) Many users want requirements for the disclosure of unusual income or expenses because:
 - (i) the separate presentation or disclosure of unusual or infrequent income or expenses provides information that is useful in making forecasts about future cash flows; and
 - (ii) definitions and requirements developed by the IASB could make such income or expenses more transparent and comparable across entities and could reduce entities' opportunistic classification of expenses as unusual.
 - (b) However, a few users commented that defining unusual or infrequent income and expenses may be difficult because they are entity-specific and identifying them would involve significant judgement.
 - (c) Many respondents that are not users of financial statements said that the IASB should not develop definitions for 'unusual' or 'infrequent' income or expenses because those items vary across entities and industries and their identification involves significant judgement. They suggested that the Board could instead consider developing general requirements for the disclosure and faithful representation of such items, for example, requiring them to be classified and presented consistently over time and labelled in a clear and non-misleading way.
35. Responding to the above feedback the IASB is of the view that defining unusual items as income or expenses with limited predictive value:
- (a) addresses the needs of users of financial statements for information about items that are unlikely to persist and hence have limited predictive value; and
 - (b) helps preparers of financial statements identify unusual items by providing them with a concept that underpins the need to identify unusual items.
36. The definition of unusual income and expenses is set out in the table below.

Unusual income and expenses

<p>Definition</p> 	<p>Unusual income and expenses are income and expenses with limited predictive value. Income and expenses have limited predictive value when it is reasonable to expect that income or expenses that are similar in type and amount will not arise for several future annual reporting periods.</p> <p>Income and expenses from the recurring remeasurement of items measured at a current value would not be expected to be classified as unusual</p>
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37. The table below contains the relevant paragraphs from the ED dealing with the disclosure requirements for unusual income and expenses.

Unusual income and expenses

- 100 *Unusual income and expenses* are income and expenses with limited predictive value. Income and expenses have limited predictive value when it is reasonable to expect that income or expenses that are similar in type and amount will not arise for several future annual reporting periods.
- 101 An entity shall, in a single note that includes all unusual income and expenses, disclose (see paragraphs B67–B75):
- (a) the amount of each item of unusual income or expense recognised in the reporting period;
 - (b) a narrative description of the transactions or other events that gave rise to that item and why income or expenses that are similar in type and amount are not expected to arise for several future annual financial reporting periods;
 - (c) the line item(s) in the statement(s) of financial performance in which each item of unusual income or expense is included; and
 - (d) an analysis of the included expenses using the nature of expense method, when an entity presents an analysis of expenses in the statement of profit or loss using the function of expense method.
- 102 Income and expenses from the recurring remeasurement of items measured at a current value are expected to change from period to period. They would not normally be classified as unusual income and expenses (see paragraph B72).

38. We would like to draw the Board's attention to the following.
- (a) The IASB proposes that information about unusual income and expenses should be disclosed in the notes and not presented on the face of the statement(s) of financial performance.
 - (b) The IASB notes that its proposal for unusual income and expenses is different from the requirement for presentation of extraordinary items that was removed from IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in 2003. Extraordinary items were defined as clearly distinct from the ordinary activities of an entity and were presented in their own category after tax, separately from profit or loss from ordinary activities. Unusual income and expenses, on the other hand, are not separately classified in the statement(s) of financial performance from 'usual' income and expenses.
 - (c) The IASB considered specifying that information about unusual items should be neutral but rejected this as unnecessary because neutrality applies to all items included in the financial statements.
 - (d) The IASB did not indicate a specific period over which an entity should assess whether it is reasonable to expect that similar income or expenses will not arise.
 - (e) The IASB recognises that, when assessing whether income and expenses are unusual, it may be helpful to consider the nature of transactions or other events that gave rise to the income or expenses, for example, a big earthquake. However, a big earthquake may give rise to increased operating costs that are expected to arise for a number of years, and as such are not unusual expenses.
 - (f) The IASB proposes that an entity provides a description of the transactions or other events that gave rise to unusual income and expenses. The IASB considers this is useful

because it enables users to understand what caused the unusual income or expense and to assess the entity's classification of the income and expense as unusual.

- (g) The IASB proposes that recurring measurements of items measured at current value would not normally be classified as unusual, for example, gains or losses from fair value measurements.
39. The IASB noted that companies may choose to adjust for unusual items in the calculation of their MPMs. However, the IASB proposes that all companies should disclose all unusual items, regardless of whether they identify any MPMs or how their measures are calculated.

Feedback from outreach to date

Investors

- Agree information about unusual items would be useful.
- Support anything that improves the transparency and the ability to pull information apart and work out what is going on.
- Agree information about unusual items should be included in the notes to the financial statements.
- Would also find information about tax and NCI impacts useful.

XRAP

- Agree with intent of the proposals, concerns that we are adding more disclosures to the financial statements.

IFRS Masterclass

- Mixed support 50/50 split – some agreement that it would provide useful information, however, concerns with costs of making the disclosure, specifically the judgements in determining if an item is an unusual income or expense.
- Also, questions regarding prior year comparatives – if an item was thought to be unusual in prior year, but was found to be reoccurring, would you need to restate disclosure in the current year.

NZAuASB feedback received at February 2020 meeting

- Need to be very clear that it is the preparer's responsibility to identify all unusual income and expenses.
- Completeness of the information is an issue.
- Yes, put in notes and analysts can then make own adjustments.
- Are we going back to extraordinary items?

TRG feedback received at 3 March meeting

- TRG members expressed concerns with the definition of unusual items, in particular "limited predictive value" and "several future periods". These terms are very subjective, and members could foresee disagreements between directors and auditors. Some members were also concerned with potential litigation at a future date as a result of items not being disclosed.
- Some TRG member commented that there is already a requirement to disclose material events and transactions and entities should be disclosing these items now. One TRG member suggested that the current requirements around the disclosure of material items/significant judgements could be strengthened rather than defining 'unusual'.
- TRG members could see the logic for requiring the disclosure in a single note and thought the disclosures would be useful information to have. However, some members thought the proposals would be burdensome on preparers, directors and auditors.
- Another TRG member commented that ensuring the completeness of the disclosure could be challenging from a preparer and auditor perspective – although they appreciated materiality would apply.
- Another member would prefer to see more granularity on the face of the statement of profit and loss.
- One TRG member thought it would be challenging for a start up to have to determine what items of income and expense are unusual.

Question for Board members**3. Unusual income and expenses (ED question 10)**

- (a) Do you agree with the proposals to require all entities to disclose unusual income and expenses in a single note? Why or why not?
- (b) Do you agree with the proposed definition of unusual income and expenses? Why or why not? If not, what alternative approach would you suggest and why?
- (c) Do you agree with the proposed disclosure requirements relating to unusual income and expenses? Why or why not? If not, what alternative approach would you suggest and why?

Preliminary staff view

- *We agree that the disclosure of information about unusual income and expenses would provide users with useful information. However, we have concerns with the proposed definition of unusual income and expenses. We consider that the proposed definition is highly subjective, particularly the references to “limited predictive value” and “several future annual reporting periods”.*
- *We believe that the subjectively involved in determining unusual income and expenses would place undue costs on preparers to identify all material unusual income and expenses. Additionally, the subjectively involved would make it challenging for auditors to audit an entity’s disclosure of unusual income and expenses, particularly the completeness of the disclosure.*
- *Staff have not yet formed a preliminary view, two options that the staff are considering are:*
 - *recommend that the IASB undertakes further work on the definition of unusual income and expenses; or*
 - *rather than seeking to define and require disclosure of unusual income and expenses, recommend that the IASB should develop general requirements for when an entity describes income and expenses as being ‘unusual’, ‘abnormal’, ‘infrequent’ or another similar term. For example, requiring them to be classified and presented consistently over time or labelled in a clear and non-misleading way.*
- *The ED does not propose to carry forward to a new general presentation and disclosures standard the requirement in paragraph 97 of IAS 1 for an entity to separately disclose the nature and amount of income and expenses that are material. We recommend that the IASB includes this paragraph in a new general presentation and disclosures standard.*

Aggregation and disaggregation (paragraphs 25–28, B5–B15, BC21–BC27)

- 40. The proposals on aggregation and disaggregation respond to feedback the IASB received from users of financial statements that financial statements do not always include information that is appropriately aggregated or disaggregated. For example, a company might disclose a large ‘other’ expenses line with no information provided to help users understand what the line item comprises. On the other hand, some users are also concerned that some companies disclose too much detail, obscuring material information.
- 41. The IASB’s proposals include principles for aggregation and disaggregation, supporting definitions and specific requirements. The principles state, in summary, that items with shared

characteristics should be grouped together and those that do not share characteristics should be separated.

Proposed principles for aggregation and disaggregation, and application of proposed principles	
Proposed principles	Application of proposed principles
<ul style="list-style-type: none"> • items shall be classified and aggregated on the basis of shared characteristics; • items that do not share characteristics shall not be aggregated; and • aggregation and disaggregation in the financial statements shall not obscure relevant information or reduce the understandability of the information presented or disclosed, 	<ul style="list-style-type: none"> • identify the assets, liabilities, equity, income and expenses that arise from individual transactions or other events; • classify assets, liabilities, equity, income and expenses into groups based on their characteristics (for example, their nature, their function, their measurement basis or another characteristic) resulting in the presentation in the primary financial statements of line items that share at least one characteristic; and • separate the line items presented in the primary financial statements on the basis of further characteristics resulting in the disclosure of items in the notes, if those items are material.
<p>When presenting information in the primary financial statements or disclosing information in the notes, the description of the items shall faithfully represent the characteristics of those items.</p>	

42. The IASB acknowledges that an entity may need to aggregate immaterial items with dissimilar characteristics to avoid obscuring relevant information. If these items cannot be described in a manner that faithfully represents the dissimilar items, an entity shall disclose in the notes information about the aggregated items.
43. From a recent desktop review of NZX 50 entities, we observed that many entities present a line item for other expense in the statement of profit or loss, less than half of those entities provide a full disaggregation in the notes to the financial statements.

Feedback from outreach to date

Investors

- *Concerns with companies using the description of “other” when describing expenses, without providing appropriate disaggregation.*
- *One Investor would like a disaggregation of costs into fixed costs and variable costs as this is useful information for forecasting future cashflows.*

TRG feedback received via email in lieu of November TRG meeting

- Support introducing enhanced requirements re: disaggregation to provide users with more granular information. However, there didn’t seem to be any specific proposals in the paper on how the requirements will differ from the current requirements re disaggregation.

TRG feedback received at 3 March meeting

- One TRG member questioned how the principles proposed are different from the existing principles/requirements in IAS 1, and questioned what is the IASB trying to fix?

- Another member commented that the IASB was trying to address the lack of disclosures provided around “other expense” line items in the financial statements.

Question for Board members

4. Aggregation and disaggregation of information (ED question 8(b))

Do you agree with the proposals relating to the aggregation and disaggregation of information? Why or why not? If not, what alternative approach would you suggest and why?

