XRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Board Meeting Agenda

In-person Meeting (Auckland) — Wednesday, 28 June 2023

Est Time	Item	Topic	Objective		Page
PUBLIC SESSION					
10.35 am	**3B**	**PBE Policy Approach: IPSAS 47 *Revenue***	(AH)		
60 min	3B.1	Board memo: IPSAS 47 *Revenue*	Consider	Paper	3
	3B.2	At-a-glance: IPSAS 47 *Revenue*	Note	Paper	29
	3B.3	Standard: IPSAS 47 *Revenue*	Note	Supp Paper	–
11.35 am	**3C**	**PBE Policy Approach: Non-exchange Expenses-related Standards**	(CB)		
60 min	3C.1	Board memo: IPSAS 48 *Transfer Expenses*	Consider	Paper	37
	3C.2	At-a-glance: IPSAS 47 *Transfer Expenses*	Note	Paper	61
	3C.3	Board memo: IPSAS 42 *Social Benefits* and *Collective and Individual Services (Amendments to IPSAS 19)*	Consider	Paper	68
	3C.4	At-a-glance: IPSAS 42 *Social Benefits*	Note	Paper	89
	3C.5	At-a-glance *Collective and Individual Services (Amendments to IPSAS 19)*	Note	Paper	98
	3C.6	Standard: IPSAS 48 *Transfer Expenses*	Note	Supp Paper	–
	3C.7	Standard: IPSAS 42 *Social Benefits*	Note	Supp Paper	–
	3C.8	Standard: *Collective and Individual Services (Amendments to IPSAS 19)*	Note	Supp Paper	–
12.35 pm	**4**	**Project update – IPSAS Measurement Related Standards**	(CH + GS)		
10 min	4.1	Board memo	Note	Paper	105
	4.2	Standard: IPSAS 45 *Property, Plant and Equipment* [amendments resulting from IPSAS 46]	Note	Supp Paper	–
	4.3	Standard: IPSAS 46 *Measurement*	Note	Supp Paper	–
	4.4	Updated IPSASB Conceptual Framework chapter: Chapter 7 *Measurement of Assets and Liabilities in Financial Statements*	Note	Supp Paper	–
12.45 pm 45 min	**Lunch**				
NON-PUBLIC SESSION					

PUBLIC SESSION					
2.30 pm	**6A**	**Approval of IASB Accounting Standards: Supplier Finance Arrangements**	(JC)		
10 min	6A.1	Board memo	Consider	Paper	111
	6A.2	Draft *Supplier Finance Arrangements*	Approve	Paper	120
	6A.3	Draft Signing memorandum	Approve	Paper	128
2.40 pm	**6B**	**Approval of IASB Accounting Standards: International Tax Reform – Pillar Two Model Rules**	(CH)		
20 min	6B.1	Board memo	Consider	Paper	132
	6B.2	Draft *International Tax Reform – Pillar Two Model Rules*	Approve	Paper	144
	6B.3	Draft Signing memorandum	Approve	Paper	152
3:00 pm	**7**	**Amendments to the Classification and Measurement of Financial Instruments**	(GS)		
20 min	7.1	Board memo	Consider	Paper	157
	7.2	Submissions received	Consider	Paper	172
	7.3	Draft comment letter	Approve	Paper	173
	7.4	ED *Amendments to the Classification and Measurement of Financial Instruments*	Note	Supp paper	–
3.20 pm 15 min	Afternoon tea break				
NON-PUBLIC SESSION					
4.40 pm	*Finish*				

Next NZASB meeting: 10 August 2023, virtual

Agenda Item 3B.1

XRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Memorandum

Date:	16 June 2023
To:	NZASB Members
From:	Anthony Heffernan, Leana van Heerden and Tereza Bublikova
Subject:	**Application of the PBE Policy Approach to IPSAS 47 *Revenue***

COVER SHEET

Project priority and complexity

Project priority	**High*** *If the Board agrees to commence the development of a PBE Standard based on IPSAS 47 *Revenue*
Complexity of Board decision-making at this meeting	**High** The Board is required to apply the PBE Policy Approach to *IPSAS 47 Revenue*. There is a high degree of judgement involved in the application of the PBE Policy Approach – and reaching a view on whether to commence a PBE project based on the recently issued IPSAS. Based on significant concerns previously raised by constituents regarding the existing revenue standards we feel there is a strong argument that a new PBE standard on revenue using IPSAS 47 as a starting point will lead to improved financial reporting. We acknowledge the need to manage the introduction of any new standard carefully to ensure the implementation costs do not exceed the benefits – this requires a focus on developing a PBE Standard with understandable principles and requirements, and ensuring users can easily navigate to the section of the standard applicable to their transaction. IPSAS 47 introduces a significant volume of new requirements and guidance mainly due to objective of seeking to achieve alignment with IFRS 15 *Revenue from Contracts with Customers* to the extent appropriate for the public sector.

Overview of agenda item

Project status	This project has not yet commenced. Applying the PBE Policy Approach at this meeting is the first step and will determine subsequent steps.
Project purpose	If we commence the recommended projects, the objective will be to develop a PBE Standard using IPSAS 47 as a starting point. We will need to ensure that any new PBE Standards on Revenue are fit-for-purpose in New Zealand.
Board action required at this meeting	1. APPLY the PBE Policy Approach to IPSAS 47 *Revenue*. 2. AGREE to commence project to develop a PBE Standard on Revenue using IPSAS 47 as a starting point. 3. PROVIDE FEEDBACK on staff's preliminary views on the focus areas for development of the new PBE Standard.

Introduction[1]

1. The International Public Sector Accounting Standards Board (IPSASB) approved IPSAS 47 *Revenue* at its March 2023 meeting. IPSAS 47 was published on 26 May 2023.

2. The purpose of the Revenue project was to develop a new Revenue Standard that provides recognition and measurement requirements for public sector revenue transactions, and addresses application issues with the existing suite of revenue IPSAS. A key objective of the project was also to achieve alignment with IFRS 15 *Revenue from Contracts with Customers* to the extent appropriate for the public sector.[2]

3. IPSAS 47 replaces the following IPSAS Standards on Revenue:

   (a) IPSAS 9 *Revenue from Exchange Transactions*;

   (b) IPSAS 11 *Construction Contracts*; and

   (c) IPSAS 23 *Revenue from Non-Exchange Transactions* (Taxes and Transfers)

4. In accordance with the *Policy Approach to Developing the Suite of PBE Standards* (PBE Policy Approach), the Board is required to consider if and when to incorporate IPSAS 47 into the suite of PBE Standards as issued by the XRB. The content of this memo therefore includes the application of the PBE Policy Approach to IPSAS 47.

Recommendation

5. We recommend that the Board:

   (a) NOTES that the IPSASB recently issued IPSAS 47 *Revenue*;

   (b) APPLIES the PBE Policy Approach and AGREES to commence a project to develop a PBE Standard, using IPSAS 47 as a starting point; and

   (c) PROVIDES FEEDBACK on staff's preliminary views on the focus areas for development of the new PBE Standard.

Structure of this memo

6. This memo has the following sections.

   (a) Summary of the revenue recognition principle in IPSAS 47

   (b) Issues raised regarding existing PBE revenue standards based on IPSAS

   (c) Application of the PBE Policy Approach

   (d) Preliminary views on focus areas for the development of a new PBE Standard

   (e) Next steps

   (f) Appendix 1: Background to the IPSASB's Transfer Expenses Project

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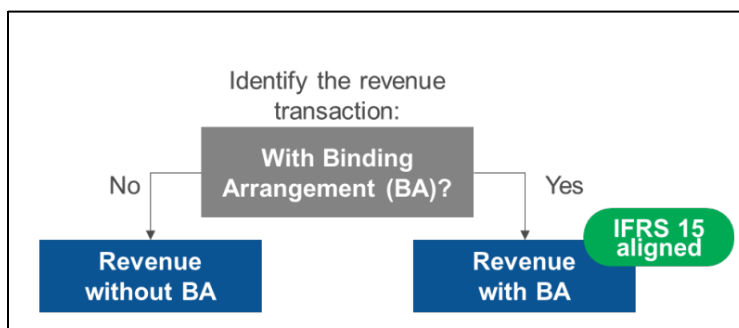
[1] This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

[2] The IPSASB has a policy of IFRS alignment and amending IASB based standards to address public sector specific issues.

(g) Appendix 2: XRB and New Zealand constituents' comments on ED 70 *Revenue with Performance Obligations* and ED 71 *Revenue without Performance Obligations*, and the IPSASB's response

Summary of the revenue recognition principle in IPSAS 47

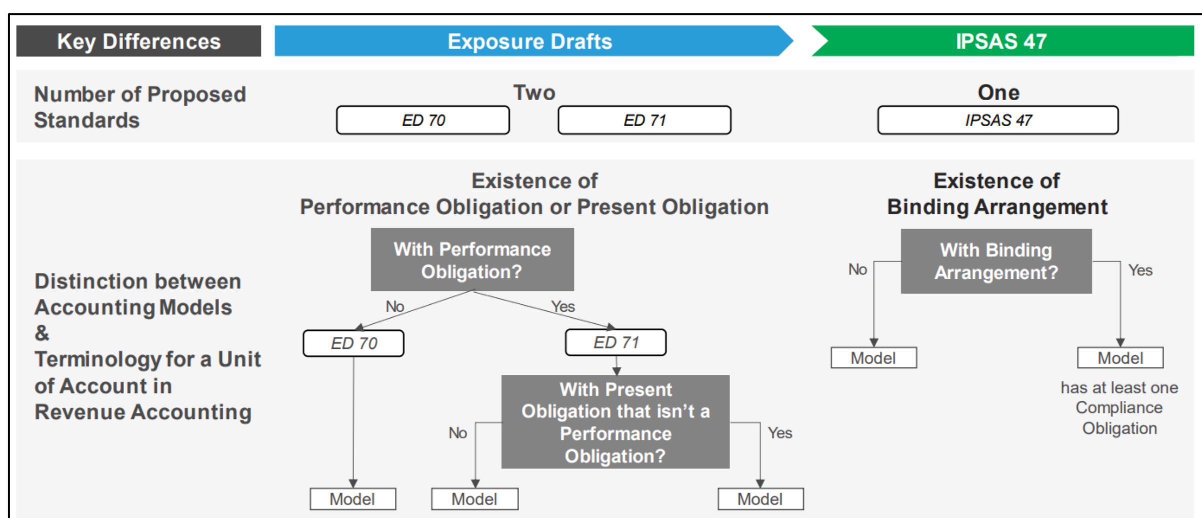
7. The diagram below sets out the core principles underpinning IPSAS 47.



8. As illustrated below the revenue recognition model in IPSAS 47 has been simplified from what was originally proposed at the ED stage. The key changes are:

(a) moving from a two-revenue standard model to one; and

(b) removing the distinction between performance obligations and present obligations arising from revenue transactions – instead, an entity is required to consider if a revenue transaction arises from a binding arrangement with enforceable compliance obligations to use the inflow of resources in a certain way.



Binding arrangement

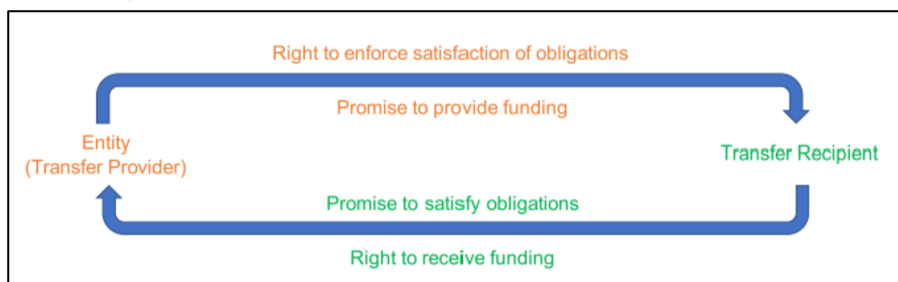
9. IPSAS 47 was developed as a single source for revenue accounting guidance in the public sector. The key feature of the new Standard is the introduction of a two-model accounting approach for revenue recognition in the public sector that distinguishes between:
    - revenue from transactions with binding arrangements; and
    - revenue from transactions without binding arrangements.

    The exchange/non-exchange distinction, as used in previous IPSAS revenue standards, has been removed. [3]

10. A binding arrangement is an arrangement that confers both enforceable rights and obligations on the parties to the arrangement. A contract is a type of binding arrangement. Each party in the binding arrangement willingly enters into the arrangement and is able to enforce their respective rights and obligations conferred on them in the arrangement.

Component	Party A	Party B
Enforceable Right	✓	✓
Enforceable Obligation	✓	✓

11. For revenue transactions, the IPSAS refers to the 'transfer recipient' as the reporting entity accounting for the revenue transaction.



12. The definition of a binding arrangement is underpinned by the principle of enforceability. A binding arrangement is an arrangement that confers both rights and obligations, enforceable through legal or equivalent means, on the parties to the arrangement.

    In the public sector, an arrangement is enforceable when each of the involved parties is able to enforce their respective rights and obligations through various mechanisms. An arrangement is enforceable if the agreement includes:

    (a) clearly specified rights and obligations for each involved party; and

    (b) remedies for non-completion by each involved party which can be enforced through the identified enforcement mechanisms.

[3] Although the IPSASB decided to move away from using exchange/non-exchange as defined terms to classify revenue, the IPSASB emphasised that it remains an appropriate concept to describe the economic substance of transactions in the public sector – i.e., the concept of non-exchange transactions remains a key concept in the IPSASB's Conceptual Framework.

13. Enforceability can arise from various mechanisms, as long as the mechanism provides the entity with the ability to enforce the terms of the binding arrangement and holds the parties accountable to the satisfaction of stated obligations.

Recognition of revenue from transactions without binding arrangements

14. IPSAS 47 requires revenue arising from transactions without binding arrangements to be recognised:

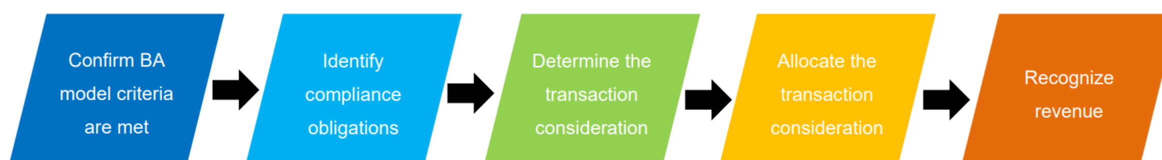
    (a) When (or as) the entity satisfies any obligation associated with the inflow of resources that meets the definition of a liability;[4] or

    (b) Immediately if the entity does not have an enforceable obligation associated with the inflow of resources.

15. The IPSAS 23 restrictions and conditions approach, which only allowed for deferral of revenue recognition for non-exchange transactions when there was a "use or return condition" has been removed. Instead, the ability to defer revenue recognition is based on the existence of obligations, which is a much broader principle based on applying the Conceptual Framework definition of a liability.

Recognition of revenue from transactions with binding arrangements

16. The revenue recognition approach for transactions with binding arrangements is based on IFRS 15 — including the five-step model that has been adapted for the public sector.



17. Under this model, an entity is required to recognise revenue from transactions with binding arrangements as compliance obligations associated with the inflow of resources are satisfied. A liability (deferred revenue) is recognised for any unsatisfied compliance obligations in respect of the inflow of resources received from the revenue transaction.

18. The key public sector amendment is the introduction of the new concept of a 'compliance obligation', which is broader than the IFRS 15 concept of a performance obligation. A compliance obligation is an entity's promise in a binding arrangement to use the inflow of resources from the revenue transaction:

    - internally for acquiring distinct goods or services;
    - to transfer distinct goods or services to a purchaser; or
    - transfer distinct goods or services to third-party beneficiaries.

[4] The entity will need to consider wheather the inflow of resources results in a present obligation – being an obligation for which it has little or no realistic alternative to avoid an outflow of resources.

19. This approach will require increased judgement but will also allow for increased flexibility to defer revenue recognition – especially for revenue funding that is required to be used in a certain way but does not necessarily require the transfer of specific goods or services.
20. A key area of expected interpretation challenge when applying IPSAS 47 is the identification of each distinct compliance obligation, which will be the unit of account for revenue recognition.

Further background information on IPSAS 47

21. Agenda paper 3B.2 contains a "snapshot" of IPSAS 47. The full Standard can be found at agenda paper 3B.3 (in supporting papers).

22. Appendix 1 to this memo includes some further background information on the IPSASB's Revenue project.

Issues raised regarding existing PBE revenue standards based on IPSAS

23. We note following issues previously raised by New Zealand constituents:

    (a) Difficulty in making the distinction between exchange and non-exchange transactions.

    - In 2016 the Controller and Auditor-General report Improving financial reporting in the public sector pointed out that, there is limited guidance about how to distinguish between exchange/non-exchange. This means that entities and their auditors are spending much time and effort trying to distinguish between types of revenue when preparing general purpose financial reports.

    - This was still an issue in 2019 and was stressed by the Part D.4 of the Productivity Commission paper Local government funding and finance – Accounting and financial management issues, which encouraged XRB to investigate this issue.

    (b) Difficulty in making the distinction between different types of stipulations in revenue arrangements — conditions and restrictions. Related to this were concerns about the restrictive nature of IPSAS 23 which only allowed for the deferral of revenue recognition when there was a use or return condition.

    (c) Lack of specific guidance on:

    - multi-year funding arrangements and general operating grants which time-based conditions;

    - taxation received in advance of the period in which it is intended to be used;

    - accounting for capital grants specifically where full or partial reimbursements are provided only once expenditure claims are submitted and audited; and

    - accounting for services in-kind.

Application of the PBE Policy Approach

24. Shortly after its publication, the Board will typically consider whether a new or amending IPSAS should be adopted into PBE Standards. These decisions are guided by the PBE Policy Approach.

25. The PBE Policy Approach identifies triggers for changes to PBE Standards. One of these triggers is the IPSASB issuing a new IPSAS. Section 4.1 (paragraphs 22–24) of the PBE Policy Approach establishes a rebuttable presumption that the NZASB will adopt a new or amended IPSAS. The PBE Policy Approach states that it is expected that the adoption of a new or amended IPSAS will lead to higher quality financial reporting by public benefit entities (PBEs) in New Zealand and the factors in the development principle are presumed to be met.

26. **Table 1** on the next page considers the factors in the development principle, as provided for in the PBE Policy Approach, as they apply to IPSAS 47.

Table 1: Factors in the Development Principle

Factors in the Development Principle	Comment
Whether the potential development will lead to higher quality financial reporting by public sector PBEs and not-for-profit entities, including public sector PBE groups and not-for-profit groups, than would be the case if the development was not made.	IPSAS literature previously included three standards for revenue transactions, IPSAS 9 *Revenue from Exchange Transactions*, IPSAS 11 *Construction Contracts*, and IPSAS 23 *Revenue from Non-Exchange Transactions* (Taxes and Transfers). The IPSASB's primary objectives for developing a new revenue standard were to consider the extent to which the new revenue recognition model in IFRS 15 *Revenue from Contracts with Customers* should be introduced into the public sector standards and to address concerns about the restrictive nature of IPSAS 23 revenue recognition requirements. IPSAS 47 was developed as a single source for revenue accounting guidance in the public sector. The issuance of IPSAS 47 is the culmination of eight years of consultation with stakeholders and in-depth standard-setting, including ensuring alignment to other IPSAS Standards. Therefore, adopting IPSAS 47 into the PBE suite of standards is expected to improve consistency in practice and lead to higher quality financial reporting by PBEs in New Zealand.
Whether the benefits of a potential development will outweigh the costs, considering as a minimum: **(i) *relevance to the PBE sector as a whole:* for example, where the potential development arises from the issue of a new or amended IFRS, whether the type and incidence of the affected transactions in the PBE sector are similar to the type and incidence of the transactions addressed in the change to the NZ IFRS;** **(ii) *relevance to the not-for-profit or public sector sub-sectors:* whether there are specific user needs in either of the sub-sectors, noting that IPSAS are developed to meet the needs of users of the financial reports of public sector entities;** **(iii) *coherence:* the impact on the entire suite of PBE Standards (e.g. can the change be adopted without destroying the coherence of the suite);** **(iv) *the impact on mixed groups*.**	The benefits of adopting IPSAS 47 into the PBE suite of standards outweigh the costs, for the following reasons: <u>Relevance to the PBE sector as a whole (and to the not-for-profit or public sector sub-sectors)</u> The requirements in IPSAS 47 would apply to any PBE (whether not-for-profit or public sector) that receives revenue with or without a binding arrangement. This type of transaction is therefore not restricted to any particular sub-set of the PBE sector. This revenue recognition approach for transactions with binding arrangements is based on IFRS 15 and has been adapted for the public sector. <u>Coherence</u> Since the PBE suite of standards is primarily based on IPSAS, adopting IPSAS 47 into the PBE suite of standards would be unlikely to weaken the coherence of the suite. Specifically, IPSAS 47 is aligned with IPSAS 48 *Transfer Expenses* with respect to the concept of a “binding arrangement”, which is fundamental to the accounting for both revenue and transfer expenses under IPSAS. Therefore, if IPSAS 48 is adopted into the PBE suite of standards (as recommended in Agenda Item 3C.1), doing the same with IPSAS 47 would enhance the coherence of the PBE suite of standards. However, if IPSAS 48 is <u>**not**</u> adopted into the PBE suite of standards (but IPSAS 47 is), then this would have the opposite effect on the coherence of the PBE suite of standards.

Factors in the Development Principle	Comment
	<u>Impact on mixed groups</u> IPSAS 47 is based on IFRS 15 Revenue principles and includes the five-step recognition model. Therefore, adopting IPSAS 47 would create alignment in recognition of revenue in mixed groups.
In the case of a potential development arising from the issue of a new or amended IFRS, the IPSASB's likely response to the change (e.g. whether the IPSASB is expected to develop an IPSAS on the topic in an acceptable time frame).	Not applicable.

27. The staff view, based on the analysis above, is weighted in favour of developing a PBE Standard using IPSAS 47 as a starting point.

Question for the Board

Q1. Does the Board AGREE to commence a project to develop a PBE Standard, using IPSAS 47 as the starting point?

Throughout the project, we will consider the extent of amendments required to ensure any new PBE Standard is fit-for-purpose for public sector and not-for-profit entities in New Zealand.

If the Board agrees to commence a project, we will bring a Project Plan to a future meeting.

