

## Board Meeting Agenda

In-person Meeting — Thursday, 12 May 2022

External Reporting Board, Level 7, 50 Manners Street, Wellington

Est Time	Item	Topic	Objective		Page
<b>NON-PUBLIC SESSION</b>					
10.30 am 20 min	Morning tea break				
<b>PUBLIC SESSION</b>					
10.50 am 40 min	<b>5</b>	<b>Disclosure of Fees Paid to Audit Firms</b>	(AH)		
	5.1	Cover memo	Consider	Late Paper	–
	5.2	Draft ITC	Approve	Late Paper	–
	5.3	Draft ED – Amendments to FRS 44	Approve	Late Paper	–
	5.4	Draft ED – Amendments to PBE IPSAS 1	Approve	Late Paper	–
	5.5	IFAC: <i>Audit Fees Survey 2022: Understanding Audit and Non-Audit Service Fees, 2013-2020</i>	Note	<a href="#">Link</a>	–
<b>NON-PUBLIC SESSION</b>					
12.20 pm 40 min	Lunch break				
<b>PUBLIC SESSION</b>					
1.30 pm 50 min	<b>8</b>	<b>Primary Financial Statements – project update (with IASB staff guest)</b>	(CB)		
	8.1	Presentation slides	Note	Paper	3
	8.2	NZASB comment letter on IASB ED <i>General Presentation and Disclosures</i>	Note	Paper	20
2.20 pm 30 min	<b>9</b>	<b>Definition of Public Accountability</b>	(AH/GS)		
	9.1	Cover memo	Consider	Paper	50
	9.2	Draft ITC	Consider	Paper	61
	9.3	Draft ED <i>Definition of public accountability – narrow-scope amendments to XRB A1</i>	Consider	Paper	72
2.50 pm 20 min	Afternoon tea break				

Est Time	Item	Topic	Objective		Page
3.10 pm	<b>10</b>	<b>IPSASB Conceptual Framework Update</b>	(GS)		
30 mins	10.1	Cover memo	Consider	Paper	80
	10.2	Draft comment letter	Approve	Paper	86
	10.3	IPSASB ED 81 <i>Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements in Financial Statements</i>	Consider	<a href="#">Link</a>	–
3.40 pm	<b>11</b>	<b>Tier 3 and Tier 4 – outreach plan</b>	(JC/CB)		
20 min	11.1	Cover memo – outreach plan	Consider	Paper – in separate batch	–
	11.2	Tier 3 and Tier 4 Consultation Documents	Consider	Paper – in separate batch	–
<b>NON-PUBLIC SESSION</b>					
4.20 pm	<i>Finish</i>				

Next NZASB meeting: 29 June 2022 (Wellington)

# Primary Financial Statements Project

Update on the IASB's deliberations  
following analysis of ED feedback



NZASB Meeting

May 2022

# Overview of the project and current status

## Objective of the project

- Improve the communication of information in the financial statements, with a focus on the information included in the statement of profit or loss (P&L)

## Main proposals

- Additional **subtotals** in the P&L
- Strengthened requirements for the **disaggregation** of information
- Disclosure of **management performance measures** (MPMs)



## Timeline

December 2019  
ED issued

Q1–Q2 2020  
ED consultation period

Q4 2020  
Discussion of feedback  
summary

2021–2023  
IASB redeliberations

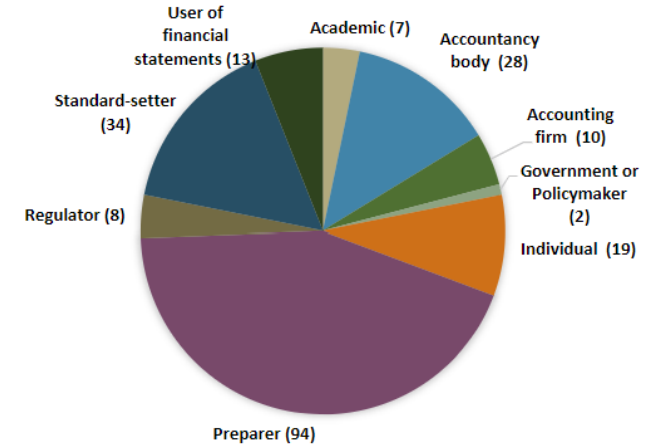
## Status of deliberations\*

Topic	Topics discussed	Remaining topics to be discussed
Subtotals and categories	<ul style="list-style-type: none"> <li>• Required subtotals</li> <li>• Classification in categories, general model</li> <li>• Associates and JVs</li> </ul>	<ul style="list-style-type: none"> <li>• Remaining issues relating to classification by entities with specified main business activities</li> <li>• Remaining issues related to investing and financing categories</li> </ul>
Disaggregation and other	<ul style="list-style-type: none"> <li>• Roles of primary financial statements and notes</li> <li>• General principles of aggregation and disaggregation</li> <li>• Direction for unusual income and expenses</li> <li>• Presentation of operation expenses</li> <li>• Direction for disclosure of operating expenses</li> <li>• Statement of cash flows</li> <li>• Disclosure of operating expenses</li> </ul>	<ul style="list-style-type: none"> <li>• Definition of unusual income and expenses, related disclosures</li> <li>• Remaining issues relating to disclosure of operating expenses</li> <li>• Proposals relating to items labelled “other” and other remaining general disaggregation topics</li> <li>• Remaining proposals for the SCF</li> <li>• Consequential amendments</li> </ul>
Management performance measures	<ul style="list-style-type: none"> <li>• Scope and definition</li> <li>• Disclosure of reconciliation</li> </ul>	<ul style="list-style-type: none"> <li>• Disclosure of tax and NCI</li> <li>• Changes in MPMs, use of columns, relationship with segments and other</li> </ul>

\* Including topics discussed at the April 2022 IASB meeting

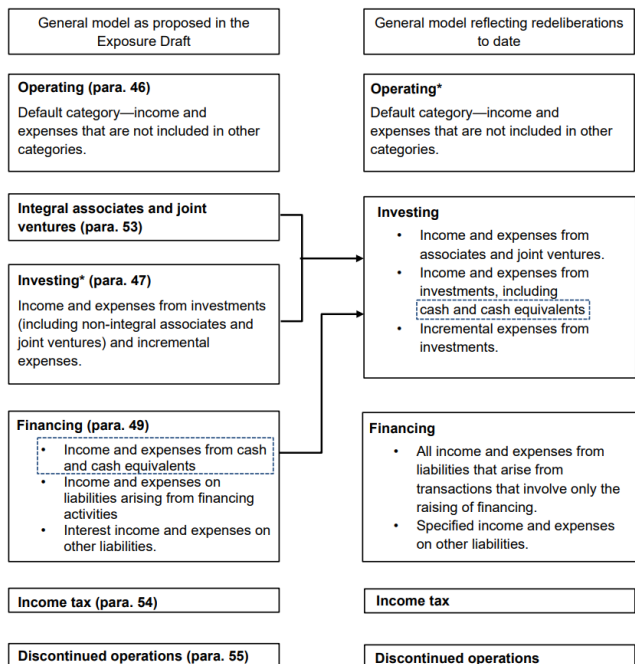
## Feedback on the ED

- 215 comment letters received
- Key messages received:
  - Proposals generally well-received, particularly by users
  - General agreement with the proposals for categories and subtotals, and management performance measures (although there were calls to expand the scope for MPMs to include more non-GAAP measures)
  - Mixed views on integral vs non-integral associates and JVs, and analysing operating expenses by nature and by function – conceptual and operational challenges
  - General agreement on proposals relating to disaggregation and unusual income and expenses, but concerns raised about the proposed definition of unusual income and expenses



# IASB deliberations – subtotals and categories

## Structure of the statement of profit or loss




\* Default category for gains and losses on derivatives and hedging instruments.

## Key changes from the ED

- Classification of income and expenses from cash and cash equivalents from financing to investing category
- Distinction between integral and non-integral associates and JVs removed, as well as the related subtotal
- Income and expenses from associates and JVs classified in the investing category
- Application guidance added for various concepts


## Subtotals and categories – matters raised by the NZASB

NZASB Submission*	IASB Response	Comments
[Q1, para. 4] Subtotals in the statement of profit or loss should be labelled consistently across entities.		The IASB will discuss this topic at a future meeting.
[Q5, para. 21-23] Users may not understand the difference between the definition of the proposed investing category in the SPL and “investing activities” in the SCF – consider using different / more descriptive terms.		The labelling of the investing category in the SPL is only used in the wording of the requirements in the new Accounting Standard (i.e. not on the face of the SPL itself) – therefore, likely to be less confusing for users. The requirements will be accompanied by an explanation of the differences between the categories in the SCF and SPL.
[Q6, para. 27] Include guidance on whether incremental expenses relating to financing activities should also be included in the financing category (ED was silent on this).		The IASB will discuss this topic at a future meeting.

\* References in square brackets are to the NZASB’s comment letter (agenda item 8.2)



## Subtotals and categories – matters raised by the NZASB

NZASB Submission*	IASB Response	Comments																													
<p>[Q6 para. 28-29] With respect to the proposed definition of “financing activities”, clarify:</p> <ul style="list-style-type: none"> <li>- how the proposed definition of “financing activities” interacts with interest recognised on interest free or low interest loans recognised initially at fair value.</li> <li>- Whether the “payment of a finance charge” would include notional interest calculated for accounting purposes, rather than a contractual interest charge.</li> </ul>		<p>The IASB decided to require an entity to classify in the financing category of the statement of profit or loss:</p> <ul style="list-style-type: none"> <li>- all income and expenses from liabilities that arise from transactions that involve only the raising of finance; and</li> <li>- specified income and expenses from other liabilities.</li> </ul>																													
<p>[Q7, para. 33] Instead of the proposed classification of associates and JVs as either integral or non-integral, the P&amp;L should reflect the following presentation:</p> <table border="1" data-bbox="137 689 929 1046"> <tbody> <tr> <td>Revenue</td> <td>X</td> <td rowspan="2">Operating</td> </tr> <tr> <td>Operating expenses</td> <td>(X)</td> </tr> <tr> <td><b>Operating profit or loss</b></td> <td><b>X</b></td> <td></td> </tr> <tr> <td>Share of profit or loss from associates and JVs</td> <td>X</td> <td rowspan="2">Investing</td> </tr> <tr> <td>FV movements for other associates and JVs measured at fair value</td> <td>X</td> </tr> <tr> <td>Income from investments</td> <td>X</td> <td></td> </tr> <tr> <td><b>Profit or loss before financing and income tax</b></td> <td><b>X</b></td> <td></td> </tr> <tr> <td>Interest revenue from cash and cash equivalents</td> <td>X</td> <td rowspan="3">Financing</td> </tr> <tr> <td>Expenses from financing activities</td> <td>(X)</td> </tr> <tr> <td>Unwinding of discount on pension liabilities and provisions</td> <td>(X)</td> </tr> <tr> <td><b>Profit or loss before tax</b></td> <td><b>X</b></td> <td></td> </tr> </tbody> </table>	Revenue	X	Operating	Operating expenses	(X)	<b>Operating profit or loss</b>	<b>X</b>		Share of profit or loss from associates and JVs	X	Investing	FV movements for other associates and JVs measured at fair value	X	Income from investments	X		<b>Profit or loss before financing and income tax</b>	<b>X</b>		Interest revenue from cash and cash equivalents	X	Financing	Expenses from financing activities	(X)	Unwinding of discount on pension liabilities and provisions	(X)	<b>Profit or loss before tax</b>	<b>X</b>			<p><b>Oct 2021</b> – the Board decided not to require an entity to distinguish between integral and non-integral associates and JVs</p> <p><b>Dec 2021</b> – the Board decided to classify income and expenses from associates and joint ventures in the investing category.</p>
Revenue	X	Operating																													
Operating expenses	(X)																														
<b>Operating profit or loss</b>	<b>X</b>																														
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\* References in square brackets are to the NZASB’s comment letter (agenda item 8.2)

# IASB deliberations – disaggregation and other

## Key themes

Analysis of operating expenses by nature and function

Roles of the primary financial statements and notes

Principles for aggregation and disaggregation

Required line items (including goodwill)



Unusual income and expenses

Requirements for grouping dissimilar immaterial items

## Key changes from the ED

- Emphasise that a single dissimilar characteristic can be enough to disaggregate if it is material.
- Add application guidance on when disaggregation in the notes would result in material information and when disaggregation in the primary financial statements would result in a more understandable overview.
- Removed the proposed prohibition on a mixed presentation approach for operating expenses.
- Remove “limited predictive value” from definition of unusual items and add application guidance.
- Amend the specified subtotal “operating profit or loss before depreciation and amortisation” to exclude impairments of assets within the scope of IAS 36.

## Disaggregation and other – matters raised by the NZASB


NZASB Submission*	IASB Response	Comments
<p>[Q8, para. 36] The new Accounting Standard should acknowledge that the primary financial statements and the notes are both equally important in meeting the objective of financial statements.</p>		<p>The IASB has decided to include the following sentence in the new Accounting Standard: “The objective [of financial statements] is achieved by providing financial information in the primary financial statements and in the notes”</p>
<p>[Q8, para. 47] Caution needed when requiring an entity to disaggregate an “other expenses” line made up of <u>immaterial</u> items where the entity has made every effort to apply the principles of disaggregation proposed in the new Accounting Standard, and the resulting amount in “other expenses” is <u>immaterial</u>. Suggest amending para. 28 in the ED to clarify this, and include this scenario in the Illustrative Examples.</p>		<p>The IASB will discuss proposals relating to “other” items at a future meeting.</p>
<p>[Q9, para. 49-50] Entities should be allowed to provide a mixed method of analysis of expenses, if a mixed method provides the most useful information to users.</p>		<p>The IASB has decided to remove the proposed prohibition on a mixed method and to explore providing application guidance in order to improve comparability and help achieve faithful representation.</p>

\* References in square brackets are to the NZASB’s comment letter (agenda item 8.2)

## Disaggregation and other - matters raised by the NZASB


NZASB Submission [response to Q9]	IASB Response	Comments
<p>It should not be mandatory for an entity to disclose an analysis of its total operating expenses if it presents an analysis of expenses using the function of expense method in the SFP.</p>		<p>The IASB has deferred a decision on the extent of the requirement for this disclosure. The IASB will make that decision after it has considered further analysis of feedback on this topic. In particular, at its April 2022 meeting the IASB had an educational session on two options for a “partial matrix approach”.</p>
<p>Remove the requirement to present minimum line items in the P&amp;L – instead, particular types of income or expenses could be disclosed in the notes, if necessary to meet user information needs (rather than presented on the face of the P&amp;L).</p>	<p style="text-align: center;">✓</p>	<p>The IASB agreed to revise the introductions to the lists of required line items in paragraphs 65 and 82 of the ED to <i>“In addition to items required by other IFRS Accounting Standards, unless doing so reduces how useful the statement is in providing an understandable overview of the entity’s income and expenses [or assets, liabilities and equity], an entity shall present in the statement of profit or loss [or statement of financial position] line items for...”</i></p> <p>The Board also agreed to use the word “specified” instead of “minimum” in paragraph 42 of the ED.</p>

## Disaggregation and other - matters raised by the NZASB

NZASB Submission*	IASB Response	Comments
<p>[Q10, para. 56-61] Do not define or require disclosure of “unusual items” – instead:</p> <ul style="list-style-type: none"> <li>- Use requirements in IAS 1 relating to the disclosure of material items</li> <li>- Add the “occurrence of other unusual or infrequently occurring items” to the list of circumstances for separate disclosure of income and expense items.</li> <li>- Add requirements for fair presentation of these unusual or other infrequently occurring items.</li> </ul>		<p>The IASB has decided to remove “limited predictive value” from the definition and develop application guidance to accompany the definition. Further aspects of this topic will be discussed at a future meeting.</p>
<p>[Q13, para. 86] No separation of cash flows from investments into those from integral and non-integral associates and JVs.</p>		<p>The IASB decided not to require an entity to distinguish between integral and non-integral associates and JVs.</p>

\* References in square brackets are to the NZASB’s comment letter (agenda item 8.2)

## Disaggregation and other - matters raised by the NZASB

NZASB Submission*	IASB Response	Comments
<p>[Q8, para. 39-44] Guidance on materiality should be included in the new Accounting Standard, as the concept of materiality and materiality judgements play a critical role in the presentation and disclosure of information in financial statements.</p>		<p>The IASB has decided to include a reference to understandability in the description of the role of the primary financial statements and provide application guidance on when disaggregation in the notes would result in material information and when disaggregation in the primary financial statements would result in a more understandable overview.</p>
<p>[Q8, para. 45] Include paragraph 97 from IAS 1 which states “when items of income and expense are material, an entity shall disclose their nature and amount separately”</p>		<p>Not specifically discussed during deliberations, but the IASB has emphasised that a single dissimilar characteristic can be enough to disaggregate if it is material.</p>

\* References in square brackets are to the NZASB's comment letter (agenda item 8.2)

# IASB redeliberations – management performance measures

## Key themes

### Definition

- Subtotals of income and expense that:
  - ❖ Are used in public communications outside the financial statements
  - ❖ Complement totals or subtotals specified by IFRS Standards
  - ❖ Communicate management's view of an aspect of an entity's financial performance
- Other financial performance measures such as free cash flow, or non-financial performance measures such as number of subscribers, would not be included.

### Disclosures

- Amount and narrative description, including:
  - ❖ Reconciliation between the MPM and the most directly comparable total or subtotal specified by IFRS Standards; and
  - ❖ Income tax effects and effects on NCI.

## Key changes from the ED




- Introduce a rebuttable presumption that a subtotal used in public communications represents management's view of an aspect of the entity's financial performance.
- Subtotal of income and expense used in the numerator or denominator of a ratio is an MPM
- Disclose, for each reconciling item, amount(s) related to each line item in the statement(s) of financial performance.