Preliminary staff view

- *We have heard concerns from investors that some companies use the label “other” when describing expenses without providing information to help them understand what those items comprise. We have observed from a desktop review of NZX 50 entities that many of those entities present an ‘other expenses’ line item in their statement of profit or loss.*
- *Therefore, we support the proposals to provide guidance on the aggregation and disaggregation of information.*
- *As noted earlier in the memo, the IASB is not proposing to carry forward paragraph 97 from IAS 1 “when items of income and expense are material, an entity shall disclose their nature and amount separately”. We believe that the IASB should include this paragraph in a new general presentation and disclosures standard.*
- *Additionally, as discussed further in agenda paper 5.3, the IASB is not proposing to carry forward the paragraphs in IAS 1 relating to the definition of materiality and associated guidance into a new general presentation and disclosures standard (the IASB is proposing to move these paragraphs this to IAS 8).*
- *The IASB has acknowledged in the ED “in the notes, it is the concept of materiality that drives aggregation and disaggregation”. The IASB state in the ED that “to achieve the objective of financial statements, items that have dissimilar characteristics shall be disaggregated into component parts when the resulting information is **material** (emphasis added).*
- *We agree that the concept of materiality and materiality judgements play a critical role in the presentation and disclosure of information in financial statements.*
- *We believe the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard. Therefore, we recommend that the Board includes in its submission a general comment that the IASB give greater emphasis to the concept of materiality in a new general presentation and disclosures standard.*

Analysis of operating expenses (paragraphs 68–72, B45–B48, BC109–BC116)

44. Entities are currently required to analyse expenses in the statement of profit or loss either ‘by nature’ (showing line items such as employee benefits and depreciation) or ‘by function’ (showing line items such as cost of sales and general and administrative expenses). Both methods can provide useful information. However, investors have raised concerns with the IASB that useful information is lost because, in practice, entities may not choose the method that provides the most useful information in their circumstances and many entities use a mixture of both methods. In addition, some investors have told the IASB they need

information about the nature of operating expenses for all companies because expenses by nature are easier to forecast than expenses by function.

45. From a recent desktop review of NZX 50 entities, we observed that many entities use a mixture of both methods.
46. In response to the feedback above, the IASB is proposing to strengthen the proposals for the presentation of operating expenses. We have provided a summary of the proposals in the table below.

Disaggregation—operating expenses—summary of proposals	Notes
<ul style="list-style-type: none"> Use method for analysis of operating expenses (by nature or by function) that provides the most useful information (not a free choice) 	<ul style="list-style-type: none"> IAS 1 currently requires an entity to choose a method that is reliable and more relevant Proposals would remove option to present analysis of expenses in the notes only
<ul style="list-style-type: none"> To help assess which method is most useful, proposals include a set of factors to consider: <ul style="list-style-type: none"> Which method provides the most useful information to users of FS about the key components or drivers of the entity’s profitability Which method most closely represents the way business is managed and how management reports internally Industry practice If allocation to function arbitrary shall use nature 	<ul style="list-style-type: none"> The IASB has noted the selection is not a free choice
<ul style="list-style-type: none"> Entities shall not mix the methods (except for the line items required by paragraph 65)⁸ 	<ul style="list-style-type: none"> In practice entities use a mixture of both methods
<ul style="list-style-type: none"> If use by function shall present cost of sales separately from other expenses 	<ul style="list-style-type: none"> IAS 1 currently identifies this as a minimum disclosure if function method used
<ul style="list-style-type: none"> Disclose analysis of total operating expenses by nature in the notes if analysis by function is presented in the statement of profit or loss 	<ul style="list-style-type: none"> IASB considered and rejected a more comprehensive approach – requiring entities to analyse each functional line item by nature IAS 1 currently requires an entity classifying by function to disclose additional information on the nature of expenses, including depreciation and amortisation expenses and employee benefits expense

⁸ Proposed paragraph 65 [IAS 1.82] lists line items (in addition to items required by other IFRS Standards) that an entity shall present in the statement of profit or loss (these items are by nature).

Disaggregation—operating expenses—summary of proposals	Notes
<ul style="list-style-type: none"> • Shall present line items required by paragraph 65 regardless of the method used 	<ul style="list-style-type: none"> • The expense line item required to be presented by paragraph 65 are by nature

Feedback from outreach to date

IFRS Masterclass

- Feedback from participants indicated confusion about the method they currently used, we got a sense that a mixture of the two methods was probably been applied in practice.
- One participant who seems to be presenting by function indicated he thought it would be costly to recut by nature and reconcile back.

TRG feedback received via email in lieu of November TRG meeting

- Analysis of operating expenses by function or by nature (ED para 68 and B45) – this is currently very poorly understood, and I am not sure that the ED goes far enough in explaining requirements properly.

TRG feedback received at 3 March meeting

- One TRG member suggested it would be helpful if the IASB defined cost of goods sold (COGS) for those entities that present an analysis of expenses by function (some entities include salary costs of employees in COGS and some do not).
- TRG members acknowledged that in practice most entities present expenses using a mixture of the by nature and by function methods.
- Most TRG members did not see a problem with using a mixture, as long as it was not materially misleading. Another member just wanted the most meaningful presentation. The decision to present expenses by function or by nature should be left up to the entity.
- TRG members thought it would be onerous to require a Tier 2 entity that presents an analysis of expenses by function on the face of the statement of profit or loss, to disclose an analysis of expenses by nature in the notes.
- One TRG member commented maybe the IASB should just require disclosure by nature in the statement of profit or loss.

Question for Board members

5. Analysis of operating expenses (ED question 9)

Do you agree with the proposals relating to the analysis of operating expenses? Why or why not? If not, what alternative approach would you suggest and why?

Preliminary staff view

- *We have concerns with the practical application of the requirement to disclose analysis of **total** operating expenses by nature in the notes if analysis by function is presented in the statement of profit or loss. Some entities may not have the ability to be able to analyse operating expenses by more than one method in their accounting/reporting systems. Therefore, these entities would need to incur additional costs to track operating expenses using another method outside of their current systems.*

- *We believe that the IASB should consider removing the distinction between nature and function analysis. In practice we observe that it is common for companies to provide a mixed method of analysis, additionally we note that despite paragraph B46 which states that an entity shall not use a mixture of the nature of expense method and the function of expense method. Paragraph B47 states that an entity shall present the line items required by paragraph 65 (which are by nature) Therefore, in practice paragraph B47 is requiring a mixture of methods for an entity analysing operating expenses by function.*

Statement presenting comprehensive income (paragraphs 73–81, B49–B52, BC117–BC118)

47. IAS 1 requires income and expenses included in other comprehensive income to be categorised into income and expenses that may be reclassified (recycled) to profit or loss in subsequent periods and items that are permanently reported outside profit or loss and will not be reclassified. This creates two categories of income and expenses included in other comprehensive income.
48. To increase the understandability of amounts included in other comprehensive income, the IASB proposes to create more descriptive labels for these two categories of other comprehensive income.

Categories of income and expenses included in other comprehensive income	
Current labels	Proposed labels
will not be reclassified subsequently to profit or loss.	remeasurements permanently reported outside profit or loss.
will be reclassified to subsequently to profit and loss when specific conditions are met.	income and expenses to be included in profit or loss in the future when specific conditions are met

Preliminary staff view

- *We do not believe that the proposed labels will significantly improve the communication of information about income and expenses included in other comprehensive income (OCI).*
- *We believe to improve the communication of information about income and expenses included in OCI the IASB needs to clearly describe the distinction between profit or loss and OCI and the role of recycling.*

Question for Board members

6. Would the Board like to include a comment in their submission encouraging the IASB to undertake a specific project on OCI?

Effective date and transition (paragraphs 117–118, BC184)

49. The IASB is proposing an effective date of 18–24 months from the date of publication. The IASB is also proposing that the standard is applied retrospectively.
50. The IASB is proposing that the presentation of headings and subtotals in condensed financial statements provided in interim financial report(s) starts in the first year an entity applies draft IFRS X *General Presentation and Disclosures*, for example, if the effective date was 1 January

202x, and entity would be required to present the headings and subtotals in financial statements provided in interim financial reports by 30 June 202x (see paragraph 118 and BC184).

Extracts from ED:

118 In the first year of application of this [draft] Standard an entity shall present each of the headings and subtotals required by paragraphs 60–64 of this [draft] Standard in condensed financial statements provided in interim financial reports, despite the requirements in paragraph 10 of IAS 34. An entity shall apply the requirements in paragraph 10 of IAS 34 for condensed financial statements after its first set of annual financial statements prepared in accordance with this [draft] Standard has been issued.

Extract from IAS 34:

10 If an entity publishes a set of condensed financial statements in its interim financial report, those condensed statements shall include, at a minimum, each of the headings and subtotals that were included in its most recent annual financial statements and the selected explanatory notes as required by this Standard. Additional line items or notes shall be included if their omission would make the condensed interim financial statements misleading.

Question for Board members

7. Effective date and transition

Does the Board agree with the proposed effective date and transition requirements? Why or why not? If not, what alternative approach would you suggest and why?

Preliminary staff view

- *We have not identified any concerns with the proposals relating to the effective date.*
- *We need to seek feedback from NZ constituents on the cost/benefit of providing the subtotals in condensed financial statements provided in interim financial reports prior to the preparation of the first set of annual financial statements under the new proposals.*

Appendix 1 Identifying management performance measures

Summary of the proposed requirements and guidance on what is an MPM and what is not an MPM	
YES MPM	Not MPM
<p>103 Management performance measures are subtotals of income and expenses that (see paragraphs B76–B81):</p> <p>(a) are used in public communications outside financial statements;</p> <p>(b) complement totals or subtotals specified by IFRS Standards; and</p> <p>(c) communicate to users of financial statements management’s view of an aspect of an entity’s financial performance.</p> <p>...</p> <p>105 Management performance measures shall:</p> <p>(a) faithfully represent aspects of the financial performance of the entity to users of financial statements; and</p> <p>(b) be described in a clear and understandable manner that does not mislead users.</p> <p>...</p> <p>109 A subtotal included in the statement(s) of financial performance applying paragraph 42 may be a management performance measure (see paragraph B81).</p> <p>...</p> <p>42 [IAS 1.85, 55] This [draft] Standard requires minimum line items and subtotals to be presented in the statement(s) of financial performance and the statement of financial position. An entity shall present additional line items (including by disaggregating required minimum line items), headings and subtotals in the statement(s) of financial performance and the statement of financial position when such presentations are relevant to an understanding of the entity’s financial performance or financial position.</p> <p>...</p> <p>B81 A subtotal presented in the statement(s) of financial performance to comply with paragraph 42 may meet the definition of a management performance measure. When such a subtotal meets that definition, an entity shall disclose all the information required by paragraph 106.</p>	<p>104 Subtotals specified by IFRS Standards that are not management performance measures include:</p> <p>(a) a total or subtotal required by paragraphs 60 and 73;</p> <p>(b) gross profit or loss (revenue less cost of sales) and similar subtotals (see paragraph B78);</p> <p>(c) operating profit or loss before depreciation and amortisation;</p> <p>(d) profit or loss from continuing operations; and</p> <p>(e) profit or loss before income tax.</p> <p>...</p> <p>60 [IAS 1.81A partial] Subject to paragraph 64, an entity shall present the following totals or subtotals in the statement of profit or loss:</p> <p>(a) operating profit or loss;</p> <p>(b) operating profit or loss and income and expenses from integral associates and joint ventures (see paragraph 53);</p> <p>(c) profit or loss before financing and income tax (see paragraphs 63–64); and</p> <p>(d) profit or loss.</p> <p>...</p> <p>73 [IAS 1.81A partial] An entity shall present in the statement presenting comprehensive income totals for:</p> <p>(a) profit or loss;</p> <p>(b) total other comprehensive income; and</p> <p>(c) comprehensive income, being the total of profit or loss and other comprehensive income.</p> <p>...</p> <p>B78 In accordance with paragraph 104(b) subtotals similar to gross profit are not management performance measures. A subtotal is similar to gross profit when it represents the difference between a type of revenue and directly related expenses incurred in generating that revenue. Examples include:</p> <p>(a) net interest income;</p> <p>(b) net fee and commission income;</p>

Summary of the proposed requirements and guidance on what is an MPM and what is not an MPM	
YES MPM	Not MPM
	<ul style="list-style-type: none"> (c) insurance service result; (d) net financial result (investment income minus insurance finance expenses); and (e) net rental income.