Preliminary views on focus areas for the development of a new PBE Standard

28. Should the Board agree to commence a project on Revenue, using IPSAS 47 as the starting point, the next step is to develop a PBE Exposure Draft (ED) for public consultation.

29. As part of the process of developing this ED, we will need to determine whether there are any New Zealand-specific issues that should be considered and/or whether any areas of the revenue accounting in IPSAS 47 require more application guidance.

30. An informal public sector advisory group, which has recently been set up and will hold its first meeting on 23 June, will assist us with ensuring that a new PBE Standard on Revenue is fit-for-purpose in New Zealand. A verbal update on the first public sector advisory group meeting will be provided at this meeting. At this stage, we have sought feedback on the need for a standard on Revenue in New Zealand – i.e. what are the issues that arise in practice when applying the existing standards?

31. Appendix 2 sets out a summary of the issues identified by the XRB and New Zealand constituents during the public consultation on ED 70 *Revenue with Performance Obligations* and ED 71 *Revenue without Performance Obligations,* which was issued in February 2020. The IPSASB has addressed some of these issues through changes and clarifications made to IPSAS 47 in response to global feedback received from constituents.

32. We feel that IPSAS 47 is a significant improvement from the previous exposure drafts. The broad areas of focus during the potential development of a PBE ED on revenue using IPSAS 47 as its starting point will include:

    (a) improvements to support understandability and accessibility (we could consider structuring the standards in different ways);

    (b) consideration of whether the principles are too broad in places and require additional guidance to ensure consistent application; and

    (c) the need for additional guidance on specific types of transactions e.g. capital grants and multi-year funding arrangements.

    (d) specific public sector transactions such as tax revenues, tax receivables, and appropriations

Question for the Board
Q2. Has the Board identified any preliminary issues based on a first read of IPSAS 47?

Next steps

33. If the Board agrees to commence a project, a Project Plan to develop a draft ED (and accompanying Consultation Document) will be considered at a future meeting.

Attachments

Agenda item 3B.2: At-a-glance: IPSAS 47 *Revenue*

Agenda item 3B.3: IPSAS 47 *Revenue*

Appendix 1: Background to the IPSASB's Revenue Project

1. The primary objective of most public sector entities is to deliver goods and services to the public, which can only be achieved by maintaining appropriate levels of funding – i.e. revenue. As a result, information about an entity's sources of revenue and how revenue is accounted for is an area of high interest to users of general purpose financial reports.

2. IPSAS literature previously included two standards for exchange revenue transactions (IPSAS 9 *Revenue from Exchange Transactions* and IPSAS 11 *Construction Contracts*), and one standard for non-exchange revenue transactions (IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers*)).

3. The IPSASB's primary objectives for developing a new revenue standard were to consider the extent to which the new revenue recognition model in IFRS 15 *Revenue from Contracts with Customers* should be introduced into the public sector standards and to address concerns about the restrictive nature of IPSAS 23 revenue recognition requirements.

4. IPSASB initiated the Revenue project in 2015. The project timeline is shown below.

Consultation Paper — Revenue and Non-exchange Expenses

5. The IPSASB issued this Consultation paper (CP) in August 2017 to seek constituent preliminary views on the strategic direction for possible improvements to accounting for revenue and non-exchange expenses.

6. The CP considered the question of whether a revenue recognition approach based on performance obligations (as described by IFRS 15) would provide for better reporting outcomes than the current (at the time) exchange and non-exchange distinction – based on the information needs of users.

7. The CP also discussed implementation issues regarding the recognition of revenue from capital grants and services in-kind as well as initial and subsequent measurement of non-contractual receivables and non-contractual payables.

Exposure Draft 70 — Revenue with Performance Obligations & Exposure Draft — 71 Revenue without Performance Obligations

6. Based on constituents' feedback on the CP, the IPSASB developed ED 70 *Revenue with Performance Obligations* and ED 71 *Revenue without Performance Obligations*, which was issued in February 2020 together with ED 72 *Transfer Expenses*.

7. ED 70 proposed:

- definition of a <u>*performance obligation*</u> being a promise in a binding arrangement with a purchaser to transfer to the purchasing or third-party beneficiary either:
  - (a) a good or service (or a bundle of goods or services) that is distinct; or
  - (b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the purchaser or third-party beneficiary;
- elaboration on public sector-specific issues to encompass revenue transactions arising from binding arrangements rather than only transactions arising from legal contracts with further focus on enforceability;
- accounting for revenue with a performance obligation under the five-step revenue recognition model based on IFRS 15:
  - (a) identify the binding arrangement;
  - (b) identify the performance obligation;
  - (c) determine the transaction price;
  - (d) allocate the transaction price;
  - (e) recognise revenue at a point in time or over time.
- Revenue arising from binding arrangements with performance obligations is recognised when (or as) the entity satisfies a performance obligation by transferring control of a promised good or service to the resource recipient. Control is typically transferred over time or at a point in time, depending on the nature of the performance obligation.

8. ED 71 proposed:

- A definition of a <u>*present obligation,*</u> being a binding obligation resulting in an outflow of resources which an entity has little or no realistic alternative to avoid;
- Accounting for revenue without a performance obligation had six relevant decision points:
  - (a) is there an asset to be recognised?
  - (b) does the inflow result from a contribution from owners?
  - (c) does the transaction arise from a binding arrangement?
  - (d) are there performance obligations in the binding arrangement?
  - (e) are there present obligations in the binding arrangement?
  - (f) recognise revenue when (or as) present obligations are met.
- The ED also made proposals to update requirements from IPSAS 23 around capital transfers, services in kind, and transfers subject to appropriation.

Development of final IPSAS

9. The IPSASB considered constituents' feedback to ED 70 and ED 71. Issues noted by New Zealand constituents can be found in Appendix 2 of this memo. In response, the IPSASB decided to:

   (a) Present revenue guidance in a single Standard;

   (b) Clarify and refine the accounting principles and concepts to account for revenue transactions in the public sector; and

   (c) Provide non-authoritative guidance to help preparers use professional judgment in applying the accounting principles consistently.

10. IPSAS 47 was developed as a single source for revenue accounting guidance in the public sector. The key features of the new Standard are summarised below.

   - The Standard uses two accounting models and distinguishes between:
     - revenue from transactions with binding arrangements; and
     - revenue from transactions without binding arrangements.
   - The definition of a binding arrangement is underpinned by the principle of enforceability.

     A binding arrangement is an arrangement that confers both rights and obligations, enforceable through legal or equivalent means, on the parties to the arrangement.

     In the public sector, an arrangement is enforceable when each of the involved parties is able to enforce their respective rights and obligations through various mechanisms. An arrangement is enforceable if the agreement includes:

     (a) clearly specified rights and obligations for each involved party; and

     (b) remedies for non-completion by each involved party which can be enforced through the identified enforcement mechanisms.
   - Introduces the new concept of a 'compliance obligation'.

     A *compliance obligation* is an entity's promise in a binding arrangement to either use resources from the revenue transaction:
     - internally for acquiring distinct goods or services;
     - to transfer distinct goods or services to a purchaser;
     - or transfer distinct goods or services to third-party beneficiaries.

   Recognition of revenue from transactions without binding arrangements

   - Requires revenue arising from transactions without binding arrangements to be recognised:

     (a) When (or as) the entity satisfies any obligation associated with the inflow of resources that meets the definition of a liability (meaning the entity as a

result of the inflow has little or no realistic alternative to avoid an outflow of resources); or

(b) Immediately if the entity does not have an enforceable obligation associated with the inflow of resources.

- The IPSAS 23 restrictions and conditions approach, which only allowed for deferral of revenue recognition for non-exchange transactions when there was a "use or return condition" has been removed. Instead, the ability to defer revenue recognition is based on the existence of enforceable obligations, which is a much broader principle built around the Conceptual Framework definition of a liability.

Recognition of revenue from transactions with binding arrangements

- The revenue recognition approach for transactions with binding arrangements is based on IFRS 15 — including the five-step model that has been adapted for the public sector.
- Under this model, an entity is required to recognise revenue from transactions with binding arrangements as compliance obligations associated with the inflow of resources are satisfied. A liability (deferred revenue) is recognised for any unsatisfied compliance obligations in respect of the inflow of resources received from the revenue transaction.

Other

- The Standard includes other public sector specific guidance on capital transfers, and services in-kind.

Appendix 2: XRB and New Zealand constituents' comments on ED 70 and ED 71 and the IPSASB's response

The table below sets out a summary of the XRB and New Zealand constituents' comments on ED 70 *Revenue with performance obligations* and ED 71 *Revenue without performance obligations*, the IPSASB's response, and XRB staff comments. This analysis will be considered during the development of a PBE Standard based on IPSAS 47.

The IPSASB received 74 comment letters on ED 70 and 66 comment letters on ED 71 from its worldwide constituents, including the submission and from NZASB, New Zealand Treasury (TSY), Auckland Council (AC), Office of the Audit-General (OAG) and a joint submission from CPA Australia and CA ANZ (CPA/CAANZ on ED 70 and ED 71)

Topic	Issue	IPSASB response
Scope – Revenue standard interaction with IPSAS 19	We noted some conflicts between ED 70 paragraph 3(c), which excludes rights and obligations arising from binding arrangements within the scope of IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*, and the proposed amendment to IPSAS 19 paragraph 13(c) which states that IPSAS 19 applies to binding arrangements with purchasers that are, or have become, onerous. We agreed with the proposed amendments to IPSAS 19 paragraph 13(c) (which are equivalent to IAS 37 paragraph 5(g)), but not with the reference to IPSAS 19 in ED 70 paragraph 3(c). Further, we noted that ED 71 paragraph 3(h) says that ED 71 does not apply to rights or obligations arising from binding arrangements within the scope of IPSAS 19. It's not clear whether an entity that has revenue that falls within the scope of ED 71 cannot apply IPSAS 19 when considering whether it has a constructive obligation or whether such an entity should apply ED 71 first and then consider whether it has a constructive obligation under IPSAS 19. Similar questions might arise for an entity applying ED 71 to an arrangement that is not binding. **[NZASB], [OAG]** We recommended IPSAS clarifying whether the whole of IPSAS 19 is excluded or only parts of it and/or adding	The IPSASB kept the proposed amendment to IPSAS 19 paragraph 13(c) as well as the scope exclusion of rights and obligations arising from binding arrangements within the scope of IPSAS 19 (IPSAS 47 paragraph 3(g) – same as ED 70 paragraph 3(e)). IPSASB stressed that where a binding arrangement becomes onerous, an entity shall account for the expected deficit in accordance with IPSAS 19 (IPSAS 47 paragraph 79) further it added BC40 stating that: *BC 40 The IPSASB considered if IPSAS 47 should include explicit guidance for binding arrangements that become onerous and noted that IPSAS 19 Provisions, Contingent Liabilities and Contingent Assets, which was developed based on IAS 37, Provisions, Contingent Liabilities and Contingent Assets, applies to onerous contracts. While this guidance refers to "contracts", the IPSASB noted that IPSAS 19 would still be applicable for binding arrangements with compliance obligations that transfer goods or services to another party. Furthermore, binding arrangements with compliance obligations to use resources for goods or services internally would not meet the definition of an onerous contract because there is no exchange of assets or services. Therefore, the IPSASB concluded that the scope exclusion in paragraph 3 of IPSAS 47 and paragraph I(c) of IPSAS 19 are sufficient, and incorporated a specific reference to IPSAS 19 in paragraph 79.*

Topic	Issue	IPSASB response
	explanations when and why IPSAS 19 applies. **[OAG]**	*XRB staff note – consider whether the interaction between PBE IPSAS 19 and the Revenue standard is clearly defined to avoid inconsistent interpretation in New Zealand. This was a fairly narrow-scope technical issue.*
Application guidance	We suggested including in the application guidance of the Revenue standard paragraph F30 of the AASB 1058 *Income of non-for-profit entities* to avoid unnecessary discussions and undue costs over separately accounting for the immaterial components of a transaction *F30 Where the presumption is rebutted, the entity shall disaggregate the transaction price and account for the component that relates to the transfer of promised goods or services in accordance with this Standard. The remainder of the transaction price shall be accounted for in accordance with AASB 1058. Whether the element not related to the performance obligation is material, and therefore needs to be accounted for separately, shall be assessed in relation to the individual contract, without reassessment at an aggregate or portfolio level.* **[NZASB]** Appendix F to AASB 15 contains useful implementation guidance for not-for-profit entities. We believe this guidance would be helpful for the IPSASB to consider in developing application guidance on this matter as it includes guidance on assessing material components. **[CPA/CAANZ]**	This comment was raised in response to the proposed guidance in ED 71 around transactions with components with performance obligations and components without performance obligations (hybrid transactions). IPSASB removed this guidance when it decided to have a single concept for obligations arising from revenue transactions with binding arrangements ("compliance obligation"), along with the decision to present revenue guidance in a single IPSAS. IPSASB hasn't added any guidance about materiality when accounting for different components within a revenue transaction. *XRB staff note – consider whether additional guidance is required in New Zealand to assist entities in applying the materiality concept over different components of the revenue transaction.*
Alignment with IFRS 15 – definition of control of asset	We noticed differences between the wording of paragraphs ED 70.32 and IFRS 15.33. We recommended adding a definition of control of asset into ED 70. *ED 70.32. Goods and services are assets, even if only momentarily, when they are received and used (as in the case of many services). The economic benefits or service potential embodied in an asset are the*	IPSASB amended paragraph 90 to include the definition of control of asset as follow: *IPSAS 47.90 Goods and services are assets, even if only momentarily, when they are received and used (as in the case of many services).* ***Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Control includes the ability to prevent other entities from directing***

Topic	Issue	IPSASB response
	potential cash flows (inflows or savings in outflows), or the capacity to provide services that contribute to achieving the entity's objectives, that can be obtained directly or indirectly in many ways, such as by: … *IFRS 15.33 Goods and services are assets, even if only momentarily, when they are received and used (as in the case of many services).* ***Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset.** The benefits of an asset are the potential cash flows (inflows or savings in outflows) that can be obtained directly or indirectly in many ways, such as by: …*	***the use of, and obtaining the benefits from, an asset.** The benefits of an asset are the potential cash flows (inflows or savings in outflows) that can be obtained directly or indirectly in many ways, such as by: …* *XRB staff note – issued has been largely resolved*
General structure	We recommended that the IPSASB considers developing one Standard that addresses the proposals in both ED 70 and ED 71. **[CPA/CAANZ]**	The IPSASB decided to present revenue guidance in a single IPSAS. The IPSASB added paragraphs BC18 – BC19 explaining this decision.
General	Inconsistencies between ED 70 and ED 71 were noticed **[NZASB], [OAG]**	Those inconsistencies were resolved by the IPSASB's decision to present revenue guidance in a single IPSAS.
General	We have a general concern about the ability of preparers and auditors to understand and consistently apply the proposed requirements in ED 71. Both EDs are long and complex. **[NZASB], [OAG]**	*XRB staff note – this remains a significant concern. The decision to go with one Revenue Standard does result in a long and complex standard.* *Preparers and auditors will need help to understand the new terms used and the new revenue recognition models.*
Main principles - present obligation vs performance obligation	We anticipate that the distinction between present obligations (as detailed in ED 71) and performance obligations (as detailed in ED 70) as well as 'no obligations' under ED 71 may be difficult to apply in practice. **[CPA/CAANZ], [NZASB]** Furthermore, we found it confusing to have the same term,	The IPSASB noted that, while there are identifiable differences between present obligation and performance obligation, the underlying concept for those obligations are the same: both require the entity to use resources in a specified manner where enforceability of the binding arrangement from which the revenue arises is of significance. The IPSASB concluded that performance obligations are a subset of

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	“present obligation” in both ED 71 and IPSAS 19. The issues around our current understanding of liabilities are complicated further by the discussion in paragraphs 22-26 of ED 71 (“Enforceability of binding arrangements – substance over form”). Those paragraphs require subjective judgements that are difficult to apply in practice. Also, the “substance over form” discussion in those paragraphs appears to conflict with the Conceptual Framework (CF). ED 71 confuses legally binding obligations (CF paragraph 5.22) with non-legally binding obligations (CF paragraphs 5.23-5.26). We encouraged the IPSASB to expand the concept of “performance obligations” to include arrangements envisaged in ED 71. **[CPA/CAANZ]**	present obligations ED 71, and both represent the notion of an enforceable promise or requirement arising from a transaction with a binding arrangement, the IPSASB decided to adopt the new term “compliance obligation" to describe all obligations arising from revenue transactions with binding arrangements. This term and concept encompass performance obligations (as in ED 70 and aligned with IFRS 15) and present obligations (as in ED 71 and consistent with legally binding present obligations in the Conceptual Framework, also capturing revenues from public sector transactions that do not transfer distinct goods or services to an external party). The diagram in paragraph 8 illustrates those changes, and IPSAS 47 paragraphs BC20 – BC30 provide further details about this decision – including an explanation of the relationship between performance obligation (in IFRS 15), compliance obligation (in IPSAS 47), legal and non-legal binding obligation (in IPSASB Conceptual Framework): *IPSASB Conceptual Framework* Legally and Non-Legally Binding **Present Obligations** *IPSASB Conceptual Framework* Legally Binding (legal and equivalent means) **Present Obligations** *IFRS 15* Legally Binding (legal means) ***‘Performance Obligations’*** **Compliance Obligations** *DIAGRAM IS NOT TO SCALE*
Main principles - eligible expenditure and specified activities	We disagreed with the IPSASB’s conceptual analysis of why, in the absence of a performance obligation, an entity may have a liability in relation to obligations to carry out specified activities or incur eligible expenditure. We therefore disagreed with the IPSASB’s conclusion that, in the absence of a performance obligation, an entity’s obligations arising	Upon reflection, the IPSASB acknowledged that the intention was not that the specified activities or eligible expenditures in and of themselves give rise to a present [compliance] obligations, but that they are an entity's actions or spending to satisfy a specific promise it agreed to by willingly entering into a binding arrangement. Specified activities and eligible expenditures are examples of ways in which an entity may satisfy

Topic	Issue	IPSASB response
	from binding arrangements represent an outflow of resources as discussed in the Conceptual Framework. **[NZASB], [TSY]** We found guidance in ED 71 insufficient to lead to consistent application of the requirements. We envisaged preparers encountering significant implementation issues as they try to determine the line between enforceable eligible expenditure and specified activities that lead to present obligations (per the ED 71) and those that do not. **[NZASB], [CPA/CAANZ], [TSY], [AC]** As the distinction between specified activities and eligible expenditure does not affect the proposed accounting, we would prefer that the IPSASB did not make this distinction. **[NZASB], [CPA/CAANZ], [OAG]**	its obligations in a binding arrangement in accordance with the requirements in that binding arrangement, thereby informing the recognition of earned revenue. An entity should apply the guidance in IPSAS 47 paragraphs 98—104 of the accounting model for binding arrangements to determine which method is appropriate for measuring its progress towards complete satisfaction of its compliance obligation. The IPSASB also added Implementation Guidance to support the principles presented in the authoritative text.
Key principle – enforceability of obligation	We think there needs to be a clear principle and guidance about the cut-off point between revenue that can and cannot be deferred. The clearest way to do this might be to require that there be an enforceable obligation to spend the resources in the manner specified by the transfer provider, with that obligation being sufficiently specific to demonstrate that enforceability exists. **[NZASB]** We do not agree with paragraph 24 of ED 71 which states: *ED71 24 If past experience or knowledge indicates that the transfer provider never enforces an arrangement if a breach occurs, then the transfer recipient may conclude that the arrangement is not enforceable in substance.* **[CPA/CAANZ], [NZASB]** We believe a binding arrangement does not require a history of enforcement of similar agreements or even an intention of the customer to enforce rights. Enforceability depends solely on the customer's (transfer provider) capacity to	IPSAS accounting guidance mentions several mechanisms or factors that may indicate enforceability. The IPSASB debated whether the presence or absence of specific factors, such as past history of enforceability, demonstrates the enforceability of a binding arrangement. The IPSASB concluded that the impact of specific factors on the assessment of enforceability will be specific to each jurisdiction and the respective binding arrangement. In other words, the principle related to enforceability of a binding arrangement remains appropriate but the application of this principle in practice may vary depending on the relevant mechanisms available to the entity. The IPSASB also confirmed that the assessment of enforceability is based on the ability to enforce. This assessment is to be completed when the entity first enters into the arrangement and when a significant change in external or internal factors indicates that there may be a change in the enforceability of that binding arrangement (i.e., a change in the substance of the arrangement).