## Management performance measures – matters raised by the NZASB

NZASB Submission [response to Q11]	IASB Response	Comments
The definition of MPMs – currently restricted only to subtotals of income and expenses – should be widened to include other non-GAAP financial measures that are derived from an IFRS amount in the financial statements	✘	The IASB decided that the scope will not be widened beyond what was proposed in the ED. The IASB also confirmed that if a numerator or denominator of a ratio meets the definition of an MPM, that numerator or denominator should included in the scope of the MPM requirements.
Guidance is required to clarify the intended scope of “public communications outside the financial statements” used in the definition of MPMs.	✔	The IASB has decided to narrow the scope by excluding oral communications, transcripts and social media posts.
An explanation should be added in the application guidance regarding the purpose of the requirement that MPMs are subtotals of income and expenses that “ <u>complement totals or subtotals specified by IFRS Standards</u> ”.	✘	The IASB has decided to remove the underlined wording from the definition.
Remove the restriction that an MPM should only be disclosed when it “faithfully represents aspects of the financial performance of the entity to users...”	✔	The IASB decided to remove this specific requirement given the general requirement for information to give a faithful representation.
The illustrative example in the ED relating to MPMs is too generic and is not very helpful.	The IASB will discuss illustrative examples at a future meeting.	



## Management performance measures – matters raised by the NZASB

NZASB Submission [response to Q11 and Q12]	IASB Response	Comments
<p>The NZASB received feedback that currently some companies do not adequately explain why a non-GAAP measure provides useful information to users – generic explanations provided.</p>		<p>The IASB decided to provide additional application guidance to support the requirement to disclose an explanation of how an MPM provides useful information about the entity's performance.</p>
<p>The new Accounting Standard should state that reconciling items must be described in a clear and understandable manner.</p>		<p>Not specifically discussed during deliberations, but application guidance has been proposed to clarify when the requirements in paragraph 106 of the ED would apply to the individual reconciling items (which may address this point).</p>
<p>Provide guidance to clarify when EBITDA could be presented on the face of the SPL – also clarify that EBITDA can be presented in the notes as an MPM.</p>		<p>The IASB decided not explicitly to prohibit “EBITDA” as a label for an “operating profit or loss before depreciation, amortisation and specified impairments” subtotal (but to explain in the BCs that such a label would rarely be a faithful representation for the subtotal).</p>
<p><b>Consider including BC165 in the new Accounting Standard:</b></p> <p>BC165 However, the Board expects that few management performance measures would meet the requirements for presentation as a subtotal in the statement(s) of financial performance. To meet the requirements, such subtotals must:</p> <ul style="list-style-type: none"> <li>(a) fit into the structure of the proposed categories (see paragraph BC28);</li> <li>(b) not disrupt the presentation of an analysis of expenses in the operating category using either the function of expense or nature of expense method (see paragraph BC109); and</li> <li>(c) comprise amounts recognised and measured applying IFRS Standards.</li> </ul>	<p>Presentation of MPMs on the face of the SPL will be discussed at a future meeting.</p>	

## Other matters raised by the NZASB

NZASB Submission [response to Q14]	IASB Response	Comments
Suggestion for a comprehensive project on going concern issues to be added to the IASB agenda.	✘	At its March 2022 meeting, the IASB added going concern disclosures to its shortlist of projects to be added to the IASB work plan for 2022 to 2026. At its April 2022 meeting the IASB decided not to add this project to the work plan.
Suggestion for a specific project on OCI to be added to the IASB agenda.	✘	At its March 2022 meeting, the IASB decided not to add a project on OCI to the shortlist of projects to be discussed at a future meeting, for the purposes of its work plan for 2022 to 2026. □
Clarification on the presentation of negative interest.	✔	The IASB confirmed that negative returns, such as those arising from unfavourable exchange rates or negative interest rates, are classified in the same category as positive returns arising from the asset. Negative interest expense on liabilities is classified in the same category as positive interest expense. □
Illustrative examples should be entity-specific, avoid boilerplate examples. Clarity on the classification of FV movements for biological assets would be helpful. Illustrative examples appear to be contradictory on whether “impairment losses on trade receivables” represents an analysis of expense by nature or function.	The IASB will discuss illustrative examples at a future meeting.	

## Questions for Board members

- Does the Board have any questions / comments on this presentation?
- The IASB is currently considering topics to test through targeted outreach, which would most likely commence after the ASAF meeting in mid-July. Does the Board have any suggestions on topics (that have been redeliberated to date) that should be included in this outreach?
- Would the Board like to participate in this targeted outreach?
- Are there any topics, which have not yet been deliberated, where the Board would encourage staff to explore approaches for influencing the direction of the IASB deliberations? We welcome any suggestions on what those approaches might be.

21 September 2020

Mr Hans Hoogervorst  
Chairman of the International Accounting Standards Board  
IFRS Foundation  
Columbus Building  
7 Westferry Circus  
Canary Wharf  
London E14 4HD  
**United Kingdom**

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

Dear Hans

**ED/2019/7 *General Presentation and Disclosures***

Thank you for the opportunity to comment on ED/2019/7 *General Presentation and Disclosures*. The ED has been exposed for comment in New Zealand and some New Zealand constituents may comment directly to you.

We are very supportive of the IASB's projects to help make financial information more useful and improve the way financial information is communicated to users of the financial statements.

***Overall comments***

We support the proposals to provide more structure to the statement of profit or loss by introducing defined and required subtotals. We acknowledge there can be tension between increasing comparability and allowing sufficient flexibility for an entity to communicate its performance story. The proposals in the ED allow an entity to communicate management's view of performance by disclosing information about management performance measures in the notes to the financial statements. We are of the view that the package of proposals can increase comparability between entities without adversely affecting the ability of individual entities to communicate their story to the users of their financial statements.

***Materiality***

We are of the view that the concept of materiality and materiality judgements plays a critical role in the presentation and disclosure of information in financial statements. Because an entity makes materiality judgements when making decisions about recognition and measurement, as well as presentation and disclosure, we can understand the IASB's rationale for proposing to move the definition of material and associated guidance to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* as the concept of materiality is pervasive in the preparation of financial

statements. However, we believe the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard.

With presentation and disclosure – and particularly disclosure – there are good reasons why a general presentation and disclosure standard should include specific guidance on applying materiality. By including such guidance in a general presentation and disclosure standard, that guidance could then be applied (via cross-reference) to all other standards containing disclosure requirements.

Please refer to our response to question 8(b) for a detailed discussion on materiality.

### ***The proposals***

While we support many of the proposals in the ED, there are some areas where we disagree or recommend improvements. We have highlighted these areas below (see our response to the questions for our detailed recommendations and responses).

#### *The investing category (Question 5)*

In relation to the proposed new categories of ‘operating’, ‘investing’ and ‘financing’ in the statement of profit or loss, we strongly recommend that the IASB considers using different terms or more descriptive terms than those used in the statement of cash flows. Using the same terms as the statement of cash flows, but with a different meaning will be very confusing for users of financial statements.

#### *Integral and non-integral associates and joint ventures (Question 7)*

We do agree that separately presenting operating profit or loss and income and expenses from associates and JVs provides useful information to users of financial statements. However, we do not agree with the proposal to classify associates and joint ventures accounted for using the equity method as integral or non-integral. The classification would require significant judgement to be applied, would result in lack of comparability and would be difficult to audit. Furthermore, IFRS 12 *Disclosure of Interests in Other Entities* already requires entities to disclose information about the nature, extent and financial effects of their interests in associates and JVs.

#### *Analysis of operating expenses (Question 9)*

We do not agree with the proposal that an entity shall present in the operating category of the statement of profit or loss an analysis of expenses using a classification based on either the nature or function of the expense. Our view is that companies should be allowed the flexibility to determine the most appropriate analysis of expenses, even if that results in a mixed analysis.

#### *Unusual income and expenses (Question 10)*

We do not agree with the IASB proposals to define and require disclosure by all entities of unusual income and expenses. We have concerns that the proposals as currently drafted will not be operable.

### *Management Performance Measures (Question 11)*

While we agree that MPMs provide useful information and should be included in the financial statements (as this will bring more transparency and discipline to the reporting of these financial performance measures), we have concerns with the proposals as they are currently drafted.

### ***Going concern***

The economic impact of the COVID-19 pandemic is expected to increase the level of uncertainty over the ability of many entities to continue as a going concern for financial reporting purposes. As a result, the NZASB recently issued domestic narrow-scope amendments to FRS-44 *New Zealand Additional Disclosures*<sup>1</sup> to improve going concern disclosures to provide better information to users of financial statements during this period of exceptional circumstances.

The issue of New Zealand specific disclosures is a short-term measure to deal with the most pressing need for improved disclosures. We strongly recommend that the IASB add a project to its agenda to look at going concern issues more comprehensively. The major economic disruption from COVID-19 has highlighted this matter as an area where improvements are needed.

### ***Questions for respondents***

Our detailed recommendations and responses to the specific questions for respondents are provided in the Appendix to this letter.

### ***New Zealand outreach***

We would like to take the opportunity to thank IASB staff member Aida Vatrenjak for her assistance with an outreach event we held on the proposals with institutional investors in New Zealand.

If you have any queries or require clarification of any matters in this letter, please contact Lisa Kelsey ([Lisa.Kelsey@xrb.govt.nz](mailto:Lisa.Kelsey@xrb.govt.nz)) or me.

Yours sincerely



Michael Bradbury

**Acting Chair – New Zealand Accounting Standards Board**

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<sup>1</sup> *Going Concern Disclosures* (Amendments to FRS-44)

## Appendix to *General Presentation and Disclosures*

### Question 1—operating profit or loss

Paragraph 60(a) of the Exposure Draft proposes that all entities present in the statement of profit or loss a subtotal for operating profit or loss.

Paragraph BC53 of the Basis for Conclusions describes the Board’s reasons for this proposal.

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

#### *Response to question 1*

1. We agree with the proposal that all entities present in the statement of profit or loss a subtotal for operating profit or loss.
2. Like the IASB, we have also seen diversity in practice, in terms of (a) entities that present an operating profit subtotal and others that do not; and (b) for those entities that do present an operating profit subtotal, what the subtotal comprises.
3. We believe that having a consistent view of the income and expenses that are included in a subtotal for operating profit or loss will reduce diversity in practice and improve comparability between entities.

#### *Other comments*

4. We note that the IASB is proposing to bring forward paragraph 8 (shown below) from IAS 1 *Presentation of Financial Statements* into the proposed new IFRS Standard (as paragraph 12). Paragraph 8 of IAS 1 has been amended to include a reference to subtotals. Paragraph 12 of the proposed IFRS X *General Presentation and Disclosures* allows entities to use another label when presenting the new operating profit or loss subtotal. In fact, entities may be able to use different labels for all the proposed new subtotals. As the main objective of the proposals to add defined subtotals to the statement of profit or loss is to increase comparability between entities, we believe that these new required subtotals should be labelled consistently across entities. We recommend that the IASB amend paragraph IFRS X.12 to exclude the subtotals required by paragraph 60 of IFRS X. This will also remove the risk that entities may label the new subtotals with existing labels which may confuse users.

<b>A comparison of proposals with requirements in IAS 1 <i>Presentation of Financial Statements</i></b>		
<b>IAS 1 para #</b>	<b>Revised text (new text underlined, deleted text struck through)</b>	<b>New para #</b>
IAS 1.8	Although this <u>[draft]</u> Standard uses <del>the</del> terms <u>such as</u> ‘other comprehensive income’, ‘profit or loss’ and ‘total comprehensive income’, an entity may use other terms to describe the totals, <u>subtotals and line items required by this [draft] Standard</u> as long as the meaning is clear. For example, an entity may use the term ‘net income’ to describe profit or loss.	IFRS X.12

## Question 2—the operating category

Paragraph 46 of the Exposure Draft proposes that entities classify in the operating category all income and expenses not classified in the other categories, such as the investing category or the financing category.

Paragraphs BC54–BC57 of the Basis for Conclusions describe the Board’s reasons for this proposal.

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

### *Response to question 2*

5. We agree with the proposal that entities classify in the operating category all income and expenses not classified in the other categories, such as the investing category or the financing category.
6. We acknowledge the challenges the IASB faced trying to define operating profit or loss. We agree that, because entities have various business activities, it is difficult to arrive at a direct definition of operating profit or loss that could be applied consistently, even between entities in the same industry. Therefore, for practical reasons we support the operating category being a default or residual category.
7. We agree that the operating category should include all income and expenses from an entity’s main business activities. We have discussed main business activities in more detail under question 3.
8. We have heard concerns that the proposal not to define operating profit or loss directly may mean that some income and expenses not arising from an entity’s core operations may be classified as operating by virtue of the fact that those income and expenses do not meet the definitions to be classified in the other categories. However, in considering this concern, we are satisfied that the disaggregation proposals should provide the users of the financial statements with enough information to enable adjustments to be made where appropriate.



**Question 3—the operating category: income and expenses from investments made in the course of an entity’s main business activities**

Paragraph 48 of the Exposure Draft proposes that an entity classifies in the operating category income and expenses from investments made in the course of the entity’s main business activities.

Paragraphs BC58–BC61 of the Basis for Conclusions describe the Board’s reasons for this proposal.

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

*Response to question 3*

9. We agree with the proposal that an entity classifies in the operating category income and expenses from investments made in the course of the entity’s main business activities.
10. The ability for an entity to classify income and expenses from investments as operating rather than investing rests on the application of judgement as to what is “generated in the course of its main business activities”. For some entities, for example, global conglomerates with multiple business activities, significant judgement may be involved in determining the entity’s main business activities. In our response to Question 2 we have agreed with the IASB’s proposals not to define operating profit or loss and agreed that, because entities have various business activities, it is difficult to arrive at a direct definition of operating profit or loss that could be applied consistently, even between entities in the same industry. We believe the IASB would have the same difficulty if we requested a definition or further guidance on what is meant by ‘main business activities’.
11. We note that the IASB is proposing to bring across paragraph 138 of IAS 1 into the new IFRS X as paragraph 99. This will require an entity to disclose in the notes (if not disclosed elsewhere) a description of the entity’s main business activities. It is this description of main business activities that will drive the classification of income and expenses into each of the categories.
12. We also note that an entity may disclose information on the significant judgements involved in determining an entity’s main business activities under paragraph 122 of IAS 1, which is moving to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* as paragraph 27E.
13. We are of view that the above disclosures should give users of the financial statements enough information about an entity’s main business activities and how this has affected the classification of income and expenses in the statement of profit or loss. Any information provided on main business activities and subsequent classification of income and expenses should also be consistent with any business model information that may be provided by an entity in its annual report, for example, in its management commentary.

*Other comments*

14. Investors have told us they would support proposals that are applicable to as many company types as possible. They agree with the proposals for banks but would not like to see other exceptions or modifications being made for other types of business.

**Question 4—the operating category: an entity that provides financing to customers as a main business activity**

Paragraph 51 of the Exposure Draft proposes that an entity that provides financing to customers as a main business activity classify in the operating category either:

- income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or
- all income and expenses from financing activities and all income and expenses from cash and cash equivalents.

Paragraphs BC62–BC69 of the Basis for Conclusions describe the Board’s reasons for the proposals.

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

*Response to question 4*

15. We agree with the proposal in paragraph 51 of the ED that an entity that provides financing to customers as a main business activity classify in the operating category either:
  - (a) income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or
  - (b) all income and expenses from financing activities and all income and expenses from cash and cash equivalents.
16. We agree that when an entity provides financing to customers as a main business activity, the difference between the interest revenue from that activity and the related interest expense (a cost of earning that income) is an important indicator of operating performance. The IASB’s proposals would enable entities such as banks to continue presenting a net interest income subtotal.
17. We initially had reservations about allowing alternative accounting policy choices because they can lead to a loss of comparability between entities. In addition, if an entity chooses to allocate all income and expenses from cash and cash equivalents and financing activities to the operating category, this could result in a loss of relevant information for users. For example, a car manufacturer that provides financing to customers as one of its main business activities may elect to allocate all income and expenses from cash and cash equivalents and financing activities to the operating category. In this case, the car manufacturer would not present a subtotal for profit or loss before financing and income tax and, effectively, the income statement would not have a separate category for financing. The user of the financial statements would therefore not have access to information about the financing activities undertaken by the car manufacturer that are unrelated to the provision of financing to customers.
18. However, we have received feedback from some New Zealand banks (the entities most likely to make use of the proposed accounting policy choice) that any methodologies to split (i) income and expenses from financing activities, and from cash and cash equivalents, that

relate to the provision of financing to customers from (ii) income and expenses from financing activities and from cash and cash equivalents that are unrelated to the provision of financing to customers would be arbitrary at best.

19. We therefore agree with the IASB that an allocation should not be required but should be permitted.

### Question 5—the investing category

Paragraphs 47–48 of the Exposure Draft propose that an entity classifies in the investing category income and expenses (including related incremental expenses) from assets that generate a return individually and largely independently of other resources held by the entity, unless they are investments made in the course of the entity’s main business activities.

Paragraphs BC48–BC52 of the Basis for Conclusions describe the Board’s reasons for the proposal.

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

#### *Response to question 5*

20. We agree that an investing category will provide users with useful information about the returns from investments that are not part of the entity’s main business activities, particularly for non-financial institutions.
21. We have concerns that users will not understand the difference in the definition of the proposed investing category in the statement of profit or loss and the existing ‘investing activities’ in the statement of cash flows. Although both are labelled as investing, the definitions are not aligned. For example, cash proceeds from the disposal of property, plant and equipment would be classified as investing activities in the statement of cash flows, but the disposal gain/loss would be classified in the operating category in the statement of profit or loss. This is because property, plant and equipment are used in combination with other resources of an entity in its main business activities and do not “generate a return individually and largely independently of other resources held by an entity”.
22. One of the main criticisms levelled at financial statements is that many users do not understand them, and they are becoming more and more complicated. If the IASB then introduces the same terms, but with different meanings for the statement of profit or loss and the statement of cash flows, this will be very confusing for users of financial statements.
23. We strongly recommend that the IASB considers using different terms or more descriptive terms in each of the statements. For example, the definition for income and expenses from investments in the statement of profit or loss seems to focus on ‘distinct’ or ‘separable’ investing activities (which generate returns independently of other assets), whereas the IAS 7 definition seems to focus on ‘long-term’ investing activities. We suggest the IASB considers using a more descriptive label, based on the key underlying principle that drives the classification in each statement. We believe this would at least make it clearer that they are not the same thing.