Appendix 2

Comparison of FMA’s Guidance on presenting non-GAAP financial information with IASB’s proposals for disclosure of information on MPMs

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
Defining the non-GAAP financial information	<i>Definition</i> Entities should define non-GAAP financial information and support it with a clear explanation of the basis of calculation.	(a) a description of why the MPM communicates management’s view of performance including an explanation of: (i) how the MPM is calculated; and (ii) how the measure provides useful information about the entity’s performance; <i>(Paragraph 106(a))</i> Paragraph 106(a)(i) requires an explanation of how a MPM is calculated. To comply with this requirement an entity shall explain the specific principles, bases, conventions, rules and practices it applies in calculating its MPMs. <i>(Paragraph B84)</i>	Requirements are essentially the same. The IASB is defining MPMs. The proposed definition of MPMs is shown below. MPMs are subtotals of income and expenses that (see paragraphs B76–B81): (a) are used in public communications outside financial statements; (b) complement totals or subtotals specified by IFRS Standards; and (c) communicate to users of financial statements management’s view of an aspect of an entity’s financial performance. <i>(Paragraph 103)</i>
	<i>Clear labelling</i> Entities should clearly label non-GAAP financial information in a way that distinguishes it from GAAP financial information. The term or label should accurately describe and reflect the non-GAAP financial information. For example, it	MPMs shall: (a) faithfully represent aspects of the financial performance of the entity to users of financial statements; and (b) be described in a clear and understandable manner that does not mislead users <i>(Paragraph 105)</i>	By definition an MPM is not a total or subtotal specified by IFRS Standards (therefore it is a non-GAAP measure). The FMA guidance goes into more detail about the term or label used. Requirements are essentially the same.

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
	is not appropriate to label a measure as EBITDA if it excludes items which are not interest, tax, depreciation or amortisation. The term or label should not cause confusion with GAAP information.		
	<i>Use of non-GAAP financial information</i> Entities should clearly explain the reasons for presenting the non-GAAP financial information, including: <ul style="list-style-type: none"> • why the information is useful to investors • how it is used internally by management⁹. 	(a) a description of why the MPM communicates management’s view of performance including an explanation of: <ul style="list-style-type: none"> (i) how the MPM is calculated; and (ii) how the measure provides useful information about the entity’s performance; <i>(Paragraph 106(a))</i> In some cases, one or more of an entity’s MPMs may be the same as part of the operating segment information disclosed by the entity in applying IFRS 8. In such cases, the entity may disclose the required information about those MPMs in the same note that it uses to disclose information about its operating segments provided the entity either:	Requirements are essentially the same. The FMA does require a description of how the measure is used internally by management.

⁹ Note for for-profit FMC reporting entities: NZ IFRS 8 *Operating Segments* (NZ IFRS 8) requires disclosure of profit or loss for segments based on the measure reported internally to management. This may be different to the profit calculated in accordance with statutory financial reporting requirements. In most cases, we expect that any non-GAAP profit information disclosed will not differ from the segment reporting disclosures in the financial statements. If non-GAAP profit information is disclosed and it differs from the segment reporting disclosures in the financial statements, an explanation should be included justifying this difference. No explanation is required if the differences comprise only normal inter-segment eliminations or corporate expense allocations.

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
		(a) includes in that note all of the information required by paragraph 106 for MPMs; or (b) provides a separate note that includes all of the information required for MPMs. (Paragraph B83)	
	Entities should make a statement that the non-GAAP financial information does not have a standardised meaning prescribed by GAAP and therefore may not be comparable to similar financial information presented by other entities. You should also disclose whether the non-GAAP financial information has been subject to audit or review ¹⁰ .	An entity shall disclose information about any management performance measures in a single note to the financial statements. That note shall include a statement that the management performance measures provide management’s view of an aspect of the entity’s financial performance and are not necessarily comparable with measures sharing similar descriptions provided by other entities. In addition, for each management performance measure an entity shall disclose in the notes (see paragraphs B82–B85): (Paragraph 106)	Requirements are essentially the same. Because the disclosure will be within the financial statements the information will be subject to audit.
Prominence	<ul style="list-style-type: none"> Entities should not present non-GAAP financial information with undue and greater prominence, emphasis or authority than the 	An entity shall not use columns to present management performance measures in the statement(s) of financial performance. (Paragraph 110)	The IASB is not prohibiting entities from presenting management performance measures as a subtotal in the statement of financial performance. But it is unlikely that

¹⁰ We do not consider non-GAAP financial information to have been subject to audit or review merely by virtue of the adjustment or component being taken from audited or reviewed financial statements.

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
	<p>most directly comparable GAAP financial information.</p> <ul style="list-style-type: none"> When presenting non-GAAP financial information, entities should not in any way confuse or obscure presentation of GAAP financial information. 	<p>All information required to be disclosed about management performance measures shall be included in a single note. (paragraph B82)</p> <p>When an entity presents additional subtotals in accordance with paragraph 42, those subtotals shall:</p> <ul style="list-style-type: none"> (a) comprise line items made up of amounts recognised and measured in accordance with IFRS Standards; (b) be presented and labelled in a manner that faithfully represents the line items that constitute the subtotal, making the subtotal clear and understandable; (c) be consistent from period to period, in accordance with paragraph 33; and (d) not be displayed with more prominence than the subtotals and totals required by IFRS Standards. <p>(Paragraph 43)</p>	<p>many MPMs will meet the requirements to be presented in the statement of financial performance. If they do then the requirements in paragraph 43 will apply and any subtotal can not be displayed with more prominence than the subtotal required by IFRS Standards.</p> <p>The IASB is prohibiting entities from using columns to present an MPM in the statement(s) of financial performance. This further restricts the circumstances in which such measures may be presented in the statement(s) of financial performance helping to address the concerns of some stakeholders that doing so would give these measures undue prominence.</p>
Reconciliation	<ul style="list-style-type: none"> Entities should provide a reconciliation from the non-GAAP financial information to the most directly comparable GAAP financial information¹¹. 	<ul style="list-style-type: none"> (b) a reconciliation between the management performance measure and the most directly comparable subtotal or total included in paragraph 104; <p>(Paragraph 106(b))</p>	Requirements are essentially the same.

¹¹ An entity may disclose a reconciliation in each document where non-GAAP financial information is disclosed, or, make a direct reference to where this information is available. If an entity provides the reconciliation by reference, the reconciliation must be easily and readily accessible.

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
	<ul style="list-style-type: none"> Entities should itemise and explain each significant adjustment separately. 	<p>(c) the income tax effect and the effect on non-controlling interests for each item disclosed in the reconciliation required by paragraph 106(b); and</p> <p>(d) how the entity determined the income tax effect required by paragraph 106(c).</p> <p>An entity shall determine the income tax effect required by paragraph 106(c) on the basis of a reasonable pro rata allocation of the current and deferred tax of the entity in the tax jurisdiction(s) concerned or by another method that achieves a more appropriate allocation in the circumstances. <i>(Paragraph 107)</i></p>	<p>The IASB noted that MPMs disclosed in the notes to the financial statements would need to comply with the general requirements for information included in financial statements. That is:</p> <p>(a) the MPM must faithfully represent the aspect of financial performance of the entity it purports to represent;</p> <p>(b) the disclosures supporting the MPM must comply with the proposed guidance on aggregation and disaggregation, for example, when disclosing reconciling items;</p> <p>(c) comparative information should be provided for the MPM and related disclosures; and</p> <p>(d) the MPM should be calculated consistently from one period to the next and be subject to change only if the new measure provides more useful information. <i>(Paragraph BC158)</i></p>
	<ul style="list-style-type: none"> If reconciling items that are components of GAAP financial information, entities should identify them in the financial statements. 		<p>If the reconciling item is an unusual income and expense item then you are required to disclose the line item in the statement of financial performance in which each item of unusual income or expense is included.</p>

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
	<ul style="list-style-type: none"> If you cannot extract a reconciling item directly from the financial statements, you should show how the number is calculated in the accompanying notes. 		No similar IASB requirement.
	<ul style="list-style-type: none"> If presenting comparative non-GAAP financial information for a previous period, entities should provide reconciliation to the corresponding GAAP financial information for that previous period. 		<p>The IASB noted that MPMs disclosed in the notes to the financial statements would need to comply with the general requirements for information included in financial statements. That is:</p> <ul style="list-style-type: none"> (a) the MPM must faithfully represent the aspect of financial performance of the entity it purports to represent; (b) the disclosures supporting the MPM must comply with the proposed guidance on aggregation and disaggregation, for example, when disclosing reconciling items; (c) comparative information should be provided for the MPM and related disclosures; and (d) the MPM should be calculated consistently from one period to the next and be subject to change only if the new measure provides more useful information. <p>(Paragraph BC158)</p>

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
Consistency	<ul style="list-style-type: none"> If an entity chooses to present non-GAAP financial information, a consistent approach should be adopted from period to period. 		<p>The IASB noted that MPMs disclosed in the notes to the financial statements would need to comply with the general requirements for information included in financial statements. That is:</p> <ul style="list-style-type: none"> (a) the MPM must faithfully represent the aspect of financial performance of the entity it purports to represent; (b) the disclosures supporting the MPM must comply with the proposed guidance on aggregation and disaggregation, for example, when disclosing reconciling items; (c) comparative information should be provided for the MPM and related disclosures; and (d) the MPM should be calculated consistently from one period to the next and be subject to change only if the new measure provides more useful information. <p>(Paragraph BC158)</p>
	<ul style="list-style-type: none"> Where presented, entities should also provide the non-GAAP financial information for comparative periods. 		<p>The IASB noted that MPMs disclosed in the notes to the financial statements would need to comply with the general requirements for information included in financial statements. That is:</p>