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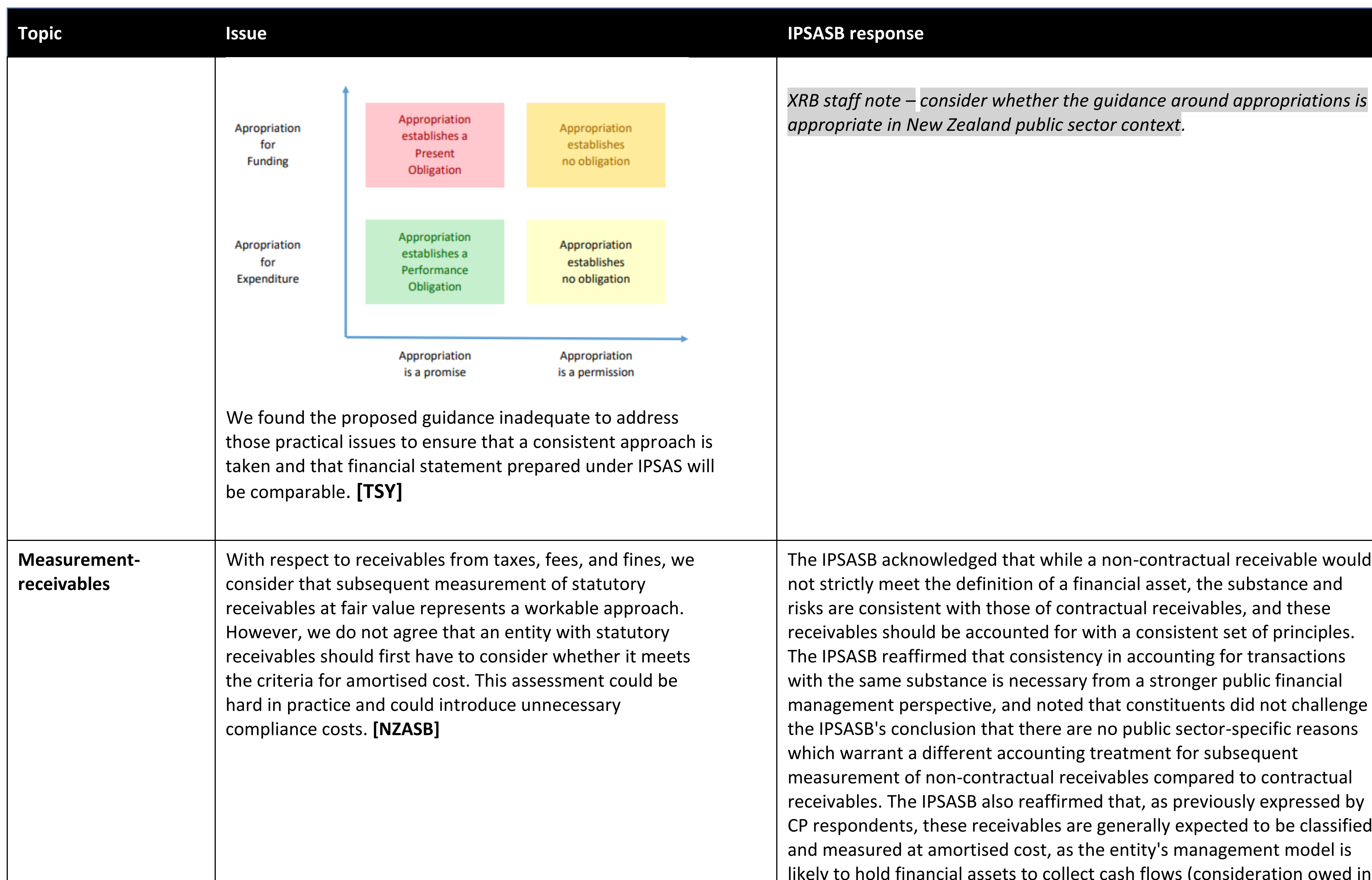
	enforce its rights. The Australian Accounting Standard AASB 15, paragraph F16 contains useful guidance to consider on this matter. **[CPA/CAANZ]** ED 71 refers in a few places to an entity repaying or returning resources to the transfer provider or incurring <u>some other form of penalty</u>. We find this wording insufficiently clear. **[NZASB]**	Based on these discussions, the IPSASB decided to revise guidance to emphasise that an entity should assess all relevant factors at the transaction date to determine whether the parties in the arrangement have the ability to enforce the rights and obligations in the arrangement. Judgment is required to determine which factors of enforceability are more demonstrative in the respective jurisdiction and binding arrangement. The IPSASB decided to provide additional authoritative guidance on the concept of enforceability in a binding arrangement which is supported by implementation guidance as well as illustrative examples. *XRB staff note – consider whether guidance around enforceability is fit for purpose in the New Zealand context.*
Main principles – existence of binding arrangement	We noted that ED 70 requires binding arrangement to be approved by parties of the binding arrangement. Where in the public sector binding arrangement can arise from a statutory mechanism - e.g. legislative or executive authority and/or cabinet or ministerial directives, where approval only from the party issuing legislative would be required. **[AC]**	The IPSASB removed the requirement for binding arrangement to be approved by parties of the binding arrangement. The IPSASB also confirmed that enforceability is an integral component of a binding arrangement. The IPSASB also clarified that enforceability can arise from various mechanisms, as long as the mechanism(s) provide(s) the entity with the ability to enforce the terms of the arrangement and hold the parties accountable for the satisfaction of their obligations, by imposing consequences on parties that do not satisfy their obligations.
Main principles – enforceability of appropriations	We noted that ED 71 states that even if an arrangement is specified as being subject to appropriations, the arrangement may still be considered binding if the transfer recipient can establish an enforceable right before the appropriation is authorised. We understand that appropriations can be understood in several different ways – e.g. it can be interpreted as a promise to the reporting entity or as a specification of the expenditure and it's upper limit.	The IPSASB noted that, in some jurisdictions, a revenue transaction might be made subject to authorisation of an appropriation. The IPSASB considered whether such a limitation should affect the recognition of revenue. The IPSASB concluded that the impact of such a limitation would depend on whether the limitation had substance. The IPSASB agreed that where the limitation has substance, the entity has no enforceable claim and should not recognise an asset prior to the appropriation being authorised. The IPSASB also agreed to add guidance on determining whether the limitation has substance.



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	We found the proposed guidance inadequate to address those practical issues to ensure that a consistent approach is taken and that financial statement prepared under IPSAS will be comparable. **[TSY]**	*XRB staff note – consider whether the guidance around appropriations is appropriate in New Zealand public sector context*.
Measurement-receivables	With respect to receivables from taxes, fees, and fines, we consider that subsequent measurement of statutory receivables at fair value represents a workable approach. However, we do not agree that an entity with statutory receivables should first have to consider whether it meets the criteria for amortised cost. This assessment could be hard in practice and could introduce unnecessary compliance costs. **[NZASB]**	The IPSASB acknowledged that while a non-contractual receivable would not strictly meet the definition of a financial asset, the substance and risks are consistent with those of contractual receivables, and these receivables should be accounted for with a consistent set of principles. The IPSASB reaffirmed that consistency in accounting for transactions with the same substance is necessary from a stronger public financial management perspective, and noted that constituents did not challenge the IPSASB's conclusion that there are no public sector-specific reasons which warrant a different accounting treatment for subsequent measurement of non-contractual receivables compared to contractual receivables. The IPSASB also reaffirmed that, as previously expressed by CP respondents, these receivables are generally expected to be classified and measured at amortised cost, as the entity's management model is likely to hold financial assets to collect cash flows (consideration owed in

Topic	Issue	IPSASB response
		the revenue arrangement) and not to sell financial assets, and the cash flows are solely payments of the principal and any interest outstanding. The IPSASB made only slight modification to the proposed requirements: ED 71 par 84(b) *After initial recognition, an entity shall subsequently measure:* *(a) A receivable asset:* *(i) …* *(ii) Not within the scope of IPSAS 41 on* ***the same basis as a financial asset at amortized cost in accordance with IPSAS 41, by analogy****.* IPSAS 47 par 31 *After initial recognition, an entity shall subsequently measure:* *(a) A receivable asset:* *(i) …* *(ii) Not within the scope of IPSAS 41 on the* ***same basis as a financial asset in accordance with IPSAS 41, by analogy****.* IPSASB also added Implementation Guidance to support the principles presented in the authoritative text, and address constituent comments and clarify how IPSAS 41 principles can be applied by analogy to subsequently measure non-contractual receivables.
Measurement-receivables	We were concerned about the application of impairment requirements in IPSAS 41 on public sector receivables – especially on statutory receivables which are levied without consideration of credit risk and which are not managed using credit risk in the way that IPSAS 41 envisages. **[NZASB], [TSY]** We suggested that if the IPSASB keeps amortised cost as an option for subsequent measurement of statutory receivables, more guidance would be needed to help entities understand how to apply the requirements to statutory receivables, particularly around the application of the complex three-stage expected credit loss model. Another option would be to require the use of the 'simplified	The IPSASB acknowledged that the availability of certain information may pose some difficulties in applying amortized cost which may not be sufficiently eased by the use of the simplified approach for receivables in paragraphs 87-89 of IPSAS 41. However, non-contractual receivables, by nature of the revenue arrangements from which they arise, are typically held to collect expected cash flows related to the revenue transaction (rather than to sell and trade), and have shorter maturity periods, similar to short-term receivables, and the required estimates would not span a long uncertain time period. Consideration of the time value of money and expected

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	approach for receivables' in IPSAS 41 for statutory receivables. **[NZASB], [TSY]**	credit losses are necessary to appropriately reflect the economic substance of both contractual and non-contractual receivables. The IPSASB concluded that another simplified approach or practical expedient would not be appropriate, as an inconsistent application of accounting principles for transactions of the same substance and risks would not reflect the economic substance of these transactions.
Application guidance – multi-year grants	We noted that the exposure drafts do not include any application guidance on how to account for multi-year grants/funding that are received, despite those are common in the public sector. We recommended IPSASB to provide application guidance on when assets and revenue should be recognised in transactions that involve multi-year grants/funding, long-term contracts and where funding is based on time periods. We also suggested inclusion of illustrative examples for multi-year grants, including where there is a mismatch of the balance date(s) to the funding. [**OAG]**	IPSASB added Implementation Guidance (IG) highlighting that the accounting principles do not differ for multi-year grants/long-term contracts. An entity will still need to consider whether the arrangement is a binding arrangement, and then apply the appropriate accounting model. The additional "complexity" that comes from multi-year arrangements lies in the timing differences between when funding is received (resources provided by the resource provider) and whether that funding can be recorded as revenue immediately. The accounting principles in each model address this, by prompting the entity to consider whether the inflow (or right to an inflow) of resources meets the definition of an asset, and if there is an associated enforceable obligation that meets the definition of a liability (which would defer revenue recognition). *XRB staff note – consider whether additional guidance for multi-year funding is needed in New Zealand context*
Application guidance – capital transfers	We found guidance regarding capital transfers insufficient and we encouraged IPSASB to: - clarify whether capital transfers should be recognised over the construction period of the underlying asset, or over both the construction period and the period over which the asset is utilised to fulfil the conditions of the binding arrangement; - clarify the definition of capital transfers with respect to whether such transfers should relate to specific assets (e.g. a building) or capital assets in general (e.g. roads)	After several deliberations the IPSASB defined capital transfers as an inflow of cash or another asset that arises from a binding arrangement with a specification that the entity acquires or constructs a non-financial asset that will be controlled by the entity. The IPSASB concluded that the accounting principles in the binding arrangement model are appropriate for capital grants (resp. capital transfers) and that revenue should be recognised as the compliance obligation to acquire or construct the non-financial asset is satisfied. The IPSASB considered that some capital transfers may include multiple compliance obligations, one being the acquisition or construction of a

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	further develop guidance on how to account for capital transfers **[CPA/CAANZ]**	capital asset and another being the operation of the capital asset in a particular way for a specified period of time. In these circumstances, the IPSASB decided that the accounting for each compliance obligation should be considered separately in accordance with the nature of each obligation. The IPSASB also revised and enhanced the Illustrative Examples to help illustrate the application of the accounting principles, using general fact patterns prevalent globally among public sector entities. *XRB staff note – the new Illustrative Example around capital transfers use scenarios in which all funding is provided upfront. In New Zealand it is more common to provide funding in tranches after milestones are achieved and audited – consider whether the guidance is sufficient to ensure consistent application of capital transfer requirements in New Zealand.*
Allocation of the transaction price between different obligations	We found the guidance around allocation of the transaction price between different obligations complex and hard to apply in practice. **[CPA/CAANZ], [NZASB], [TSY], [AC]** We referred back to our criticism of concept of "performance obligations" and "present obligation", and "eligible expenditure" vs "specified activities". **[CPA/CAANZ], [NZASB], [TSY]** We were also concerned about inconsistent application of the allocation method in practice. **[AC]** Very often in the public sector, there is no reference in the market to determine the transaction price of specific service. We suggest that further guidance is included on how preparers can determine the transaction price of the service component for the price allocation method. **[AC]**	The guidance around allocation of the transaction price between different obligations remained largely consistent with the ED proposals. The IPSASB just added Implementation Guidance around Allocation Based on Stand-Alone Values and Illustrative Example 35-Provision of Vaccines to Third-Party Beneficiary *XRB staff note – consider sufficiency of the guidance in light of the new concepts of "constructive obligation" and simplified model based on existence/non-existence of a binding arrangement*
Disclosures	We found the disclosure requirements in ED 71 excessive and we questioned whether sufficient consideration has been given to the disclosure requirements in ED 71 in light of	The IPSASB acknowledged feedback from respondents about the volume of disclosures in the two EDs and decided to take a principle-based approach in reassessing disclosure requirements, focusing on the nature

Topic	Issue	IPSASB response
	the scope of the standard and user information needs. We also highlighted concerns about the structure of the disclosure requirements as we found it hard to identify which disclosures relate to revenue with/without present obligations and which are general requirements. **[all respondents]** Further, we encouraged IPSASB to include the rationale for the disclosure requirements in the Basis for Conclusions. **[NZASB], [CPA/CAANZ]**	of the transactions and their risks. With this approach in mind, the IPSASB noted that its decisions since the issuance of ED 70 and ED 71, in particular to present revenue guidance in a single standard with a revised order, partially address constituent comments as the overall volume of disclosures has been reduced and has resulted in a more succinct and clear set of disclosures. IPSASB explained its rationale for the disclosure requirements in BC109-BC117. *XRB staff note – consider whether disclosure requirements are appropriate in the New Zealand context noting that IPSASB stressed that an entity may be required to apply all the disclosure requirements if they are relevant for specific transactions, but is not required to apply the disclosure requirements that are not relevant (BC115). NZASB should also consider RDR concessions for Tier 2 entities.*
Compulsory contributions and levies	We expressed concern that the guidance in ED 71 is insufficient to lead to the consistent classification of transactions as taxes or other compulsory contributions and levies and could lead to unhelpful debates about classification. Given that the IPSASB is effectively treating compulsory contributions and levies as taxes, we suggested ED 71 would be clearer if compulsory contributions and levies (i) were not a defined term and (ii) were explicitly included in the definition of taxes. This would lead to the proposed disclosures for taxes and compulsory contributions and levies in paragraph 131(a)(i) and (ii) being combined. Further we disagreed with IPSASB's view that all compulsory contributions and levies can be classified as a subset of taxes. As those vary in nature and some, such as development contributions which are levied by a council on a developer, may be refundable if a council does not complete land development works within a certain period. We noted that IPSAS 23 (paragraph 63) allowed for the	IPSASB hasn't reflected the recommendation to combine taxes and other compulsory contributions and levies and kept the following requirements: IPSAS 47 par 7 *Taxes, which include compulsory contributions and levies, are …* IPSAS 47 par 169 *An entity shall disclose either on the face of, or in the notes to, the general purpose financial statements:* *(a) The amount of revenue from transactions recognized during the period, showing separately, and by major classes:* *(i) Taxes;* *(ii) Other compulsory contributions and levies; …* IPSAS 47 par 41 *Taxes are a transaction without performance obligations because the taxpayer transfers resources to the government, and the government is not required to transfer distinct goods or services to the taxpayer or a third-party beneficiary in return. While the taxpayer may benefit from a range of social policies established by the government, the taxpayer has no control over which benefits they receive as a result of the payment of taxes.*

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	recognition of liabilities for compulsory contributions and levies whereas ED 71 (paragraph 93) stated that taxes do not give rise to performance obligations and paragraph 29 stated that taxes do not create binding arrangements. **[NZASB]**	
Term 'transfer recipient'	We found it confusing for readers (especially in the disclosure section) if the term 'transfers' excludes taxes, but the term 'transfer recipients' includes recipients of taxes.	IPSASB reflected this comment and replaces the term 'transfer recipients' with the general term "entity".
Term 'Promise'	ED 70 used term "goods or services that an entity promises to transfer …". We found the term "promises" difficult to interpret in the public sector as is often compelled to commit to performance obligations by virtue of binding arrangements. We suggest using a term "commits". **[CPA/CAANZ]**	The IPSASB hasn't reflected this comment and IPSAS 47 paragraph 71 says: "*A binding arrangement generally explicitly states the goods or services that an entity promises to either obtain for use internally or transfer to a purchaser or third-party beneficiary. …*" *XRB staff note – consider whether the terminology used can be confusing or misleading.*
Terminology - "operator" and "grantor"	Given the comprehensive guidance on principal versus agent considerations in ED 70, we suggested it may be helpful to clarify whether this relationship includes or excludes service concession arrangements, i.e. "operator" and "grantor" relationships that fall under IPSAS 32 *Service Concession Arrangements: Grantor*. We also suggested considering clarifying the differences between the two sets of terms, i.e. whether grantor/operator arrangements are limited to service concession arrangements**. [CPA/CAANZ]**	The IPSASB hasn't reflected this recommendation in the final standard IPSAS 47. Considering that Scope of IPSAS 47 clearly excludes rights or obligations arising from binding arrangements within the scope of IPSAS 32 we found this approach reasonable. *XRB staff note – considering that the Scope of IPSAS 47 clearly excludes rights or obligations arising from binding arrangements within the scope of IPSAS 32 we found this approach reasonable*
Revenue with high collection uncertainty	ED 71 paragraph 101 establishes requirements for the measurement of tax revenue with high collection uncertainty while referencing other paragraphs of ED 71. We found this reference confusing and recommended establishing separate requirements in paragraph 101. **[NZASB]**	IPSASB reflected this recommendation and extended the requirements in IPSAS 47 paragraph 49 (equivalent to ED 71.101) by IPSAS 47 paragraph 50.

IPSAS 47, *Revenue*

This summary provides an overview of IPSAS 47, *Revenue*.

Project Objective: To develop a new Standard that sets out the accounting requirements for revenue transactions in the public sector. This IPSAS replaces IPSAS 9, *Revenue from Exchange Transactions*, IPSAS 11, *Construction Contracts*, and IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*.

Approved: The International Public Sector Accounting Standards Board® (IPSASB®) approved IPSAS 47, *Revenue* in March 2023. It was issued in May 2023.

Project History: The IPSASB initiated the Revenue project in 2015.

In February 2020, the IPSASB issued Exposure Draft (ED) 70, *Revenue with Performance Obligations* and ED 71, *Revenue without Performance Obligations* which proposed different accounting guidance based on whether the revenue transaction has a performance obligation.

In developing IPSAS 47, the IPSASB considered constituents' feedback to ED 70 and ED 71. The IPSASB decided to:

(a) Present revenue guidance in a single Standard;

(b) Clarify and refine the accounting principles and concepts to account for revenue transactions in the public sector; and

(c) Provide non-authoritative guidance to help preparers use professional judgment in applying the accounting principles consistently.

This At a Glance publication has been prepared by staff of the IPSASB for information purposes only. It does not form part of the standards or other authoritative publications of the IPSASB. It has not been reviewed, approved or otherwise acted upon by the IPSASB.

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Project Overview

The purpose of the Revenue project was to develop a new Revenue Standard that provides recognition and measurement requirements for public sector revenue transactions, and addresses application issues with the existing suite of revenue IPSAS.

Why the IPSASB Undertook this Project

The primary objective of most public sector entities is to deliver goods or services to the public. As a result, a large volume of transactions in the public sector relate to revenue.

IPSAS literature previously included two Standards for exchange revenue transactions (IPSAS 9, *Revenue from Exchange Transactions* and IPSAS 11, *Construction Contracts*), and one Standard for non-exchange revenue transactions (IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*). These Standards were issued prior to the IPSASB's 2014 *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (the Conceptual Framework).

IPSAS 47, *Revenue* is the result of the IPSASB's work to:

- Review and update IPSAS 23, as necessary, for consistency with the current Conceptual Framework and to address application issues with the existing IPSAS; and
- Consider the accounting approach in IFRS 15, *Revenue from Contracts with Customers*, issued by the International Accounting Standards Board (IASB) in 2014. IFRS 15 replaced International Accounting Standard (IAS) 18, *Revenue*, and IAS 11, *Construction Contracts*, and related interpretations, which provided the IPSASB an opportunity to evaluate the existing principles in IPSAS 9 and IPSAS 11 (drawn primarily from IAS 18 and IAS 11, respectively).

Benefits of IPSAS 47

IPSAS 47 is a single source for revenue accounting guidance in the public sector. The enhancements introduced by this IPSAS have the following benefits:

(a) Addressed application issues in the legacy revenue IPSAS, and confirmed consistency with the concepts in the Conceptual Framework;

(b) Increased transparency related to the substance of an entity's revenue transactions by introducing a more robust and objective approach to the recognition and measurement of revenue; and

(c) Enhanced disclosure requirements to provide more useful information to users.

Two Accounting Models

IPSAS 47 presents two accounting models, based on the existence of a binding arrangement.

IPSAS 47 includes comprehensive guidance for an entity to determine which accounting model to apply.

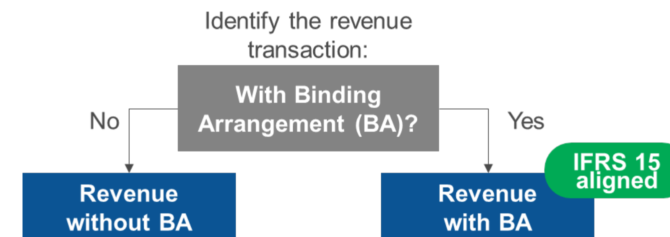
IPSAS 47 first requires an entity to determine whether its revenue arises from a transaction with a binding arrangement, to determine the appropriate accounting model. The principles within the models enable an entity to reflect the substance of its revenue transaction. The Standard provides additional guidance to support entities in accounting for public sector specificities.

The Binding Arrangement Concept

The concept of a binding arrangement is prevalent throughout IPSAS literature and is fundamental for revenue accounting in the public sector.

A binding arrangement is an arrangement that confers both rights and obligations, enforceable through legal or equivalent means, on the parties to the arrangement. As such, an entity must have at least an enforceable right and an enforceable obligation. For example, in a two-party binding arrangement:

Component	Party A	Party B
Enforceable Right	✓	✓
Enforceable Obligation	✓	✓



Enforceability

Enforceability underpins the definition of a binding arrangement. An entity uses judgment to consider all relevant factors in their jurisdiction and the specific transaction to assess whether enforceability exists in its arrangement. Enforceability can:

- Arise from various mechanisms (i.e., "what"), to hold the parties accountable to fulfilling each of their respective obligations by compelling them to fulfill their obligations or face imposed consequences (i.e., "how"); and
- Be through legal or equivalent means in the public sector. Equivalent means (which include executive authority, and cabinet or ministerial directives) captures enforcement outside the judicial system that is similar to the force of law.

Revenue from Transactions without Binding Arrangements

The accounting model for revenue without binding arrangements requires an entity to consider whether any of its rights or its obligations in the revenue transactions are enforceable, and meet the definitions of an asset or liability, respectively.

Core Principles

A significant volume of revenue transactions in the public sector are expected to be without binding arrangements, such as taxes.

In a transaction without binding arrangements, the entity does not have both an enforceable right and an enforceable obligation, but may have an:

- Unenforceable right, and unenforceable obligation – e.g., a donation, where an entity (aid organization) is not able to enforce payment from a resource provider (donor), and is not required to use the donation in a specific way;
- Enforceable right, but unenforceable obligation – e.g., income taxes, where an entity (national government) is able to enforce payment from a taxpayer, but is not required to use the tax revenue to provide specific services to the taxpayer; or
- Unenforceable right, but enforceable obligation – e.g., an education grant, where an entity (university) is not able to enforce payment from the resource provider (national government), but is required to provide the grant to students that meet predetermined eligibility criteria.