**Question 6—profit or loss before financing and income tax and the financing category**

- (a) Paragraphs 60(c) and 64 of the Exposure Draft propose that all entities, except for some specified entities (see paragraph 64 of the Exposure Draft), present a profit or loss before financing and income tax subtotal in the statement of profit or loss.
- (b) Paragraph 49 of the Exposure Draft proposes which income and expenses an entity classifies in the financing category.

Paragraphs BC33–BC45 of the Basis for Conclusions describe the Board’s reasons for the proposals.

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

*Response to question 6*

- 24. We support the proposal for entities to present a profit or loss before financing and income tax subtotal in the statement of profit or loss, other than some specific entities (i.e. entities that provide financing to customers as a main business activity (e.g. banks) and classify all income and expenses from financing activities and all income and expenses from cash and cash equivalents in the operating category).
- 25. We support the proposals for entities to classify in the financing category:
  - (a) income and expenses on liabilities arising from financing activities;
  - (b) income and expenses from cash and cash equivalents; and
  - (c) interest income and expenses on liabilities that do not arise from financing activities.
- 26. We acknowledge that some users have different views on the appropriate classification of income and expenses from cash and cash equivalents (e.g. as investing, financing, or operating). However, we support the inclusion of income and expenses from cash and cash equivalents in the financing category (with the proposed exceptions for some specific entities) for reasons similar to including interest income and expenses on liabilities that do not arise from financing activities in the financing category (i.e. a consistent location for the presentation of information). This consistent location would enable users to reclassify income and expenses from cash and cash equivalents to other categories if they wish to do so.
- 27. The ED stipulates that entities would classify in the investing category incremental expenses incurred to generate income and expenses from investments. However, the ED is silent on incremental expenses related to the financing category. We recommend that the IASB includes guidance on whether incremental expenses related to financing activities should also be in the financing category as this would be useful.

*Other comments*

28. The proposals define financing activities as follows:

*financing activities*: Activities involving the receipt or use of a resource from a provider of finance with the expectation that:

- (a) the resource will be returned to the provider of finance; and
- (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.

29. We suggest the IASB clarifies the following.

- (a) How the proposed definition interacts with interest recognised on interest free or low interest loans recognised initially at fair value? (The definition implies the lender is expected to be compensated for extending credit, which is not the case for interest free or low interest loans).
- (b) Whether the 'payment of a finance charge' would include notional interest calculated for accounting purposes, rather than a contractual interest charge.

### Question 7—integral and non-integral associates and joint ventures

- (a) The proposed new paragraphs 20A–20D of IFRS 12 would define ‘integral associates and joint ventures’ and ‘non-integral associates and joint ventures’; and require an entity to identify them.
- (b) Paragraph 60(b) of the Exposure Draft proposes to require that an entity present in the statement of profit or loss a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures.
- (c) Paragraphs 53, 75(a) and 82(g)–82(h) of the Exposure Draft, the proposed new paragraph 38A of IAS 7 and the proposed new paragraph 20E of IFRS 12 would require an entity to provide information about integral associates and joint ventures separately from non-integral associates and joint ventures.

Paragraphs BC77–BC89 and BC205–BC213 of the Basis for Conclusions describe the Board’s reasons for these proposals and discuss approaches that were considered but rejected by the Board.

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

#### Response to question 7

- 30. We do not agree with the proposal to classify associates and joint ventures (JVs) accounted for using the equity method as integral or non-integral. Our reasons are as follows.
  - (a) Our outreach with investors does not suggest there is a demand for this information.
  - (b) IFRS 12 *Disclosure of Interests in Other Entities* already requires entities to disclose information about the nature, extent, and financial effects of their interests in associates and JVs.
  - (c) Preparers have suggested it would be more beneficial for the IASB to reconsider whether equity accounting for associates and JVs is appropriate or whether another method should be considered.
  - (d) Any definition of ‘integral’ and ‘non-integral’ would require significant judgement to be applied, would result in lack of comparability, and would be difficult to audit.
- 31. However, we have heard from investors that it would be useful to have an entity’s share of profit or loss of associates and JVs accounted for using the equity method presented separately from operating profit or loss.
- 32. Although we do not agree with classifying associates and JVs as integral or non-integral, we do agree that separately presenting operating profit or loss and income and expenses from associates and JVs provides useful information to users of financial statements.
- 33. We suggest, for simplicity, that the IASB considers requiring the separate presentation of associates and JVs immediately below operating profit (so effectively part of the investing

category but as a separate line item). We recommend requiring the presentation of two line items to differentiate between

- (a) share of profit or loss from associates and JVs (for equity-accounted associates and JVs); and
- (b) FV movements for other associates and JVs measured at fair value (given the feedback from users).

We have shown what our suggestion would look like in Figure 1 below.

**Figure 1—Summary of a statement of profit or loss**

Revenue	X	Operating
Operating expenses	(X)	
<b>Operating profit or loss</b>	<b>X</b>	
Share of profit or loss from associates and JVs	X	Investing
FV movements for other associates and JVs measured at fair value	X	
Income from investments	X	
<b>Profit or loss before financing and income tax</b>	<b>X</b>	
Interest revenue from cash and cash equivalents	X	Financing
Expenses from financing activities	(X)	
Unwinding of discount on pension liabilities and provisions	(X)	
<b>Profit or loss before tax</b>	<b>X</b>	



**Question 8—roles of the primary financial statements and the notes, aggregation and disaggregation**

- (a) Paragraphs 20–21 of the Exposure Draft set out the proposed description of the roles of the primary financial statements and the notes.
- (b) Paragraphs 25–28 and B5–B15 of the Exposure Draft set out proposals for principles and general requirements on the aggregation and disaggregation of information.

Paragraphs BC19–BC27 of the Basis for Conclusions describe the Board’s reasons for these proposals.

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

*Response to question 8(a)*

- 34. We agree that clarifying the role of the primary financial statements and the notes would:
  - (a) help entities decide what information to disclose in the notes to explain and supplement the primary financial statements; and
  - (b) assist the IASB in deciding what information it should require to be presented in the primary financial statements or permit disclosure in the notes instead.
- 35. We agree with the proposed description of the roles of the primary financial statements and the notes.
- 36. In our view, the notes form an integral part of the financial statements. It is the combination of the primary financial statements and the notes that meets the objective of financial statements. We would like the IASB to acknowledge in IFRS X that while the primary financial statements and the notes do have separate roles to play, they are both equally important in meeting the objective of financial statements.

*Response to question 8(b)*

- 37. We are supportive of the IASB providing principles and guidance on aggregation and disaggregation. We have received feedback from users of financial statements that financial statements do not always include information that is appropriately aggregated or disaggregated. Aggregating items that have shared characteristics makes large volumes of information understandable and avoids obscuring relevant information. Similarly, disaggregating items with dissimilar characteristics provides users of financial statements with relevant information and avoids obscuring material information.
- 38. While we generally agree with the principles and guidance for aggregation and disaggregation included in the ED, we have identified below some areas for further consideration by the IASB.

*Materiality*

- 39. We are of the view that the concept of materiality and materiality judgements plays a critical role in the presentation and disclosure of information in financial statements. Because an entity makes materiality judgements when making decisions about recognition and

measurement, as well as presentation and disclosure, we can understand the IASB's rationale for proposing to move the definition of material and associated guidance to IAS 8 as the concept of materiality is pervasive in the preparation of financial statements. However, we believe the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard.

40. 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. In general, the application of recognition and measurement requirements results in quantitative information. Because recognition and measurement requirements result in quantitative information, materiality judgements are typically judgements about the magnitude of the amounts concerned, i.e. a quantitative assessment. Therefore, when applying materiality to recognition and measurement, it is often judgements about whether, and the extent to which, it is necessary to comply with the recognition and measurement requirements in standards.
41. In contrast, when applying materiality to presentation and disclosure, the following judgements are needed.
  - (a) Information might be qualitative rather than quantitative, especially information disclosed in the notes.
  - (b) Whether information is material might depend on the nature of the item, instead of (or in addition to) its magnitude (for example, the definition of unusual items considers not just the magnitude of the item but also its nature), so it is not simply a quantitative assessment.
  - (c) Materiality judgements do not merely relate to whether, and the extent to which, it is necessary to comply with the requirements of the standard. They also relate to how to apply those requirements, so are a key driver in determining what information is disclosed (as is acknowledged in the guidance on aggregation and disaggregation in paragraph B9 "In the notes, it is the concept of materiality that drives aggregation and disaggregation. To achieve the objective of financial statements, items that have dissimilar characteristics shall be disaggregated into component parts when the resulting information is material").
42. All the above points mean that materiality is not only a very important concept for presentation and disclosure, but also that it is much harder to apply in practice. The reality is that it is easier for preparers and auditors to make materiality judgements when dealing with quantitative information, so it is an easier concept to apply to recognition and measurement requirements. Therefore, it is sufficient to have materiality guidance in IAS 8 when dealing with recognition and measurement requirements. But with presentation and disclosure – and particularly disclosure – there are good reasons why a general presentation and disclosure standard should include specific guidance on applying materiality. And by including such guidance in a general presentation and disclosure standard, that guidance could then be applied (via cross-reference) to all other standards containing disclosure requirements.

43. Section 8 of the IASB’s DP/2017/1 *Disclosure Initiative—Principles of Disclosure* (POD DP) included the New Zealand Accounting Standards Board staff’s proposed approach to drafting disclosure requirements in IFRS® Standards. One of the main features of this proposed approach was placing greater emphasis on the need to exercise judgement when deciding how and what to disclose to meet the disclosure objectives.
44. Below is an extract from section 8 of the POD DP. A lot of the guidance in the section below has been picked up by the IASB in the new guidance on aggregation and disaggregation, but not all – for example, the guidance on considering the extent and mix of quantitative and qualitative information. We have included this as it may be of some help when considering what specific guidance on materiality judgements to include in a general presentation and disclosure standard.

**NZASB staff example 1—Guidance on the use of judgement**

This is an example of clarifying paragraphs emphasising the need to use judgement and could be placed in each Standard that contains disclosure requirements or could be placed in a general disclosure standard, such as in IAS 1.

- X1.1 To achieve the [overall] disclosure objective in a Standard, an entity shall use its judgement to determine the extent and appropriate mix of quantitative and qualitative information to disclose, including the extent of aggregation or disaggregation of that information. Assessments about the amount of information to disclose depend on the relative importance of an item or transaction to the entity (taking into account the nature and/or size of that item or transaction) and the amount of judgement involved in accounting for that item or transaction. Therefore, assessments need to take into account the extent to which the entity’s financial position, financial performance or cash flows are affected by:
- (a) the item or transaction; and
  - (b) risks and uncertainties associated with the item or transaction.
- X1.2 When using judgement to determine the information to be disclosed in accordance with a Standard, an entity considers:
- (a) how much emphasis to place on particular disclosures;
  - (b) the level of detail needed (taking into account the expectation that users of financial statements should have a reasonable knowledge of business and economic activities);
  - (c) how much aggregation or disaggregation to undertake; and
  - (d) whether users of the financial statements need additional information to meet the disclosure objective.
- X1.3 An entity aggregates or disaggregates disclosures in accordance with this Standard or another IFRS Standard so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics.

*Materiality – other comments*

45. The IASB is not proposing to carry forward paragraph 97 from IAS 1 which states “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.

*The label ‘other’*

46. 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.

47. We are in complete agreement that disaggregation of material items of income and expenses provides useful information to users. However, we would caution the IASB against requiring an entity to disaggregate an 'other expenses' line made up of immaterial items where the entity has made every effort to apply the principles set out in paragraphs 25 to 28 in the ED, and the resulting amount in the line item 'other expenses' is immaterial. We recommend amending paragraph 28 to clarify this. We also suggest including this scenario in the illustrative examples.
48. In support of our comments in the paragraph above, we have received feedback that too much emphasis on disaggregation is counterinitative with the focus in recent years on decluttering financial statements. The concern is that the proposals in the ED may cause the pendulum to swing too far in the other direction and have the effect of cluttering the financial statements.

### Question 9—analysis of operating expenses

Paragraphs 68 and B45 of the Exposure Draft propose requirements and application guidance to help an entity to decide whether to present its operating expenses using the nature of expense method or the function of expense method of analysis. Paragraph 72 of the Exposure Draft proposes requiring an entity that provides an analysis of its operating expenses by function in the statement of profit or loss to provide an analysis using the nature of expense method in the notes.

Paragraphs BC109–BC114 of the Basis for Conclusions describe the Board’s reasons for the proposals.

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

#### *Response to question 9*

49. We do not agree with the proposal that an entity shall present in the operating category of the statement of profit or loss an analysis of expenses using a classification based on either their nature or function. Our reasons are as follows.
- (a) In practice, we observe that it is common for companies to provide a mixed method of analysis based on the type of analysis that companies regard as providing the most useful information to users of their financial statements. Our view is that companies should be allowed the flexibility to determine the most appropriate analysis of expenses, even if that results in a mixed analysis.
  - (b) We have received feedback that companies report an analysis of expenses that reflects the way they track and manage the expenses internally. Requiring companies to then report in a different manner in our view will add to the costs for little benefit.
  - (c) Our outreach has shown that there is not a good understanding of what is meant by an analysis of expenses by nature or function.
  - (d) 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.
50. We acknowledge that our comments above may be seen as inconsistent with views expressed earlier in our comment letter, where we agreed with increased structure in the statement of profit or loss (by way of categories and subtotals) to aid comparability. In our view standardisation of the structure of the statement of profit or loss—including the key subtotals—is sufficient to improve comparability, without the need to take that standardisation a step further by being overly prescriptive in how expense line items are presented.

51. We do not agree with the proposal that an entity presenting an analysis of expenses using the function of expense method shall also disclose in a single note an analysis of its total operating expenses using the nature of expense method. Our reasons are as follows.
- (a) Some may argue that the above is already required under the existing requirement in IAS 1, but in our experience the existing requirement is not interpreted as requiring a comprehensive analysis in the notes. Rather, selected additional information is provided, for example, depreciation, amortisation, and employee benefit expense (possibly because these items are individually listed in paragraph 104 of IAS 1).
  - (b) We have concerns with the practical application of the requirement. 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.
  - (c) As well as the practical application problem above, there is also a conceptual problem with requiring 'cost of goods sold' to be reanalysed. Conceptually, if this line item is just made up of inventory, then it is not actually a functional line item. Rather, it is the cost of an asset (inventory) that is expensed at the point that it is sold to another party. For a manufacturing entity, the analysis required under the proposals (and existing IAS 1, if you follow the illustrative example) involves a decapitalisation process, to break down the cost of this asset into the original inputs (for example, raw materials, employee costs, etc) that were then capitalised into inventory under IAS 2 *Inventories*. Then, to balance the total cost of inputs purchased back to the COGS expense, there is an adjusting line item for the movement in inventory. Therefore, these input costs included in the analysis are not "expenses" as defined in the conceptual framework.
52. The IASB has acknowledged in the Basis for Conclusions that it did think about the costs to preparers when it developed this proposal. However, the IASB went ahead with the proposal due to the strong demand from users for this information to forecast future operating expenses. We do understand the driver for the proposal, but we suggest that the IASB considers alternatives. For example, given that users seem to be looking for information that is based on cash flows rather than accrual accounting, an alternative is to consider the presentation and disclosure requirements in IAS 7.

*Other comments*

53. We would like the IASB to consider the removal of paragraph 65 in the ED. This paragraph requires the presentation in the statement of profit or loss of minimum line items. We would like to challenge the status quo here – why do we need to continue to have minimum line items in a general presentation and disclosure standard? The IASB has worked hard to develop new proposals, including principles and general requirements on the aggregation and disaggregation of information. The application of the IASB's proposals plus our recommendation in question 8 above to give greater emphasis to the concept of materiality should be sufficient for preparers to determine what information is presented and disclosed in the statement of profit or loss.

54. Further to the above, the requirements in paragraph 65 are an ad hoc collection of line items that have accumulated over the years, with no coherent rationale for singling out particular income or expense items.
55. As an alternative to paragraph 65, we would be supportive of the IASB retaining requirements for entities to disclose particular types of income or expenses in the notes to the financial statements, if necessary to meet user information needs, as opposed to requiring the disclosure of these line items on the face of the statement of profit or loss.

### Question 10—unusual income and expenses

- (a) Paragraph 100 of the Exposure Draft introduces a definition of ‘unusual income and expenses’.
- (b) Paragraph 101 of the Exposure Draft proposes to require all entities to disclose unusual income and expenses in a single note.
- (c) Paragraphs B67–B75 of the Exposure Draft propose application guidance to help an entity to identify its unusual income and expenses.
- (d) Paragraphs 101(a)–101(d) of the Exposure Draft propose what information should be disclosed relating to unusual income and expenses.

Paragraphs BC122–BC144 of the Basis for Conclusions describe the Board’s reasons for the proposals and discuss approaches that were considered but rejected by the Board.

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

#### *Response to question 10*

- 56. We do not agree with the IASB’s proposals to define and require disclosure by all entities of unusual income and expenses.
- 57. IAS 1 already includes a requirement to separately disclose the nature and amount of material income and expenses (paragraph 97). Paragraph 98 of IAS 1 includes examples of circumstances that would give rise to the separate disclosure of income and expenses.

#### **Information to be presented in the statement(s) of profit or loss and other comprehensive income or in the notes**

- 97 When items of income or expense are material, an entity shall disclose their nature and amount separately.**
- 98 Circumstances that would give rise to the separate disclosure of items of income and expense include:
  - (a) write-downs of inventories to net realisable value or of property, plant and equipment to recoverable amount, as well as reversals of such write-downs;
  - (b) restructurings of the activities of an entity and reversals of any provisions for the costs of restructuring;
  - (c) disposals of items of property, plant and equipment;
  - (d) disposals of investments;
  - (e) discontinued operations;
  - (f) litigation settlements; and
  - (g) other reversals of provisions.