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
			<p>(a) the MPM must faithfully represent the aspect of financial performance of the entity it purports to represent;</p> <p>(b) the disclosures supporting the MPM must comply with the proposed guidance on aggregation and disaggregation, for example, when disclosing reconciling items;</p> <p>(c) comparative information should be provided for the MPM and related disclosures; and</p> <p>(d) the MPM should be calculated consistently from one period to the next and be subject to change only if the new measure provides more useful information.</p> <p>(Paragraph BC158)</p>
	<ul style="list-style-type: none"> If there has been a change in approach from the previous period, an explanation about the nature of the change, entities should provide the reasons for the change, and the financial impact of the change. 	<p>If an entity changes the calculation of its management performance measures, introduces a new management performance measure or removes a previously disclosed management performance measure from its financial statements, it shall:</p> <p>(a) disclose sufficient explanation for users of financial statements to understand the change, addition or removal and its effects;</p>	<p>Requirements are essentially the same. The IASB does not require the financial impact of the change.</p>

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
		(b) disclose the reasons for the change, addition or removal; and (c) restate its comparative information, including in the required note disclosures, to reflect the change, addition or removal. (Paragraph 108)	
Unbiased	<ul style="list-style-type: none"> Non-GAAP financial information should be unbiased. Entities should not use it to avoid presenting adverse information to the market or to over-emphasise favourable information. 	Management performance measures shall: <ul style="list-style-type: none"> (a) faithfully represent aspects of the financial performance of the entity to users of financial statements; and (b) be described in a clear and understandable manner that does not mislead users. (Paragraph 105)	Paragraph 2.13 of New Zealand equivalent to the IASB <i>Conceptual Framework for Financial Reporting (2018 NZ Conceptual Framework)</i> states that a faithful representation is complete, neutral and free from error (emphasis added). Paragraph 2.15 then goes on to say a neutral depiction is without bias in the selection or presentation of financial information.
One-off / non-recurring items	<ul style="list-style-type: none"> Entities should not describe items that have occurred in the past or are reasonably likely to occur in a future period as ‘one-off’ or ‘nonrecurring.’ For example, it may be misleading to describe items such as impairment losses and restructuring costs as ‘non-recurring’ or ‘one-off’ when they are generally of a recurring nature in many businesses and usually occur over the life of a business 		The IASB is introducing proposals defining and requiring the disclosure of unusual income and expenses in financial statements. Unusual income and expenses are income and expenses with limited predictive value. Income and expenses have limited predictive value when it is reasonable to expect that income or expenses that are similar in type and amount will not arise for several future annual reporting periods. (Paragraph 100)

FMA’s Guidance on presenting non-GAAP information https://www.fma.govt.nz/assets/Guidance/120901-guidance-note-disclosing-non-gaap-financial-information.pdf		IASB Proposals for disclosure of information on MPMs An entity shall disclose information about any MPMs, if any, in a single note to the financial statements (emphasis added). (paragraph 106 and B82)	
Principle	Explanation	Requirement (include paragraph numbers)	Staff notes
	(although they may only arise every few years).		
	<ul style="list-style-type: none"> No ‘cherry picking’ adjustments. In the case of exclusion of nonrecurring items, the exclusion should reflect all non-recurring items for the relevant period (i.e. both non-recurring charges as well as any non-recurring gains) regardless of whether they are related or not. 		The IASB considered specifying that information about unusual items should be neutral but rejected this as unnecessary because neutrality applies to all items included in the financial statements.

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NZ ACCOUNTING
STANDARDS
BOARD

Memorandum

Date: 13 March 2020

To: NZASB Members

From: Lisa Kelsey

Subject: **Amendments to other IFRS Standards**

Introduction¹

1. This memo sets out the information that Board members need to provide feedback on the proposals in Exposure Draft ED/2019/7 *General Presentation and Disclosures* (the ED) relating to the proposed amendments to other IFRS Standards. Therefore, it is **not** expected that Board members have read the ED.

Recommendations

2. We recommend that the Board:
 - (a) CONSIDERS the proposals outlined in this memo; and
 - (b) PROVIDES feedback on the questions in this memo.

Structure of this memo

3. The remaining sections in this memo are:
 - (a) amendments to other IFRS standards:
 - (i) IAS 7 *Statement of Cash Flows*;
 - (ii) IFRS 12 *Disclosure of Interests in Other Entities*;
 - (iii) IAS 33 *Earnings per Share*;
 - (iv) IAS 34 *Interim Financial Reporting*;
 - (v) IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; and
 - (vi) IFRS 7 *Financial Instruments: Disclosures*; and
 - (b) Going concern.
4. In each section of the memo we have summarised the proposals in the ED. The section headings include references to the Basis for Conclusions should Board members wish to read the IASB's considerations in developing the proposals.

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

Amendments to other IFRS Standards

5. The amendments to other IFRS Standards can be split into two groups: (i) amendments relating to new proposals; and (ii) amendments to move existing parts of IAS 1 into other Standards.
6. Amendments relating to new proposals:
 - (a) IAS 7 *Statement of Cash Flows*;
 - (b) IFRS 12 *Disclosure of Interests in Other Entities*;
 - (c) IAS 33 *Earnings per Share*; and
 - (d) IAS 34 *Interim Financial Reporting*.
7. Amendments to move existing parts of IAS 1 into:
 - (a) IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; and
 - (b) IFRS 7 *Financial Instruments: Disclosures*.

IAS 7 *Statement of Cash Flows* (paragraphs BC185–BC208)

8. Stakeholders have expressed various concerns to the IASB regarding the statement of cash flows. However, the IASB has concluded that a complete overhaul of the statement of cash flows is not within the scope of this project. The IASB is instead focusing on targeted improvements to eliminate diversity in classification and presentation.
9. The IASB found that there is diversity, even within an industry, in:
 - (a) how companies classify interest and dividend cash flows; and
 - (b) which starting point companies use for the indirect method for reporting cash flows from operating activities. For example, some companies use 'profit after tax', others use 'operating profit' or 'profit before tax'.

Investors have indicated that such diversity reduces comparability between companies, making their analysis difficult.

10. The IASB proposes to:
 - (a) require that the operating profit or loss subtotal specified by IFRS Standards be used as the starting point for the indirect method for reporting cash flows from operating activities;
 - (b) require that an entity separate cash flows from investments in integral and non-integral associates and joint ventures, consistent with the IASB's proposals for the statement of profit or loss;
 - (c) remove the classification choice for interest and dividend cash flows for most companies; and
 - (d) expand and clarify the definition of financing activities.

Classification of interest and dividend cash flows

11. The table below summaries the proposals to classify interest and dividend cash flows.

Cash flow item	IAS 7	Proposed approach	
		Most companies	Companies with particular business activities incl. banks
Interest paid	Operating or financing	Financing	Depends on the classification of the related income and expenses in the statement of profit or loss
Interest received	Operating or investing	Investing	
Dividends received	Operating or investing	Investing	
Dividends paid	Operating or financing	Financing	

12. The proposals would require that all entities classify dividends paid as cash flows from financing activities.
13. Entities, other than those described in the paragraph 14 below, shall classify:
- interest paid as cash flows from financing activities. This includes interest that is capitalised as part of the cost of an asset in accordance with IAS 23 *Borrowing Costs*; and
 - interest and dividends received as cash flows from investing activities.
14. For those entities that provide financing to customers as a main business activity or invest in the course of their main business activities in assets that generate a return individually and largely independently of other entity resources, the IASB is proposing that an entity determine a single category in which to classify the cashflows (that is, either as operating, investing or financing activities). In determining the single category an entity shall refer to the classification of the income or expenses corresponding to such cash flows in the statement of profit or loss.
- If the entity classifies related income or expenses in a single category of the statement of profit or loss, the entity shall classify the cash flows in the corresponding category in the statement of cash flows.
 - If the entity classifies related income or expenses in more than one category of the statement of profit or loss, the entity shall make an accounting policy choice to classify the cash flows in one of the corresponding categories of the statement of cash flows.

The definition of financing activities

15. The IASB proposes to expand and clarify the definition of financing activities in IAS 7 and apply it to the statement of profit or loss, as shown in the table below.

Proposed amended definition of financing activities in IAS 7	Proposed definition of financing activities to apply to the statement of profit or loss
<p><i>Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of the entity.</i></p> <p><u>In relation to borrowings, financing activities involve the receipt or use of a resource from a provider of finance with the expectation that:</u></p> <p><u>(a) the resource will be returned to the provider of finance; and</u></p> <p><u>(b) the provider of finance will be appropriately compensated through the payment of a finance charge that is dependent on both the amount of the credit and its duration.</u></p>	<p>Financing activities are those involving the receipt or use of a resource from a provider of finance with the expectation that:</p> <p>(a) the resource will be returned to the provider of finance; and</p> <p>(b) the provider of finance will be compensated through the payment of a finance charge that is dependent on both the amount of the credit and its duration.</p>

16. As highlighted above, the proposals to amend the definition of financing activities in IAS 7 includes the word “appropriately”, which has not been included in the definition of financing activities to apply to the statement of profit and loss. We will query this difference with IASB staff.
17. We would like to draw the Board’s attention to the following:
- (a) The IASB expects that, in most cases, the classification of interest and dividends in the statement of cash flows of “general corporates” will align with the classification of interest and dividends in the statement of profit or loss. However, the IASB acknowledges that this approach will not achieve full alignment. For example, under the proposals:
- (i) interest revenue from cash and cash equivalents is classified in the financing category in the statement of profit or loss, whereas all interest received is classified as cash flows from investing activities in the statement of cash flows; and
 - (ii) interest capitalised as part of the cost of an item of property, plant and equipment would be recognised in profit or loss through depreciation expenses, which would be included in operating profit or loss, whereas capitalised interest paid would be included in cash flows from financing activities.
- However, the IASB concluded that classification of interest or dividend cash flows in a single category in the statement of cash flows is more useful than full alignment.
- (b) The IASB developed proposals for the categories in the statement of profit or loss without trying to align classifications with the statement of cash flows. Therefore, under the proposals both the statement of profit or loss and the statement of cash flows will

have three different categories with similar labelling (operating, investing and financing) which are not aligned.

BC30 The Board developed proposals for the categories in the statement of profit or loss without trying to align classifications across the primary financial statements. Instead, the Board focused on providing information in the statement of profit or loss that meets the needs of users of financial statements for that statement.

Feedback from outreach to date

TRG (received via email in lieu of November TRG meeting)

- One TRG member questioned why the IASB has not aligned the classification of operating, investing and financing between the statement of profit and loss and the statement of cash flows.
- Another TRG member commented that having different definitions of investing between the statement of profit and loss and statement of cash flows would likely lead to confusion in practice.