An entity determines whether any of its rights in the arrangement meet the definition and recognition criteria of an asset, and whether any of its obligations meet the definition and recognition criteria of a liability.

The existence of a liability associated with the inflow or right to an inflow of resources impact the timing of revenue recognition.

This accounting model is consistent with the core principles presented in IPSAS 23, and addresses issues raised by constituents in the application of the existing Standard for non-exchange revenues.

Recognition

An entity shall recognize revenue from a transaction without a binding arrangement:

- When (or as) the entity satisfies any enforceable obligations associated with the inflow (or right to inflow) of resources that met the definition of a liability; or
- Immediately if the entity does not have an enforceable obligation associated with the inflow (or right to inflow) of resources.

Measurement

Revenue is measured at the amount of the increase in the entity's net assets (e.g., the consideration received or receivable).

Revenue from Transactions with Binding Arrangements – Adapting IFRS 15

The accounting model for revenue with binding arrangements is primarily aligned with IFRS 15, but has been adapted and expanded for operability in the public sector.

Public Sector Considerations

While aligned in principles, the accounting model for revenue with binding arrangements in IPSAS 47 broadens the approach in IFRS 15 to address public sector transactions. Two key aspects adapted for the public sector are binding arrangements and compliance obligations.

A binding arrangement in IPSAS 47 is broader than a 'contract' in IFRS 15, to allow for jurisdictions where government and public sector entities cannot enter into legal contracts (with enforceability through legal means) but do enter into arrangements that are in substance the same as contracts (with enforceability through equivalent means).

In addition, IPSAS 47 acknowledges that public sector transactions often involve third-party beneficiaries, which can be an entity, individual or household, receiving those goods or services.

A compliance obligation is an entity's promise in a binding arrangement to either use resources internally for distinct goods or services or transfer distinct goods or services to a purchaser or third-party beneficiary. A 'compliance obligation' in IPSAS 47 is broader than a 'performance obligation' in IFRS 15. While both are units of account for the recognition and measurement of revenue, compliance obligations also include any:

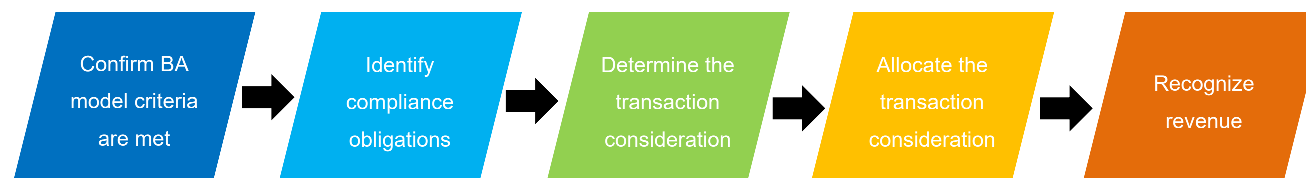
- Present obligations that are legally binding through equivalent means;
- Requirements for the entity to use resources internally for distinct goods or services; and
- Requirements to transfer distinct goods and services to a party other than the resource provider, such as to a third-party beneficiary.

	IPSAS 47 **Compliance Obligation**	*IFRS 15* **Performance Obligation**
Legally binding through…	Legal **and equivalent** means	Legal means
Recipient of distinct good / service is…	**The entity**, purchaser (i.e., resource provider)**, or third-party beneficiary**	The customer (equivalent of resource provider)

IPSASB®

Revenue from Transactions with Binding Arrangements – The Model

Identification of the compliance obligations in the binding arrangement is integral to the correct application of the accounting model for revenue with binding arrangements.



Recognition

An entity's binding arrangement must meet specific criteria to apply the binding arrangement accounting model: the approval and commitment by the parties to the respective obligations, identification of each party's rights and payment terms, economic substance, and probable collection of the entitled consideration.

At the inception of the binding arrangement, the entity must identify all compliance obligations in the binding arrangement. A binding arrangement has at least one compliance obligation.

Revenue is recognized at the amount allocated to a compliance obligation when (or as) the entity satisfies that compliance obligation. An entity shall determine the appropriate method to measure progress towards complete satisfaction of the compliance obligation.

IPSAS 47 also requires an entity to consider whether it shall recognize any right or obligation that meet definition of an asset or liability, respectively, and any costs of obtaining or fulfilling the binding arrangement.

Measurement

An entity measures revenue by determining the transaction consideration, which is the amount of resources to which an entity expects to be entitled for satisfying a compliance obligation. Determining the transaction consideration may be complex because of certain factors, such as variable consideration, the existence of a significant financing component, non-cash consideration, and consideration payable to a resource provider.

The total transaction consideration is allocated to each individual compliance obligation identified in the binding arrangement, typically based on their relative stand-alone values. The stand-alone value is the price of a good or service that is required to be used internally or provided separately to a purchaser or third-party.

IPSAS 47 also provides measurement principles for any assets and liabilities in the revenue transaction.

Other Public Sector Considerations

IPSAS 47 includes guidance to help entities apply the revenue accounting principles to specific types of transactions that are prevalent in the public sector.

Additional Supporting Guidance

IPSAS 47 includes a substantial amount of additional guidance to support understanding and application of the principles. This includes new implementation guidance and detailed basis for conclusions, as well as a robust set of illustrative examples. In particular, the illustrative examples adapt examples from IFRS 15, using general fact patterns prevalent globally amongst public sector entities, to illustrate the application of the accounting principles to transactions that are both relevant and prevalent in the public sector.

Services In-Kind

IPSAS 47 permits, but does not require, entities to recognize services in-kind.

If recognized, entities are required to disclose qualitative and quantitative information about those services in-kind. If not recognized, entities are encouraged to disclose the qualitative information about the nature and types of services in-kind received, particularly if those services in-kind received are integral to the operations of the entity.

Compelled Transactions

In the public sector, there may be circumstances where an entity is compelled to satisfy a compliance obligation regardless of the resource provider's ability or intention to pay. IPSAS 47 includes additional guidance to help constituents with the recognition, measurement and disclosure of these transactions.

Capital Transfers

Capital transfers are an important aspect of the public sector. A **capital transfer** is defined as an inflow of cash or another asset that arises from a binding arrangement with a specification that the entity acquires or constructs a non-financial asset that will be controlled by the entity.

Since capital transfers arise from binding arrangements, an entity shall apply the binding arrangement accounting model to recognize and measure its revenue from the transaction. IPSAS 47 provides application guidance, implementation guidance, and illustrative examples to support entities in identifying and accounting for capital transfers.

Effective Date and Project History

The effective date of IPSAS 47 is January 1, 2026.

Effective Date

The effective date of IPSAS 47 is January 1, 2026, with earlier application permitted.

The IPSASB selected this effective date because:

(a) It allows public sector entities sufficient time to apply IPSAS 47, after applying other major pronouncements recently issued;

(b) It strikes the balance from a public interest perspective, as the adoption of IPSAS 47 will address existing issues and challenges with the existing suite of revenue IPSAS; and

(c) It allows public sector entities time to identify the impacts of and to prepare for the implementation of IPSAS 47.

Project History

To learn more about the project history, and to view the consultation documents and responses, please visit:

https://www.ipsasb.org/consultations-projects/revenue

EXRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Memorandum

Date:	16 June 2023
To:	NZASB Members
From:	Carly Berry
Subject:	**Application of the PBE Policy Approach to IPSAS 48 *Transfer Expenses***

COVER SHEET

Project priority and complexity

Project priority	**High*** **If the Board decides to commence a project to develop a PBE Standard on transfer expenses.*
Complexity of Board decision-making at this meeting	**High** The Board is required to apply the PBE Policy Approach to IPSAS 48 *Transfer Expenses*. There is a degree of judgement involved in the application of the PBE Policy Approach – and reaching a view on whether to commence a PBE project based on the recently issued IPSAS. We believe that introducing a new PBE Standard on Transfer Expenses in New Zealand will ultimately lead to improved financial reporting. However, we need to manage the introduction of any new standard carefully to ensure the cost of implementation does not exceed the benefits – this requires a focus on developing a PBE Standard with clear, understandable principles and requirements and ensuring users can easily navigate between the core requirements and additional guidance material.

Overview of agenda item

Project status	This project has not yet commenced. Applying the PBE Policy Approach to IPSAS 48 at this meeting is the first step and will determine subsequent steps.
Project purpose	If we commence a project, the objective will be to develop a PBE Standard using IPSAS 48 as a starting point, while also ensuring that the new PBE Standard is fit-for-purpose in New Zealand.
Board action required at this meeting	• NOTE the recent issue of IPSAS 48 • APPLY the PBE Policy Approach to IPSAS 48 • AGREE to commence a project to develop a PBE Standard, using IPSAS 48 as a starting point • PROVIDE FEEDBACK on staff's preliminary views on the focus areas for development of the new PBE Standard.

Introduction[1]

1. The International Public Sector Accounting Standards Board (IPSASB) approved IPSAS 48 *Transfer Expenses* at its March 2023 meeting. IPSAS 48 was published on 26 May 2023.

2. IPSAS 48 defines a transfer expense as:

   An expense arising from a transaction, other than taxes, in which an entity provides a good, service or other asset to another entity (which may be an individual) without directly receiving any good, service or other asset in return.

   Examples of transfer expenses included donations and grants from a transfer provider perspective, either involving the transfer of cash or other assets.

3. IPSAS 48 fills a significant gap in the IPSASB's literature – previously there was no explicit guidance on transfer expenses in IPSAS.

4. In accordance with the *Policy Approach to Developing the Suite of PBE Standards* (PBE Policy Approach), the Board is required to consider if and when to incorporate IPSAS 48 into the suite of PBE Standards as issued by the XRB. The content of this memo therefore includes the application of the PBE Policy Approach to IPSAS 48.

Recommendation

5. We recommend that the Board:

   (a) NOTES that the IPSASB recently issued IPSAS 48 *Transfer Expenses*;

   (b) APPLIES the PBE Policy Approach and AGREES to commence a project to develop a PBE Standard, using IPSAS 48 as a starting point; and

   (c) PROVIDES FEEDBACK on staff's preliminary views on the focus areas for development of the new PBE Standard.

Structure of this memo

6. This memo has the following sections.

   (a) Summary of the transfer expense recognition principle in IPSAS 48

   (b) Application of the PBE Policy Approach

   (c) Preliminary views on focus areas for the development of a new PBE Standard

   (d) Next steps

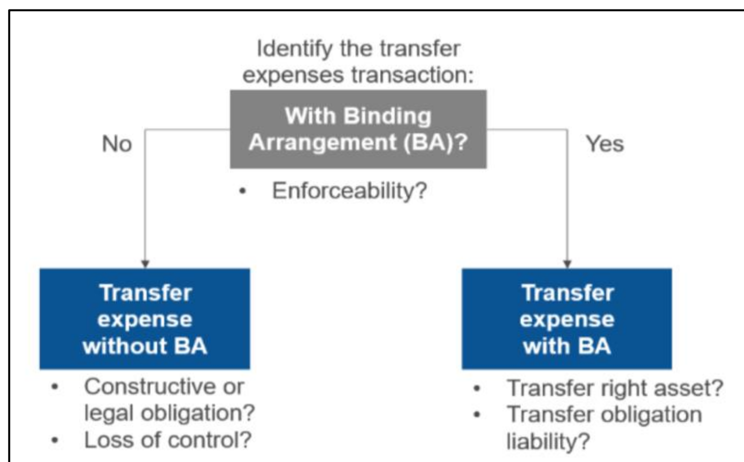
   (e) Appendix 1: Background to the IPSASB's Transfer Expenses project

   (f) Appendix 2: XRB and New Zealand constituents' comments on ED 72 *Transfer Expenses*, and the IPSASB's response

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

Summary of the transfer expense recognition principle in IPSAS 48

7. The diagram below sets out the core principles underpinning IPSAS 48.



At A Glance – Transfer Expenses

Binding arrangement

8. A reporting entity (transfer provider) is first required to consider whether the transfer expense transaction arises from a binding arrangement or not.

9. A binding arrangement is an arrangement that confers both enforceable rights and obligations on the parties to the arrangement. A contract is a type of binding arrangement. Each party in the binding arrangement willingly enters into the arrangement and is able to enforce their respective rights and obligations conferred on them in the arrangement.

10. For an arrangement to be binding, it must be enforceable through legal or equivalent means. Enforceability can arise from various mechanisms, so long as the mechanism provides the entity with the ability to enforce the terms of the binding arrangement and holds the parties accountable to the satisfaction of stated obligations. The minimum two-way enforceability in a binding arrangement is illustrated in the diagram below.

IPSAS 48.AG27

Transfer Expenses from transactions not arising from a binding arrangement

8. Where the transfer expense transaction does not arise from a binding arrangement (i.e., the transfer provider does not have both an enforceable right and an enforceable obligation), the transfer provider is required to recognise an expense as follows:

(a) At the point when a constructive obligation or legal obligation to transfer resources arises and results in the recognition of a provision in accordance with paragraph 22[2] of IPSAS 19 *Provisions, Contingent Liabilities, and Contingent Assets;* or

(b) When the transfer provider ceases to control the resources; this will usually be the date at which it transfers the resources to the transfer recipient.

9. In general, a transfer expense transaction arising from a non-binding arrangement will be recognised immediately when the transfer provider loses control of the resources transferred.

Transfer Expenses from transactions arising from a binding arrangement

10. Where the transfer expense transaction does arise from a binding arrangement, the accounting for transfer expenses is driven by the enforceable rights and enforceable obligations in the binding arrangement, and whether the transfer provider or the transfer recipient has fulfilled its respective obligations. In general, a transfer expense arising from a binding arrangement will be recognised as the transfer recipient satisfies the enforceable obligations arising from entering the binding arrangement.

11. A transfer expense transaction arising from a binding arrangement may be able to be recognised over time as the transfer recipient satisfies the agreed obligations – in these circumstances, when the transfer provider loses control of its resources (usually when cash is transferred), a *transfer right asset* may be recognised (akin to a prepayment) instead of an expense.

12. When determining whether a transfer right asset can be recognised for resources transferred to an individual or other entity (i.e., to defer expenditure recognition) — the transfer provider is required to consider if it can reliably estimate the transfer recipient's progress towards satisfying its obligations in the binding arrangement. If the entity cannot reliably estimate the transfer recipient's progress, the resources transferred are required to be expensed immediately. To defer expenditure recognition, the resource provider must have a way of reliably measuring the transfer recipient's satisfaction of the agreed obligations.

13. We have received feedback that the principle above will be a high hurdle for many New Zealand public sector entities to reach, which will result in many cases where transfer expenses are recognised immediately even when they are considered to arise from a binding arrangement.

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[2] A provision shall be recognised when:

(a) an entity has a present obligation (legal or constructive) as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision shall be recognised.

Further background information on IPSAS 48

14. Agenda paper 3C.2 contains a "snapshot" of IPSAS 48. The full Standard can be found at agenda paper 3C.6 (in supporting papers).

15. Appendix 1 to this memo includes some background information on the IPSASB's Transfer Expenses project.

Application of the PBE Policy Approach

16. Shortly after its publication, the Board will typically consider whether a new or amending IPSAS should be adopted into PBE Standards. These decisions are guided by the PBE Policy Approach.

17. The PBE Policy Approach identifies triggers for changes to PBE Standards. One of these triggers is the IPSASB issuing a new IPSAS. Section 4.1 (paragraphs 22–24) of the PBE Policy Approach establishes a rebuttable presumption that the NZASB will adopt a new or amended IPSAS. The PBE Policy Approach states that it is expected that the adoption of a new or amended IPSAS will lead to higher quality financial reporting by public benefit entities (PBEs) in New Zealand and the factors in the development principle are presumed to be met.

18. **Table 1** on the next page considers the factors in the development principle, as provided for in the PBE Policy Approach, as they apply to IPSAS 48.

Table 1: Factors in the Development Principle

Factors in the Development Principle	Comment
Whether the potential development will lead to higher quality financial reporting by public sector PBEs and not-for-profit entities, including public sector PBE groups and not-for-profit groups, than would be the case if the development was not made.	Until the publication of IPSAS 48, there was no specific guidance on transfer expenses within IPSAS. Also, there is currently no domestic standard addressing the accounting for transfer expenses. Therefore, PBEs in New Zealand are currently responsible for determining their own accounting policies for the recognition, measurement and disclosure of funding arrangements where they are the resource provider. This has led to diversity in practice, with entities looking to various sources such as: • the PBE Conceptual Framework • PBE IPSAS 23 *Revenue from Non-Exchange Transactions* (applying a 'reverse' approach) • PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets* IPSAS 48 fills a significant gap in the IPSASB literature by providing a new accounting model for the recognition and measurement of transfer expenses in the public sector. The issuance of IPSAS 48 is the culmination of eight years of consultation with stakeholders and in-depth standard-setting, with alignment to the concepts within the IPSASB's Conceptual Framework at the core of the new Standard. Therefore, adopting IPSAS 48 into the PBE suite of standards is expected to reduce diversity in practice and lead to higher quality financial reporting by PBEs in New Zealand.
Whether the benefits of a potential development will outweigh the costs, considering as a minimum: **(i) *relevance to the PBE sector as a whole:* for example, where the potential development arises from the issue of a new or amended IFRS, whether the type and incidence of the affected transactions in the PBE sector are similar to the type and incidence of the transactions addressed in the change to the NZ IFRS;** **(ii) *relevance to the not-for-profit or public sector sub-sectors:* whether there are specific user needs in either of the sub-sectors, noting that IPSAS are developed to meet the needs of users of the financial reports of public sector entities;**	The benefits of adopting IPSAS 48 into the PBE suite of standards outweigh the costs, for the following reasons: Relevance to the PBE sector as a whole (and to the not-for-profit or public sector sub-sectors) The requirements in IPSAS 48 would apply to any PBE (whether not-for-profit or public sector) that provides resources to another entity without receiving anything directly in return (e.g., government departments, funding organisations, etc). This type of transaction is therefore not restricted to any particular sub-set of the PBE sector. Coherence Since the PBE suite of standards is primarily based on IPSAS, adopting IPSAS 48 into the PBE suite of standards would be highly unlikely to destroy the coherence of the suite. Specifically, IPSAS 48 is aligned with IPSAS 47 *Revenue* with respect to the concept of a "binding arrangement", which is fundamental to the accounting for both revenue and transfer expenses under IPSAS. Therefore, if IPSAS 47 is adopted into the PBE suite of standards (as recommended in Agenda Item 3B.1), doing the same with IPSAS 48 would enhance the coherence of the PBE suite of standards.

Factors in the Development Principle	Comment
(iii) ***coherence:*** **the impact on the entire suite of PBE Standards (e.g. can the change be adopted without destroying the coherence of the suite);** **(iv)** ***the impact on mixed groups*.**	However, if IPSAS 47 is **not** adopted into the PBE suite of standards (but IPSAS 48 is), then this would have the opposite effect on the coherence of the PBE suite of standards. Impact on mixed groups This is not a relevant factor in the decision on whether to adopt IPSAS 48 into the PBE suite of standards, as there is no for-profit equivalent to IPSAS 48, nor is there any other for-profit standard that deals with this topic (as it is a topic which primarily concerns PBEs).
In the case of a potential development arising from the issue of a new or amended IFRS, the IPSASB's likely response to the change (e.g. whether the IPSASB is expected to develop an IPSAS on the topic in an acceptable time frame).	Not applicable.

19. The staff view, based on the analysis above, is weighted in favour of developing a PBE Standard using IPSAS 48 as a starting point.

Question for the Board

Q1. Does the Board AGREE to commence a project to develop a PBE Standard, using IPSAS 48 as the starting point?

Throughout the project, we will consider the extent of amendments required to ensure any new PBE Standard is fit-for-purpose for the public sector and not-for-profit entities in New Zealand.

If the Board agrees to commence a project, we will bring a Project Plan to a future meeting.

Preliminary views on focus areas for the development of a new PBE Standard

20. Should the Board agree to commence a project on Transfer Expenses, using IPSAS 48 as the starting point, the next step is to develop a PBE Exposure Draft (ED) for public consultation.

21. As part of the process of developing this ED, we will need to determine whether there are any New Zealand-specific issues that should be considered and/or whether any areas of the transfer expense accounting in IPSAS 48 require more application guidance or illustrative examples in the PBE Standard, or through non-authoritative guidance.

22. An informal public sector advisory group, which has recently been set up and will hold its first meeting on 23 June, will assist us with ensuring that a new PBE Standard on transfer expenses is fit-for-purpose in New Zealand. A verbal update on the first public sector advisory group meeting will be provided at this meeting. At this stage we have sought feedback on the need for a standard on transfer expenses in New Zealand – i.e., what are the challenges that arise in practice.

23. Appendix 2 sets out a summary of the issues identified by the XRB and New Zealand constituents during public consultation on ED 72 *Transfer Expenses,* which was issued in February 2020. The IPSASB has addressed some of these issues through changes and clarifications made to IPSAS 48 in response to global feedback received from constituents. The key issues from Appendix 2 are discussed below.

Standards applicable to non-exchange expenses

24. In agenda paper 3C.3, we are recommending that a PBE Standard, using IPSAS 42 *Social Benefits* as a starting point, is developed. Also, in agenda paper 3C.3 we are recommending amendments to PBE IPSAS 19 using *Collective and Individual Services (amendments to IPSAS 19)* as a starting point. Entities may therefore struggle to determine which PBE Standard applies to a particular non-exchange expense transaction. We could address this issue through:

    (a) non-authoritative guidance.

    (b) additional application guidance and / or illustrative examples in PBE IPSAS 19, the transfer expenses PBE Standard and social benefits PBE Standard.

25. If, as recommended in agenda paper 3C.3, we issue a consultation paper on non-exchange expenses (which includes requirements for transfer expenses, social benefits and collective and individual services), we would need to be clear on the differences between these various types of non-exchange expenses and the rationale for why these non-exchange expenses are accounted for differently.

Milestone-based arrangements

26. It is common for milestone grants to be provided in the public sector where future funding is conditional on the recipient performing certain actions. The accounting for these types of arrangements has been identified as an issue by New Zealand PBEs.

27. The principles of IPSAS 48 are applicable to these types of arrangements, but we could consider being more explicit on the accounting for these arrangements in the new PBE Standard.