- 58. The IASB has not carried forward paragraph 97. Paragraph 98 is carried forward into the application guidance as paragraph B15 (with minor amendments). In question 8 we commented that in our view the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard. An alternative to trying to refine the definition of unusual income and expenses is to focus on the existing requirements in IAS 1 (paragraph 97 and 98) and strengthen these requirements to ensure users receive information about material income and expenses to enable them to assess prospects for future cash flows.



59. As we acknowledged in our comment letter to the IASB on the POD DP “information on unusual or infrequently occurring items is useful to users of financial statements, because it helps them to assess the recurring/sustainable performance and make assessments about the future, provided the items are genuinely unusual or infrequently occurring”.
60. In our comment letter to the IASB on the POD DP, we did not support the development of definitions of, and requirements for, the presentation of unusual or infrequently occurring items. We suggested instead that the IASB develop principles for the fair presentation of these items.
61. Our suggestion is that the IASB relies on the existing requirements in IAS 1 (existing paragraphs 97 and 98) for the disclosure of material items, adds “occurrence of other unusual or infrequently occurring items” to the list of circumstances that would give rise to the separate disclosure of items of income and expense, and adds requirements for the fair presentation of these unusual or other infrequently occurring items.

### Question 11—management performance measures

- (a) Paragraph 103 of the Exposure Draft proposes a definition of ‘management performance measures’.
- (b) Paragraph 106 of the Exposure Draft proposes requiring an entity to disclose in a single note information about its management performance measures.
- (c) Paragraphs 106(a)–106(d) of the Exposure Draft propose what information an entity would be required to disclose about its management performance measures.

Paragraphs BC145–BC180 of the Basis for Conclusions describe the Board’s reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Do you agree that information about management performance measures as defined by the Board should be included in the financial statements? Why or why not?

Do you agree with the proposed disclosure requirements for management performance measures? Why or why not? If not, what alternative disclosures would you suggest and why?

#### *Response to question 11*

##### *Overall*

62. We agree:

- (a) That MPMs can provide useful information to users of financial statements.
- (b) There is a demand from users for information about MPMs.
- (c) That information about MPMs should be included in the financial statements and be subject to audit.
- (d) That the proposals will bring more transparency and discipline to the reporting of these financial performance measures.

63. There is currently an audit expectation gap as users think that information about non-GAAP measures included in an entity’s annual report has been audited. Disclosing MPMs in the financial statements will make it clear these measures have been subject to audit.

64. We acknowledge that in the case of some MPMs (such as measures based on tailor-made accounting policies), the audit work may be restricted to checking that the measure has been calculated in accordance with the entity’s definition of the measure and that the entity has complied with the disclosure requirements for MPMs. However, we do not think that this should prevent these measures from being included in the audited financial statements.

##### *MPM definition – subtotals of income and expenses*

65. The IASB is proposing to limit MPMs to financial performance measures that are subtotals of income and expenses. This is in line with the IASB’s focus on improving the reporting of financial performance in the statement of profit or loss. Paragraph BC154 is the key paragraph that explains why the IASB is limiting MPMs.

BC154 Feedback from users of financial statements led the Board to focus on improvements to the reporting of financial performance in the statement(s) of financial performance and the related notes. Therefore, the Board's proposed definition for management performance measures is limited to subtotals of income and expenses. Thus, other financial measures (such as currency adjusted revenue or return on capital employed) and non-financial measures (such as customer retention rate) are not management performance measures and would not be included in the proposed disclosure.

66. Limiting MPMs to financial performance measures that are subtotals of income and expenses will mean in some cases only a subset of the non-GAAP financial measures used by management in its public communications will be MPMs. The remainder of the non-GAAP financial measures used by management will continue to be reported outside the financial statements, for example, in management commentary.
67. We recommend that the definition of MPMs is widened to include non-GAAP financial measures that are derived from an IFRS amount in the financial statements. The first part of the MPM definition could be replaced with: "a numerical/financial measure of historical financial performance, financial position, or cash flows..... (insert rest of definition)".
68. Internationally, this would be consistent with the approach taken in the ESMA's *Guidelines on Alternative Performance Measures*, IOSCO's *Statement on Non-GAAP Financial Measures* (IOSCO's statement) and US SEC *Conditions for Use of Non-GAAP Financial Measures*.
69. In New Zealand, this would align with the FMA guidance on *Disclosing non-GAAP financial information* (which is broadly aligned with the IOSCO statement). The FMA guidance sets out guidelines for FMC reporting entities to follow when they disclose non-GAAP financial information outside the financial statements. We are of the view that analysts and investors would welcome the inclusion in the financial statements of other key financial measures that are used by management.

#### *Definition of an MPM – scope of public communications*

70. We believe that the IASB needs to provide guidance to clarify the intended scope of 'public communications outside the financial statements' used in the definition of MPMs for the following reasons.
  - (a) The proposed guidance (see paragraph B79) provides examples of public communications (management commentary, press releases and investor presentations). However, the guidance does not limit public communications to these forms of communication.
  - (b) Some constituents have questioned whether public communications outside the financial statements would include posts on social media made by the company.
  - (c) Other constituents have raised concerns from an audit perspective, noting the challenges of having to review all an entity's public communications for possible MPMs.
  - (d) We also have concerns that the IASB has not provided guidance on the timeframe regarding 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.

- (e) Do financial statements meet the definition of public communications – if a measure is only in the financial statements does it meet the MPM definition?
- (f) It is not clear whether an entity must make the required MPM disclosures when it publicly communicates adjusted profit measures for different branches/business activities. For example, an entity publicly communicates, via investor presentations, different adjusted profit measures regarding its activities in two different cities. Is the entity then required to make the disclosures proposed in the ED for both of these adjusted profit measures?

*Definition of an MPM – complement totals or subtotals specified by IFRS Standards*

71. We have received feedback that the purpose of subparagraph 103(b) of the proposed definition of MPMs is not clear. This subparagraph states that MPMs are subtotals of income and expenses that “complement totals or subtotals specified by IFRS Standards”. We believe that the requirement in subparagraph 103(b) is needed in order for an MPM to be reconciled back to an IFRS specified subtotal in the statement of profit or loss. But we also question whether the IASB intended this subparagraph to restrict MPMs to those that are subtotals of income and expenses that cover the same reporting period as the financial statements (see previous comment on the scope of ‘public communications’). We recommend that the IASB considers adding an explanation for the purpose of this requirement in the application guidance.

*Faithful representation*

72. We have concerns with paragraph 105(a) of proposed IFRS X 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”.
- (a) 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.
  - (b) 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.”
  - (c) We note that IFRS 8 *Operating Segments* does not place a similar explicit restriction on the disclosure of segment information which reflects the views of management (see paragraph BC160).
  - (d) The restriction in paragraph 105(a) does not prevent entities from using such MPMs outside of the financial statements.
  - (e) In our view, there can be tension between:
    - (i) communicating to users of financial statements management’s view of an aspect of an entity’s financial performance; and

- (ii) the restriction that MPMs must faithfully represent an aspect of an entity's financial performance.
  - (f) We believe that where entities are reporting such MPMs outside the financial statements, information about these MPMs is still useful to users of the financial statements and should be disclosed in the financial statements and be subject to audit.
  - (g) 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.
73. Therefore, we recommend that the IASB removes this restriction. We consider that paragraph 105(b) of proposed IFRS X, which requires MPMs to be described in a clear and understandable manner that does not mislead users, will be sufficient.
74. 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 could 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.
75. 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*

76. Generally, we agree with the proposed disclosure requirements.
77. We have received feedback that some companies do not adequately explain why a non-GAAP measure provides useful information to users (regardless of whether this non-GAAP information is inside or outside the financial statements). In most cases companies are providing very generic explanations. We have also received feedback that the illustrative example in the ED is too generic and is not very helpful.
78. We have heard concerns that the reconciling items between the MPM and the IFRS number may not be described in a useful manner. We note that paragraph B85 requires that reconciling items meet the requirements in paragraphs 25 to 28, which includes a requirement that the description of the items in the financial statements shall faithfully represent the characteristics of those items. We recommend the IASB considers whether it should add to paragraph 106(b) that reconciling items must be described in a clear and understandable manner.

## Question 12—EBITDA

Paragraphs BC172–BC173 of the Basis for Conclusions explain why the Board has not proposed requirements relating to EBITDA.

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

### *Response to question 12*

79. We agree with not proposing requirements relating to EBITDA. In our view, the calculation of EBITDA is diverse in practice. It would be difficult for the IASB to come up with a globally accepted definition of EBITDA.
80. However, as EBITDA is an almost universal measure of performance (not just in financial statements), we would suggest that the IASB provides guidance to clarify when EBITDA would be able to be presented on the face of the statement of profit or loss. We suggest it would also be helpful to clarify that EBITDA can be presented in the notes to the financial statements as an MPM. In paragraph 85 below we recommend that the IASB considers including the content of paragraph BC165 in the ED, as this explains when the IASB would expect that an MPM such as EBITDA would meet the requirements for presentation on the face of the statement of profit or loss.
81. We consider paragraph BC165 (shown below) is helpful and should be included in the ED.
- BC165 However, the Board expects that few management performance measures would meet the requirements for presentation as a subtotal in the statement(s) of financial performance. To meet the requirements, such subtotals must:
- (a) fit into the structure of the proposed categories (see paragraph BC28);
  - (b) not disrupt the presentation of an analysis of expenses in the operating category using either the function of expense or nature of expense method (see paragraph BC109); and
  - (c) comprise amounts recognised and measured applying IFRS Standards.
82. We support the IASB’s proposal to include operating profit before depreciation and amortisation in the list of IFRS specified subtotals.

**Question 13—statement of cash flows**

- (a) The proposed amendment to paragraph 18(b) of IAS 7 would require operating profit or loss to be the starting point for the indirect method of reporting cash flows from operating activities.
- (b) The proposed new paragraphs 33A and 34A–34D of IAS 7 would specify the classification of interest and dividend cash flows.

Paragraphs BC185–BC208 of the Basis for Conclusions describe the Board’s reasons for the proposals and discusses approaches that were considered but rejected by the Board.

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

*Response to question 13(a)*

- 83. The indirect method of reporting cash flows from operating activities is not prevalent in New Zealand. Therefore, we have not commented on this question.

*Response to question 13(b)*

- 84. We agree with the feedback received by the IASB that diversity in how companies classify interest and dividend cash flows reduces comparability between companies, making analysis by investors/users difficult. Therefore, we support the proposal to remove the classification choice for interest and dividend cash flows for most entities.

*Other comments*

- 85. As highlighted in our response to question 5 above, 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 substantial confusion in practice. Therefore, we strongly recommend that the IASB explores further the use of different labels between the two statements before finalising the proposals.
- 86. In line with our response to question 7 above, we do not agree with the proposal to separate cash flows from investments into those from integral and non-integral associates and JVs.

**Question 14—other comments**

Do you have any other comments on the proposals in the Exposure Draft, including the analysis of the effects (paragraphs BC232–BC312 of the Basis for Conclusions, including Appendix) and Illustrative Examples accompanying the Exposure Draft?

*Response to question 14**Going concern*

87. The economic impact of the COVID-19 pandemic is expected to increase the level of uncertainty over the ability of many entities to continue as a going concern for financial reporting purposes. As a result, the NZASB recently issued domestic narrow-scope amendments to FRS-44 *New Zealand Additional Disclosures*<sup>2</sup> to improve going concern disclosures to provide better information to users of financial statements during this period of exceptional circumstances.
88. The issue of New Zealand specific disclosures is a short-term measure to deal with the most pressing need for improved disclosures. We strongly recommend that the IASB adds a project to its agenda to look at going concern issues more comprehensively. The major economic disruption from COVID-19 has highlighted this matter as an area where improvements are needed.

*Statement presenting comprehensive income*

89. IAS 1 requires income and expenses included in other comprehensive income (OCI) 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.
90. 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.

<b>Categories of income and expenses included in other comprehensive income</b>	
<b>Current labels</b>	<b>Proposed labels</b>
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

91. We support the proposed new labels for the categories of income and expenses included in other comprehensive income. The new labels use plain English and are easier to understand.

<sup>2</sup> *Going Concern Disclosures* (Amendments to FRS-44)



92. We would encourage the IASB to undertake a specific project on OCI. We have received feedback that users do not understand the distinction between profit or loss and OCI and the role of recycling.

#### *Negative interest rates*

93. During discussions on the ED, an issue was raised regarding the presentation of income and expenses in a negative interest rate environment. We are aware of the January 2015 IFRS Interpretations Committee agenda decision *Income and expenses arising on financial instruments with a negative yield—presentation in the statement of comprehensive income (IAS 39 Financial Instruments: Recognition and Measurement and IAS 1 Presentation of Financial Statements)—January 2015*. While this agenda decision clarified that you cannot present negative interest as a revenue line item, it did not clarify how the resulting expense should be presented. We have received feedback that clarification of presentation would be helpful to ensure consistent reporting and remove potential diversity in practice.

#### *Illustrative Examples*

94. We recommend the IASB provides examples that are entity specific and avoids boiler plate examples. For example, we have received feedback that note 2 to part 1 of the illustrative examples does not contain entity specific information on how the three MPMs provide useful information about the entity's performance (proposed required disclosure under paragraph 106(a) of IFRS X).
95. We have received feedback that the IASB should provide an example regarding the classification of the fair value movements for biological assets (are the movements in fair value operating or investing in nature?) There is currently diversity in practice so clarity would be helpful.
96. We note that the illustrative statement of profit and loss in Part I (analysis of expenses by function) includes a line item 'impairment losses on trade receivables'. We also note that impairment losses on trade receivables is listed separately in note 1, which is an analysis of operating expenses by nature. We question how the same item can be by nature and by function.

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**Date:** 4 May 2022

**To:** NZASB Members

**From:** Gali Slyuzberg

**Subject:** **XRB A1 Definition of Public Accountability**

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### Purpose and introduction<sup>1</sup>

1. This memo outlines draft proposals for clarifying the application of the definition of ‘public accountability’ in XRB A1 *Application of the Accounting Standards Framework* (XRB A1). The purpose of this memo is to seek the Board’s agreement to recommend these proposals to the XRB Board. Any changes to XRB A1 would need to be approved by the XRB Board.
2. The definition of public accountability in XRB A1 is important in the context of both financial reporting and assurance, as explained below.
  - (a) For an entity that is required to prepare general purpose financial reports in accordance standards issued by the XRB, the definition of public accountability is a key element in determining the entity’s reporting tier. If a for-profit or PBE reporting entity has public accountability (as defined), that entity is required to apply Tier 1 reporting requirements – regardless of any other considerations, including size.<sup>2</sup>
  - (b) The definition of public accountability is also important for determining when a reporting entity is classified as a Public Interest Entity (PIE) for audit and assurance purposes. A PIE in New Zealand is defined as any entity that meets the Tier 1 reporting criteria in XRB A1.<sup>3</sup> Auditors of PIEs have additional independence requirements. The NZAuASB recently considered whether to break the link between the definition of PIE and the definition of public accountability in XRB A1, but decided not to propose this.
3. As discussed with the Board in December 2021, we are aware of certain concerns regarding the application of the definition of public accountability in XRB A1. In response to these concerns, the Board tentatively agreed to develop proposals for narrow-scope amendments to XRB A1, to clarify the definition of public accountability.

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<sup>1</sup> 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).

<sup>2</sup> XRB A1, paragraph 17 and 37.

<sup>3</sup> Professional and Ethical Standards 1 (PES 1).

## Recommendations

4. We recommend that the Board:
  - (a) provides FEEDBACK on the draft Exposure Draft (ED) and accompanying Consultation Document (previously known as 'Invitation to Comment'), which are included as items 9.2 and 9.3 respectively; and
  - (b) AGREES to recommend that the XRB Board publishes the Consultation Document and ED for public comment.

## Structure of this memo

5. The remaining sections of this memo are:
  - (a) [The current definition of public accountability in XRB A1](#)
  - (b) [The concerns we are aiming to address](#)
  - (c) [Proposed narrow-scope amendments to XRB A1](#)
  - (d) [Draft Consultation Document and ED](#)
  - (e) [Next steps](#)
  - (f) [Appendix 1](#): Concerns relating to the definition of public accountability – summary of the Board's discussion in December 2022

## The current definition of public accountability in XRB A1

6. The definition of public accountability in XRB A1 has two 'legs':
  - (a) the IASB definition of public accountability (paragraphs 7(a) and 8 of XRB A1); and
  - (b) the New Zealand-specific 'deeming provision' (paragraphs 7(b) and 9 of XRB A1).

The relevant paragraphs of XRB A1 are included below.

### ***Extract from XRB A1***

#### **Public accountability**

- 7 For the purpose of applying the Tier 1 criteria, an entity has public accountability if:
  - (a) it meets the IASB definition of public accountability as specified in paragraph 8 (subject to paragraph 10); or
  - (b) it is deemed to have public accountability in New Zealand in accordance with paragraph 9.

8	In accordance with the IASB definition, an entity has public accountability if: <ul style="list-style-type: none"> <li>(a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or</li> <li>(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks would meet this second criterion).</li> </ul>
9	An entity is deemed to have public accountability in New Zealand if: <ul style="list-style-type: none"> <li>(a) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” than other FMC reporting entities under section 461K of the Financial Markets Conduct Act 2013; or</li> <li>(b) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” by a notice issued by the Financial Markets Authority (FMA) under section 461L(1)(a) of the Financial Markets Conduct Act 2013.</li> </ul>
10	Notwithstanding paragraph 8(b), an FMC reporting entity is not considered to have public accountability unless it is considered to have a “higher level of public accountability” than other FMC reporting entities in accordance with paragraph 9(a) or 9(b).