Question for Board members

1. Statement of cash flows (ED question 13)

- (a) The ED proposes amending IAS 7 to require operating profit or loss to be the starting point for the indirect method of reporting cash flows from operating activities.
- (b) The ED proposes adding new paragraphs to IAS 7 to specify the classification of interest and dividend cash flows.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

Preliminary staff view

- *We agree with the feedback received by the IASB that that diversity in: (i) how companies classify interest and dividend cash flows; and (ii) the starting point that companies use for the indirect method for reporting cash flows from operating activities, reduces comparability between companies, making analysis by investors/users difficult. Therefore, we support the proposal to:*
 - *require operating profit as the single starting point for the indirect method for reporting cash flows from operating activities; and.*
 - *remove the classification choice for interest and dividend cash flows for most entities.*
- *We have received feedback that the use of similar labels to describe the categories in the statement of profit or loss and the classifications in the statement of cash flows will create confusion in practice. Therefore, we recommend that the IASB explore further the use of different labels between the two statements before finalising the proposals.*
- *We do not agree with the proposals to separate cash flows from investments in integral and non-integral associates and joint ventures.*

IFRS 12 Disclosure of Interests in Other Entities (Paragraphs BC79, BC209–BC213)

18. The IASB proposes to amend IFRS 12 to define integral and non-integral associates and joint ventures and to provide indicators to help entities apply those definitions, as well as

establishing requirements for when a change in classification is appropriate. The Board provided feedback on these amendments at its February 2020 meeting.

IAS 33 Earnings per Share (Paragraphs BC214–BC218)

19. The IASB proposes to amend IAS 33 to restrict the numerator used to calculate adjusted earnings per share to subtotals specified by IFRS Standards or an MPM attributable to ordinary equity holders of the parent.
20. Currently, applying IAS 33 requirements, an adjusted earnings per share could be calculated based on any component of the statement(s) of financial performance. The numerator used in an adjusted earnings per share need not be a subtotal specified by IFRS Standards or an MPM. Because adjusted earnings per share result in fewer disclosure requirements than those for management performance measures, users of financial statements would receive less information if an entity chose to disclose an adjusted earnings per share instead of a management performance measure. Restricting the numerator used in adjusted earnings per share to subtotals presented in IFRS Standards or a management performance measure attributable to holders of equity claims of the parent means that users should receive the same information about adjusted earnings per share as they receive for management performance measures (paragraph BC215).
21. If an entity discloses an adjusted earnings per share, the IASB also proposes that it shall:
 - (a) disclose both basic and diluted amounts per share with equal prominence;
 - (b) be calculated using the weighted average number of ordinary shares determined in accordance with IAS 33; and
 - (c) be disclosed in the notes to the financial statements, but not be presented in the primary financial statement(s).

IAS 34 Interim Financial Reporting (Paragraphs BC219–BC225)

22. Currently, IAS 34 requires an entity to disclose in the notes to its interim financial report the nature and amount of items affecting assets, liabilities, equity, net income or cash flows that are unusual because of their nature, size or incidence (paragraph 16A(c) of IAS 34). The IASB proposes to amend paragraph 16A(c) of IAS 34 to align the description of unusual items with the IASB's proposed definition of unusual income and expenses from the ED.
23. The IASB is also proposing amendments to IAS 34 to require the disclosure of information about MPMs in the notes to an entity's condensed financial statements in its interim report.

Preliminary staff view

Amendments to IAS 33

- *There is no specific question in the ED relating to the proposed amendments to IAS 33. We have not identified any significant concerns with the proposed amendments.*
- *Therefore, we recommend that the Board does not comment on the proposed amendments to IAS 33.*

Amendments to IAS 34

- *There is no specific question in the ED relating to the proposed amendments to IAS 34.*
- *In agenda item 5.2 we have raised concerns with the definition of unusual income and expenses and concerns relating to the proposed definition of and disclosure requirements for MPMs.*
- *We agree with the proposed requirement for entities to disclose information about MPMs in their interim financial statements. We believe that MPMs will be used by entities in investor presentations at the interim period. Therefore, we believe the proposals will result in useful information for users of interim financial statements.*
- *We have not identified any other significant concerns with the proposed amendments.*
- *Therefore, we recommend that the Board does not comment on the proposed amendments to IAS 34.*

Question for Board members**2. Proposed amendment to IAS 33 and IAS 34 (no specific question in the ED)**

Does the Board agree not to comment on the proposed amendments to IAS 33 and IAS 34?

IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors (BC226–BC229)

24. IAS 1 includes requirements relating to the general features of financial statements as well as general presentation and disclosure requirements. The IASB proposes to move the paragraphs setting out general features of financial statements as well as some disclosure requirements from IAS 1 to IAS 8, and to withdraw IAS 1.
25. The paragraphs that the IASB is proposing to move from IAS 1 to IAS 8 are shown below.
- (a) the definition of material and associated guidance:

Material:

Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.

Materiality depends on the nature or magnitude of information, or both. An entity assesses whether information, either individually or in combination with other information, is material in the context of its financial statements taken as a whole.

Information is obscured if it is communicated in a way that would have a similar effect for primary users of financial statements to omitting or misstating that information. The following are examples of circumstances that may result in material information being obscured:

- (a) information regarding a material item, transaction or other event is disclosed in the financial statements but the language used is vague or unclear;
- (b) information regarding a material item, transaction or other event is scattered throughout the financial statements;
- (c) dissimilar items, transactions or other events are inappropriately aggregated;
- (d) similar items, transactions or other events are inappropriately disaggregated; and
- (e) the understandability of the financial statements is reduced as a result of material information being hidden by immaterial information to the extent that a primary user is unable to determine what information is material.

Assessing whether information could reasonably be expected to influence decisions made by the primary users of a specific reporting entity's general purpose financial statements requires an entity to consider the characteristics of those users while also considering the entity's own circumstances.

Many existing and potential investors, lenders and other creditors cannot require reporting entities to provide information directly to them and must rely on general purpose financial statements for much of the financial information they need. Consequently, they are the primary users to whom general purpose financial statements are directed. Financial statements are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyse the information diligently. At times, even well-informed and diligent users may need to seek the aid of an adviser to understand information about complex economic phenomena.

- (b) the requirements relating to fair presentation and compliance with IFRSs:

<u>Fair presentation and compliance with IFRSs Standards</u>	
6A	[IAS 1.15] Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the <i>Conceptual Framework for Financial Reporting</i> (<i>Conceptual Framework</i>). The application of IFRSs <u>IFRS Standards</u> , with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.
6B	[IAS 1.16] An entity whose financial statements comply with IFRSs <u>IFRS Standards</u> shall make an explicit and unreserved statement of such compliance in the notes. An entity shall not describe financial statements as complying with IFRSs <u>IFRS Standards</u> unless they comply with all the requirements of IFRSs <u>IFRS Standards</u> .
6C	[IAS 1.17] In virtually all circumstances, an entity achieves a fair presentation by compliance with applicable IFRSs <u>IFRS Standards</u> . A fair presentation also requires an entity: <ul style="list-style-type: none"> (a) to select and apply accounting policies in accordance with this Standard IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. IAS 8 <u>This Standard</u> sets out a hierarchy of authoritative guidance that management considers in the absence of an IFRS <u>Standard</u> that specifically applies to an item. (b) to present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information. (c) to provide additional disclosures when compliance with the specific requirements in IFRSs <u>IFRS Standards</u> is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.
6D	[IAS 1.18] An entity cannot rectify inappropriate accounting policies either by disclosure of the accounting policies used or by notes or explanatory material.
6E	[IAS 1.19] In the extremely rare circumstances in which management concludes that compliance with a requirement in an IFRS <u>Standard</u> would be so misleading that it would conflict with the objective of financial statements set out in the <i>Conceptual Framework</i> , the entity shall depart from that requirement in the manner set out in paragraph 20-6E if the relevant regulatory framework requires, or otherwise does not prohibit, such a departure.
6F	[IAS 1.20] When an entity departs from a requirement of an IFRS <u>Standard</u> in accordance with paragraph 19-6E , it shall disclose: <ul style="list-style-type: none"> (a) that management has concluded that the financial statements present fairly the entity's financial position, financial performance and cash flows; (b) that it has complied with applicable IFRSs <u>IFRS Standard</u>, except that it has departed from a particular requirement to achieve a fair presentation; (c) the title of the IFRS <u>Standard</u> from which the entity has departed, the nature of the departure, including the treatment that the IFRS <u>Standard</u> would require, the reason why that treatment would be so misleading in the circumstances that it would conflict with the objective of financial statements set out in the <i>Conceptual Framework</i>, and the treatment adopted; and (d) for each period presented, the financial effect of the departure on each item in the financial statements that would have been reported in complying with the requirement.
6G	[IAS 1.21] When an entity has departed from a requirement of an IFRS <u>Standard</u> in a prior period, and that departure affects the amounts recognised in the financial statements for the current period, it shall make the disclosures set out in paragraph 20(c) and (d) <u>paragraphs 6F(c)–6F(d)</u> .
6H	[IAS 1.22] Paragraph 21-6G applies, for example, when an entity departed in a prior period from a requirement in an IFRS <u>Standard</u> for the measurement of assets or liabilities and that departure affects the measurement of changes in assets and liabilities recognised in the current period's financial statements.
6I	[IAS 1.23] In the extremely rare circumstances in which management concludes that compliance with a requirement in an IFRS <u>Standard</u> would be so misleading that it would conflict with the objective of financial statements set out in the <i>Conceptual Framework</i> , but the relevant regulatory framework prohibits departure from the requirement, the entity shall, to the maximum extent possible, reduce the perceived misleading aspects of compliance by disclosing: <ul style="list-style-type: none"> (a) the title of the IFRS <u>Standard</u> in question, the nature of the requirement, and the reason why management has concluded that complying with that requirement is so misleading in the circumstances that it conflicts with the objective of financial statements set out in the <i>Conceptual Framework</i>; and (b) for each period presented, the adjustments to each item in the financial statements that management has concluded would be necessary to achieve a fair presentation.
6J	[IAS 1.24] For the purpose of paragraphs 19–23-6E–6I , an item of information would conflict with the objective of financial statements when it does not represent faithfully the transactions, other events and conditions that it either purports to represent or could reasonably be expected to represent and, consequently, it would be likely to influence economic decisions made by users of financial statements. When assessing whether complying with a specific requirement in an IFRS <u>Standard</u> would be so

misleading that it would conflict with the objective of financial statements set out in the *Conceptual Framework*, management considers:

- (a) why the objective of financial statements is not achieved in the particular circumstances; and
- (b) how the entity's circumstances differ from those of other entities that comply with the requirement. If other entities in similar circumstances comply with the requirement, there is a rebuttable presumption that the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of financial statements set out in the *Conceptual Framework*.

(c) the requirements relating to going concern:

Going concern

6K [IAS 1.25] When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern. An entity shall prepare financial statements on a going concern basis unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so. When management is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity shall disclose those uncertainties. When an entity does not prepare financial statements on a going concern basis, it shall disclose that fact, together with the basis on which it prepared the financial statements and the reason why the entity is not regarded as a going concern.

6L [IAS 1.26] In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period. The degree of consideration depends on the facts in each case. When an entity has a history of profitable operations and ready access to financial resources, the entity may reach a conclusion that the going concern basis of accounting is appropriate without detailed analysis. In other cases, management may need to consider a wide range of factors relating to current and expected profitability, debt repayment schedules and potential sources of replacement financing before it can satisfy itself that the going concern basis is appropriate.

(d) the requirements relating to the accrual basis of accounting:

Accrual basis of accounting

6M [IAS 1.27] An entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting.