Multi-year arrangements

28. As for milestone-based arrangements, these types of arrangements have been identified as an issue for New Zealand PBEs. The principles of IPSAS 48 are applicable to these types of arrangements but there is no explicit reference to them, except in the implementation guidance section of the Standard. We could consider being more explicit on the accounting for these arrangements in the new PBE Standard.

Readability and understandability of the PBE Standard

29. We note that IPSAS 48 introduces several new terms, such as "transfer expenses", and new concepts such as "transfer right asset". These terms could be confusing for entities, especially not-for-profit entities. We have also identified the following formatting issues with IPSAS 48.

    (a) The core text of IPSAS 48 is relatively brief and is followed by an application guidance section which provides more detail on the principles and concepts. This could result in readers failing to fully grasp the concepts until they reach the application guidance section.

    (b) Some of the key requirements in IPSAS 48 are included in other Standards (such as IPSAS 19), which would require readers to refer to another document to find the relevant requirements.

30. We could address these issues through one or more of the following.

    (a) Renaming terms and concepts to align more with the New Zealand experience.

    (b) Rearranging the core text and application guidance paragraphs so that the requirements of the standard and the explanatory text is included in one place for ease of reading, i.e., we could bring the key provisions of the application guidance forward into the core text of the standard.

    (c) Incorporating the relevant requirements in other Standards (such as in PBE IPSAS 19) into the new PBE Standard.

Other clarifications

31. Certain other clarifications can be made to the new PBE Standard, relating to:

    (a) the applicability of the requirements for onerous contracts in PBE IPSAS 19 to transfer expense transactions. The definition of onerous contract excludes transfer expenses (as it only applies to exchange transactions) but this is not explicitly stated within IPSAS 48.

    (b) The interaction of the requirements in PBE IPSAS 41 *Financial Instruments* with the requirements in the new PBE Standard, in relation to transfer obligation liabilities that

meet the definition of a financial asset. Currently there is no scope exclusion in IPSAS 41 for these types of liabilities.

(c) Whether the time value of money should be taken into account for transfer expenses, if material. Currently those liabilities that are provisions as defined in IPSAS 19 are accounted for in accordance with IPSAS 19 (which requires discounting, if material) whereas other types of liabilities do not have this requirement, as discounting is not required in accordance with IPSAS 48.

Questions for the Board

Q2. Does the Board have any FEEDBACK on staff's preliminary views?

Q3 Has the Board identified any other preliminary issues based on a first read of the IPSAS 48?

Next steps

32. If the Board agrees to commence a project, a Project Plan to develop a draft ED (and accompanying Consultation Document) will be considered at a future meeting.

Attachments

Agenda item 3C.2: At-a-glance: IPSAS 48 *Transfer Expenses*

Agenda item 3C.6: IPSAS 48 *Transfer Expenses* (in supporting papers)

APPENDIX 1: Background to the IPSASB's Transfer Expenses project

1. The primary objective of most public sector entities is to deliver services to the public, rather than to make profits and generate a return on equity to investors. For many governments, the delivery of services to the public through social benefits, collective and individual services, and transfer expenses accounts for a significant portion of their expenditures.

2. The IPSASB undertook a phased program of work to address non-exchange transactions from the provider's perspective, beginning with IPSAS 42 *Social Benefits* (issued in January 2019), then continuing with *Collective and Individual Services* (amendments to IPSAS 19) (issued in January 2020). The PBE Policy Approach has been applied to IPSAS 42 and the amendments to IPSAS 19 in agenda paper 3C.3.

3. For the remaining non-exchange expenses (i.e., transfer expenses), the project timeline is shown below. Various steps in the timeline are described in more detail in paragraphs 4–7 of this Appendix.

Consultation paper *Revenue and Non-exchange Expenses*

4. The IPSASB issued this consultation paper (CP) in August 2017 to seek constituent views on potential recognition approaches for significant non-exchange expense transactions. In the CP, the IPSASB explained the drivers behind the development of the revenue and non-exchange expenses projects. For the non-exchange expenses project, these included:

   (a) the problems in operationalizing the exchange versus non-exchange distinction; and consideration of whether to replace this with a focus on whether transactions include a performance obligation.

   (b) the gap in the current IPSASB literature on accounting for non-exchange expenses, which could lead to ambiguity and inconsistency of accounting policies in highly significant areas of expenditure.

   (c) the scope for ensuring consistency of approaches between resource providers (for non-exchange expense transactions) and resource recipients (for revenue transactions).

Exposure Draft 72 *Transfer Expenses*

5. Based on constituents' feedback on the CP, the IPSASB developed ED 72 *Transfer Expenses*, which was issued in February 2020 together with ED 70 *Revenue with Performance Obligations* and ED 71 *Revenue without Performance Obligations*. ED 72 proposed:

   (a) a definition for transfer expenses;

   (b) the classification of transfer expenses based on whether the transfer recipients has at least one performance obligation; and

   (c) accounting and disclosure requirements for:

(i) transfer expenses without performance obligations; and

(ii) transfer expenses with performance obligations, which were largely based on application of the Public Sector Performance Obligation Approach (PSPOA) and mirrored the accounting for revenue with performance obligations.

Development of the final IPSAS

6. The IPSASB received mixed feedback on ED 72, with some constituents supporting the proposals but also raising significant concerns. Issues noted by New Zealand constituents can be found in Appendix 2 of this memo.

7. As a result of the feedback, the IPSASB decided not to proceed with the proposals in ED 72 and to revisit the proposed accounting and disclosures for transfer expenses. Specifically, the new IPSAS:

   (a) uses the transfer provider's perspective when developing accounting and disclosure requirements;

   (b) moves away from the PSPOA and the distinction between transfer expenses with and without performance obligations;

   (c) focuses on whether the transfer results in the recognition of an asset when developing accounting requirements; and

   (d) uses the fundamental concept of a "binding arrangement" for transfer expense accounting.

APPENDIX 2: XRB and New Zealand constituents' comments on ED 72 *Transfer Expenses* and the IPSASB's response

The table below sets out a summary of the XRB and New Zealand constituents' comments on ED 72, the IPSASB's response and XRB staff comments. This analysis will be considered during the development of a PBE Standard, using IPSAS 48 as a starting point.

Topic	Issue	IPSASB response[3]
Scope of ED 72	We prefer consistent requirements for the recognition of liabilities and expenses in relation to non-exchange expense transactions with similar characteristics. Consistent requirements help avoid debates about whether a transaction falls within the scope of one standard or another (i.e., transfer expense vs social benefit). **[XRB]**	There is a separate standard which deals with social benefits (i.e., IPSAS 42). Social benefits are therefore scoped out of IPSAS 48. IPSAS 42.IG2 contains guidance that illustrates the scope of IPSAS 42 and the boundaries between social benefits and other transactions. *XRB staff note – consider whether additional guidance is required in New Zealand to assist entities in applying the various standards relevant to non-exchange expenses.*
	The interaction of ED 72 with IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets* is not clear. **[XRB, OAG and CAANZ]** Specifically: • If a transfer provider has a binding arrangement with liabilities that are of uncertain timing or amount, what would it do? **[XRB]** • How does an entity apply the discounting requirements in ED 72 to a transfer expense transaction without performance obligations? **[XRB]** • If a transfer provider has a binding arrangement that becomes onerous, what would it do? **[XRB and OAG]** • How should a transaction be accounted for where a provision was recognised under IPSAS 19, and the parties subsequently entered into a binding arrangement in relation to that obligation? **[OAG]**	Provisions as defined in IPSAS 19 were scoped out of ED 72. This scope exclusion has been removed in IPSAS 48. • An entity applies IPSAS 19 where there are liabilities that are of uncertain timing or amount under binding arrangements • With respect to discounting – the requirements in ED 72 to consider the time value of money and the effect of financing were removed. Respondents noted that transfers are typically funded in tranches rather than one large upfront payment and so it would be rare for discounting to have a material effect on the financial statements. • Onerous contacts are no applicable to transfer expenses, as the definition of "onerous contract" in IPSAS 19 explicitly refers to "exchanges" of assets or services (and transfer expense transactions are non-exchange in nature). Therefore, there is no need for an explicit scope exclusion included in IPSAS 48.

[3] IPSASB responses were sourced from the Basis for Conclusions and/or a comparison of the ED to the final pronouncement.

Topic	Issue	IPSASB response[3]
		XRB staff notes: • *IPSAS 48 requires entities to refer to IPSAS 19 for the relevant requirements when necessary (e.g., if there is variable consideration). Consider whether a PBE Standard on transfer expenses could include the PBE IPSAS 19 requirements, for ease of use.* • *Where there is variable consideration (or where the definition of a provision is met for a legal or constructive obligation in a transaction without a binding arrangement) the discounting requirements in IPSAS 19 to discount apply (if material). This creates an inconsistency in the measurement of liabilities which are not provisions and those liabilities that meet the definition of a provision, without a clear rationale for the inconsistency. The new PBE Standard should make it clear that either discounting is not required for any liabilities arising from transfer expense transactions, or it is required when material.* • *There is no specific scope exclusion for onerous contracts in IPSAS 48. Consider making this clear in the new PBE Standard.*
	The scope of ED 72 is not clear. **[CAANZ and Treasury]** • There should be more clarity between the scope of this ED and the requirements in IPSAS 32 *Service Concession Arrangements: Grantor*, including consideration of whether IPSAS 32 is scoped in or out of the proposed standard. **[CAANZ]** • We suggest clarifying the term "capital transfers" from a transfer provider's perspective. **[CAANZ]** • It is not clear why the subsequent measurement of other non-contractual payables is brought into the scope of ED 72. **[CAANZ and OAG]** • We suggest providing further application guidance and illustrative examples on how to apply paragraph 7 (which relates to a binding arrangement which may be partially within scope of the ED and partially within scope of other Standards). **[CAANZ]**	• IPSAS 48 includes a scope exclusion for service concession arrangements as defined in IPSAS 32 • IPSAS 48 includes a definition, from the transfer provider's perspective, for capital transfers. The Standard also includes application guidance relating to capital transfers (AG53–AG55). • Subsequent measurement of other non-contractual payables has been removed from the scope of IPSAS 48. • No further application guidance or illustrative examples have been added relating to application of paragraph 7 (now paragraph 5 in the new Standard). • No specific guidance is included in IPSAS 48 on whether transactions where the transfer provider receives goods, services or other assets <u>indirectly</u> in return for the provision of funding are within scope of the new Standard.

Topic	Issue	IPSASB response[3]
	• It is not clear whether an expense is a transfer expense if a transfer provider receives any good, service or other assets indirectly in return for the provision of transfer expenses. **[CAANZ]** • It would be helpful if application guidance and illustrative examples could be provided to demonstrate how the provision of services could constitute transfer expenses. **[CAANZ]** • There is a section in the ED which addresses the proposed requirements for "consideration receivable by a transfer provider", which creates an inconsistency with the scoping paragraphs. **[CAANZ]**	• Several illustrative examples in IPSAS 48 make reference to services provided to transfer recipients. • The section in ED 72 that addresses the proposed requirements for "consideration receivable by a transfer provider" has been removed.
Monitoring satisfaction of the transfer recipient's performance obligations throughout the duration of the binding arrangement.	• ED 72 should be worded more generally to reflect the principle that the transfer provider needs to have the ability to assess the satisfaction of the transfer recipient's performance obligations (rather than specifically referring to the need to "monitor" satisfaction, as this implies continuous assessment and there are alternatives to monitoring satisfaction, such as periodic monitoring). **[XRB]** • The ED should include application guidance (e.g., to explain how an entity could satisfy itself and others about the extent to which the performance obligations have been satisfied, and whether the transfer provider need access to real-time information) **[XRB and CAANZ]** • The transfer provider may apply a number of monitoring regimes, not all of which will necessarily directly provide evidence of satisfaction of the transfer recipient's performance obligations (e.g., a focus on outcomes rather than the outputs delivered by the transferee) **[Treasury]** • Monitoring only be done when the transfer recipient also commits to a process for both parties to agree when a performance obligation is satisfactorily met. **[Auckland Council]** • Monitoring alone is not sufficient. Unless a transfer recipient is obligated to confirm the satisfaction of performance obligations to	ED 72 applied the PSPOA, whereby the transfer provider had to monitor the satisfaction of the transfer recipient's performance obligations throughout the duration of the binding arrangement. This was necessary to ensure the transfer provider had the information required to apply the PSPOA. IPSAS 48 moves away from the PSPOA and instead applies the concept of a "binding arrangement" as a core principle (with enforceability of the binding arrangement being a key determination that a transfer provider has to make). Therefore, the requirement to monitor satisfaction of a transfer recipient's performance obligations throughout the duration of the binding arrangement has been removed. Instead, under IPSAS 48, a transfer provider considers whether it has (and continues to have) an enforceable right to have the transfer recipient satisfy its obligation under the binding arrangement. IPSAS 48 states that typically, a transfer recipient's satisfaction (or lack of satisfaction) of their obligations can serve as an indicator for whether the transfer provider continues to have this right. IPSAS 48 also contains guidance on the methods a transfer provider can use to measure progress towards complete extinguishment of a transfer right (e.g., surveys of performance completed to date, milestones reached, time elapsed, etc). The method must provide a faithful depiction of the progress towards complete extinguishment.

Topic	Issue	IPSASB response[3]
	the transfer provider throughout the duration of the binding arrangement, the transaction should be accounted for as a transfer expense without performance obligations. **[Auckland Council]** • The PSPOA will be difficult to monitor where the provider does not have access to the relevant information. Feedback from stakeholders indicates this approach will be very difficult to apply in practice in most circumstances. **[CAANZ and OAG]** • Requiring the transfer provider to assess when the transfer recipient loses control of the asset may, in some circumstances, be a challenge. Practically, it may be even more of a challenge if the transfer provider had to assess when the third-party beneficiary obtains control of the asset. **[OAG]** • It may be difficult if the transfer provider had to monitor the satisfaction of the transfer recipient's performance obligations throughout the duration of the binding arrangement where these are long term arrangements that span multiple periods. **[OAG]**	*XRB staff note: we have received feedback that the requirement to reliably measure progress will be a high hurdle for many New Zealand public sector entities to reach, which will result in many cases where transfer expenses are recognised immediately even when they are considered to arise from a binding arrangement.*
Distinction between transfer expenses with and without performance obligations	The distinction between transfer expenses with and without performance obligations is sometimes difficult to apply in practice. Further guidance or illustrative examples on this issue would be helpful. **[Treasury]**	IPSAS 48 has moved away from the distinction between transfer expenses with and without performance obligations.
Binding arrangements and enforceability	Paragraph 93 of ED 72 states that "*transfers to be made outside of a binding arrangement are not enforceable*". We do not think that deeds would meet the definition of a binding arrangement in ED 70, but deeds are enforceable. In New Zealand, a range of legal documents, not all of which establish obligations on the other party, might be used as the basis for an agreement to make a grant. A promise, made verbally or in writing, is legally enforceable if the other party is giving something in return, or the promise is recorded in a deed. Unlike a contract, a promise in a deed is	The content of paragraph 93 of ED 72 has not been reproduced in IPSAS 48; however, the definition of "binding arrangement" in IPSAS 47 has not changed substantively from the ED stage. A binding arrangement must confer both rights and obligations on the parties to the arrangement. Therefore, an arrangement where, for example, a party has an enforceable right but no enforceable obligation would not meet the definition of a binding arrangement. The transaction would be accounted for as a transfer expense transaction without a binding arrangement in those circumstances.

Topic	Issue	IPSASB response[3]
	enforceable whether or not there is any payment or consideration given for it. [XRB]	
Recognition and measurement	The proposed requirements for subsequent measurement of certain binding arrangement liabilities associated with transfer expenses with present obligations are not complete, specifically with respect to the following. • Contractual conditional obligation • Non-contractual conditional obligation • Non-contractual unconditional payable **[XRB]**	IPSAS 48 includes requirements for the subsequent measurement of: • legal or constructive obligations arising from transactions without binding arrangements (and that meet the definition of a provision) • transfer obligation liabilities arising from a transaction with a binding arrangement (where the consideration is not variable) • transfer obligation liabilities arising from a transaction with a binding arrangement (where the consideration is variable) IPSAS 48 excludes financial instruments from its scope. *XRB staff note: IPSAS 48 requires an entity to apply IPSAS 41 to a financial asset arising from a binding arrangement (i.e., where the transfer recipient is required to repay funding received if it fails to satisfy its obligations). However, a transfer obligation liability to transfer cash arising from a contract is still accounted for under IPSAS 48, despite the fact that this liability would meet the definition of a financial liability. There does not appear to be a scope exclusion in IPSAS 41 for these types of liabilities. IPSAS 48 also specifically states that the disclosure requirements in IPSAS 30 for financial liabilities measured at amortised cost would apply to this type of transfer obligation liability.*
Recognition and measurement	It is unclear at what point in time an obligation arises for a transfer provider in relation to the provision of milestone grants – at the inception of the binding arrangement or when the milestones are met. If an expense is recognised when the binding arrangement is signed, it would not meet the requirement that certain actions/milestones are required to be met by the transfer recipient in order to be entitled to the next tranche of funding. **[OAG]**	IPSAS 48 does not include specific requirements for the accounting for these types of arrangements. However, there are certain sections of the Standard that may be applied by transfer providers, depending on the terms of the binding arrangement: Paragraph 23 states that a transfer obligation liability is recognised when it is more likely than not that a present obligation exists for the transfer of variable consideration. Paragraph 35 states that consideration can be variable if the transfer provider's obligation to transfer resources is contingent on the occurrence or non-occurrence of a future event (e.g., an additional amount of funds

Topic	Issue	IPSASB response[3]
		may become payable to the transfer recipient if it satisfies its obligations in the binding arrangement within a specified period). Paragraph AG44 also notes that, in many cases, a transfer recipient will have an unconditional right to payment only at an agreed-upon milestone or upon complete satisfaction of the obligation. In assessing whether a transfer recipient has a right to payment for satisfaction of the obligation completed to date, an entity shall consider whether the transfer recipient would have an enforceable right to demand or retain payment for satisfaction of its obligation completed to date if the binding arrangement were to be terminated before completion for reasons other than the transfer recipient's failure to satisfy its obligations as promised. *XRB staff note: The accounting for milestone-based arrangements has been identified as an issue in the past for New Zealand PBEs. Therefore, this may be a focus area when developing the new PBE Standard.*
Recognition and measurement	The definition of transfer expenses in ED 72 does not address the extent to which the transfer provider's overhead expenses should be attributed. **[Treasury]**	IPSAS 48 does not address the extent to which the transfer provider's overhead expenses should be attributed.
Recognition and measurement	There appears to be no practical method by which it can be established that both the transfer recipient and transfer provider have arrived at the same conclusions in recognising revenue and transfer expenses respectively (as we presume there is an expectation that the estimates and judgments leading to revenue recognition by the transfer recipient should be mirrored by the transfer provider). **[CAANZ]**	There is no requirement in IPSAS 48 for the estimates and judgements made by a transfer provider to mirror those made by the transfer recipient when recognising revenue.
Recognition and measurement	Paragraph BC 28 states that the transfer provider has an asset because "*the right to have goods or services transferred to the specified third parties will satisfy the definition of a resource as that right will be an item with service potential*." Presumably, the transfer recipient will also recognise an asset which is the resource received from the transfer provider, and that asset also reflects the service potential to third party beneficiaries. Although both the transfer provider and the transfer recipient recognise an asset on the basis that it has the service potential,	IPSAS 48 states that a transfer right asset is the asset recognised for the existence of one or more transfer rights arising from a binding arrangement. A transfer right is an entity's enforceable right to have the transfer recipient satisfy its obligation in a manner as specified in a binding arrangement or face the consequences as specified in the binding arrangement. IPSAS 48 does not specifically refer to the transfer of goods or services to third parties within its definition of a transfer right asset. Instead, it refers

Topic	Issue	IPSASB response[3]
	arguably the service potential does not differ between the two parties. It is presumed that the distinction lies in the fact that whilst the transfer provider has control over a right to have goods or services delivered, the transfer recipient has control over the resource itself that will enable it to deliver the goods or services. **[CAANZ]**	to a transfer recipient's "obligations", which could include providing the resources to a third party. BC28 has therefore been removed.
Recognition and measurement	For transfer expenses with performance obligations, if the transfer provider has not transferred the resources at the point at which recognition requirements for a binding arrangement asset are met, this would give rise to a liability and an asset. When the asset and liability extend over a year, the subsequent measurement is unclear, i.e., whether IPAS 41 is applicable and how that would interact with an impairment test under IPSAS 21 *Impairment of Non-cash Generating Assets.* We note that the subsequent measurement of a liability for a transfer expense without performance obligations is proposed to be under IPSAS 41. **[CAANZ]**	Under IPSAS 48, if the resource recipient has satisfied its compliance obligations before the transfer provider transfers the resources, then there is a transfer obligation liability (which is a liability recognised for the existence of one or more transfer obligations arising from a binding arrangement). The resource provider would not have a transfer right asset, as there is no enforceable right to have the transfer recipient satisfy its obligations under the binding arrangement (as the transfer recipient has already performed). No assets, liabilities or expenses associated with the binding arrangement are recognised when the binding arrangement is wholly unsatisfied.
Recognition and measurement	Paragraph 103 sets out proposed requirements of the measurement of transfer expenses before resources are transferred to the transfer recipient. It states such transfer expenses may include fixed costs, variable costs, or both. We suggest clarifying that such costs should be directly attributable to the specific binding arrangement, i.e. they are incremental costs. **[CAANZ]**	IPSAS 48 specifies that a transfer right asset is measured, at initial recognition, at the total carrying amount of the resources which have been transferred in accordance with the binding arrangement. When or as the transfer right is extinguished, a transfer expense is recognised and measured at the amount of the transfer consideration that is allocated to the extinguished transfer right. The transfer consideration represents the total amount of resources (i.e., goods, services and other assets) which an entity expects to transfer. The guidance in ED 72 relating to fixed costs, variable costs, or both, has therefore been removed.
Recognition and measurement	ED 72 states that the transfer provider does not revalue non-cash assets before they are derecognised. We question the rationale behind this proposal. For example, if the transfer provider was to transfer a non-current asset (e.g., a building) to a transfer recipient as part of the binding arrangement, the transfer recipient presumably has the ability to revalue the asset in their own accounting records. Arguably, this	The explicit prohibition on revaluing non-cash assets before they are derecognised is not included in IPSAS 48. However, IPSAS 48 requires a transfer right asset to be measured, at initial recognition, at the total carrying amount of the resources which have been transferred in accordance with the binding arrangement (which could include non-cash assets).