### The concerns we are aiming to address

7. As discussed with the Board in December 2021, we are aware of concerns that the definition of public accountability in XRB A1 can be unclear and difficult to apply in certain circumstances. These concerns mainly relate to the second criterion of the IASB definition of public accountability, in paragraph 8(b) of XRB A1:

*“An entity has public accountability if it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks would meet this second criterion).”*
8. Specifically, for securities brokers/dealers and fund managers, it can sometimes be unclear whether the entity is considered to “hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses”. Therefore, for such entities it can be unclear whether the entity has public accountability, and therefore whether it needs to apply Tier 1 reporting requirements.
9. Some of the reasons for this application challenge are summarised below (based on feedback received from practitioners).
  - (a) Paragraph 8(b) of XRB A1 notes that *most* ‘securities brokers/dealers’ would meet the ‘fiduciary capacity’ part of the IASB definition of public accountability. However, practitioners have noted that in New Zealand, some entities referred to as ‘brokers’ do

not hold client money or property. In many cases, the primary business of securities brokers/dealers is to buy/sell securities on behalf of clients and/or provide investment advisory and portfolio administration services. Under the FMC Act, some securities brokers/dealers are classified as having “higher levels of accountability” than other FMC entities based on the nature of the service provided, and others are not.

- (b) Paragraph 8(b) of XRB A1 also notes that most ‘mutual funds’ would meet the ‘fiduciary capacity’ part of the IASB definition of public accountability. We understand that in practice, there is some uncertainty over whether *fund managers* are caught by the IASB definition of public accountability and are required to apply Tier 1 reporting requirements. The FMC Act and other FMA regulations generally classify fund managers who provide discretionary investment management services (DIMS) as having a lower level of public accountability.
  - (c) Practitioners have also noted that paragraph 10 of XRB A1 adds unnecessary complexity to the application of the definition of public accountability. They have highlighted difficulties interpreting this paragraph.
  - (d) Furthermore, practitioners raised questions about the outcome of applying paragraph 10. Under paragraph 10, *all non-FMC reporting entities* that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses *must report under Tier 1*. However, *FMC reporting entities* that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses *can report under Tier 2* if they *do not have ‘higher level of public accountability’* under the FMC Act. That is, an FMC reporting entity effectively need not consider the second part of the IASB definition in determining the entity’s reporting tier – but a non-FMC reporting entity must consider this part of the IASB definition. Practitioners have questioned whether this outcome is logical.
10. We have received feedback from the Accounting Technical Reference Group (TRG) that the abovementioned issues are not considered pervasive. However, we continue to receive feedback from individual assurance practitioners that the XRB A1 definition of public accountability is causing application issues for certain types of entities. We also understand that the IASB is unlikely to consider clarifications to the definition of public accountability in the short-to-medium term.
  11. Therefore, in response to the abovementioned concerns, in December 2021 the Board tentatively agreed to develop proposals for narrow-scope amendments to XRB A1 – to clarify the definition of public accountability for New Zealand constituents.
  12. We have also discussed with the Board other concerns that we are aware of in relation to the definition of public accountability. However, the Board agreed that standard-setting activities in relation to these other concerns are not needed at this stage. Please see Appendix 1 for more detail.

### Proposed narrow-scope amendments to XRB A1

13. In December 2021, the Board agreed that we should explore the development of narrow-scope amendments based on one or both of the following options.
  - (a) Paragraph 8(b) of XRB A1: Amendments to *remove the specific reference to 'securities brokers/dealers'* (and the other specific examples of entities that hold assets in fiduciary capacity) from the definition of public accountability. As part of this option, staff also recommended *considering the addition of guidance material*, explaining that some securities brokers/dealers and fund managers will be considered to have public accountability and others will not.
  - (b) Paragraph 10 of XRB A1: Amendments to specify that if an entity meets the 'fiduciary capacity' part of the IASB definition of public accountability, the entity is considered to have public accountability *only if it also has 'higher level of public accountability' under the FMC Act*.
14. We note that we also discussed with the Board the option of completely removing the IASB 'leg' of the definition of public accountability from XRB A1. However, the Board was not in favour of this option (and the TRG was of a similar view).
15. Having considered the two options in paragraph 13 above, we now recommend proposing *both* sets of amendments. We think that both proposals have merit and will complement each other. The proposed amendments and our reasons for recommending these proposals are summarised in the table on the next page.
16. With respect to the proposed additional guidance for securities brokers/dealers and fund managers: We note that XRB A1 already includes guidance for determining when an entity holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. The following guidance is included in paragraphs 11 and 12 of XRB A1.
  - (a) Guidance noting that if an entity holds/manages resources entrusted to it by outsiders, but it does so for reasons that are *incidental* to the entity's primary business, the entity does not have public accountability under paragraph 8(b) of XRB A1. This guidance mentions the following types of entities where this may be the case: schools, travel agents, real estate agents, charitable organisations, certain co-operatives, sellers receiving payment in advance, a government department that provides state housing but also holds tenants rental bonds, and a not-for-profit entity that provides welfare services and holds beneficiaries' benefit payments while assisting them with budgeting.
  - (b) Guidance for trusts – which do not have public accountability under paragraph 8(b) if the resources that they hold are not the resources of specified individual beneficiaries.
17. We plan to add to this existing guidance additional specific guidance for securities brokers/traders and fund managers.
18. In addition, we recommend specifying in XRB A1 that an entity that is required to report in Tier 1 is treated as a PIE for assurance purposes – given that the concerns we have heard about the definition of public accountability originated mainly from assurance practitioners.

Table 1 Proposed narrow-scope amendments to XRB A1

Proposals	What it would the amendment look like	Staff comments
<p><b>Amendment 1</b></p> <ul style="list-style-type: none"> <li>Removing the bracketed text from paragraph 8(b) of XRB 1, i.e. the text listing securities brokers/dealers, funds and other specific entity types as examples of entities that would meet the definition on public accountability;</li> <li>Amending paragraph 12, so that it does not refer to “the entities listed in paragraph 8(b)”;</li> <li>Adding guidance to explain that in the New Zealand context, only some securities brokers/traders and fund managers have public accountability.</li> </ul>	<p>8 In accordance with the IASB definition, an entity has public accountability if:</p> <p>(a) [...]</p> <p>(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (<del>most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks would meet this second criterion</del>).</p> <p>12 [...] For example, a trust would not have public accountability when the financial resources or other resources held and managed by the trust are not the resources of specified individual beneficiaries, in the <u>same</u> manner that the financial resources of <u>banks and credit unions the entities listed in paragraph 8(b) are held for the resources of</u> the individual clients, customers and members of those entities.</p> <p><u>12A The IASB literature on public accountability provides that most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. In the New Zealand context, not all securities brokers/dealers and fund managers will meet the criterion in paragraph 8(b). For example, some financial service provider known as ‘brokers’, such as some insurance brokers or mortgage brokers, do not hold client money or property as part of their primary businesses. Also, some securities brokers/dealers and fund managers do not hold client assets, but instead only provide investment portfolio advice. Judgement is required, based on the entity’s primary businesses, in determining whether paragraph 8(b) applies to a broker or fund manager.</u></p>	<p>This proposal aims to address the abovementioned concerns regarding the practical application of paragraph 8(b) to brokers and fund managers.</p> <p>This option is consistent with the approach taken in Australia. In Appendix A of AASB 1053 <i>Application of Tiers of Australian Accounting Standards</i>, the AASB removed the bracketed text from the AASB definition of public accountability. However, the bracketed text has instead been included in the accompanying integral guidance material within the AASB standard.</p> <p>The proposed amendment to paragraph 12 is a consequence of the proposed amendment to paragraph 8(b). We included a reference to banks and credit unions in that paragraph to ensure the paragraph remains understandable (but we have not referred to brokers/funds).</p> <p>We acknowledge that the proposed amendment to paragraph 8(b) would introduce some inconsistency with IASB literature. However, we note that in the proposed amendment, the text deleted from paragraph 8(b) is still acknowledged in the proposed guidance in new paragraph 12A.</p> <p>We recommend including this guidance in the main body of XRB A1 (rather than in an appendix) because we note that paragraphs 11–12 of XRB A1 already provide some guidance on the application paragraph 8(b).</p>

**Table 1 Proposed narrow-scope amendments to XRB A1**

Proposals	What it would the amendment look like	Staff comments
<p><b>Amendment 2</b></p> <p>Amend paragraph 10 of XRB A1 – to specify that an entity does not have public accountability under paragraph 8(b) unless it has ‘higher level of public accountability’ as defined in the FMC Act or other FMA notices.</p> <p>The impact of the amendment is that <i>any entity</i> (including FMC reporting entities) that holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses will only be a Tier 1 reporting entity <i>if it is an FMC reporting entity that has ‘higher level of public accountability’ under the FMC Act.</i></p>	<p>10 <del>Notwithstanding paragraph 8(b)),</del> An <del>FMC reporting</del> entity is not considered to have public accountability <del>under the second part of the IASB definition (paragraph 8(b)) unless it is deemed to have public accountability considered to have a “higher level of public accountability” than other FMC reporting entities</del> in accordance with paragraph 9(a) or 9(b).</p>	<p>This proposal aims to provide further certainty as to whether securities brokers/dealers, fund managers and other entities have public accountability under XRB A1.</p> <p>The proposal also helps streamline and simplify the requirement in paragraph 10 – in response to the concern that this paragraph can be challenging to understand and apply, and the concern that applying this paragraph may not result in a logical outcome.</p> <p>The main risk associated with this proposal is as follows: Under these proposals, a non-FMC reporting entity that holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses <i>would not be required to report in Tier 1.</i><sup>4</sup> There could be non-FMC reporting entities that in principle should apply Tier 1 reporting requirements. However, this risk is considered to be low, because we expect that most entities that hold holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses would be captured by FMA regulations.</p>

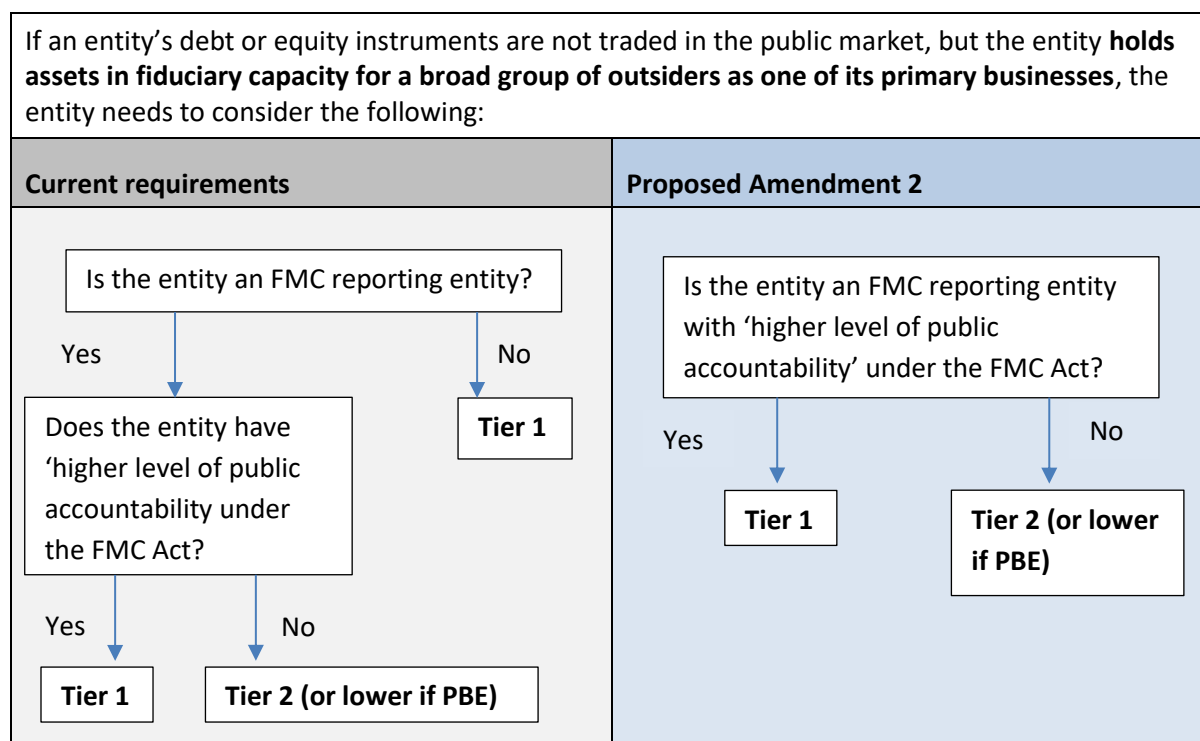
<sup>4</sup> Unless the entity meets another aspect of the definition of public accountability.



**Table 1 Proposed narrow-scope amendments to XRB A1**

Proposals	What it would the amendment look like	Staff comments
<p><b>Amendment 3</b> Add paragraphs 19A and 38A, to clarify that an entity that is required to report in Tier 1 is also considered to be a PIE for assurance purposes.</p>	<p><u>19A</u> <u>The Tier 1 criteria also determine whether a for-profit entity is treated as a public interest entity (PIE) for audit and assurance purposes. Specifically, an entity that meets the Tier 1 criteria in this Standard and is not eligible to report in accordance with the accounting requirements of another tier is treated as a PIE for audit and assurance purposes. Auditors of PIEs have additional independence requirements.</u></p> <p><u>38A</u> <u>The Tier 1 criteria also determine whether a public benefit entity is treated as a public interest entity (PIE) for audit and assurance purposes. [The rest of this paragraph has the same text as paragraph 19A above].</u></p>	<p>The concerns we have heard in relation to the definition of public accountability originated mainly from assurance practitioners. To acknowledge and emphasise the link between the Tier 1 and assurance requirements, we are proposing to add paragraphs 19A and 38A to XRB A1.</p>

19. The effect of Amendment 2 above is demonstrated in the diagram below.



**Draft Consultation Document and ED**

20. The amendments recommended in this memo have been reflected in the draft ED and accompanying Consultation Document, which are included as agenda items 9.3 and 9.2 respectively. The rationale for the amendments is explained in the consultation document and in the Basis for Conclusions of the ED.
21. We recommend the standard comment period of approximately 90 days for the ED. In drafting the Consultation Document, we have assumed that the XRB Board will approve the ED at its meeting on 20 June 2022, and that the ED is published by 1 July 2022. Therefore, we propose to close the consultation period on 30 September 2022.
22. As the finalised amendments are likely to be issued in Q4 of 2022, we recommend proposing that the amendments be effecting from 1 January 2024, with early application permitted.

**Questions for the Board**

Q1. Does the Board agree with the proposed amendments referred to as Amendment 1 in this memo? Specifically, does the Board agree with:

- (a) deleting the bracketed text from paragraph 8(b);
- (b) amending paragraph 12 as a consequence of the amendment to paragraph 8(b);
- (c) adding the proposed guidance in paragraph 12A; and
- (d) locating the proposed new guidance in the main body of XRB A1, rather than in an appendix or in the Basis for Conclusions?

Q2. Does the Board agree with the proposed amendments referred to as Amendment 2 in this memo? Specifically:

- (a) Does the Board agree to specify that an entity does not have public accountability under paragraph 8(b) of XRB A1 unless the entity is an FMC reporting entity with higher level of public accountability?
- (b) Is the Board comfortable with the outcome of this proposal, being that *non-FMC reporting entities that hold assets in a fiduciary capacity* for a broad group of outsiders as one of its primary businesses *would not need to report under Tier 1, and would instead be able to report under Tier 2 or lower?*<sup>5</sup>

Q3. Does the Board agree with the proposed amendments referred to as Amendment 3 in this memo? Specifically, does the Board agree that the link between the Tier 1 requirements in XRB A1 and the PIE requirements for auditing/assurance purposes should be explicitly acknowledged in XRB A1?

<sup>5</sup> Unless the entity meets another aspect of the definition of public accountability.

**Questions for the Board (continued)**

Q4. Does the Board have any comments on the draft Consultation Document and ED in agenda items 9.2 and 9.3?

Q5. Does the Board agree that staff should seek approval from the XRB Board to issue the consultation document and ED?

**Next steps**

23. If the Board agrees with the recommendations in this memo, staff will seek the XRB Board’s approval to issue the proposed amendments to XRB A1 for public consultation. We plan to do this at the XRB Board’s meeting on 20 June 2022. We also plan to discuss the draft proposals with the FMA before issuing for public consultation.
24. We note that the XRB’s Explanatory Guidance A1 *Guide to Application of the Accounting Standards Framework* (EG A1) refers to the definition of public accountability and related guidance in XRB A1. Therefore, EG A1 would need to be updated in line with the proposed amendments to XRB A1.
25. However, we note that EG A2 *Overview of the Accounting Standards-Setting Process* says the following about Explanatory Guidance (italics added for emphasis): “The NZASB occasionally issues other documents, such as explanatory guides. These are usually *issued without formal public consultation* because they contain explanatory material, have no legal status and their application is not mandatory”. While this paragraph refers to Explanatory Guidance issued by the NZASB, we understand that the same applies to Explanatory Guidance issued directly by the XRB.
26. On this basis, we did not include proposed amendments to EG A1 in the ED or consultation document. However, we plan to update EG A1 in line with the amendments to XRB A1, if and when these amendments are issued as final pronouncements.