6N [IAS 1.28] When the accrual basis of accounting is used, an entity recognises items as assets, liabilities, equity, income and expenses (the elements of financial statements) when they satisfy the definitions and recognition criteria for those elements in the Conceptual Framework.

(e) the requirements relating to disclosure of accounting policies and sources of estimation uncertainty:

Disclosure of selection and application of accounting policies

27A [IAS 1.117] An entity shall disclose in the notes its significant accounting policies² comprising:

- (a) the measurement basis (or bases) used in preparing the financial statements; and
- (b) the other accounting policies used that are relevant to an understanding of the financial statements.

27B [IAS 1.118] It is important for an entity to inform users of financial statements of the measurement basis or bases used in the financial statements (for example, historical cost, current cost, net realisable value, fair value or recoverable amount or current value) because the basis on which an entity prepares the financial statements significantly affects users' analysis. When an entity uses more than one measurement basis in the financial statements, for example when particular classes of assets are revalued, it is sufficient to provide an indication of the categories of assets and liabilities to which each measurement basis is applied.

27C [IAS 1.119] In deciding whether a particular accounting policy should be disclosed in the notes, management considers whether disclosure would assist users of financial statements in understanding how transactions, and other events and conditions are reflected in reported financial performance and financial position. Each entity considers the nature of its operations and the policies that the users of its financial statements would expect to be disclosed for that type of entity. Disclosure of particular accounting policies is especially useful to users when those policies are selected from alternatives allowed in IFRSs/IFRS Standards. An example is disclosure of whether an entity applies the fair value or cost model to its investment property (see IAS 40 *Investment Property*). Some IFRSs/IFRS Standards specifically require disclosure of particular accounting policies, including choices made by management between different policies they allow. For example, IAS 16 *Property, Plant and Equipment* requires disclosure of the measurement bases used for classes of property, plant and equipment.

27D [IAS 1.121] An accounting policy may be significant because of the nature of the entity's operations even if amounts for current and prior periods are not material. It is also appropriate to disclose in the notes each

² Exposure Draft ED/2019/6 *Disclosure of Accounting Policies* proposes amendments to the disclosure requirements for accounting policies.

	significant accounting policy that is not specifically required by IFRSs <u>IFRS Standards</u> but the entity selects and applies in accordance with IAS 8 <u>this Standard</u> .
27E	[IAS 1.122] An entity shall disclose in the notes, along with its significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph 42531A), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.
27F	[IAS 1.123] In the process of applying the entity's accounting policies, management makes various judgements, apart from those involving estimations, that can significantly affect the amounts it recognises in the financial statements. For example, management makes judgements in determining: <ul style="list-style-type: none"> (a) [deleted] (b)(a) when substantially all the significant risks and rewards of ownership of financial assets and, for lessors, assets subject to leases are transferred to other entities; (c)(b) whether, in substance, particular sales of goods are financing arrangements and therefore do not give rise to revenue; and (d)(c) whether the contractual terms of a financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.
27G	[IAS 1.124] Some of the disclosures made in accordance with paragraph 42227E are required by other IFRSs <u>IFRS Standards</u> . For example, IFRS 12 <i>Disclosure of Interests in Other Entities</i> requires an entity to disclose in the notes the judgements it has made in determining whether it controls another entity. IAS 40 <i>Investment Property</i> requires disclosure in the notes of the criteria developed by the entity to distinguish investment property from owner-occupied property and from property held for sale in the ordinary course of business, when classification of the property is difficult.
...	
	Disclosure of sources Sources of estimation uncertainty
31A	[IAS 1.125] An entity shall disclose in the notes information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In respect of those assets and liabilities, the notes shall include details of: <ul style="list-style-type: none"> (a) their nature; and (b) their carrying amount as at the end of the reporting period.
31B	[IAS 1.126] Determining the carrying amounts of some assets and liabilities requires estimation of the effects of uncertain future events on those assets and liabilities at the end of the reporting period. For example, in the absence of recently observed market prices, future-oriented estimates are necessary to measure the recoverable amount of classes of property, plant and equipment, the effect of technological obsolescence on inventories, provisions subject to the future outcome of litigation in progress, and long-term employee benefit liabilities such as pension obligations. These estimates involve assumptions about such items as the risk adjustment to cash flows or discount rates, future changes in salaries and future changes in prices affecting other costs.
31C	[IAS 1.127] The assumptions and other sources of estimation uncertainty disclosed in the notes in accordance with paragraph 42531A relate to the estimates that require management's most difficult, subjective or complex judgements. As the number of variables and assumptions affecting the possible future resolution of the uncertainties increases, those judgements become more subjective and complex, and the potential for a consequential material adjustment to the carrying amounts of assets and liabilities normally increases accordingly.
31D	[IAS 1.128] The <u>note</u> disclosures in paragraph 42531A are not required for assets and liabilities with a significant risk that their carrying amounts might change materially within the next financial year if, at the end of the reporting period, they are measured at fair value based on a quoted price in an active market for an identical asset or liability. Such fair values might change materially within the next financial year but these changes would not arise from assumptions or other sources of estimation uncertainty at the end of the reporting period.
31E	[IAS 1.129] An entity presents <u>provides</u> the <u>note</u> disclosures in paragraph 42531A in a manner that helps users of financial statements to understand the judgements that management makes about the future and about other sources of estimation uncertainty. The nature and extent of the information provided vary according to the nature of the assumption and other circumstances. Examples of the types of disclosures an entity makes are: <ul style="list-style-type: none"> (a) the nature of the assumption or other estimation uncertainty; (b) the sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation, including the reasons for the sensitivity; (c) the expected resolution of an uncertainty and the range of reasonably possible outcomes within the next financial year in respect of the carrying amounts of the assets and liabilities affected; and (d) an explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved.
31F	[IAS 1.130] This [draft] Standard does not require an entity to disclose in the notes budget information or forecasts in making the <u>note</u> disclosures in paragraph 42531A.
31G	[IAS 1.131] Sometimes it is impracticable to disclose in the notes the extent of the possible effects of an assumption or another source of estimation uncertainty at the end of the reporting period. In such cases, the entity discloses in the notes that it is reasonably possible, on the basis of existing knowledge, that outcomes within the next financial year that are different from the assumption could require a material adjustment to the carrying amount of the asset or liability affected. In all cases, the entity discloses in the notes the nature and carrying amount of the specific asset or liability (or class of assets or liabilities) affected by the assumption.

31H	[IAS 1.132] The <u>note</u> disclosures in paragraph 42227E of particular judgements that management made in the process of applying the entity's accounting policies do not relate to the <u>note</u> disclosures of sources of estimation uncertainty in paragraph 425-31A .
31I	[IAS 1.133] Other IFRSs IFRS Standards require the <u>note</u> disclosure of some of the assumptions that would otherwise be required in accordance with paragraph 425-31A . For example, IAS 37 <i>Provisions, Contingent Liabilities and Contingent Assets</i> requires <u>note</u> disclosure, in specified circumstances, of major assumptions concerning future events affecting classes of provisions. IFRS 13 <i>Fair Value Measurement</i> requires <u>note</u> disclosure of significant assumptions (including the valuation technique(s) and inputs) the entity uses when measuring the fair values of assets and liabilities that are carried at fair value.
...	

26. The IASB is proposing to change the title of IAS 8 to *Basis of Preparation, Accounting Policies, Changes in Accounting Estimates and Errors*. The IASB is also proposing to review the objective and scope paragraphs.

Feedback from outreach to date

TRG

- One TRG member did not support the proposal to include the requirements re materiality, going concern, compliance with IFRS, fair presentation etc in IAS 8 – The member believes that keeping them where they are in IAS 1 [or a new *General Presentation and Disclosures Standard*] is a more logical place.

Preliminary staff view

- *There are no specific questions in the ED relating to the proposals to move requirements from IAS 1 to IAS 8.*
- *We have not identified any significant concerns with the proposals to move requirements from IAS 1 to IAS 8.*
- *We support moving the definition of material and associated guidance to IAS 8 as the concept of materiality is pervasive in the preparation of financial statements. In other words, an entity makes materiality judgements when making decisions about recognition and measurement, as well as presentation and disclosure.*
- *However, we consider that materiality is well established as a concept in relation to recognition and measurement but is less so in relation to presentation and disclosure. For example, some may argue that the proposed principles and guidance relating to aggregation and disaggregation would not be needed if materiality was applied appropriately to presentation and disclosure requirements. Therefore, we believe that there is a need for additional guidance on materiality in a new general presentation and disclosures standard.*
- *Overall, we recommend that the Board does not comment on the proposals to move requirements from IAS 1 to IAS 8. However, we believe the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard. Therefore, we recommend that the Board includes in its submission a general comment that the IASB give greater emphasis to the concept of materiality in a new general presentation and disclosures standard.*

Question for Board members**3. Proposals to move requirements from IAS 1 to IAS 8 (no specific question in the ED)**

Does the Board agree with the recommendations:

- (a) not to comment on the proposals to move requirements from IAS 1 to IAS 8; and
- (b) to make a general comment that the IASB give greater emphasis to the concept of materiality in a new general presentation and disclosures standard?

IFRS 7 Financial Instruments: Disclosures (BC230–BC231)

27. The IASB proposes to move the disclosure requirements on puttable instruments *classified as equity* from IAS 1 to IFRS 7.

3	This IFRS shall be applied by all entities to all types of financial instruments, except:
...	
	(f) instruments that are required to be classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D of IAS 32. <u>However, the disclosures required by paragraphs 19A–19B are required for such instruments.</u>
...	
	Statement of financial position
...	
	<u>Financial instruments classified as equity in accordance with paragraphs 16A–16B or paragraphs 16C–16D of IAS 32</u>
19A	[IAS 1.136A] For puttable financial instruments classified as equity instruments <u>in accordance with paragraphs 16A–16B of IAS 32</u> , an entity shall disclose (to the extent not disclosed elsewhere):
	(a) summary quantitative data about the amount classified as equity;
	(b) its objectives, policies and processes for managing its obligation to repurchase or redeem the instruments when required to do so by the instrument holders, including any changes from the previous period;
	(c) the expected cash outflow on redemption or repurchase of that class of financial instruments; and
	(d) information about how the expected cash outflow on redemption or repurchase was determined.
19B	[IAS 1.80A] <u>If an entity has reclassified any of the following financial instruments between financial liabilities and equity, it shall disclose the amount reclassified into and out of each category (financial liabilities or equity), and the timing and reason for that reclassification:</u>
	(a) <u>a puttable financial instrument classified as an equity instrument <u>applying paragraphs 16A–16B of IAS 32</u>; or</u>
	(b) <u>an instrument that imposes on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and is classified as an equity instrument <u>applying paragraphs 16C–16D of IAS 32</u>.</u>
	between financial liabilities and equity, it shall disclose the amount reclassified into and out of each category (financial liabilities or equity), and the timing and reason for that reclassification.
...	