Topic	Issue	IPSASB response[3]
	revalued amount reflects the service potential in the transferred asset. However, the transfer provider is unable to reflect the same value relating to the service potential due to the restriction in ED 72. **[CAANZ]** Occasionally, there can be significant differences between the carrying value of the non-cash asset transferred and its fair value, for example, in the case of land. We recommend, under those circumstances, that the transfer provider be required to disclose that there is a significant difference between the value of the non-cash asset transferred and its fair value. **[OAG]**	IPSAS 48 does not contain a disclosure requirement for when there is a significant difference between the value of the non-cash asset transferred and its fair value.
Recognition and measurement	This recognition principle could lead to a situation where a transfer recipient recognises revenue on a different date to when the transfer provider recognises corresponding expense. Although this would not be mirroring the requirement of ED 71 in the transfer provider's financial statements, asymmetrical recognition can be justified if it represents the substance of the economic phenomenon in the financial statements of the transfer provider and transfer recipient respectively. However, the lack of symmetry may cause challenges in consolidated financial statements, therefore the IPSASB should give further consideration to this point. **[CAANZ]**	It does not appear that the IPSASB has given further consideration to the consolidation challenges caused by asymmetry.
Recognition and measurement	It is common for milestone grants to be provided in the public sector where future funding is conditional on the recipient performing certain actions, but the recipient is not providing goods or services to third parties. The concept of milestone grants is not clearly articulated in ED 72. We assume that such milestone grants are binding arrangements that impose present obligations other than performance obligations on the transfer recipient. **[OAG]**	IPSAS 48 uses the term "compliance obligation", which is defined in IPSAS 47 as "an entity's promise in a binding arrangement to either use resources internally for distinct goods or services or transfer distinct goods or services to a purchaser or third-party beneficiary". Therefore, depending on the terms of the binding arrangement, a resource recipient may be required to use the resources from the transfer provider for internal purposes, instead of for the purpose of providing goods or services to third parties.
Recognition and measurement	It is unclear from ED 72 whether discount rates have to be reset at the reporting date in the subsequent measurement of a liability for a transfer expense that is not a financial liability as defined in IPSAS 41. Currently, the discount rate is required to be reset at each reporting	IPSAS 48 does not require consideration of the time value of money and the effect of financing, as the IPSASB considers that it would be rare for the discounting of transfers to have a material impact on the financial statements.

Topic	Issue	IPSASB response[3]
	date in IPSAS 19 but not under IPSAS 41, if measured at amortised cost. We recommend that the proposed standard provides some application guidance. **[OAG]**	
Recognition and measurement	ED 70 and ED 71 use IFRS 15's high hurdle as a constraint to recognise variable revenue. Having a high hurdle ("highly probable") as a constraint is appropriate for revenue recognition. ED 72 mirrors the paragraphs in ED 70 and ED 71 and requires the same high hurdle as a constraint to recognise variable expense. We do not consider that it is necessary to have the same high hurdle for expenses given that, in most cases, the hurdle used for expenses is "probable" rather than "highly probable". **[OAG]**	IPSAS 48 requires a transfer provider to apply the requirements of IPSAS 19 in situations where there is variable consideration. Therefore, a transfer provider would only need to determine that it is more likely than not that a present obligation exists for the transfer of variable consideration. This represents a substantive change from the requirements of ED 72.
Disclosure	New Zealand constituents had several comments on the disclosure requirements: • There are too many disclosure requirements in ED 72. **[XRB]** • The level of detail to be disclosed is not appropriate – users are most likely to be interested in the overall balance of accruals, not the detail. **[XRB]** • The proposed disclosure requirements may be detailed and onerous, particularly at the level of individual agencies. **[Treasury]** • The disclosure requirements also appear to be adapted from the requirements in ED 70 and 71, which is not necessarily the most appropriate decision **[Treasury, CAANZ, Auckland Council]** • We also do not agree with the disclosure requirements relating to impairment losses recognised in accordance with IPSAS 21 on any transfer provider's binding arrangement assets, which the transfer provider shall disclose separately from other impairment losses from other binding arrangements. We do not believe this requirement is necessary because these assets are different from a normal receivable where we expect to recover the amount owing. **[Auckland Council]**	IPSAS 48 contains substantially reduced disclosures compared to ED 72, as the IPSASB decided that many of the display and disclosure requirements in existing IPSAS are also applicable to transfer expenses and related balances (e.g., analysis of expenses required under IPSAS 1, display and disclosure requirements in IPSAS 19 for provisions, etc).

Topic	Issue	IPSASB response[3]
Specific issues – multi-year grants	There is not enough guidance to lead to consistent treatment of multi-year grants. Although there is an example that specifically addresses multi-year agreements in ED 72, the requirements should be clearer within the ED itself. **[XRB]** ED 72 does not provide explicit guidance on the treatment of multi-year grants. In paragraph 97, on transfer expenses without performance obligations made as a series of transfers, a transfer provider is required to apply the requirements of paragraphs 91–94 to each transfer of resources to determine whether an expense is to be recognized. However, the paragraphs do not assist, for example, in determining whether the transfer provider recognises a liability for the entire amount at the point that they commit to the funding, or whether they recognise a portion in each year. **[OAG]**	IPSAS 48 does not include specific reference to multi-year grants in the core text – instead, implementation guidance (G.1) states that the application of the accounting principles in IPSAS 48 to multi-year arrangements is consistent with the accounting for other transfer expense transactions. *XRB staff note: consider whether the new PBE Standard should include more guidance on multi-year grants, as the accounting for these types of arrangements has been identified as an issue in New Zealand.*
Specific issues – appropriations	The discussion and guidance on the accounting when a binding arrangement is subject to appropriations is inadequate. **[Treasury]** ED 72 does not seem to provide explicit guidance on the treatment of multi-year grants. In paragraph 97, on transfer expenses without performance obligations made as a series of transfers, a transfer provider is required to apply the requirements of paragraphs 91–94 to each transfer of resources to determine whether an expense is to be recognized. However, the paragraphs do not assist, for example, in determining whether the transfer provider recognises a liability for the entire amount at the point that they commit to the funding, or whether they recognise a portion in each year. **[OAG]**	In developing IPSAS 48, the IPSASB noted that where a transfer expense arises from a transaction that is subject to an appropriation, the appropriation may limit the enforceability of the related arrangements and impact whether they are binding. This conclusion results from the application of the principles on binding arrangements and enforceability. IPSAS 48 therefore includes implementation guidance on how the concept of enforceability applies to transfers subject to appropriations as well as some illustrative examples.
Ease of application of ED 72	The IPSASB should revisit the terms used to categorise transfer expenses within the scope of ED 72 and use terminology that would be more easily understood by users of financial statements. **[XRB]** A common sense definition of present obligation is needed and application guidance is required on when a provider is required to recognise an expense where the recipient is not providing goods or services to third parties but is required “to do something”, for example, grants with that are “conditional” on other actions, for	IPSAS 48 introduces several new terms, such as: • Transfer right • Transfer right asset • Transfer obligation • Transfer obligation liability • Transfer consideration

Topic	Issue	IPSASB response[3]
	instance, where funding is to be provided on the condition that the recipient raises a matching amount of funding. **[OAG]**	IPSAS 48 also uses certain terms from IPSAS 47 with the same meaning, such as "compliance obligation" and "binding arrangement". *XRB staff note: these terms may be confusing for preparers and users. When developing the PBE Standard, we could consider how best to reduce any confusion arising from use of these terms.*
Ease of application of ED 72	ED 72 is hard to read and apply. The outcome of this ED could result in large amounts of additional administrative work, that does not lead to more useful information for the readers of the financial statements. Specifically: • It is difficult to apply the PSPOA • Users may be confused as to why no expense is recognised at the time the money leaves the entity's bank account (where the lifespan of the transfer expense is more than a year) • We would be forced to create a reconciliation between what is reported in the financial statements and the Appendix to our Annual Report (which reports every grant physically given in cash in the financial year), which could be confusing to our stakeholders and would be onerous and time-consuming for us. **[NZ Film Commission]**	IPSAS 48 has moved away from the PSPOA and has arguably been simplified compared to ED 72. *XRB staff note: a PBE Standard developed using IPSAS 48 as a starting point may be no less confusing in certain areas, but we could consider additional guidance where necessary (either in application guidance in the PBE Standard, or in non-authoritative guidance material). Topics requiring additional guidance will be determined both during the development of the consultation document and during final development of the new PBE Standard.*
Ease of application of ED 72	The ED is overly long, difficult to follow and therefore makes it difficult to reach a conclusion on how to apply it. There is likely to be a substantial increase in administration to collect information on performance obligations in a way which aligns with the ED for a significant number of grants. For a government entity which provides funding for an NGO to provide services to the public, it is hard to see how – where there are performance obligations – the ED would achieve the objectives to improve the "the relevance, faithful representativeness and comparability of the information provided about transfer expenses". For example, with a time lag between approving funding and completion of up to two years, the financial statements would not	As noted above, IPSAS 48 has arguably been simplified compared to ED 72. *XRB staff note: a PBE Standard developed using IPSAS 48 as a starting point may be no less confusing in certain areas, but we could consider additional guidance where necessary (either in application guidance in the PBE Standard, or in non-authoritative guidance material). Topics requiring additional guidance will be determined both during the development of the consultation document and during final development of the new PBE Standard.*

Topic	Issue	IPSASB response[3]
	provide the readers with a clear view of how the Crown funding for the year under review has been spent. **[NZ On Air]**	
Ease of application of ED 72	ED 72 refers to the reporting entity mostly as the "transfer provider" and sometimes interchangeably as "the entity." Given that ED 70 refers to the reporting entity as "the entity" and not the "transfer recipient," and ED 71 refers to the reporting entity as the "transfer recipient," we suggest ED 72 (and ED 70 and 71) makes use of consistent terminology to avoid confusion in application. **[CAANZ]**	The IPSASB was aware of the need to ensure consistency across the revenue and transfer expenses standards. *XRB staff note: during development of the new revenue and transfer expense PBE Standards, we will ensure consistency across both standards.*
Ease of application of ED 72	It is confusing to refer to "present obligation" in two different contexts. It is used to refer to the transfer provider's present obligation to provide resources to the transfer recipient (under paragraph 91(a)) and to the present obligations imposed on the transfer recipient in relation to a binding arrangement. **[OAG]**	IPSAS 48 now refers to a transfer recipient's "compliance obligation" and a transfer provider's "transfer obligation" in the relevant areas of the Standard.
Other issues	Paragraph 13 in ED 72 discusses the three parties that are relevant to transfer expenses, i.e., transfer provider, transfer recipient and third-party beneficiaries. AG 22 states that "the third-party beneficiaries in three party arrangements do not have any rights to force the transfer recipient to deliver goods and services because they are not parties to the binding arrangement." We suggest including reference to AG22 clarifying that "parties" identified in paragraph 13(b) are restricted to the transfer provider and the transfer recipient. **[CAANZ]**	Paragraphs AG26 – AG29 in IPSAS 48 contain guidance on the parties in a binding arrangement.

AT A GLANCE
May 2023

IPSAS 48 Summary—Transfer Expenses

This summary provides an overview of IPSAS 48, *Transfer Expenses*

Project Objective: To develop an IPSAS that provides accounting requirements for transfer expenses.

Approved: The International Public Sector Accounting Standards Board® (IPSASB®) approved IPSAS 48, *Transfer Expenses*, in March 2023. It was issued in May 2023.

Project History: The IPSASB initiated the Transfer Expenses project in 2015 as part of a combined project on the accounting for revenue and non-exchange expenses. In February 2020, the IPSASB issued Exposure Draft 72, *Transfer Expenses* (ED 72), which proposed an accounting model based on the Public Sector Performance Obligation Approach (PSPOA).

In developing IPSAS 48, the IPSASB considered constituents' feedback to ED 72 and decided to:

(a) Revise the accounting of transfer expenses to move away from the PSPOA and to focus on whether the transfer transaction results in the recognition of an asset;

(b) Focus on the accounting from the perspective of the transfer provider (the entity); and

(c) Where possible, streamlined the requirements for measurement, as well as presentation and disclosure.

IPSAS 48 is the IPSASB's response to comments received in the ED consultation.

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IPSASB®

Project Overview

The purpose of the Transfer Expenses project is to develop a new IPSAS on the accounting of transfer expenses.

A transfer expense is an expense arising from a transaction, other than taxes, in which an entity provides a good, service, or other asset to another entity, without directly receiving any good, service, or other asset in return.

Why the IPSASB Undertook this Project

The primary objective of most public sector entities is to deliver services to the public. For many governments, the delivery of services to the public through social benefits, collective and individual services, and transfer expenses accounts for a significant portion of their expenditure.

Until recently, there had been little guidance in the IPSASB's literature on how to account for these expenditures. The IPSASB undertook a phased program of work to address these transactions, culminative with IPSAS 42, *Social Benefits*, issued in January 2019, and *Collective and Individual Services* (Amendments to IPSAS 19), issued in January 2020.

IPSAS 48, *Transfer Expenses*, is the final step of the IPSASB's work program on social benefits, collective and individual services, and transfer expenses. This new standard sets out the accounting requirements for transfer expenses and fills a significant gap in the IPSASB's literature.

Benefits of IPSAS 48

The accounting requirements introduced in IPSAS 48 have the following benefits:

(a) Prior to IPSAS 48, there was no explicit guidance on transfer expenses in the IPSASB's literature. This lack of guidance led to ambiguity and potential inconsistencies in the accounting for transfer expenses, as constituents needed to develop their own accounting policy for these transactions; and

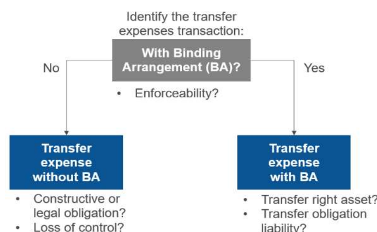
(b) Compared to ED 72, the accounting in IPSAS 48 is driven by whether a transfer transaction results in recognition of an asset. This approach is more intuitive and better aligned with the definition of an asset in the IPSASB's Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities.

IPSASB®

Two Accounting Models

IPSAS 48 presents two accounting models based on the existence of a binding arrangement.

IPSAS 48 includes comprehensive guidance for an entity to determine whether their transaction arises from a binding arrangement, and consequently, which accounting model to apply.



Under IPSAS 48, the accounting for transfer expenses is driven by whether the transaction results in an enforceable right to have the transfer recipient satisfy their obligations. Such an enforceable right is recognized as an asset and subsequently expensed as the enforceable right is extinguished.

The identification of whether the transaction arises from a binding arrangement impacts the determination of whether the transaction results in the recognition of an asset, as the rights and obligations from a binding arrangement provides inputs into the assessment of the asset recognition criteria.

The Binding Arrangement Concept

The concept of a 'binding arrangement' is prevalent throughout IPSAS literature and is fundamental for the accounting for transfer expenses.

A binding arrangement is an arrangement that confers both rights and obligations, enforceable through legal or equivalent means, on the parties to the arrangement. As such, an entity must have at least an enforceable right and an enforceable obligation

For example, in a two-party binding arrangement:

Component	Party A	Party B
Enforceable Right	✓	✓
Enforceable Obligation	✓	✓

Enforceability

Enforceability underpins the definition of a binding arrangement. An entity uses judgment to consider all relevant factors in their jurisdiction and specific transaction, to assess whether enforceability exists in its transfer expense arrangement. Enforceability can:

- Arise from various mechanisms (i.e., "what"), to hold the parties accountable to fulfilling each of their respective obligations by compelling them to fulfill their obligations or face imposed consequences (i.e., "how"); and
- Be through legal or equivalent means in the public sector. Equivalent means (which include executive authority and cabinet or ministerial directives) capture enforcement outside the judicial system that is similar to the force of law.

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Transfer Expenses from Transactions without Binding Arrangements

The accounting model for transfer expenses without binding arrangements requires an entity to consider whether any of its rights or its obligations in the transfer expenses transactions are enforceable, and meet the definition of an asset or liability, respectively.

Core Principles

In a transfer expense transaction without binding arrangements, the entity does not have both an enforceable right and an enforceable obligation, but may have an:

- Unenforceable right, and unenforceable obligation—e.g., a donation where the transfer provider cannot direct how the funds are to be used by the transfer recipient;
- Enforceable right, but unenforceable obligation—e.g., certain education grants where a government directs how the funds are to be distributed, but the educational institution has no rights to demand payment; or
- Unenforceable right, but enforceable obligation—e.g., an obligation to pay a fine or penalty.

An entity determines whether any of its rights in the arrangement meet the definition and recognition criteria of an asset, and whether any of its obligations meet the definition and recognition criteria of a liability.

Recognition

When a transfer expense arises from a transaction without a binding arrangement:

- The entity would need to first consider whether it has a constructive or legal obligation related to the transfer. If so, the entity recognizes an expense and a provision under IPSAS 19, *Provisions, Contingent Liabilities, and Contingent Assets*. The subsequent transfer of resources to the transfer recipient settles the provision; and
- If there is no related constructive or legal obligation, the entity derecognizes the assets to be transferred and recognizes a transfer expense when it ceases to control these resources.

Measurement

In situations where a constructive or legal obligation exists and a provision is recognized, the provision and expense are measured in accordance with IPSAS 19.

When a transfer expense is recognized upon the transfer of resources, the expense is measured at the carrying amount of the transferred assets.

Transfer Expenses from Transactions with Binding Arrangements

The accounting model for transfer expenses with binding arrangements is driven by the enforceable rights and enforceable obligations in the binding arrangement, and whether the entity or the transfer recipient has fulfilled its respective obligations

Recognition

In a transfer expense transaction with binding arrangements, the enforceable right from the binding arrangement meets the definition of an asset in the IPSASB's Conceptual Framework. As a result:

- Upon the transfer of resources, the entity derecognizes the transferred asset and recognizes a transfer right asset; and
- Subsequent to the transfer, the transfer right asset is derecognized and expensed when or as the transfer right is extinguished. This typically occurs when or as the transfer recipient satisfies its obligations in the binding arrangement.

In situations where the transfer recipient satisfies its obligations in the binding arrangement, the binding arrangement imposes an enforceable obligation to the entity. This enforceable obligation results in the recognition of a liability by the entity.

Measurement

When an entity transfers resources as part of a transfer expense transaction arising from a binding arrangement, the resulting transfer right asset is measured at the carrying amount of the transferred asset.

When an entity recognizes a liability for the enforceable obligation to transfer resources, the liability is measured at the carrying amount of the resources which the entity is obligated to transfer.

Some binding arrangements may involve the transfer of variable consideration. Under IPSAS 48, variable consideration is measured using the same requirements as the measurement of provisions in IPSAS 19.

Other Considerations

IPSAS 48 includes implementation guidance and illustrative examples to help entities apply the accounting principles to specific types of transfer expenses that are prevalent in the public sector.

In response to comments from constituents, the requirements for presentation and disclosures, as well as transitional provisions, were streamlined.

Supporting Guidance

IPSAS 48 includes additional guidance to support understanding application of the principles. This includes new implementation guidance and detailed basis for conclusions, as well as a robust set of illustrative examples. In particular, the illustrative examples use general fact patterns to illustrate the application of the accounting principles to transactions that are both relevant and prevalent in the public sector.

Presentation and Disclosure

IPSAS 48 retains the requirements to disclose certain information regarding transfer arrangements and the basis for the recognition of transfer right assets. However, many constituents noted that the remaining presentation and disclosure requirements proposed in ED 72 were overly onerous and that the relevant information related to transfer expenses was already presented or disclosed in the financial statements as part of the information on an entity's programs and activities. As a result, IPSAS 48 leverages the general presentation and disclosures requirements in IPSAS 1 for the presentation and disclosures of transfer expenses and related balances.

Transitional Provisions

Based on constituents' feedback, the IPSASB also simplified the transitional provisions for the application of IPSAS 48. To provide the flexibility to adjust prior-period financial statements, the transitional provisions allow entities to apply IPSAS 48 prospectively or on a retrospective basis in accordance with IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors*.

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Effective Date and Project History

The effective date of IPSAS 48 is January 1, 2026.

Effective Date

The effective date of IPSAS 48 is January 1, 2026, with earlier application permitted for entities that apply IPSAS 47, *Revenue*, at or before the date of initial application of this Standard.

The IPSASB selected this effective date because IPSAS 48 leverages certain definitions and principles from IPSAS 47. The IPSASB decided that public sector entities will need sufficient time to apply IPSAS 48, after applying other recently issued pronouncements.

Project History

To learn more about the project history, and to view the consultation documents and responses, please visit:

https://www.ipsasb.org/consultations-projects/transfer-expenses

Memorandum

Date:	16 June 2023
To:	NZASB Members
From:	Carly Berry
Subject:	**Application of the PBE Policy Approach to IPSAS 42 *Social Benefits* and *Collective and Individual Services* (Amendments to IPSAS 19)**

COVER SHEET

Project priority and complexity

Project priority	**Medium*** **If the Board decides to commence the recommended projects on Social Benefits and Collective and Individual Services.*
Complexity of Board decision-making at this meeting	**High** The Board is required to apply the PBE Policy Approach to IPSAS 42 *Social Benefits and Collective and Individual Services (Amendments to PBE IPSAS 19 Provisions, Contingent Liabilities and Contingent Assets).* There is a high degree of judgement involved in the application of the PBE Policy Approach. Based on the analysis in this paper, it is not clear whether adopting these IPSASB pronouncements into the PBE suite of standards will lead to improved financial reporting. It is possible that a decision to commence the recommended projects may have to be revisited, depending on information obtained during our work with the relevant Government departments during development of the Exposure Drafts.

Overview of agenda item

Project status	This project has not yet commenced. Applying the PBE Policy Approach at this meeting is the first step and will determine subsequent steps.
Project purpose	If we commence the recommended projects, the objective will be to develop a PBE Standard using IPSAS 42 as a starting point, and amendments to PBE IPSAS 19 using *Collective and Individual Services* as a starting point. We will need to ensure that any new PBE Standards on social benefits and individual and collective services are fit-for-purpose in New Zealand.
Board action required at this meeting	• APPLY the PBE Policy Approach to IPSAS 42 and *Collective and Individual Services* • AGREE to commence projects to develop a PBE Standard and amendments to PBE IPSAS 19, based on IPSAS 42 and *Collective and Individual Services* respectively. • PROVIDE FEEDBACK on staff's preliminary views on the nature of the consultation document to be issued for public consultation.