**Attachments**

- |                 |                                                                                         |
|-----------------|-----------------------------------------------------------------------------------------|
| Agenda item 9.2 | Draft Consultation Document                                                             |
| Agenda item 9.3 | Draft ED <i>Definition of public accountability – narrow-scope amendments to XRB A1</i> |

**Appendix 1: Concerns relating to the definition of public accountability – summary of the Board’s discussion in December 2022**

Concerns we are aware of <sup>6</sup>	Staff comments (Dec 2021)	Board feedback (Dec 2021)
<p><u>Issue 1:</u> Concerns that the current <b>definition of public accountability in XRB A1 is too broad</b> – leading to too many New Zealand entities being required to report in Tier 1 – and therefore <b>too many entities being classified as PIEs for assurance purpose</b>.</p> <p>Entities classified as PIEs are required to comply <b>additional independence requirements</b>, including around auditor rotation.</p> <p>This concern has been expressed mainly by audit practitioners.</p>	<p>On its own, the concern that too many entities are classified as PIEs for assurance purposes does not seem to be an appropriate reason for making significant changes to the definition of public accountability in XRB A1.</p> <p>The primary driver for any proposed change to the definition of public accountability should be based on public interest considerations, including the need to maintain a trusted financial sector.</p> <p>We note that the XRB’s <i>Targeted Review of the New Zealand Accounting Standards Framework</i> (2019) did not highlight significant concerns with the Tier 1 reporting criteria.</p>	<p>In relation to Issue 1, the Board agreed with our recommendation that:</p> <ul style="list-style-type: none"> <li>• Standard-setting action is <b>not required</b> at this time.</li> <li>• Instead, staff will continue to <b>monitor the NZAuASB’s discussions</b> on the PIE definition for assurance purposes.<sup>7</sup></li> </ul>
<p><u>Issue 2:</u> Concerns that the definition of public accountability in XRB A1 is <b>difficult to apply in certain circumstances</b> – which means that it is <b>not clear whether certain types of entities have public accountability</b>.</p> <p>The lack of clarity and resulting diversity in application relates to the second part of IASB definition of public accountability.</p> <p>Specifically, it can sometimes be unclear whether <b>securities brokers/dealers and fund managers</b> are considered to “<b>hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses</b>”.</p>	<p>We have received feedback from the Accounting Technical Reference Group (TRG) that this issue is not considered pervasive.</p> <p>However, we continue to receive feedback from individual practitioners that the XRB A1 definition of public accountability is causing application issues for certain types of entities.</p> <p>Based on discussion with IASB staff, the IASB is unlikely to consider clarifications to the definition of public accountability in its own literature in the short-to-medium term.</p> <p>Therefore, we have therefore considered limited-scope standard-setting activity to address Issue 2.</p>	<p>In relation to Issue 2, the Board <b>tentatively agreed</b> with our recommendation to <b>develop proposals</b> for narrow-scope amendments to <b>clarify the definition of public accountability</b> in XRB A1.</p>

<sup>6</sup> We have discussed the application of the XRB A1 definition of public accountability with key stakeholder groups, but we have not conducted broad public outreach activities.

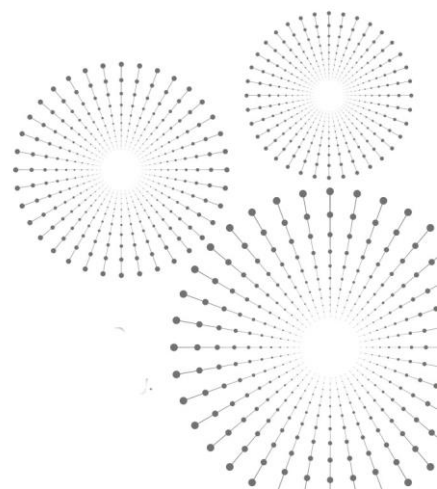
<sup>7</sup> Staff had also recommended a broader discussion of this issue at the joint NZASB/NZAuASB meeting in March 2022. However, in light of recent discussion on the definition of PIE by the XRB Board, it was ultimately decided that this topic need not be discussed at the joint NZASB/NZAuASB meeting at this stage.



**Exposure Draft:**  
**Definition of public accountability –**  
**narrow-scope amendments to XRB A1**

**Consultation document**

**June 2022**



## Table of Contents

	Page
<b>Consultation questions .....</b>	<b>3</b>
<b>How to provide feedback .....</b>	<b>4</b>
<b>List of abbreviations.....</b>	<b>4</b>
<b>1. Introduction .....</b>	<b>5</b>
1.1 Objective of the exposure draft .....	5
1.2 Scope of amendments .....	5
1.3 Background .....	5
1.4 Consultation period and next steps .....	7
<b>2. Overview of the consultation document and ED .....</b>	<b>8</b>
2.1 Summary of proposals.....	8
2.2 Proposed amendments .....	8
Amendments relating to references to securities brokers/dealers and fund managers...	8
Amendments to simplify and streamline paragraph 10.....	9
Amendments to specify the link between the Tier 1 requirements in XRB A1 audit/assurance requirements .....	10
2.4 Effective date.....	10

<b>Consultation questions</b>		<b>Paragraphs</b>
1	<p>Do you agree with the proposed amendments to XRB A1 that relate to references to securities brokers/traders, fund managers and other specific entities?</p> <p>That is, do you agree that the XRB should:</p> <p>(a) remove from paragraph 8(b) the specific reference to securities brokers/traders, fund managers and other specific entity types; and</p> <p>(b) add guidance in paragraph 12A, to clarify that in New Zealand, not all brokers and fund managers hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses?</p>	18-23
2	<p>Do you agree with the proposed amendments to XRB A1 to simplify and streamline the requirements in paragraph 10?</p> <p>That is, do you agree that the XRB should specify that an entity does not have public accountability under paragraph 8(b) unless it is deemed to have public accountability in accordance with paragraph 9 (i.e. unless it is an FMC reporting entity with 'higher level of public accountability' under the Financial Markets Conduct Act 2013)?</p> <p>If you disagree, please explain why.</p> <p>In response to this question, we would be particularly interested in any examples of non-FMC reporting entities that are currently classified as Tier 1 entities for reporting purposes, due to them holding assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses. Such entities would likely not be required to report in Tier 1 under the proposed amendments to paragraph 10.</p>	24-28
3	<p>Do you agree with the proposed amendments to specify the link between the Tier 1 requirements in XRB A1 and auditing/assurance requirements?</p> <p>If you disagree, please explain why.</p>	29-30
4	<p>Do you agree with the proposed effective date of the amendments of 1 January 2024 with early adoption permitted?</p> <p>If you disagree, please explain why.</p>	31
5	<p>Do you have any other comments on the proposals in this ED?</p>	1-31

## How to provide feedback

### Responding to questions

We are seeking comments on the questions raised in this consultation document. We will consider all comments before finalising the proposed amendments to XRB A1 *Application of the Accounting Standards Framework*.

Please feel free to comment on any or all of the questions.

We appreciate formal or informal comments, whether supportive or critical, as both supportive and critical comments are essential to a balanced view.

### Making a submission

You can provide feedback to us via:

- the online form on our website; or
- emailing your formal or informal comments to [accounting@xrb.govt.nz](mailto:accounting@xrb.govt.nz).

The consultation closes on **30 September 2022**.

We will put all written submissions on our website unless advised otherwise, and we reserve the right not to publish defamatory submissions.

## List of abbreviations

The following abbreviations are used in this consultation document.

ED	Exposure Draft
FMA	Financial Markets Authority
FMC Act	Financial Markets Conduct Act 2013
GAAP	Generally Accepted Accounting Practice
NZ IFRS	New Zealand Equivalents to International Financial Reporting Standards
PBE	Public benefit entity
PBE Standards	Public Benefit Entity Standards (standards that are primarily based on International Public Sector Accounting Standards)
XRB	External Reporting Board
XRB A1	External Reporting Board Standard A1 <i>Application of the Accounting Standards Framework</i>



## 1. Introduction

### 1.1. Objective of the exposure draft

1. The objective of this Exposure Draft (ED) is to clarify the application of the definition of public accountability in XRB A1 *Application of the Accounting Standards Framework*, for the purpose of determining an entity's reporting tier.
2. We have become aware of concerns that the definition of public accountability in XRB A1 can be challenging to apply in some situations. To address these concerns, the ED proposes narrow-scope amendments to XRB A1.
3. The amendments aim to enhance the consistency of applying the definition of public accountability, and to make it easier for entities to apply this definition when determining their reporting tier.

### 1.2 Scope of amendments

4. The proposals are relevant for entities that prepare general purpose financial reports in accordance with standards issued by the XRB.

### 1.3 Background

5. In New Zealand, some entities are required by legislation (or choose) to prepare general purpose financial reports in accordance with accounting standards issued by the XRB. This includes entities that report in accordance with 'GAAP'. Such entities need to apply XRB A1 *Application of the Accounting Standards Framework* to determine their reporting tier.
6. There are two tiers for for-profit entities and four tiers for public benefit entities (PBEs). A for-profit entity in Tier 1 must comply with the full requirements of NZ IFRS, and a PBE in Tier 1 must comply with the full requirements of PBE Standards – without any concessions.
7. The definition of 'public accountability' in XRB A1 is a key element in determining an entity's reporting tier. If a for-profit entity or a PBE has public accountability (as defined in XRB A1), that entity is required to apply Tier 1 reporting requirements – regardless of the entity's size or any other considerations.
8. The definition of public accountability in XRB A1 is also important from an audit and assurance perspective. In New Zealand, an entity is classified as a Public Interest Entity (PIE) for audit and assurance purposes if it meets the Tier 1 reporting criteria in XRB A1. Auditors of PIEs have additional independence requirements.
9. The current definition of public accountability in XRB A1 is reproduced on the next page. This definition has two 'legs':
  - (a) the IASB definition of public accountability – which covers entities whose debt or equity instruments are traded (or about to be traded) in a public market, and;

- (b) the New Zealand-specific ‘deeming provision’ – which cover entities that are classified as ‘FMC reporting entities’ with ‘higher level of public accountability’ under the Financial Markets Conduct Act 2013 (FMC Act).

***Extract from XRB A1***

**Public accountability**

7 For the purpose of applying the Tier 1 criteria, an entity has public accountability if:

- (a) it meets the IASB definition of public accountability as specified in paragraph 8 (subject to paragraph 10); or
- (b) it is deemed to have public accountability in New Zealand in accordance with paragraph 9.

8 In accordance with the IASB definition, an entity has public accountability if:

- (a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or
- (b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks would meet this second criterion).

9 An entity is deemed to have public accountability in New Zealand if:

- (a) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” than other FMC reporting entities under section 461K of the Financial Markets Conduct Act 2013; or
- (b) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” by a notice issued by the Financial Markets Authority (FMA) under section 461L(1)(a) of the Financial Markets Conduct Act 2013.

10 Notwithstanding paragraph 8(b), an FMC reporting entity is not considered to have public accountability unless it is considered to have a “higher level of public accountability” than other FMC reporting entities in accordance with paragraph 9(a) or 9(b).

10. The XRB became aware of some challenges relating to the application of to the second part of the IASB definition of public accountability (paragraph 8(b) of XRB A1). This part of the definition refers to entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses. Specifically, certain constituents expressed concerns that this part of the definition can be challenging to apply in some situations – particularly for brokers and fund managers. We have also heard some concerns in relation to paragraph 10 of XRB A1, which relates to the application of the second part of the IASB definition to FMC reporting entities. Some constituents noted that this paragraph can be challenging to apply and questioned the logic of the outcome of this paragraph.

11. Based on feedback received, the XRB understands that the application challenges mentioned above are not considered pervasive. However, we continue to receive feedback about these challenges from time to time.
12. Therefore, this ED proposes narrow-scope amendments to XRB A1, to address the abovementioned application challenges in relation to the definition of public accountability.

#### **1.4 Consultation period and next steps**

13. We welcome feedback on the proposed amendments before incorporating them into our PBE Standards.
14. Submissions on this ED are due by **30 September 2022**. Information on how to make submissions is provided on page 4 of this consultation document.
15. After the consultation period ends, we will consider all the submissions received, and subject to the comments in those submissions, we expect to finalise and issue the amendments.

## 2. Overview of proposed amendments

### 2.1. Summary of proposals

16. To clarify the application of the definition of public accountability, the ED proposes narrow-scope amendments to XRB A1. These amendments relate to the application of the second part of the IASB definition of public accountability, which refers to entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses.
17. In summary, the ED proposes the following narrow-scope amendments to XRB A1.
  - (a) Amendments relating to references to securities brokers/dealers and fund managers;
  - (b) Amendments to simplify and streamline paragraph 10 of XRB A1; and
  - (c) Amendments to specify the link between the Tier 1 requirements in XRB A1 and audit/assurance requirements.

### 2.2. Proposed amendments

#### Amendments relating to references to securities brokers/dealers and fund managers

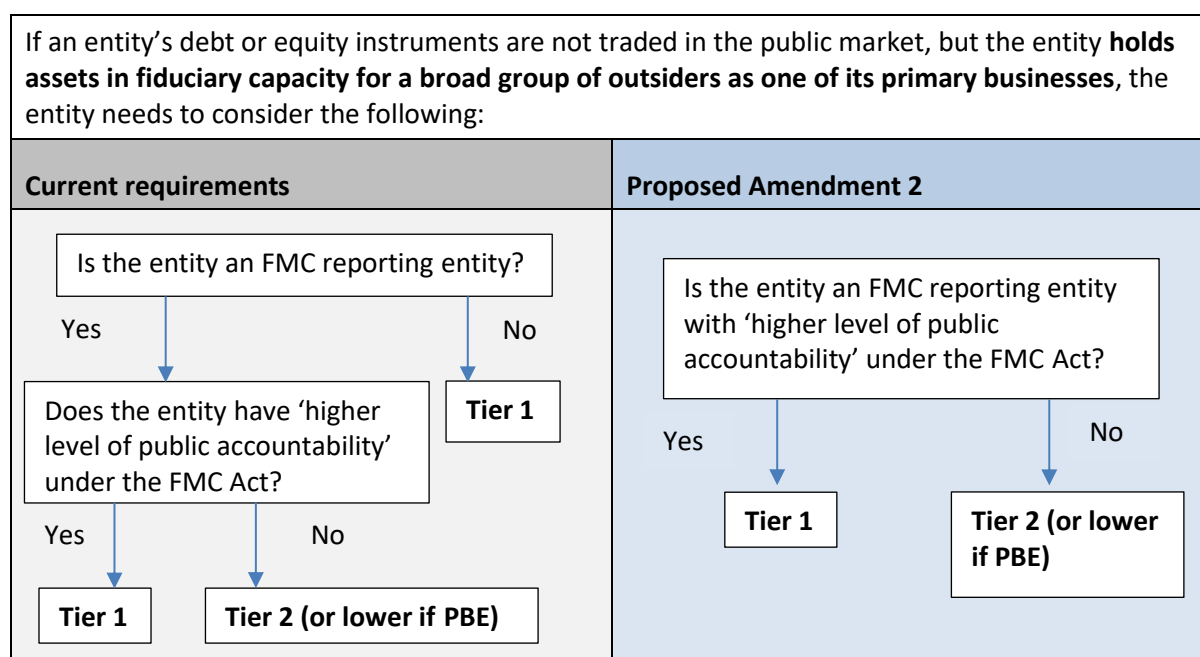
18. Under paragraph 8(b) in the current version of XRB A1, an entity that holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses has public accountability.
19. Some constituents noted that paragraph 8(b) can be challenging to apply for certain securities brokers/dealers and fund managers. Specifically, these constituents expressed the following concerns in relation to paragraph 8(b).
  - (a) Paragraph 8(b) of XRB A1 notes that *most* 'securities brokers/dealers' would meet the 'fiduciary capacity' part of the IASB definition of public accountability. However, in New Zealand, some entities referred to as 'brokers' do not hold client money or property. In many cases, the primary business of securities brokers/dealers is to buy/sell securities on behalf of clients and/or provide investment advisory and portfolio administration services. Under the FMC Act, some securities brokers/dealers are classified as having 'higher level of public accountability' than other FMC reporting entities based on the nature of the service provided, and others are not.
  - (b) Paragraph 8(b) of XRB A1 also notes that most 'mutual funds' would meet the 'fiduciary capacity' part of the IASB definition of public accountability. In practice, there is some uncertainty over whether fund managers are caught by the IASB definition of public accountability and are required to apply Tier 1 reporting requirements. The FMC Act and other FMA regulations generally classify fund managers who provide discretionary investment management services as having a lower level of public accountability.

20. In response to these concerns, the ED proposes to:
- (a) remove the specific reference to securities brokers/traders and fund managers (and other specific entities) from paragraph 8(b), and amend paragraph 12 accordingly; and
  - (b) add guidance in paragraph 12A, to clarify that in New Zealand, not all brokers and fund managers hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses.
21. The XRB is aware that the amendment to paragraph 8(b) introduces a difference between the definition of public accountability in New Zealand and the definition of public accountability in the IASB's literature.
22. However, while the ED propose to remove from paragraph 8(b) the specific examples of entities that would mostly meet the definition of public accountability in the IASB's view, the ED also proposes to acknowledge and refer to these examples in the added paragraph 12A. Therefore, there will still be a clear link between the discussion on public accountability in XRB A1 and the definition of public accountability in the IASB's literature.
23. Furthermore, the deletion of specific examples of entities from paragraph 8(b) is consistent with the definition of public accountability in the Australian standard AASB 1053 *Application of Tiers of Australian Accounting Standards*.

#### **Amendments to simplify and streamline paragraph 10**

24. Paragraph 10 of XRB A1 currently states that an *FMC reporting entity* does not have public accountability under paragraph 8(b) unless it has 'higher level of public accountability' under the FMC Act, as per paragraph 9 of XRB A1.
25. Some constituents noted the following concerns with respect to paragraph 10 of XRB A1.
- (a) Paragraph 10 of XRB A1 adds unnecessary complexity to the application of the definition of public accountability. It can be difficult to interpret this paragraph.
  - (b) Under paragraph 10, all non-FMC reporting entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses must report under Tier 1. However, FMC reporting entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses can report under Tier 2 if they do not have 'higher level of public accountability' under the FMC Act. That is, an FMC reporting entity effectively need not consider the second part of the IASB definition in determining the entity's reporting tier – but a non-FMC reporting entity must consider this part of the IASB definition. Questions were raised as to whether this outcome is logical.
26. In response to these concerns, the ED proposes to simplify the requirements in paragraph 10 – by specifying that an entity does not have public accountability under paragraph 8(b) unless it is deemed to have public accountability in accordance with paragraph 9. That is, an entity does not have public accountability under paragraph 8(b) unless it is an FMC reporting entity with 'higher level of public accountability' under the FMC Act.

27. The diagram below demonstrates the effect of the proposed amendment to paragraph 10.



28. The XRB is aware that as a consequence of the amendments to paragraph 10, entities that hold assets in fiduciary capacity for a broad group of outsiders as one of their primary businesses, but which are *not FMC reporting entities*, would no longer be required to report in Tier 1 (unless they meet any other aspects of the definition of public accountability). Instead, such entities would be able to report under Tier 2, or a lower Tier if they are a PBE. However, the XRB considers that most entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses would be captured by FMC regulations.