Preliminary staff view

- *There are no specific questions in the ED relating to the proposals to move the requirements on puttable instruments classified as equity from IAS 1 to IFRS 7.*
- *We are broadly supportive of the proposals and have not identified any significant concerns.*
- *Therefore, we recommend that the Board does not comment on the proposals to move the requirements on puttable instruments classified as equity from IAS 1 to IFRS 7.*

Question for Board members

4. Proposals to move requirements from IAS 1 to IFRS 7 (no specific question in the ED)

Does the Board agree with not to comment on the proposals to move the requirements on puttable instruments classified as equity from IAS 1 to IFRS 7?

Going concern

28. The inaugural joint Board meeting of the NZASB and NZAuASB was held on 13 February 2020. Going concern was one of the topics that was discussed.
29. Board members broke into small groups to discuss ways in which the NZASB and the NZAuASB can work to influence the international debate to develop a holistic solution for increased focus on going concern matters by those charged with governance/management and auditors.
30. The Boards agreed that the NZASB and AASB should:
 - (a) raise this matter in response to the IASB 2020 Agenda Consultation; and
 - (b) request that the IASB consider going concern risks in its Management Commentary project.
31. We believe that the IASB should consider matters relating to going concern as part of a *separate* project. However, we would like to seek feedback from Board members as to whether they would like to include any general comments regarding going concern in the Board's submission on the ED.

Question for Board members

5. Going concern

Would the Board like to make any comments about going concern in its submission to the IASB?



**NZ ACCOUNTING
STANDARDS
BOARD**

Memorandum

Date: 13 March 2020

To: NZASB Members

From: Tracey Crookston

Subject: *Classification of liabilities as Current or Non-current*

Recommendations¹

1. We recommend that the Board:
 - (a) APPROVES for issue *Classification of Liabilities as Current or Non-current*, which contains amendments to NZ IAS 1 *Presentation of Financial Statements* (NZ IAS 1); and
 - (b) APPROVES the signing memorandum from the Chair of the NZASB to the Chair of the XRB Board requesting approval to issue the Standard.

Introduction

2. The purpose of the amendments is to clarify how to classify, in the statement of financial position, debt and other liabilities as current or non-current. As part of the amendments, the IASB has clarified that the classification of liabilities as current or non-current:
 - (a) should be based on rights that are in existence at the end of the reporting period; and
 - (b) is unaffected by expectations about whether an entity will exercise its rights to defer settlement.

Background

3. Please refer to the signing memo (agenda item 6.3, under the heading Due process) for details about the background to the amendments.

RDR concessions and consistency with Australian Accounting Standards

4. The amending standard does not create any new disclosure requirements. Therefore, there are no changes to RDR concessions in NZ IAS 1.
5. The Australian Accounting Standards Board (AASB) staff have proposed no RDR concessions for the amendments to the equivalent Australian standard. Therefore, the Tier 1 and Tier 2 for-profit reporting requirements will continue to be aligned with those in Australia. The AASB

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

approved *Classification of Liabilities as Current or Non-current* in the equivalent Australian standard at the March AASB meeting.

Due process

6. Following its consideration of comments from constituents, the IASB reviewed the due process steps that it had taken since the publication of ED/2015/1 *Classification of Liabilities* (Proposed amendments to IAS 1) and concluded that the applicable due process steps had been completed. This review of due process occurred at the IASB's September 2019 meeting.²
7. The due process followed by the NZASB complied with the due process requirements established by the XRB Board and, in our view, meets the requirements of section 22 of the Financial Reporting Act 2013.
8. In accordance with section 22(2) of the Financial Reporting Act 2013 we have considered whether the amending standard is likely to require the disclosure of personal information. In our view the amending standard does not include requirements that would result in the disclosure of personal information, and therefore no consultation with the Privacy Commissioner is required.

Draft amending standard and signing memorandum

9. Attached as Agenda item 6.2 is a copy of the draft NZ IFRS amending standard *Classification of Liabilities as Current or Non-current*. A paragraph has been added to limit the application of the Standard to Tier 1 and Tier 2 for-profit entities only.
10. Attached as Agenda item 6.3 is a draft signing memorandum from the Chair of the NZASB to the Chair of the XRB Board.

Attachments

Agenda item 6.2: Draft: *Classification of Liabilities as Current or Non-current*

Agenda item 6.3: Draft: signing memorandum

² A summary of the IASB's September 2019 meeting is available at: [IASB Update September 2019](#)

CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT



Classification of Liabilities as Current or Non-current

Issued April 2020

This Standard was issued on 2 April 2020 by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This Standard 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 30 April 2020.

Reporting entities that are subject to this Standard are required to apply it in accordance with the effective date set out in Part D.

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

This Tier 1 and Tier 2 For-profit Accounting Standard is based on amendments issued by the International Accounting Standards Board to clarify the classification of liabilities as current or non-current.

CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT

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CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT

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The following is available within New Zealand on the XRB website as additional material

APPROVAL BY THE IASB OF CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT ISSUED IN JANUARY 2020

AMENDMENTS TO THE IASB BASIS FOR CONCLUSIONS ON IAS 1 PRESENTATION OF FINANCIAL STATEMENTS

CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT
(AMENDMENTS TO NZ IAS 1)

Part A – Introduction

This Standard sets out amendments to clarify the classification of liabilities as current or non-current. Tier 2 entities are required to comply with all the requirements in this Standard.

Part B – Scope

This Standard applies to Tier 1 and Tier 2 for-profit entities.

Part C – Amendments to NZ IAS 1 *Presentation of Financial Statements*

Paragraphs 69, 73, 74 and 76 are amended. Paragraphs 72A, 75A, 76A, 76B and 139U are added. Paragraph 139D is deleted. Headings are added before paragraphs 70, 71, 72A and 76A. Paragraphs 70, 71, 72 and 75 are not amended, but are included for ease of reading. New text is underlined and deleted text is struck through.

Structure and content

...

Statement of financial position

...

Current liabilities

69 An entity shall classify a liability as current when:

- (a) it expects to settle the liability in its normal operating cycle;
- (b) it holds the liability primarily for the purpose of trading;
- (c) the liability is due to be settled within twelve months after the reporting period; or
- (d) it does not have an unconditional right at the end of the reporting period to defer settlement of the liability for at least twelve months after the reporting period ~~(see paragraph 73). Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.~~

An entity shall classify all other liabilities as non-current.

Normal operating cycle (paragraph 69(a))

70 Some current liabilities, such as trade payables and some accruals for employee and other operating costs, are part of the working capital used in the entity's normal operating cycle. An entity classifies such operating items as current liabilities even if they are due to be settled more than twelve months after the reporting period. The same normal operating cycle applies to the classification of an entity's assets and liabilities. When the entity's normal operating cycle is not clearly identifiable, it is assumed to be twelve months.

CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT

Held primarily for the purpose of trading (paragraph 69(b)) or due to be settled within twelve months (paragraph 69(c))

- 71 Other current liabilities are not settled as part of the normal operating cycle, but are due for settlement within twelve months after the reporting period or held primarily for the purpose of trading. Examples are some financial liabilities that meet the definition of held for trading in NZ IFRS 9, bank overdrafts, and the current portion of non-current financial liabilities, dividends payable, income taxes and other non-trade payables. Financial liabilities that provide financing on a long-term basis (ie are not part of the working capital used in the entity's normal operating cycle) and are not due for settlement within twelve months after the reporting period are non-current liabilities, subject to paragraphs 74 and 75.
- 72 An entity classifies its financial liabilities as current when they are due to be settled within twelve months after the reporting period, even if:
- (a) the original term was for a period longer than twelve months; and
 - (b) an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the reporting period and before the financial statements are authorised for issue.

Right to defer settlement for at least twelve months (paragraph 69(d))

- 72A An entity's right to defer settlement of a liability for at least twelve months after the reporting period must have substance and, as illustrated in paragraphs 73–75, must exist at the end of the reporting period. If the right to defer settlement is subject to the entity complying with specified conditions, the right exists at the end of the reporting period only if the entity complies with those conditions at the end of the reporting period. The entity must comply with the conditions at the end of the reporting period even if the lender does not test compliance until a later date.
- 73 If an entity ~~expects, and has the discretion, right, at the end of the reporting period, to refinance or~~ roll over an obligation for at least twelve months after the reporting period under an existing loan facility, it classifies the obligation as non-current, even if it would otherwise be due within a shorter period. ~~However, when refinancing or rolling over the obligation is not at the discretion of the entity (for example, there is no arrangement for refinancing) If the entity has no such right,~~ the entity does not consider the potential to refinance the obligation and classifies the obligation as current.
- 74 When an entity breaches a ~~provision condition~~ of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand, it classifies the liability as current, even if the lender agreed, after the reporting period and before the authorisation of the financial statements for issue, not to demand payment as a consequence of the breach. An entity classifies the liability as current because, at the end of the reporting period, it does not have ~~an unconditional~~ the right to defer its settlement for at least twelve months after that date.
- 75 However, an entity classifies the liability as non-current if the lender agreed by the end of the reporting period to provide a period of grace ending at least twelve months after the reporting period, within which the entity can rectify the breach and during which the lender cannot demand immediate repayment.
- 75A Classification of a liability is unaffected by the likelihood that the entity will exercise its right to defer settlement of the liability for at least twelve months after the reporting period. If a liability meets the criteria in paragraph 69 for classification as non-current, it is classified as non-current even if management intends or expects the entity to settle the liability within twelve months after the reporting period, or even if the entity settles the liability between the end of the reporting period and the date the financial statements are authorised for issue. However, in either of those circumstances, the entity may need to disclose information about the timing of settlement to enable users of its financial statements to understand the impact of the liability on the entity's financial position (see paragraphs 17(c) and 76(d)).
- 76 ~~In respect of loans classified as current liabilities, if~~ If the following events occur between the end of the reporting period and the date the financial statements are authorised for issue, those events are disclosed as non-adjusting events in accordance with NZ IAS 10 *Events after the Reporting Period*:
- (a) refinancing on a long-term basis of a liability classified as current (see paragraph 72);
 - (b) rectification of a breach of a long-term loan arrangement classified as current (see paragraph 74); and
 - (c) the granting by the lender of a period of grace to rectify a breach of a long-term loan arrangement ending at least twelve months after the reporting period, classified as current (see paragraph 75); and
 - (d) settlement of a liability classified as non-current (see paragraph 75A).

CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT
(AMENDMENTS TO NZ IAS 1)

Settlement (paragraphs 69(a), 69(c) and 69(d))

76A For the purpose of classifying a liability as current or non-current, settlement refers to a transfer to the counterparty that results in the extinguishment of the liability. The transfer could be of:

- (a) cash or other economic resources—for example, goods or services; or
- (b) the entity’s own equity instruments, unless paragraph 76B applies.

76B Terms of a liability that could, at the option of the counterparty, result in its settlement by the transfer of the entity’s own equity instruments do not affect its classification as current or non-current if, applying NZ IAS 32 *Financial Instruments: Presentation*, the entity classifies the option as an equity instrument, recognising it separately from the liability as an equity component of a compound financial instrument.

...

Transition and effective date

...

139D [Deleted by IASB]

...