Introduction[1]

1. The International Public Sector Accounting Standards Board (IPSASB) issued IPSAS 42 *Social Benefits* in January 2019 and *Collective and Individual Services* (Amendments to IPSAS 19) in January 2020. In accordance with the *Policy Approach to Developing the Suite of PBE Standards* (PBE Policy Approach), the Board is required to consider if and when to incorporate IPSAS 42 and *Collective and Individual Services* into the suite of PBE Standards as issued by the XRB.

2. At its February 2019 meeting, the Board agreed to defer a decision to adopt IPSAS 42 until the IPSASB completed other related projects dealing with non-exchange expenses. A similar decision was taken with respect to *Collective and Individual Services* at the Board's December 2019 meeting.

3. Now that IPSAS 48 *Transfer Expenses* has been issued (refer to agenda paper 3C.1), the content of this memo includes the application of the PBE Policy Approach to IPSAS 42 and *Collective and Individual Services*.

Recommendation

4. We recommend that the Board:
   (a) APPLIES the PBE Policy Approach and AGREES to:
      (i) commence a project to develop a PBE Standard, using IPSAS 42 *Social Benefits* as a starting point;
      (ii) commence a project to develop amendments to PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*, using *Collective and Individual Services* (Amendments to IPSAS 19) as a starting point; and
   (b) PROVIDES FEEDBACK on staff's preliminary views on the nature of the consultation document to be issued for public consultation.

Structure of this memo

5. This memo has the following sections.
   - Summary of the key concepts in IPSAS 42 and *Collective and Individual Services*
   - Application of the PBE Policy Approach
   - Development of a new PBE Standard and amendments to PBE IPSAS 19
   - Next steps
   - Appendix 1: Background to the IPSASB's projects on Social Benefits and Collective and Individual Services

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

- Appendix 2: XRB and New Zealand constituents' comments on ED 63 *Social Benefits* and the IPSASB's response
- Appendix 3: XRB and Audit New Zealand's comments on ED 67 *Collective and Individual Services and Emergency Relief (Amendments to IPSAS 19)* and the IPSASB's response

Summary of the key concepts in IPSAS 42 and *Collective and Individual Services*

6. The table below sets out a high-level overview of the relationship between social benefits and collective and individual services.

	Social Benefits	**Individual Services**	**Collective Services**
Involves a cash transfer to eligible beneficiaries?	✔	✘	✘
Provided to individuals and/or households, rather than to a community?	✔	✔	✘
Intended to address the needs of society?	✔	✔	✔

At A Glance – Collective and Individual Services

7. The following sections set out a summary of the key concepts in IPSAS 42 and *Collective and Individual Services*.

IPSAS 42 Social Benefits

8. IPSAS 42 defines "social benefits" and contains requirements for the recognition, measurement and disclosure of expenses and liabilities for social benefits. IPSAS 42 defines social benefits as **cash transfers** provided to:

    (a) specific individuals and/or households who meet eligibility criteria;

    (b) mitigate the effect of social risks[2]; and

    (c) address the needs of society as a whole.

9. IPSAS 42 sets out the General Approach[3], which includes a single recognition point for all social benefits and requires that expenses be measured at an amount equal to the amount of the liability. The table on the next page sets out a summary of the accounting under the General Approach.

[2] Social risks are events or circumstances that: (a) relate to the characteristics of individuals and/or households (e.g., age, health, poverty and employment status); **and** (b) may adversely affect the welfare of individuals and/or households, either by imposing additional demands on their resources or by reducing their income.

[3] Referred to as the Obligating Event Approach in ED 63 *Social Benefits*

Recognition of the liability	When the eligibility criteria[4] to receive the next social benefit have been satisfied.
Initial measurement of the liability	At the best estimate of the costs that the entity will incur in fulfilling the present obligations represented by the liability, i.e., the cash it expects to transfer to the beneficiary.
Subsequent measurement of the liability	Upon settlement: any difference between the cost of making the social benefit payments and the carrying amount of the liability is recognised in surplus or deficit in the period in which the liability is settled. Not settled at reporting date: the liability is reviewed and adjusted to reflect the current best estimate of the social benefit payment required to fulfil the liability.
Measurement of the expense	At the amount of the next payment following satisfaction of the eligibility criteria (discounting will not be required for most social benefits).
Disclosure	Explain the characteristics of its social benefit schemes. Explain the demographic, economic and other external factors that may affects its social benefit schemes.

10. IPSAS 42 includes the Insurance Approach as a possible alternative approach. Entities are permitted, but not required to use this approach where:

    (a) the social benefit scheme is intended to be fully funded from contributions; and

    (b) there is evidence that the entity manages the scheme in the same way as an issuer of an insurance contracts, including assessing the financial performance and financial position of the scheme on a regular basis.

11. When an entity is eligible, and elects to apply, the Insurance Approach, it is required to apply the relevant international or national accounting standards by analogy. In this context, IPSAS 42 refers to IFRS 17 *Insurance Contracts* and national standards that have adopted substantially the same principles as IFRS 17. When applying the Insurance Approach, the entity will be required to make certain disclosures on top of those required by the international or national standard (e.g., information about the characteristics of its social benefit schemes).

12. Agenda paper 3C.4 contains a "snapshot" of IPSAS 42. The full Standard can be found at Agenda paper 3C.7 (in supporting papers). Appendix 1 to this memo includes some background information on the IPSASB's Social Benefits project.

[4] Examples of eligibility criteria include reaching retirement age or becoming unemployed.

Collective and Individual Services

13. *Collective and Individual Services* addresses transactions for collective and individual services. The table below sets out the definitions for collective and individual services, which are now included in IPSAS 19.

	What?	**To whom?**	**For what purpose?**
Collective services	Services e.g., street lighting	Simultaneously to all members of the community	To address the needs of society as a whole
Individual services	Goods and services e.g., rubbish collection	Individuals and/or households	

14. IPSAS 19 has also been amended to include application guidance paragraphs which:
    (a) explain collective services and individual services and how they differ from social benefits; and
    (b) specify that no provision is to be recognised for collective services or individual services before the services are delivered. The rationale for this is that these are ongoing activities of a government, and no provision is recognised for ongoing activities.

15. The amendments to IPSAS 19 do not address emergency relief – this was a change to the proposals in ED 67. Respondents raised a number of issues in relation to the proposed guidance on emergency relief, including the difficulty of distinguishing between emergency relief that is an ongoing activity of government and emergency relief provided in response to specific emergencies. The IPSASB agreed to consider doing more work on this topic when it develops its future work plans.

16. Agenda paper 3C.5 contains a "snapshot" of IPSAS 42. The full Standard can be found at Agenda paper 3C.8 (in supporting papers). Appendix 1 to this memo includes some background information on the IPSASB's project.

Application of the PBE Policy Approach

17. Shortly after its publication, the Board will typically consider whether a new or amending IPSAS should be adopted into PBE Standards. These decisions are guided by the PBE Policy Approach.

18. As noted in paragraphs 2–3, now that the IPSASB has issued IPSAS 48 *Transfer Expenses*, the Board will need to apply the PBE Policy Approach to IPSAS 42 and *Collective and Individual Services*. Assuming the Board decides to adopt IPSAS 42 and *Collective and Individual Services* into PBE Standards, we need to decide how and when to give effect to that decision.

19. The PBE Policy Approach identifies triggers for changes to PBE Standards. One of these triggers is the IPSASB issuing a new IPSAS. Section 4.1 (paragraphs 22–24) of the PBE Policy Approach establishes a rebuttable presumption that the NZASB will adopt a new or amended IPSAS. The PBE Policy Approach states that it is expected that the adoption of a new or

amended IPSAS will lead to higher quality financial reporting by public benefit entities (PBEs) in New Zealand and the factors in the development principle are presumed to be met.

20. **Table 1** on the next page considers the factors in the development principle, as provided for in the PBE Policy Approach, as they apply to IPSAS 42 and *Collective and Individual Services*.

Table 1: Factors in the Development Principle

<table>
<tr><th>Factors in the Development Principle</th><th>Comment</th></tr>
<tr><td>Whether the potential development will lead to higher quality financial reporting by public sector PBEs and not-for-profit entities, including public sector PBE groups and not-for-profit groups, than would be the case if the development was not made.</td><td>IPSAS 42 Social Benefits
Until the publication of IPSAS 42, there was no specific guidance on the accounting for social benefits within IPSAS. The IPSASB believes that IPSAS 42 will promote consistency and comparability in how social benefits are reported by public sector entities.
However, the following factors suggest that adopting IPSAS 42 into the PBE suite of standards may not lead to significant improvements in the quality of financial reporting by PBEs in New Zealand.
• Most social benefit payments involving cash transfers are made by the Ministry of Social Development (MSD) and Inland Revenue on behalf of the Government, and by ACC. The Government already applies insurance accounting to some major social benefits and accrues payments due for the remainder. IPSAS 42 may result in the Government accruing slightly different amounts for certain benefits than at present
• Although there is currently no PBE Standard dealing with social benefits in the form of cash transfers, this has not led to significant diversity in accounting practice.
• We are currently not aware of any concerns with the current reporting of such social benefits.
Applying the requirements in IPSAS 42 may result in the Government accruing slightly different amounts for certain benefits than at present. At this stage, we do not have enough information to assess the impact of applying the requirements in IPSAS 42 to particular benefits – the actual impact would depend on the detailed aspects of a benefit, including how often payments are made and how close to the reporting date the last payment occurs. It is, however, arguable as to whether a slightly different pattern of accrual would lead to higher quality financial reporting by PBEs.
Collective and Individual Services
These amendments to IPSAS 19 may not have much impact on New Zealand's public sector PBEs as the amendments are fairly consistent with current accounting. Existing public sector guidance in New Zealand has led to a reasonably consistent approach to the recognition of provisions[5].</td></tr>
</table>

[5] See the Treasury *Guidance on Recognising Liabilities and Expenses*.

Factors in the Development Principle	Comment
Whether the benefits of a potential development will outweigh the costs, considering as a minimum: **(i) *relevance to the PBE sector as a whole:* for example, where the potential development arises from the issue of a new or amended IFRS, whether the type and incidence of the affected transactions in the PBE sector are similar to the type and incidence of the transactions addressed in the change to the NZ IFRS;** **(ii) *relevance to the not-for-profit or public sector sub-sectors:* whether there are specific user needs in either of the sub-sectors, noting that IPSAS are developed to meet the needs of users of the financial reports of public sector entities;** **(iii) *coherence:* the impact on the entire suite of PBE Standards (e.g. can the change be adopted without destroying the coherence of the suite);** **(iv) *the impact on mixed groups*.**	Relevance to the PBE sector as a whole As noted above, most social benefit payments are made by the Government and by ACC. Therefore, the requirements in IPSAS 42 would only affect a very specific sub-set of public sector PBE. *Collective and Individual Services* is similarly only relevant to a very specific sub-set of public sector PBE. Relevance to the not-for-profit or public sector sub-sectors The requirements in IPSAS 42 and *Collective and Individual Services* are not relevant to the not-for-profit sector, as noted above. Coherence Since the PBE suite of standards is primarily based on IPSAS, adopting IPSAS 42 and *Collective and Individual Services* into the suite would be highly unlikely to destroy the coherence of the suite. We note that the scope of a PBE Standard on social benefits would have to work together with the scope of other PBE Standards such as: (i) PBE IPSAS 19 (ii) PBE IFRS 17 *Insurance Contracts* (iii) a PBE Standard developed using IPSAS 48 *Transfer Expenses* as a starting point IPSAS 48 contains a scope exclusion for social benefits as defined in IPSAS 42. Therefore, if IPSAS 42 is **not** adopted into the PBE suite of standards, a New Zealand-specific scope exclusion would need to be added to a PBE Standard on transfer expenses. Impact on mixed groups This is not a relevant factor in the decision on whether to adopt IPSAS 42 into the PBE suite of standards, as there is no for-profit equivalent to IPSAS 42, nor is there any other for-profit standard that deals with the topic of social benefits – it is a topic that exclusively affects public sector PBEs. The same applies to *Collective and Individual Services*.
In the case of a potential development arising from the issue of a new or amended IFRS, the IPSASB's likely response to the change (e.g. whether the IPSASB is expected to develop an IPSAS on the topic in an acceptable time frame).	Not applicable.

21. The conclusion, based on the analysis above, is **not** heavily weighted in favour of adopting IPSAS 42 and *Collective and Individual Services* into the PBE suite of standards. However, according to paragraph 25 of the PBE Policy Approach, rebutting the presumption that a new or amended IPSAS will not be adopted in New Zealand is expected to occur only in exceptional circumstances. Paragraph 26 of the PBE Policy Approach provides examples of such exceptional circumstances:

    (a) Adoption of a new or amended IPSAS would not be either appropriate or relevant (based on the development principle); **and**

    (b) The costs of adoption of a new or amended IPSAS would outweigh the benefits to users of PBE financial reports.

22. There is nothing in the analysis to suggest that adopting IPSAS 42 and *Collective and Individual Services* would be either inappropriate or irrelevant to New Zealand. Therefore, even though it is likely that the costs of adoption would outweigh the benefits to users of PBE financial reports, there is not a strong enough argument to rebut the presumption. As such, we recommend developing a PBE Standard using IPSAS 42 as a starting point, and amending PBE IPSAS 19 using *Collective and Individual Services* as a starting point.

23. If the Board decides to commence a project to develop a PBE Standard using IPSAS 42 as a starting point, and amendments to PBE IPSAS 19 using *Collective and Individual Services* as a starting point, we intend to work with the relevant Government departments during development of the Exposure Drafts (EDs). Information obtained during this development stage may result in the need for the Board's PBE Policy Approach decision to be revisited, given the analysis to date is not heavily weighted in favour of adopting IPSAS 42 and *Collective and Individual Services* into the PBE suite of standards.

Question for the Board

Q1. Does the Board AGREE to:

(a) commence a project to develop a PBE Standard, using IPSAS 42 as the starting point?

(b) commence a project to develop amendments to PBE IPSAS 19, using *Collective and Individual Services* as the starting point?

Throughout the project, we will consider the extent of amendments required to ensure any new PBE Standard is fit-for-purpose for public and not-for-profit sectors.

Development of a new PBE Standard and amendments to PBE IPSAS 19

24. Should the Board agree to commence projects on Social Benefits and Collective and Individual Services, using IPSAS 42 and *Collective and Individual Services* as the respective starting points, the next step is to develop PBE EDs for public consultation.

25. As part of the process of developing these EDs, we will need to determine whether there are any New Zealand-specific issues that should be considered and/or whether any areas of the accounting in IPSAS 42 and *Collective and Individual Services* require more application guidance or illustrative examples in the PBE Standards or through non-authoritative guidance. As noted in paragraph 23, we intend to work with the relevant Government departments to obtain their input during development of the EDs.

26. Appendix 2 and Appendix 3 set out a summary of the issues identified by the XRB and New Zealand constituents during public consultation on ED 63 *Social Benefits* and ED 67 *Collective and Individual Services and Emergency Relief* respectively. The IPSASB has addressed some of these issues through changes and clarifications made to IPSAS 42 and *Collective and Individual Services* in response to global feedback received from constituents.

27. Since social benefits, collective and individual services and transfer expenses are all types of non-exchange expense, we intend to explore the possibility of issuing one Non-exchange Expenses Consultation Document to cover the requirements for social benefits, collective and individual services and transfer expenses. Our preliminary views on the costs and benefits of such an approach are included in the table below.

Advantages	**Disadvantages**
Only one consultation document for constituents to consider. Multiple documents could lead to confusion among constituents and a sense that there are "too many consultations at once".	There would be a lot of detail within the Consultation Document for constituents to grasp (potential "information overload). This disadvantage is mitigated by the fact that some of the proposals would only be applicable to a very small sub-set of PBEs.
The opportunity to clearly highlight the relationship between the various types of non-exchange transactions. Having separate consultation documents would make it harder to demonstrate this.	There is an increased risk of confusion among constituents if the proposals relating to each type of non-exchange expense are not clearly demarcated within the consultation document and explained. This risk would be mitigated through a clear, logical format and structure to the consultation document.
Reduces the administrative tasks involved in issuing a consultation document.	

Question for the Board

Q2. Does the Board have any FEEDBACK on staff's preliminary views on the nature of the consultation document to be issued?

Next steps

28. If the Board agrees to commence these projects, a project plan to develop draft EDs (and accompanying Consultation Document) will be tabled at a future meeting.

Attachments

Agenda item 3C.4:	At-a-glance: IPSAS 42 *Social Benefits*
Agenda item 3C.5:	At-a-glance: *Collective and Individual Services* (Amendments to IPSAS 19)
Agenda item 3C.7:	IPSAS 42 *Social Benefits* (in supporting papers)
Agenda item 3C.8:	*Collective and Individual Services* (Amendments to IPSAS 19) (in supporting papers)

APPENDIX 1: Background to the IPSASB's projects on Social Benefits and Collective and Individual Services

1. The primary objective of most public sector entities is to deliver services to the public, rather than to make profits and generate a return on equity to investors. For many governments, the delivery of services to the public through social benefits, collective and individual services, and transfer expenses accounts for a significant portion of their expenditures.

2. The IPSASB undertook a phased program of work to address non-exchange transactions from the provider's perspective, beginning with IPSAS 42 *Social Benefits* (issued in January 2019), then continuing with *Collective and Individual Services* (amendments to IPSAS 19) (issued in January 2020). The IPSASB concluded this program of work with the issue of IPSAS 48 *Transfer Expenses* in May 2023. The PBE Policy Approach has been applied to IPSAS 48 in agenda paper 3C.1.

Social Benefits

3. The IPSASB issued ED 63 *Social Benefits* in October 2017, with comments due by 31 March 2018. ED 63 proposed:

    (a) to define social benefits as those benefits "provided to specific individuals and/or households who meet eligibility criteria; mitigate the effect of social risks; and address the needs of society as a whole; but are not universally accessible services"

    (b) to distinguish between social risks and other risks (e.g., risks related to the characteristics of geography or climate, such as the risk of an earthquake or flooding occurring). The hazards or events that give rise to these risks are not related to the characteristics of individuals and/or households, which is a distinguishing feature of social risks. The IPSASB also noted that governments' responses to social risks are often different to their response to other risks. The IPSASB considered that the reactive nature of responses to other risks was more suited to its non-exchange expenses project than its social benefits project.

    (c) to distinguish between those benefits that are provided to specific individuals and/or households and those that are universally accessible. This distinction was intended to provide a more principles based, less artificial boundary between social benefits and other non-exchange expenses.

    (d) two approaches – the Obligating Event Approach and the Insurance Approach.

        (i) The Obligating Event Approach proposes a single recognition point for all social benefits. A liability for a social benefit is recognised when the eligibility criteria to receive the next social benefit have been satisfied. "Being alive" at the point at which the eligibility criteria are required to be satisfied is an eligibility criterion, whether explicitly stated or implicit.

        (ii) The Insurance Approach is an optional for those entities meeting certain criteria. ED 63 did not include requirements for the Insurance Approach but directed entities to apply relevant international or national accounting standards by analogy.

4. ED 63 also contained an Alternative View, as not all IPSASB members agreed with the requirements proposed in ED 63. In the Alternative View, some members proposed that the obligating event should be dependent on the economic substance of the social benefit scheme. For some social benefits, recognising a liability when the eligibility criteria for the next benefit are satisfied will be appropriate. For others, a liability would be recognised at an earlier point. Preparers would determine which obligating event is most appropriate for their social benefit schemes, based on their economic substance.

5. Feedback on ED 63 reflected a wide range of views, with a number of respondents supporting the proposals in ED 67 and a similar number supporting the Alternative View referred to in paragraph 4. Issues noted by New Zealand constituents can be found in Appendix 2 of this memo.

6. IPSAS 42 *Social Benefits* was approved in December 2018. In finalising IPSAS 42, the IPSASB:
   (a) clarified the definition of social benefits to put the focus on cash transfers
   (b) removed the definition of "universally accessible services"
   (c) renamed the Obligating Event Approach to the General Approach
   (d) reduced the emphasis on "being alive" (but being alive is still seen as important)
   (e) amended the wording in the General Approach to clarify that the liability is for the next social benefit payment.
   (f) removed the disclosure requirements in respect of the reconciliation of the social benefit liability and the best estimate of the undiscounted projected cash outflows.

Collective and Individual Services

7. The IPSASB issued ED 67 *Collective and Individual Services and Emergency Relief* (Amendments to IPSAS 19) in January 2019, with comments due by 31 May 2019. ED 67 proposed to:
   (a) define collective and individual services. Examples of collective services are street lighting and defence. Examples of individual services are public sector healthcare services and education;
   (b) specify that no provision should be recognised for collective services or individual services on the grounds that they are ongoing activities of governments. The IPSASB linked its proposals to paragraph 26 of IPSAS 19 which states "no provision is recognized for costs that need to be incurred to continue an entity's ongoing activities in the future"; and
   (c) differentiate between ongoing and other emergency services. It proposed that ongoing emergency services would not give rise to a provision. It also proposed that emergency services delivered in response to specific emergencies could, in certain circumstances, give rise to present obligations and therefore provisions or contingent liabilities.

8. The ED proposed that all of the additional paragraphs (apart from the new definitions) be inserted as Application Guidance.

9. Although many respondents were broadly supportive of the proposals in ED 67, some of the XRB's comments and concerns were raised by other respondents, among other concerns. Issues noted by New Zealand constituents can be found in Appendix 3 of this memo.

10. *Collective and Individual Services*, as approved in December 2019:

    (a) defines collective services and individual services (no change to definitions in ED 67);

    (b) adds application guidance paragraphs to IPSAS 19, explaining collective services and individual services and how they differ from social benefits;

    (c) adds application guidance paragraphs to IPSAS 19, specifying that no provision is to be recognised for collective services or individual services before the services are delivered. The rationale is the same as that put forward in the ED – these are ongoing activities of a government and no provision is recognised for ongoing activities;

    (d) does **not** address emergency relief – this was a change to the proposals in the ED. Respondents raised a number of issues in relation to the proposed guidance on emergency relief, including the difficulty of distinguishing between emergency relief that is an ongoing activity of government and emergency relief provided in response to specific emergencies. The IPSASB agreed to consider doing more work on this topic when it develops its future work plans.

APPENDIX 2: XRB and New Zealand constituents' comments on ED 63 *Social Benefits* and the IPSASB's response

The table below sets out a summary of the XRB and New Zealand constituents' comments on ED 63 and the IPSASB's response. This analysis will be considered during the development of a PBE Standard using IPSAS 42 as a starting point.