**Amendments to specify the link between the Tier 1 requirements in XRB A1 and audit/assurance requirements**

29. As noted in Section 1 of this Consultation Document, the definition of public accountability is important not only for financial reporting purposes, but also for audit and assurance purposes. This is because the definition of public accountability is a key factor in determining whether an entity must apply Tier 1 reporting requirements in XRB A1 – and an entity that must apply Tier 1 reporting requirements is classified as a public interest entity (PIE) for audit and assurance purposes. The auditors of PIEs have additional independence requirements.

30. Given that the abovementioned concerns about the definition of public accountability originated mainly from assurance practitioners, we propose to specify and emphasise in XRB A1 the link between the Tier 1 criteria in XRB A1 and the definition of PIE for audit and assurance purposes.

**2.3. Effective date**

31. The proposed effective date of the amendments is 1 January 2024, with early adoption permitted.



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## Definition of public accountability – narrow-scope amendments to XRB A1

### Issued [Date]

This [draft]<sup>1</sup> Standard was issued on [Date] by the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This [draft] Standard is a disallowable instrument for the purposes of the Legislation Act 2019, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on [Date].

Reporting entities that are subject to this [draft] Standard are required to apply it in accordance with the effective date, which is set out in Part D.

In finalising this [draft] 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 [draft] Standard has been issued to clarify the application of the definition of public accountability for the purpose of determining an entity's reporting tier.

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<sup>1</sup> References to “this Standard” throughout this Exposure Draft should be read as referring to “this draft Standard”.



DEFINITION OF PUBLIC ACCOUNTABILITY – NARROW-SCOPE AMENDMENTS TO XRB A1

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ISBN

DEFINITION OF PUBLIC ACCOUNTABILITY – NARROW-SCOPE AMENDMENTS TO XRB A1

**CONTENTS**

	<i>from page</i>
<b>PART A: INTRODUCTION</b>	<b>4</b>
<b>PART B: SCOPE</b>	<b>4</b>
<b>PART C: AMENDMENTS TO XRB A1</b>	<b>5</b>
<b>PART D: EFFECTIVE DATE</b>	<b>8</b>

## Part A – Introduction

This [draft] Standard includes amendments to clarify the application of the definition of public accountability, for the purpose of determining what reporting tier applies to an entity that is required to prepare general purpose financial statements in accordance with standards issued by the XRB.

Specifically, this [draft] Standard:

- (a) Deletes from paragraph 8(b) the list of specific examples of entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses;
- (b) Amends paragraph 12 as a consequence of the amendment to paragraph 8(b);
- (c) Adds guidance on the application of paragraph 8(b) in the New Zealand context – namely, that in New Zealand, not all securities brokers/traders hold assets in a fiduciary capacity for a broad group of outsiders as one of their main businesses; and
- (d) Specifies that an entity does not have public accountability under paragraph 8(b) unless paragraphs 9(a) or 9(b) apply to the entity (that is, unless the entity is an FMC reporting entity with ‘higher level of public accountability’ under the Financial Markets Conduct Act 2013).

## Part B – Scope

**This Standard applies to entities that prepare, or opt under an enactment to prepare, GPFR in accordance with accounting standards issued by the XRB.**

## Part C – Amendments to XRB A1

Paragraphs 8, 10 and 12 are amended and paragraphs 12A, 19A, 38A and 78 are added. Paragraphs 9, 11, 12, 17 and 37 are not amended but are included for reference. New text is underlined and deleted text is struck through.

- 8 In accordance with the IASB definition, an entity has public accountability if:
- (a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or
  - (b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (~~most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks would meet this second criterion~~).
- 9 An entity is deemed to have public accountability in New Zealand if:
- (a) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” than other FMC reporting entities under section 461K of the Financial Markets Conduct Act 2013;<sup>2</sup> or
  - (b) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” by a notice issued by the Financial Markets Authority (FMA) under section 461L(1)(a) of the Financial Markets Conduct Act 2013.
- 10 ~~Notwithstanding paragraph 8(b), an FMC reporting~~ An entity is not considered to have public accountability under the second part of the IASB definition (paragraph 8(b)) unless it is deemed to have public accountability considered to have a “higher level of public accountability” than other FMC reporting entities in accordance with paragraph 9(a) or 9(b).
- 11 Some entities may hold assets in a fiduciary capacity for a broad group of outsiders because they hold and manage financial resources entrusted to them by clients, customers or members not involved in the management of the entity. However, if they do so for reasons incidental to a primary business, that does not mean that they have public accountability. For example:
- (a) this may be the case for travel or real estate agents, schools, charitable organisations, co-operative enterprises requiring a nominal membership deposit and sellers that receive payment in advance of delivery of the goods or services such as utility companies;
  - (b) in the public sector, a government department whose primary business is the provision of state housing to tenants does not have public accountability if it also manages trust money (rental bonds) on behalf of those tenants as an incidental activity to its primary business; and
  - (c) in the not-for-profit sector, a not-for-profit entity that provides a wide range of welfare services to beneficiaries as its primary activity does not have public accountability merely because it holds welfare benefits on behalf of some of those beneficiaries to assist them with budgeting. While the entity is holding assets in a “fiduciary capacity for a broad group of outsiders” it is not holding them “as one of its primary businesses”. This is because providing the budgeting services is an incidental activity to its primary activity of providing a range of welfare services to beneficiaries.
- 12 Trustees of a trust are required to act in a fiduciary capacity for the benefit of the beneficiaries of that trust or in achieving the objects of the trust. However, this does not necessarily mean that the trust has public accountability as defined in paragraph 8(b). For example, a trust would not have public accountability when the financial resources or other resources held and managed by the trust are not the resources of specified individual beneficiaries, in the same manner that the financial resources of banks and credit unions ~~the entities listed in paragraph 8(b)~~ are held for the resources of the individual clients, customers and members of those entities.

<sup>2</sup> The terms “FMC reporting entity” and an FMC reporting entity with a “higher level of public accountability” are set out in the Financial Markets Conduct Act 2013. Under the Financial Markets Conduct Act 2013, certain FMC reporting entities are considered to have a higher level of public accountability for financial reporting purposes. These include issuers of equity securities or debt securities under a regulated offer; managers of registered schemes (in respect of financial statements of a scheme or fund); listed issuers; registered banks; licensed insurers; credit unions and building societies. In addition, the FMA may, by notice, specify that an entity (or a group of entities) is considered to have a higher level of public accountability or not to have a higher level of public accountability than other FMC reporting entities.

## DEFINITION OF PUBLIC ACCOUNTABILITY – NARROW-SCOPE AMENDMENTS TO XRB A1

12A The IASB literature on public accountability provides that most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. In the New Zealand context, not all securities brokers/dealers and fund managers will meet the criterion in paragraph 8(b). For example, some financial service provider known as ‘brokers’, such as some insurance brokers or mortgage brokers, do not hold client money or property as part of their primary businesses. Also, some securities brokers/dealers and fund managers do not hold client assets, but instead only provide investment portfolio advice. Judgement is required, based on the entity’s primary businesses, in determining whether paragraph 8(b) applies to a broker or fund manager.

...

## B. FOR-PROFIT ENTITIES

### Tier structure

...

#### Tier 1 criteria

- 17 Subject to the requirements on moving between tiers (set out in paragraphs 24 to 30), a for-profit entity shall report in accordance with Tier 1 For-profit Accounting Requirements if it:
- (a) (i) has public accountability at any time during the reporting period; or
  - (ii) is a large for-profit public sector entity; or
  - (b) is eligible to report in accordance with the accounting requirements of Tier 2 but does not elect to report in accordance with that tier.

...

19A The Tier 1 criteria also determine whether a for-profit entity is treated as a public interest entity (PIE) for audit and assurance purposes. Specifically, an entity that meets the Tier 1 criteria in this Standard and is not eligible to report in accordance with the accounting requirements of another tier is treated as a PIE for audit and assurance purposes. Auditors of PIEs have additional independence requirements.

...

## C. PUBLIC BENEFIT ENTITIES

### Tier structure

...

- 37 Subject to the requirements on moving between tiers (set out in paragraphs 47 to 72), a PBE shall report in accordance with Tier 1 PBE Accounting Requirements if it:
- (a) (i) has public accountability<sup>3</sup> at any time during the reporting period; or
  - (ii) is large; or
  - (b) is eligible to report in accordance with the accounting requirements of another tier but does not elect to report in accordance with that other tier.

...

38A The Tier 1 criteria also determine whether a public benefit entity is treated as a public interest entity (PIE) for audit and assurance purposes. Specifically, an entity that meets the Tier 1 criteria in this Standard and is not eligible to report in accordance with the accounting requirements of another tier is treated as a PIE for audit and assurance purposes. Auditors of PIEs have additional independence requirements.

<sup>3</sup> The term “public accountability” is used here with the meaning specified in this document. It is different from the manner in which it was used prior to 2011 in the Accounting Standards Framework. This meaning is also different from the way in which “publicly accountable” is normally used in the public sector and not-for-profit sector. While entities in the public sector and not-for-profit sector are generally considered to be publicly accountable, it does not mean that all entities in those sectors have public accountability (and are therefore in Tier 1). The definition of public accountability has a particular technical meaning and is narrower than the generic term publicly accountable as it is commonly used.

...

**Effective Date**

...

**78** **Definition of public accountability – narrow scope amendments to XRB A1, issued in [Date], amended paragraphs 8 and 10 and added paragraph 12A. An entity shall apply these amendments for annual financial statements covering periods beginning on or after 1 January 2024. Earlier application is permitted.**

Paragraphs BC46–BC51 and the preceding heading are added. New text is underlined.
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**Basis for Conclusions**

...

**Definition of public accountability – narrow-scope amendments to XRB A1**

BC46. The definition of public accountability in XRB A1 determines the reporting tier that applies to an entity that is required to prepare GPFR in accordance with standards issued by the XRB. The XRB issued *Definition of public accountability – narrow scope amendments to XRB A1* to clarify the application of the definition of public accountability in XRB A1.

BC47. The amendments were issued to address application challenges relating to the second part of the IASB definition of public accountability, which refers to entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses. The XRB received feedback that certain constituents had the following concerns in relation to this part of the definition. The concerns below refer to the text of XRB A1 before it was amended by *Definition of public accountability – narrow scope amendments to XRB A1*.

- (a) Paragraph 8(b) of XRB A1 notes that *most* ‘securities brokers/dealers’ would meet the ‘fiduciary capacity’ part of the IASB definition of public accountability. However, in New Zealand, some entities referred to as ‘brokers’ do not hold client money or property. In many cases, the primary business of securities brokers/dealers is to buy/sell securities on behalf of clients and/or provide investment advisory and portfolio administration services. Under the FMC Act, some securities brokers/dealers are classified as having “higher levels of accountability” than other FMC entities based on the nature of the service provided, and others are not.
- (b) Paragraph 8(b) of XRB A1 also notes that *most* ‘mutual funds’ would meet the ‘fiduciary capacity’ part of the IASB definition of public accountability. In practice, there is some uncertainty over whether *fund managers* are caught by the IASB definition of public accountability and are required to apply Tier 1 reporting requirements. The FMC Act and other FMA regulations generally classify fund managers who provide discretionary investment management services as having a lower level of public accountability.
- (c) Paragraph 10 of XRB A1 adds unnecessary complexity to the application of the definition of public accountability. It can be difficult to interpret this paragraph.
- (d) Under paragraph 10, all non-FMC reporting entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses must report under Tier 1. However, FMC reporting entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses can report under Tier 2 if they do not have ‘higher level of public accountability’ under the FMC Act. Questions were raised as to whether this outcome is logical.

## DEFINITION OF PUBLIC ACCOUNTABILITY – NARROW-SCOPE AMENDMENTS TO XRB A1

BC48. To address these concerns, the XRB issued *Definition of public accountability – narrow scope amendments to XRB A1*. These amendments:

- (a) remove the specific reference to securities brokers/traders and fund managers (and other specific entities) from paragraph 8(b), and amend paragraph 12 accordingly;
- (b) add guidance in paragraph 12A to clarify that in New Zealand, not all brokers and fund managers hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses; and
- (c) simplify the requirements in paragraph 10, by specifying that an entity does not have public accountability under paragraph 8(b) unless it is deemed to have public accountability in accordance with paragraph 9 (i.e. unless it is an FMC reporting entity with ‘higher level of public accountability’ under the Financial Markets Conduct Act 2013).

BC49. The XRB is aware that the amendment to paragraph 8(b) introduces a difference between the definition of public accountability in New Zealand and the definition of public accountability in the IASB’s literature. However, the XRB notes that bracketed text that was removed from paragraph 8(b) – namely, the examples of entities that would mostly meet the definition of public accountability in the IASB’s view – is acknowledged and referred to in the added paragraph 12A. Furthermore, the deletion of specific examples of entities from paragraph 8(b) is consistent with the definition of public accountability in the Australian standard AASB 1053 *Application of Tiers of Australian Accounting Standards*.

BC50. The XRB is also aware that as a consequence of the amendments to paragraph 10, entities that hold assets in fiduciary capacity for a broad group of outsiders as one of their primary businesses, but which are *not FMC reporting entities*, would no longer be required to report in Tier 1. Instead, such entities would be able to report under Tier 2, or a lower Tier if they are a PBE. The XRB considers that most entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses would be captured by FMC regulations.

BC51. The XRB notes that the definition of public accountability is important not only for the purpose of financial reporting, but also for audit and assurance purposes. The definition of public accountability is a key factor when determining whether an entity meets the Tier 1 criteria in this Standard. An entity that meets the Tier 1 criteria in this Standard and is not eligible to report in accordance with the requirements of another tier is classified as a ‘public interest entity’ (PIE) for audit and assurance purposes. Auditors of PIEs have additional independence requirements. As the abovementioned concerns about the definition of public accountability originated mainly from assurance practitioners, the XRB added paragraphs 19A and 38A into XRB A1 – to specify and emphasise the link between the Tier 1 criteria in this Standard and the definition of a public interest entity (PIE) for audit and assurance purposes.

## Part D – Effective Date

This [draft] Standard shall be applied for annual financial statements covering periods beginning on or after 1 January 2024. Earlier application is permitted.

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**Date:** 29 April 2022

**To:** NZASB Members

**From:** Gali Slyuzberg

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

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### **Purpose and introduction<sup>1</sup>**

1. This paper relates to the IPSASB Exposure Draft 81 *Conceptual Framework Update: Chapter 3, Qualitative Characteristics and Chapter 5, Elements in Financial Statements* (the ED). The purpose of this paper is to seek the Board's approval of our draft comment letter on this ED.
2. The full ED is provided as agenda item 10.3 (in the supporting papers). We note that the ED includes Chapters 3 and 5 of the IPSASB Conceptual Framework in their entirety. For the Board's convenience, Appendix A of this paper includes references to the specific paragraphs in the ED where amendments are proposed.

### **Recommendation**

3. The Board is asked to APPROVE the draft comment letter (agenda item 10.2).

### **Background**

4. The IPSASB issued the ED in February 2022. The ED proposes limited-scope updates to the IPSASB Conceptual Framework. The proposals arise from the following developments since the Framework was approved in 2014:
  - (a) the IPSASB's experience in applying the Framework to the development and maintenance of IPSAS; and
  - (b) developments in international thinking about conceptual issues (specifically, the IASB's updates to its Conceptual Framework in 2018).
5. In summary, the ED proposes the following amendments to the IPSASB Conceptual Framework.
  - (a) Chapter 3, Qualitative Characteristics: The amendments clarify the role of prudence and update the guidance on materiality.
  - (b) Chapter 5, Elements in Financial Statements: Amendments include a revised definition of a liability that refers to 'transfer of resources', amendments to the description of a 'resource' in the context of the definition of an asset, and amendments to the related guidance on assets and liabilities. New guidance is also proposed on the 'unit of account'.

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<sup>1</sup> 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).



6. At its February 2022 meeting, the Board agreed to comment on the ED, and that staff should carry out targeted outreach to inform the comment letter. Comments are due to the NZASB by 15 April 2022.
7. We have discussed the ED with the TRG in March 2022. We also discussed the ED and the first draft of our comment letter with the Board at its April 2022 meeting. The draft comment letter reflects Board members’ and TRG members’ feedback.
8. After the Board’s April meeting, we also reached out to the Treasury, OAG and Audit New Zealand, to seek their views on the ED. At the time of writing, these constituents did not identify any issues relating to the ED proposals that we should add to our comment letter. If these constituents raise additional issues before the Board’s May meeting, we will update the Board verbally at the meeting.
9. Comments on the ED are due to the IPSASB by 31 May 2022. This meeting is the Board’s last meeting before comments are due to the IPSASB. Therefore, we are seeking the Board’s approval of the draft comment letter at this meeting.

**Updated draft comment letter**

10. The table below summarises the changes we made to the draft comment letter, based on feedback received from Board members in April 2022.

**Table 1: Summary of changes to the draft comment letter**

Comment letter part	Description of changes made in response to Board feedback
Cover letter	Added the key points of our comment letter into the cover letter.
SMC 2: Obscuring information as a factor relevant to materiality judgement	<p><i>Obscuring information:</i></p> <p>Added a recommendation to make it clear that material information can be obscured if an entity includes too much detailed information in the financial statements – and such information may not be useful.</p>
SMC 3: Rights-based approach to resources (Also relates to SMC 4: Definition of a liability)	<p><i>Reference to past events:</i></p> <p>Added recommendation to clarify the following:</p> <ul style="list-style-type: none"> <li>• When an asset/liability arises from an accumulation of multiple events, it may be possible to identify a single event after which the definition of a liability is met. However, that event may not on its own cause the definition of a liability to be met – and the reference to ‘past events’ would cover such situations.</li> <li>• However, we still think that an asset/liability could arise from a single past event or multiple past events, and we recommend clarifying this to avoid confusion.</li> </ul>

Comment letter part	Description of changes made in response to Board feedback
SMC 5: Guidance on the transfer of resources	<p><i>Recommendation to enhance the guidance on the recognition of liabilities (and assets):</i></p> <p>Added text about the difference between liabilities that are recognised in the statement of financial position and contingent liabilities – to strengthen our recommendation to enhance the guidance on the recognition of liabilities.</p>
SMC 6: Revised structure of guidance on liabilities	<p><i>Recommendation to amend paragraph 5.15A</i></p> <p>There is a potential inconsistency between what paragraph 5.15A says about public communication of intentions and what paragraph 5.15C says on this subject. We previously recommended enhancing the link between these two paragraphs.</p> <p>However, we are now recommending instead to delete the reference to public communication in paragraph 5.15A. This should help eliminate the inconsistency between the two paragraphs (whereas our original recommendation risked exacerbating the effect of the inconsistency, by drawing further attention to it).</p>

11. In addition, in response to the Board’s feedback in April, we also made the following general edits throughout the comment letter.
- (a) Edits to enhance the clarity and focus of our comments – by reducing wording, focusing up-front on what we disagree with or recommend improving, and deleting or reducing comments relating to ‘alternative’ recommendations.
  - (b) Edits to replace the general reference to ‘constituents’ with specific references to the Accounting TRG. This was done to clarify the type of constituents whose feedback is reflected in our letter.