139U *Classification of Liabilities as Current or Non-current*, issued in April 2020, amended paragraphs 69, 73, 74 and 76 and added paragraphs 72A, 75A, 76A and 76B. An entity shall apply those amendments for annual reporting periods beginning on or after 1 January 2022 retrospectively in accordance with NZ IAS 8. Earlier application is permitted. If an entity applies those amendments for an earlier period, it shall disclose that fact.

Part D – Effective Date

This Standard shall be applied for annual periods beginning on or after 1 January 2022 retrospectively in accordance with NZ IAS 8. Earlier application is permitted.



NZ ACCOUNTING
STANDARDS
BOARD

Memorandum

Date: 25 March 2020

To: Michele Embling, Chair External Reporting Board

From: Kimberley Crook, Chair NZASB

Subject: *Classification of Liabilities as Current or Non-current*

Introduction¹

1. In accordance with the protocols established by the XRB Board, the NZASB seeks your approval to issue *Classification of Liabilities as Current or Non-current* which amends NZ IAS 1 *Presentation of Financial Statements*.
2. The purpose of the amendments is to clarify how to classify, in the statement of financial position, liabilities as current or non-current. As part of the amendments, the IASB has clarified that the classification of liabilities as current or non-current:
 - (a) should be based on rights that are in existence at the end of the reporting period; and
 - (b) is unaffected by expectations about whether an entity will exercise its rights to defer settlement.
3. The proposed amending standard is equivalent to the IASB's amending standard of the same name.

Due process

4. Proposals regarding the classification of liabilities were originally included in IASB ED/2012/1 *Annual Improvements to IFRSs 2010–2012 Cycle*.² In 2013, the IASB decided to deal with this issue as a separate project.
5. In February 2015, the IASB issued ED/2015/1 *Classification of Liabilities* (Proposed amendments to IAS 1) (the ED). In March 2015, the New Zealand Accounting Standards Board (NZASB) agreed not to comment on the ED. The NZASB did not receive any comment letters from New Zealand constituents.
6. The IASB received 88 comment letters. Most respondents agreed with the proposals in the ED:
 - (a) to base the classification of liabilities as current or non-current on rights in place at the end of the reporting period; and

¹ This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

² This project contained an amendment to paragraph 73 of IAS 1 *Presentation of Financial Statements*.

- (b) that the settlement of liabilities, for the purposes of classification as current or non-current, should be based on the transfer to the counterparty of cash, other economic resources (for example, goods or services) or the entity's own equity instruments.
7. The IASB considered comments received from constituents but decided in April 2016 to defer this project until the revisions to the definitions of asset and liability in the IASB *Conceptual Framework for Financial Reporting* were finalised.
 8. The IASB issued its revised *Conceptual Framework* in March 2018 and resumed its discussions on classification of liabilities as current or non-current in September 2018.
 9. Responding to constituent feedback on the ED, the IASB clarified the classification requirements (as current or non-current) for debt that could, at the option of the counterparty, be settled by transfer of an entity's own equity instruments.
 10. At its September 2019 meeting the IASB reviewed the due process steps that it had taken since the publication of ED/2015/1 and concluded that the applicable due process steps had been completed.³
 11. The IASB issued *Classification of Liabilities as Current or Non-current* in January 2020. This amending standard is effective for annual periods beginning on or after 1 January 2022 retrospectively with early application permitted.
 12. The NZASB has approved *Classification of Liabilities as Current or Non-current*. The due process followed by the NZASB complied with the due process requirements established by the XRB Board and, in the NZASB's view, meets the requirements of section 22 of the Financial Reporting Act 2013.
 13. In accordance with section 22(2) of the Financial Reporting Act 2013 the NZASB has considered whether the amending standard is likely to require the disclosure of personal information. In the NZASB's view the amending standard does not include requirements that would result in the disclosure of personal information and therefore no consultation with the Privacy Commissioner is required.

Consistency with XRB Financial Reporting Strategy

14. The amending standard is a standard in its own right. *Classification of Liabilities as Current or Non-current* is identical to the IASB standard *Classification of Liabilities as Current or Non-current* except for the New Zealand-specific introduction and a scope paragraph limiting the application of the Standard to Tier 1 and Tier 2 for-profit entities.
15. The Australian Accounting Standards Board (AASB) approved *Classification of Liabilities as Current or Non-current* in the equivalent Australian standard at the March AASB meeting.
16. The amending standard does not create any new disclosure requirements. As such, there are no changes to the RDR concessions in NZ IAS 1 and no changes to AASB 101 *Presentation of*

³ A summary of the IASB's September 2019 meeting is available at: [IASB Update September 2019](#)

Financial Statements. Therefore, the Tier 1 and Tier 2 for-profit reporting requirements will continue to be aligned with those in Australia.

17. The issuance of this amending standard is consistent with all three elements of the Financial Reporting Strategy: it adopts the international standard, retains a harmonised position with Australia and is consistent with the Accounting Standards Framework.

Effective date

18. The amending standard will be applicable for annual reporting periods beginning on or after 1 January 2022 retrospectively in accordance with NZ IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, with early application permitted.

Other matters

19. There are no other matters relating to the issue of this amending standard that the NZASB considers to be pertinent or that should be drawn to your attention.

Recommendation

20. The NZASB recommends that you sign the attached certificate of determination on behalf of the XRB Board.

Attachments

Classification of Liabilities as Current or Non-current

Certificate of determination

Kimberley Crook
Chair NZASB



NZ ACCOUNTING
STANDARDS
BOARD

Memorandum

Date: 13 March 2019

To: NZASB Members

From: Tracey Crookston

Subject: **PBE Policy Approach: *Classification of Liabilities as Current or Non-current***

Recommendations¹

1. The Board is asked to:
 - (a) CONSIDER the application of the [Policy Approach to the Development of PBE Standards](#) (the PBE Policy Approach) to *Classification of Liabilities as Current or Non-current*; and
 - (b) AGREE to wait for the IPSASB to propose adopting the amendments into IPSAS via its improvements to IPSAS project in 2020.

Background

2. The IASB issued *Classification of Liabilities as Current or Non-current* to clarify how to classify, in the statement of financial position, debt and other liabilities as current or non-current. Refer to the signing memorandum at agenda 6.3 for further detail.
3. The next step is to consider whether the amendments should be incorporated in PBE Standards, and if so, when. In this memo we have applied the relevant parts of the PBE Policy Approach to *Classification of Liabilities as Current or Non-current*.

PBE Policy Approach

4. The relevant triggers for considering whether to amend PBE Standards are set out in paragraph 4.2 of the PBE Policy Approach. In this case the IASB has issued amendments to an existing IFRS Standard which the IPSASB has used as the basis for an IPSAS. In addition, the amendments affect an IFRS Standard (IAS 1) that the NZASB has used as the basis for a PBE Standard.
5. Paragraphs 28–31 of the PBE Policy Approach set out the matters to be considered. Paragraphs 28–29 highlight the need to consider whether the IPSASB will address the change in an acceptable timeframe and the need to balance this against the costs and benefits of getting ahead of the IPSASB. Paragraph 30 establishes a rebuttable presumption that the

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NZASB will not get ahead of the IPSASB if the amendments are minor. Table 2 sets out our thoughts on these matters.

Table 2 Applying the PBE Policy Approach

<p>Will the IPSASB consider these issues in an acceptable timeframe?</p> <p>The IPSASB staff have indicated that these amendments will be considered for inclusion in the 2020 improvements to IPSAS project. An exposure draft (ED) for the improvements project is scheduled for June 2020 on the IPSASB’s workplan.</p>
<p>Are the amendments minor?</p> <p>The amendments are not extensive. They clarify, rather than change, the existing requirements. However, they could result in some entities reclassifying some liabilities from current to non-current and vice versa.</p>
<p>Costs and benefits of getting ahead of the IPSASB</p> <p><u>Costs</u></p> <p>There is a risk that the IPSASB could decide not to issue the amendments which would result in a permanent difference between IPSAS and PBE Standards.</p> <p>Waiting for the IPSASB would not affect the resources required to develop and issue a domestic standard.</p> <p><u>Who would benefit?</u></p> <p>Tier 1 and Tier 2 PBEs would benefit from greater clarification about the assessment of whether a liability should be classified as current or non-current.</p>
<p>RDR</p> <p>There are no new disclosures and therefore no RDR concessions are proposed.</p>

Next steps

6. Based on the analysis in Table 2 above, staff are of the view that it is appropriate to wait for the IPSASB to issue the equivalent amendments in an ED as part of the improvements to IPSAS project in June 2020.
7. The NZASB would then consider these amendments as part of the Omnibus Amendments to PBE Standards project. The current workplan proposes that an ED for this project be approved by the Board at its August 2020 meeting.

<p>Question for the Board</p> <p>Q1. Does the Board agree to wait for the IPSASB to propose these amendments as part of its improvements to IPSAS project in 2020?</p>



APPROVAL NZASB 113

Approval to Issue *PBE Interest Rate Benchmark Reform*

In accordance with the protocols established between the New Zealand Accounting Standards Board (NZASB) and the External Reporting Board (XRB Board), the NZASB has:

- approved for issue *PBE Interest Rate Benchmark Reform*; and
- provided a signing memo outlining the due process followed before reaching that decision, and other related information.

I have reviewed the signing memo and am satisfied with the information provided. Accordingly, the NZASB is hereby authorised to issue *PBE Interest Rate Benchmark Reform* pursuant to section 12(a) of the Financial Reporting Act 2013.

Dated this 14th day of February 2010

A handwritten signature in black ink, appearing to read 'Michele Embling', written over a dotted line.

Michele Embling
Chair
External Reporting Board



APPROVAL NZASB 114

Approval to Issue:

Withdrawal of PBE FRS 46 (Amendments to PBE FRS 47)

In accordance with the protocols established between the New Zealand Accounting Standards Board (NZASB) and the External Reporting Board (XRB Board), the NZASB has:

- approved for issue *Withdrawal of PBE FRS 46 (Amendments to PBE FRS 47)*;
- provided a signing memo outlining the due process followed before reaching that decision, and other related information.

I have reviewed the signing memo and am satisfied with the information provided. Accordingly, the NZASB is hereby authorised to issue *Withdrawal of PBE FRS 46 (Amendments to PBE FRS 47)* pursuant to section 12(a) of the Financial Reporting Act 2013.

Dated this 14th day of February 2020

A handwritten signature in black ink, appearing to read 'Michele Embling', written over a dotted line.

Michele Embling
Chair
External Reporting Board



APPROVAL NZASB 115

Approval to Issue:
Revocation of PBE FRS 46

In accordance with the protocols established between the New Zealand Accounting Standards Board (NZASB) and the External Reporting Board (XRB Board), the NZASB has:

- approved for issue *Revocation of PBE FRS 46*; and
- provided a signing memo outlining the due process followed before reaching that decision, and other related information.

I have reviewed the signing memo and am satisfied with the information provided. Accordingly, the NZASB is hereby authorised to issue *Revocation of PBE FRS 46* pursuant to section 12(f) of the Financial Reporting Act 2013.

Dated this 14th day of February 2020

A handwritten signature in black ink, appearing to read 'Michele Embling', written over a dotted line.

Michele Embling
Chair
External Reporting Board