**Questions for the Board**

- Q1. Does the Board approve the draft comment letter in agenda item 10.2?
- Q2. Does the Board agree that any changes to the draft comment letter raised at this meeting should be finalised through review by the Chair?

**Next steps**

12. We will update the draft comment letter for any feedback received from the Board at this meeting and will submit the letter to the IPSASB before the due date of 31 May 2022.

**Attachments**

- Agenda item 10.2: Draft comment letter
- Agenda item 10.3: IPSASB ED 81 (in the Supporting Papers)

## Appendix A: Summary of the proposals in ED 81

### Summary of proposed amendments to Chapter 3, *Qualitative Characteristics*

Proposed amendments	ED Ref
<p><b>Prudence</b></p> <p>The ED proposes to clarify the role of prudence in supporting neutrality, which is an aspect of faithful representation. The amendments note the following.</p> <ul style="list-style-type: none"> <li>• Prudence is the exercise of caution when making judgements under conditions of uncertainty. Exercising prudence means that assets, liabilities, revenue, and expenses are not overstated or understated.</li> <li>• The exercise of prudence does not imply a need for asymmetry (e.g. systematically requiring more evidence for recognising assets or revenue as compared to liabilities and expenses). However, some standards may include asymmetric requirements.</li> </ul> <p>These amendments are aligned with the IASB’s Conceptual Framework.</p>	<p>Para 3.14A – 3.14B</p>
<p><b>Materiality</b></p> <p>The ED proposes to update the guidance on materiality by adding a reference to the <i>obscuring</i> of information. That is, information is material if omitting, misstating <i>or obscuring</i> it could be reasonably expected to influence the discharge of accountability by the entity or the decisions made by users of the financial statements. This amendment is aligned with the IASB’s Conceptual Framework.</p> <p>In addition, the ED proposes to add a sentence about considering disclosure when an item is not separately or prominently displayed on the face of the financial statements, and to explain that it is not possible to specify a uniform set of characteristics that makes information material.</p>	<p>Para 3.32– 3.32A</p>

### Summary of proposed amendments to Chapter 5, *Elements in Financial Statements*

Proposed amendments	ED Ref
<p><b>Definition of an asset:</b></p> <p><i>Rights-based approach to description of ‘resource’</i></p> <p>The ED proposes amendments to the description of a ‘resource’ – which is an element of the definition of an asset – and to the related guidance.</p> <p>Specifically, the IPSASB proposes to adopt a rights-based approach to the description of a resource – similarly to the IASB Framework.</p> <p>The IPSASB Conceptual Framework currently describes a resource as an ‘item’ with service potential or the ability to generate economic benefits. The related guidance refers to benefits arising either from the resource itself or from rights to use it.</p> <p>As explained in the ED’s Basis for Conclusions, in 2018 the IASB decided that the guidance on assets in its Conceptual Framework should not distinguish between benefits that arise from owning an object and those that arise from the right to use an object. The IASB noted that rights conferred by legal ownership of an object and rights to use the object for some of its useful life are both types of rights – not separate phenomena. The IPSASB found this argument persuasive.</p> <p>The proposed new description of a resource in the ED is: “a right to either service potential or the capability to generate economic benefits, or a right to both”.</p>	<p>Para 5.6– 5.13</p>

Proposed amendments	ED Ref
<p>Most of the added guidance on rights is based on the guidance in the IASB's Conceptual Framework. However, unlike the IASB, the IPSASB has had to refer both to economic benefits and service potential in its proposed description of a resource and the accompanying guidance.</p> <p><i>Minor amendment to the definition of an asset</i></p> <p>The IPSASB proposes to refer to 'past events' (plural), rather than a 'past event', in the definition of an asset. The IPSASB notes that an asset may arise from a single past event or from multiple past events.</p>	
<p><b>Definition of a liability</b></p> <p><i>Reference to 'transfer of resources'</i></p> <p>The ED proposes to define a liability as the present obligation to <i>transfer resources</i> – rather than a present obligation for an outflow of resources.</p> <p>In 2018, the IASB made a similar amendment to the definition of a liability in its Conceptual Framework. The previously used term 'outflow of [economic] resources' was linked to guidance on <i>expected</i> outflow of resources. The IASB considered that this focus on expectation of outflow conflates the requirements for meeting the <i>definition</i> of a liability with the requirements for the <i>recognition</i> of a liability. Therefore, in the IASB's Conceptual Framework, the IASB replaced the notion of expected outflow of resources with the notion of potential to require transfer of resources. The IPSASB found this argument persuasive and proposed a similar amendment.</p> <p>The IPSASB also proposes to amend the guidance on the definition of a liability, based on the IASB's guidance in its Conceptual Framework – with modifications to reflect the public sector context. As noted above, similarly to the IASB's amendments to its Conceptual Framework, previous references to the <i>probability/expectation</i> of outflows of resources are removed, as such notions are deemed to relate to the recognition of a liability.</p> <p>For example, paragraph 5.16A states that to meet the definition of a liability, an obligation must have the <i>potential to require the entity to transfer a resource</i> to another party – but the <i>transfer does not have to be certain or even likely</i> and might be dependent on a specified uncertain future event occurring.</p> <p>The amendments to the guidance on the definition of a liability include new guidance on the concept of 'transfer of resources'. This guidance is particularly important in the context of the IPSASB's project on <i>Revenue and Transfer Expenses</i>, where proposals focus on liabilities arising from binding arrangements.</p> <p><i>Minor amendment to the definition of a liability</i></p> <p>As with the definition of an asset, the IPSASB proposes to refer to 'past events' (plural), rather than a 'past event', in the definition of a liability.</p> <p><i>Reorganisation of the section on liabilities</i></p> <p>The ED proposes to rearrange the section on liabilities in Chapter 5, so that the order of topics discussed in the guidance are aligned with the proposed new definition of a liability.</p>	<p>Para 5.14 – 5.26</p>
<p><u>Unit of account</u></p> <p>The 'unit of account' is the unit to which recognition criteria and measurement concepts are applied. Currently, there is no specific guidance on the 'unit of account' in the IPSASB Conceptual Framework. The ED proposes to add into Chapter 5 a new section on the 'unit of account'. The proposed guidance is largely based on the equivalent guidance in the IASB's Conceptual Framework.</p>	<p>Para 5.26A– 5.26J</p>

Proposed amendments	ED Ref
<p><u>Binding arrangements that are equally unperformed (executory contracts)</u></p> <p>The proposed new guidance on the unit of account includes guidance on 'binding arrangements that are equally unperformed'.</p> <p>This guidance is based on the IASB's guidance on executory contracts in its Conceptual Framework. However, the IPSASB decided not to use the term 'executory contracts', because in some jurisdictions the term 'contract' is problematic in the public sector.</p> <p>Unlike the IASB, the IPSASB decided to integrate the guidance on 'binding arrangements that are equally underperformed' into the section on 'unit of account'.</p>	<p>Para 5.26G– 5.26H</p>

**Note to Board members:** This draft comment letter reflects edits made in response to Board members' feedback received at the April 2022 meeting. For ease of reading, the edits are not shown as mark-ups – but the locations and descriptions of the edits are indicated using comment bubbles.

XX May 2022

Mr Ross Smith  
Program and Technical Director  
International Public Sector Accounting Standards Board  
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CANADA

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

Dear Ross

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

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

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

- **Materiality:** We recommend not to include in the Conceptual Framework the proposed sentence about display vs disclosure of information, because we are not convinced that it is necessary to discuss this specific matter within the general guidance on materiality, and the wording of the sentence seems unclear.
- **Definition of an asset:** We recommend further simplifying/streamlining the description of a resource, to enhance the understandability of the description.

**Commented [GS1]:** The cover letter has been updated to include a summary of the updated comments in the Appendix.

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

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

Yours sincerely

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

## APPENDIX

### Response to Specific Matters for Comment

#### Specific Matter for Comment 1: Prudence

In paragraphs 3.14A and 3.14B, the IPSASB has provided guidance on the role of prudence in supporting neutrality, in the context of the qualitative characteristic of faithful representation. Paragraphs BC3.17–BC3.17E explain the reasons for this guidance. Do you agree with this approach?

If not, why not? How would you modify these paragraphs?

#### NZASB response

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

**Commented [GS2]:**  
General edit throughout the letter – replaced the general reference to 'constituents' with a specific reference to TRG members, in response to Board feedback from the April 2022 meeting.

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

In discussing materiality in paragraph 3.32 the IPSASB has added obscuring information to misstating or omitting information as factors relevant to materiality judgments. The reasons for this addition are in paragraphs BC3.32A and 3.32B.

Do you agree with the addition of obscuring information to factors relevant to materiality judgments? If not, why not?

#### NZASB response

#### *Obscuring information*

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

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



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

3. In addition, we recommend that the IPSASB considers further clarifying what is meant by ‘obscuring information’. This clarification can be provided in paragraph 3.32 or in a footnote to that paragraph. The clarification could explain that if financial statements include excessive amounts of detailed information, this could negatively affect a user’s ability to find the information that the user needs to be able to make decisions, or to confirm that the entity has discharged its accountability. Therefore, for financial statements to provide useful information to users, it is important to ensure that material information is not obscured by immaterial information.

**Commented [GS3]:** New paragraph added to reflect Board feedback from the April 2022 meeting.

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

4. While SMC 2 focuses on the proposed reference to ‘obscuring information’, we note that the ED also proposes to add the following sentence to paragraph 3.32 of the IPSASB Conceptual Framework:

*“Where an entity judges that a material item is not separately displayed on the face of a financial statement (or displayed sufficiently prominently) an entity considers disclosure”.*

5. We recommend not to add this proposed sentence to the Conceptual Framework, for the following reasons.
- (a) Firstly, we are not convinced that it is necessary to discuss the specific matter of display vs disclosures in the general materiality guidance in the Conceptual Framework. We note that the individual standard IPSAS 1 *Presentation of Financial Statements* discusses separate presentation of items in the primary financial statements and disclosures in the notes – including the presentation of additional items that are not specified in IPSAS 1, and disclosure of items that are not presented in the financial statements.
  - (b) Secondly, we think the wording of the proposed sentence on ‘display and disclosure’ is unclear and may not reflect the intent behind the sentence. Presumably, the intent of this sentence was to explain that if an entity decides that an item is not material enough to be displayed separately or prominently on the face of the financial statements, the entity should consider whether the item is sufficiently material to be disclosed in the notes. However, the current drafting of the sentence seems to imply that when an entity did not display a material item with sufficient prominence (which implies an omission), the entity should remedy this by considering disclosure in the notes.

**Commented [GS4]:** To reflect Board members’ feedback from the April 2022 meeting, this section was generally edited to increase the clarity and focus of this comment – by focusing upfront on what we disagree with, and reducing word count, particularly in relation to the alternative recommendation at the end.

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

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

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

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

NZASB response

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

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

*Recommendation to simplify the description of a resource*

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

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

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

**Commented [GS5]:** To reflect Board members' feedback from the April 2022 meeting, this section was generally edited to make our comment more focused – by stating the recommendation upfront and deleting the 'alternative' recommendation at the end.

**Commented [GS6]:** New paragraph added to reflect Board feedback from the April 2022 meeting.

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

The revised definition of a liability is in paragraph 5.14:

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

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

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

NZASB response

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

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

The IPSASB has included guidance on the transfer of a resource in paragraphs 5.16A-5.16F of the section on Liabilities. The reasons for including this guidance are in paragraphs BC5.19A-BC5.19D.

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

NZASB response*General comment*

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

*Recommendation to enhance the guidance on the recognition of liabilities (and assets)*

19. The proposed amendments to the guidance on liabilities in the ED emphasise that an obligation may meet the definition of a liability even if the probability of having to transfer resources is low. For example:
- (a) the proposed new paragraph 5.16A says: "To satisfy the definition of a liability the obligation must have the potential to require the entity to transfer a resource to another party (or parties). For that potential to exist, it does not need to be certain, or even likely, that the entity will be required to transfer a resource [...]"; and
  - (b) the proposed new paragraph 5.16B says: "An obligation can meet the definition of a liability even if the probability of a transfer of a resource is low. [...]".
20. We understand the rationale for these proposals, i.e. to avoid conflating the principles of the definition of a liability with the recognition principles. We also note that the IASB made similar amendments to the guidance of the definition of a liability in its Conceptual Framework in 2018.
21. However, in light of the abovementioned proposals, we think it would be useful to consider enhancing the guidance on the *recognition* of liabilities in the IPSASB Conceptual Framework.

22. We note that the guidance on the recognition of liabilities in the IASB’s Conceptual Framework appears to be more detailed and robust than the IPSASB’s existing guidance on the recognition of liabilities. The chapter on recognition in the IPSASB Conceptual Framework includes some references to considering the qualitative characteristics. However, the chapter on recognition in the IASB’s Conceptual Framework includes specific sections on considering relevance and faithful representation when determining whether a liability (or an asset) is recognised. These sections include a specific discussion on low probability of outflow (and inflow) of economic resources, as well as a discussion on existence uncertainty and measurement uncertainty.
23. We recommend enhancing the guidance on the recognition of liabilities (and assets) in the IPSASB Conceptual Framework in a similar vein to the abovementioned IASB guidance. Such enhancements would help clarify that when the likelihood of a transfer of resources is low, an item may meet the definition of a liability but might not meet the criteria for recognition.
24. An example of where the abovementioned enhanced guidance could be useful is when a preparer considers whether an obligation is a contingent liability – which is disclosed but is not recognised in the statement of financial position – or whether it is a liability that needs to be recognised in the statement of financial position.

**Commented [GS7]:**  
Added reference to contingent liabilities, as per Board feedback at the April 2022 meeting.

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

In addition to including guidance on the transfer of resources, the IPSASB has restructured the guidance on liabilities so that it aligns better with the revised definition of a liability. This guidance is in paragraphs 5.14A-5.17D. Paragraph BC 5.18H explains the reasons for this restructuring.

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

NZASB response

*General comment*

25. We agree with the restructure of the guidance on liabilities, to match the order in which terms are described in the revised definition of a liability. However, we recommend amending the wording of one of the restructured paragraphs (paragraph 5.15A), as explained below.

Recommendation to amend paragraphs 5.15A

26. Paragraphs 5.15A and 5.17C both refer to public communication of intentions in the context of a liability. We note that there is a possible inconsistency between these references, as explained below.
- (a) Paragraph 5.15A states that an obligation must be to an external party to give rise to a liability, and that an entity “cannot be obligated to itself, *even where it has publicly communicated an intention to behave in a particular way*” [italics added for emphasis].
- (b) Paragraph 5.17C then discusses the point at which a liability arises. This paragraph states that a promise made in an election is unlikely to give rise to a present obligation that meets the definition of a liability, but an announcement might have “such political support that the government has little option to withdraw”. This implies that public

**Commented [GS8]:**  
Changed our recommendation in response to Board feedback at the April 2022 meeting. Instead of recommending to enhance the link between paragraphs 5.15A and 5.17C, we now recommend deleting the words that refer to public communication in paragraph 5.15A.

communication could give rise to a liability – and there is no qualification in this paragraph that the liability must be to an external party. Therefore, this paragraph could be read as being inconsistent with what paragraph 5.15A says about public communication of intentions.

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

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

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

Do you agree with the addition of a section on Unit of Account and its content? If not, how would you modify it and why?

NZASB response

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

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

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

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

If you do not agree, please give your reasons.

NZASB response

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

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

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

30. Our Accounting TRG questioned the rationale for including the guidance on binding arrangements that are equally unperformed within the section on 'unit of account' – noting that in the IASB Conceptual Framework, the equivalent guidance on executory contracts is included in a separate section. The Basis for Conclusions explains that the IPSASB decided that a separate section on this topic is 'unnecessary', but the reason for this decision is not provided.
31. We are concerned that including the guidance on 'binding arrangements that are equally unperformed' within the section on 'unit of account' would imply to readers of the Conceptual Framework that the concepts in this guidance are confined solely to the determination of the unit of account. We do not think that this implication is correct. For example, we note the following.
  - (a) Paragraph 5.26G states that "The entity has an asset if the terms of the exchange are currently favourable; it has a liability if the term of the exchange are currently unfavourable". Arguably, this guidance relates to meeting the definition of an asset or a liability.
  - (b) Paragraph 5.26H states "To the extent that either party fulfils its obligations under the binding arrangement, the binding arrangement changes character. If the reporting entity performs first under the binding arrangement, that performance is the event that changes the reporting entity's right and obligation to exchange resources into a right to receive a resource. That right is an asset. If the other party performs first, that performance is the event that changes the reporting entity's right and obligation to exchange resources into an obligation to transfer a resource. That obligation is a liability". Arguably, this guidance relates to meeting the definition of an asset or a liability, as well as the timing of recognition of an asset or a liability.
32. Therefore, we would recommend including the guidance on 'binding arrangements that are equally unperformed' in a separate section in Chapter 5, rather than within the 'unit of account' section (similarly to the IASB).
33. If the IPSASB does not relocate the guidance on binding arrangements that are equally unperformed to a separate section, then we think it would be important to clarify in the Basis for Conclusions that the principles in this guidance have broader application than just the 'unit of account' topic, and the reason why it is not necessary to have a separate section for this guidance.