Topic	Issue	IPSASB response[6]
Scope of ED 63 and definitions	We consider that there are no significant conceptual differences between the types of transactions that would fall within the scope of ED 63 and universally accessible services and collective services. **[XRB, Audit NZ and CAANZ]** The definitions of social benefits, social risks and universally accessible services are not clear **[CAANZ, XRB and Audit NZ]** Where expense transactions such as social benefits, collective services and universally accessible services have similar characteristics, a consistent approach for liability and expense recognition is required. **[XRB and CAANZ]** We agree with the proposal to scope out universally accessible services from ED 63. However, it is important there is a clear boundary between social benefits and universally accessible services given the similar characteristics of these benefits. If that boundary is not clear, this could give rise to implementation issues in determining when the standard applies. **[Audit NZ and CAANZ]** The scope of ED 63 is: • insufficiently clear • creates boundary issues with other standards (both current and proposed) • invites the possibility that transactions with similar economic substance will be treated differently. **[Treasury]**	IPSAS 42 makes no reference to "universally accessible services". As noted in the row below, the scope of IPSAS 42 has been limited to cash transfers, which eliminates the need to include a specific scope exclusion for universally accessible services. The IPSASB noted that defining social benefits as cash transfers would remove much of the confusion regarding the boundary between social benefits and universally accessible services. Collective and individual services are also, therefore, clearly out of scope of IPSAS 42.
Scope of ED 63 and definitions	Our preferred option is that a standard on social benefits would cover both cash benefits and services provided to beneficiaries. **[XRB]**	In response to some concerns from respondents, the IPSASB decided to clarify the scope and definitions in IPSAS 42. The IPSASB noted that respondents had different understandings of the scope and definitions in ED 63. Some respondents

[6] IPSASB responses were sourced from the relevant Basis for Conclusions and/or a comparison of the ED to the final pronouncement.

Topic	Issue	IPSASB response[6]
	The social benefit standard should be limited to non-reciprocated benefits paid in cash, either directly to beneficiaries or through third parties providing specified services to beneficiaries. **[Treasury]**	considered that social benefits were limited to cash transfers, whereas other respondents considered that social benefits included the provision of some services. The IPSASB concluded that the economic substance of cash transfers made to individuals and households was different to the economic substance of services provided to individuals and households. The IPSASB therefore decided that the scope of IPSAS 42 should be limited to cash transfers.
Scope of ED 63 and definitions	We disagree that social risks and other risks (e.g., earthquakes and flooding) are different. Governments do react to specific disasters, but they may also have standing benefits available for natural disasters. The concept of social risk is also not well understood by the accounting community in all jurisdictions and the interpretation of this term could lead to diversity in practice. **[XRB]**	The IPSASB noted that respondents to both the CP, *Recognition and Measurement of Social Benefits* and ED 63 had generally supported the reference to social risks. The IPSASB also remained of the view that governments' responses to social risks are often different to their response to other risks (see paragraph BC21(b) above). For these reasons, the IPSASB decided to retain the reference to social risks in the definition of social benefits.
The Insurance Approach	The Insurance Approach should not be optional. **[XRB, CAANZ, Audit NZ]** • The insurance approach should be required for schemes that are managed in the same way as insurance obligations, as the insurance approach aligns the reporting with the management of such schemes. If such schemes were permitted to use the obligating event approach this would result in material understatement of an entity's liabilities. **[XRB and CAANZ]** • It could be significantly misleading if an entity that meets the criteria of paragraph 9 were to present financial statements with significant assets for contributions invested but were to record minimal liabilities because the liability criteria of the obligating event approach were not met. **[Audit NZ]**	There were mixed views from respondents on whether or not the Insurance Approach should be optional. On balance, after considering the costs and benefits, the IPSASB decided to keep the Insurance Approach as optional. The IPSASB noted that this decision could be revisited at a future date, once entities have experience with applying IPSAS 42 and the Insurance Approach.
The Insurance Approach	We do not support the criterion that the social benefit scheme is intended to be fully funded from contributions **[XRB and CAANZ].** Although we agree that this would be a desirable characteristic of schemes (and in most cases the criterion would be satisfied by an entity wanting to use the insurance approach), we consider that how the entity manages the scheme is more important than whether or not it is fully funded. **[XRB]**	Most respondents to ED 63 agreed that the criteria for determining whether an entity was permitted to apply the insurance approach were appropriate. However, some respondents had doubts regarding the requirement that the social benefit scheme is intended to be fully funded from contributions.

Topic	Issue	IPSASB response[6]
	More guidance should be provided on the "fully funded by contributions" criterion (i.e., the Standard could be clarified further in relation to Government funding into a social benefit scheme on behalf of beneficiaries who are not in a position to contribute themselves). **[Audit NZ]** The criteria for determining the insurance approach do not allow an on-balance decision where the management and funding intentions are clearly to take an insurance approach, but where the criteria are not fully met, that the insurance approach can be taken. **[Treasury]**	The IPSASB agreed that where an entity made contributions on behalf of those who could not afford to do so, these should be treated as contributions and the scheme classified as being fully funded from contributions. The IPSASB has therefore included Application Guidance in IPSAS 42 to clarify this point.
The Insurance Approach	Certain aspects of IFRS 17 may not be appropriate in the public sector, i.e., • discount rates **[Audit NZ, CAANZ]** • risk adjustments **[Audit NZ, CAANZ and XRB]**	The IPSASB decided not to amend the requirements in IFRS 17 when applying that standard by analogy to social benefit schemes in IPSAS 42. One of the reasons for this is the time and cost involved in amending the requirements of IFRS 17. The IPSASB also noted that a number of standard setters were undertaking work relating to the application of discount rates. *XRB staff note: the NZASB will soon issue Insurance Contracts in the Public Sector, which amends PBE IFRS 17 Insurance Contracts. These amendments will ensure that PBE IFRS 17 is suitable for the public sector context in New Zealand. PBE IFRS 17 is aligned with NZ IFRS 17 Insurance Contracts, which in turn is aligned with IFRS 17 Insurance Contracts.*
The Obligating Event Approach	In the case of schemes which are managed in the same way as an insurer would manage its insurance contracts and which are substantially fully funded, we consider that it is appropriate to report both the assets and liabilities associated with that activity. In the case of other benefits which are not managed in this way and which are to be funded through future taxes, the recognition of large liabilities for social benefits, without the recognition of future cash flows that will fund those benefits, is unlikely to result in financial statements that meet the objectives of general purpose financial reporting and satisfy the qualitative characteristics. **[XRB]**	The IPSASB noted that there was no consensus about whether recognizing a large liability for social benefits without also recognizing an asset for the future taxation or contribution revenue that would fund the settlement of that liability would provide useful information. However, the long history of the IPSASB's work on social benefits suggested to the IPSASB that strong views held by stakeholders on both sides of the argument were unlikely to be changed by any further work at this stage. Consequently, the IPSASB agreed to proceed with the proposals in ED 63.
The Obligating Event Approach	The obligating event for all benefits where the meeting of eligibility criteria provides an entitlement to the benefit should be the meeting of eligibility criteria. If benefits are only paid to living persons (which may not always be the	Many respondents were concerned that "being alive" had been over-emphasised in ED 63.

Topic	Issue	IPSASB response[6]
	case) the application guidance should make clear that being alive is one of the eligibility criteria for determining an obligating event. We consider that being alive is a measurement criterion, not a recognition criterion. **[CAANZ]** Treasury does not see the relevance of reference to "the next benefit" – if benefits are settled in instalments, in advance or in arrears, that should not impact on the recognition point, therefore reference to the next benefit should be removed. **[Treasury]**	The IPSASB considered that in many cases, being alive would be an eligibility criterion, and that being alive would therefore affect recognition of a liability. The IPSASB acknowledged, however, that this might not always be the case, and that IPSAS 42 should reflect this. No changes to the Obligating Event Approach have been made with respect to reference to the "next benefit".
The Obligating Event Approach	The obligating event approach and Alternative View are at opposite ends of the spectrum. We consider that the obligating event approach as proposed is too narrow and is out of step with the recognition principles for other liabilities. **[CAANZ]** Overall, we can support the Obligating Event Approach as a reasonable and pragmatic outcome. However, we recommend that the rationale is further developed based on discussions around both views, and that recognition is supported by appropriate long-term fiscal sustainability information. **[CAANZ]**	The Basis for Conclusions in IPSAS 42 sets out a detailed examination of the Alternative View and why the IPSASB has decided to retain the Obligating Event Approach (renamed to the General Approach). As in ED 63, IPSAS 42 encourages, but does not require, preparation of general purpose financial reports that provide information on the long-term sustainability of the entity's finances. Reference is made to the guidance in RPG 1, *Reporting on the Long-Term Sustainability of an Entity's Finances*.
Disclosure	Some of the proposed requirements may increase the length of financial statements. We support the recent focus on trying to limit the length of financial statements and keep disclosures understandable and accessible. **[XRB]** The current focus of standard-setters is generally on reducing disclosures to avoid cluttering the financial statements with unnecessary information. As information about the benefits available, eligibility criteria and recent amendments must be widely known for citizens to be able to make claims, we question the benefit in replicating this information in the financial report. **[Treasury]** The IPSASB should consider including provisions for cross-referencing to other documents to avoid adding unnecessary length and clutter to financial reports. **[XRB and CAANZ]**	The IPSASB has decided to remove some of the disclosure requirements in ED 63, such as: • the proposed reconciliation of the opening and closing balances of liabilities for each social benefit scheme. • The proposed disclosure of future cash outflows (see below). Most respondents were supportive of the proposed disclosures, except for those noted above.
Disclosure	We do not support the requirement to disclose five years of projected cash outflows. We ask that the IPSASB reconsider whether this requirement	The IPSASB noted the concerns raised by respondents on the proposed disclosure of future cash outflows, in particular the

Topic	Issue	IPSASB response[6]
	satisfies the objective of the disclosures, as outlined in the IPSASB's Basis for Conclusions. **[Treasury]** With respect to the proposed disclosure of five years of projected cash outflows – financial statements report on the current financial position of the entity. The Treasury notes that this is budget forecast information. **[Treasury]**	concern that the disclosure would go beyond reporting on the current position of an entity. Consequently, the IPSASB agreed to remove the requirement to disclose future cash outflows.

APPENDIX 3: XRB and Audit New Zealand's comments on ED 67 *Collective and Individual Services and Emergency Relief* (amendments to IPSAS 19) and the IPSASB's response

The table below sets out a summary of the XRB and Audit New Zealand's comments on ED 67, the IPSASB's response and XRB staff comments. This analysis will be considered during the development of amendments to PBE IPSAS 19 using *Collective and Individual Services* as a starting point.

Issue	IPSASB response[7]
Where non-exchange expense transactions have similar characteristics, a consistent approach to liability and expense recognition is required. The IPSASB should consider the linkage between the ED and the current project on grants, contributions and other transfers. **[XRB]**	There are now two separate IPSAS which deal with non-exchange expenses: • IPSAS 42 *Social Benefits* • IPSAS 48 *Transfer Expenses* *Collective and Individual Services* amend IPSAS 19 in order to provide guidance on the accounting treatment of collective and individual services. *XRB staff note – consider whether additional guidance is required in New Zealand to assist entities in applying the various standards applying to non-exchange expenses.*
ED 67 proposes separate definitions of, and requirements and guidance on, "individual services" and "collective services", although the outcome appears to be the same. It is unclear whether this distinction has any practical impact. We disagree with the proposed definitions of collective services and individual services. Both definitions contain references to "address the needs of society as a whole" and this notion is one of the reasons the ED has distinguished between collective and individual services and emergency relief. There is no definition of, or guidance on, what is meant by "address the needs of society as a whole" in the context of collective and individual services. We note there is some discussion of this notion in paragraph AG8 of IPSAS 42, but that discussion is unclear and is only in the context of social benefits. **[XRB]**	The IPSASB considered that the fact that the nature of collective services is different from the nature of individual services meant that retaining separate definitions were appropriate. The IPSASB has not added further guidance on what is meant by "society as a whole". However, the IPSASB has removed the guidance relating to emergency relief (see last row in this table).
Although there is agreement on the accounting outcome in the ED, the rationale should be strengthened. **[XRB and Audit NZ]**	The rationale in *Collective and Individual Services* is the same as that put forward in ED 67 – these are ongoing activities of a government, and no provision is recognised for ongoing activities;

[7] IPSASB responses were sourced from the relevant Basis for Conclusions and/or a comparison of the ED to the final pronouncement.

Issue	IPSASB response[7]
This will assist in applying the provisions standard to other government funding decisions. **[Audit NZ]**	
The requirements on collective and individual services and emergency relief should be established within the body of IPSAS 19 **[XRB and Audit NZ]**	Guidance on determining whether a provision arises for collective and individual services remains in the Application Guidance section of IPSAS 19. Guidance relating to emergency relief has been removed (see above). *XRB staff note – when developing amendments to PBE IPSAS 19, we can consider putting this guidance in the core text.*
It would be helpful if the proposed guidance included discussion that entities that deliver collective services may need to recognise a provision under IPSAS 19 in connection with the delivery of collective services, such as for onerous contracts, rehabilitation obligations, or for restructuring. **[Audit NZ]**	*Collective and Individual Services* includes guidance stating that in some circumstances, binding arrangements that an entity enters into to acquire resources and incur expenses (to deliver collective services) may give rise to provisions, for example where a contract or other binding arrangement becomes onerous (but that these provisions relate to the binding arrangement and not to the intention to deliver individual and collective services to the public). This was not explicitly stated in ED 67.
Where emergency relief has similar characteristics to grants, we would expect a consistent and coherent approach to the accounting of such transactions. **[XRB]** The proposals for emergency relief are not sufficiently clear on what activities are caught by the emergency relief guidance and how that guidance applies – further guidance required. **[XRB and Audit NZ]** Provide more guidance on the distinction between (a) other forms of government assistance that are not part of the ongoing activities of the government and are not emergency relief provided in response to specific events and (b) individual and collective services. **[XRB]**	Respondents raised a number of issues in relation to the proposed guidance on emergency relief, including the difficulty of distinguishing between emergency relief that is an ongoing activity of government and emergency relief provided in response to specific emergencies. The IPSASB agreed to consider doing more work on this topic when it develops its future work plans. Therefore, the IPSASB has decided not to proceed with the guidance on emergency relief proposed in ED 67.

IPSASB

IPSAS® 42 Summary—*Social Benefits*

This summary provides an overview of IPSAS 42, *Social Benefits.*

Project objective: To define social benefits, and determine when expenses and liabilities for social benefits are recognized and how they are measured.

Approved: The International Public Sector Accounting Standards Board® (IPSASB®) approved IPSAS 42, *Social Benefits* in December 2018. It was issued in January 2019

Project History: The IPSASB initiated a project on social benefits in 2002, and issued the Invitation to Comment, *Accounting for Social Policies of Government* in 2004.

Subsequently, in 2008 the IPSASB issued Exposure Draft (ED) 34, *Social Benefits: Disclosure of Cash Transfers to Individuals or Households*, and a Consultation Paper (CP), *Social Benefits: Issues in Recognition and Measurement*.

The IPSASB did not reach a consensus on when a present obligation arises for social benefits within the scope of the CP, and decided to defer further work on this topic until the completion of the *Conceptual Framework* (which was issued in 2014).

Meanwhile, in 2013, the IPSASB published Recommended Practice Guideline (RPG) 1, *Reporting on the Long-Term Sustainability of an Entity's Finances*. This reflected the IPSASB's view that the financial statements cannot satisfy all of a user's information needs on social benefits. Further information about the long-term fiscal sustainability of those social benefit schemes is required.

The IPSASB issued a further CP, *Recognition and Measurement of Social Benefits*, in July 2015, followed by ED 63, *Social Benefits* (issued in October 2017).

IPSAS 42 is based on ED 63, but responds to comments received to that consultation.

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Why the IPSASB Undertook this Project

The purpose of the IPSASB's project on social benefits is to establish requirements for defining, recognizing and measuring social benefits.

The delivery of social benefits to the public is a primary objective of most governments, and accounts for a large proportion of their expenditure.

Prior to IPSAS 42, *Social Benefits*, IPSAS did not provide guidance on accounting for social benefits; IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*, excluded social benefit provisions in non-exchange transactions from its scope. The absence of such guidance was seen as one of the major gaps in the IPSASB's literature.

As a result, users may not have been able to obtain the information needed to evaluate the nature and financial effect of an individual social benefit scheme, or of the impact of social benefits on the finances of the government as a whole. IPSAS 42 addresses this need.

IPSAS 42 will enhance accountability and transparency, and increase comparability, which are in the public interest.

As well as building on the previous work of the IPSASB on social benefits, IPSAS 42 was influenced by more recent developments in the IPSASB's literature:

- *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*
- Recommended Practice Guideline 1, *Reporting on the Long-Term Sustainability of an Entity's Finances*
- Policy Paper, *Process for Considering GFS Reporting Guidelines during Development of IPSASs*

IPSAS 42 defines social benefits, and includes requirements for the recognition and measurement of social benefit schemes. IPSAS 42 also includes disclosure requirements that will provide additional information that users may need to evaluate the effect that social benefits have on a government's finances.

The IPSASB believes that IPSAS 42 will promote consistency and comparability in how social benefit schemes are reported by public sector entities.

As well as social benefits, governments also provide services, for example healthcare and defense. Such services are outside the scope of social benefits.

The IPSASB is addressing the accounting for these services as part of its non-exchange expenses project. ED 67, *Collective and Individual Services and Emergency Relief* (Amendments to IPSAS 19) was issued alongside IPSAS 42, to enable stakeholders to identify and account more consistently for the full range of social obligations of government.

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Scope of IPSAS 42

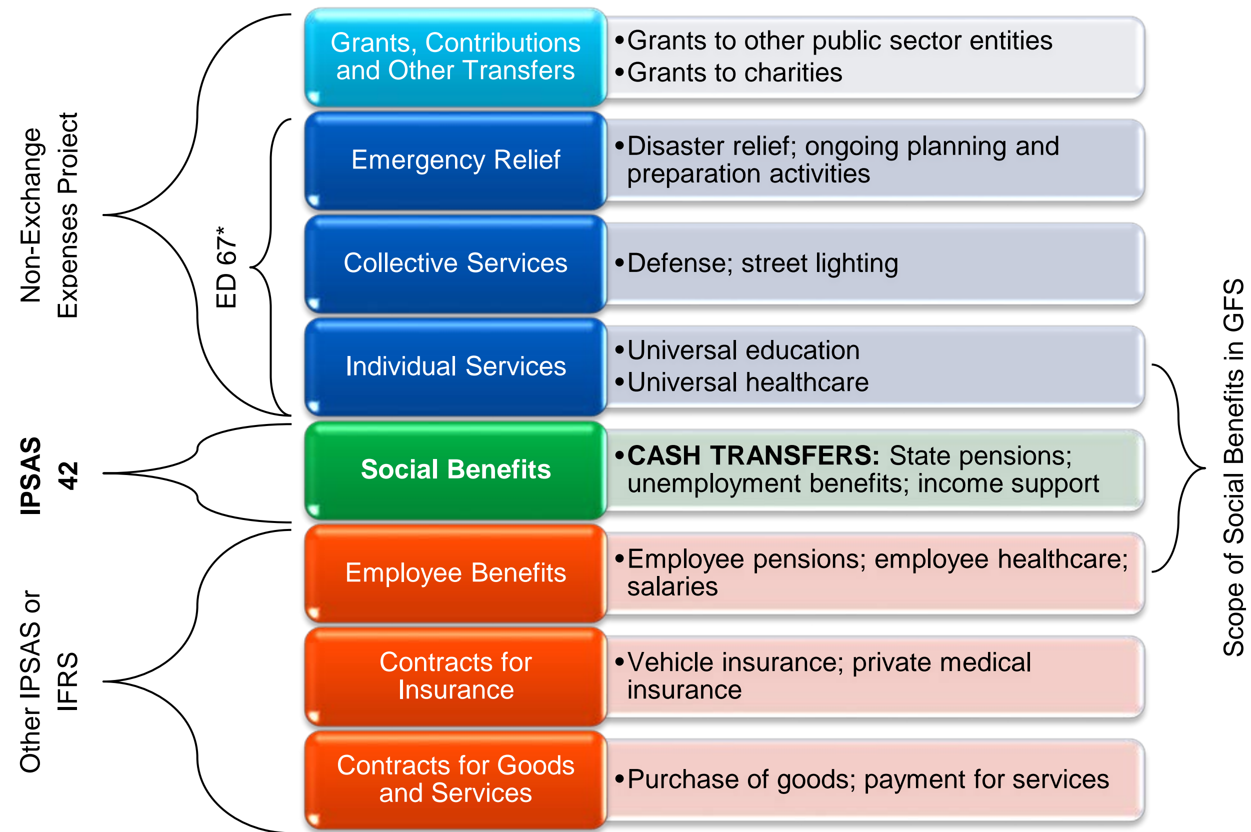
Figure 1 illustrates the scope of IPSAS 42 and the boundaries between social benefits and other transactions, with examples.

Where a transaction is outside the scope of IPSAS 42, Figure 1 indicates how IPSAS will address the transaction.

For many governments, alignment with Government Finance Statistics (GFS) is important. Figure 1 illustrates those transactions within the GFS scope of social benefits.

Transactions within the scope of ED 67, issued alongside IPSAS 42, are separately identified (within the non-exchange expenses project).

Figure 1: Scope of IPSAS 42



* **ED 67, *Collective and Individual Services and Emergency Relief* (Amendments to IPSAS 19)** was issued on January 31, 2019, alongside IPSAS 42.

Definitions

IPSAS 42 defines social benefits and social risks

Definitions in IPSAS 42

Social benefits are cash transfers provided to:

(a) Specific individuals and/or households who meet eligibility criteria;

(b) Mitigate the effect of social risks; and

(c) Address the needs of society as a whole.

Social risks are events or circumstances that:

(a) Relate to the characteristics of individuals and/or households – for example, age, health, poverty and employment status; and

(b) May adversely affect the welfare of individuals and/or households, either by imposing additional demands on their resources or by reducing their income.

Reasons for Changes to Social Benefits Definition since ED 63, *Social Benefits*

ED 63 specifically excluded collective services and universally accessible services (referred to as individual services in ED 67) from the scope of social benefits. Most respondents supported this scope.

However, respondents considered it important that the boundary between social benefits and individual services was clearly defined; and that the accounting treatments for social benefits and individual services should have the same conceptual basis. Any differences in treatment should relate to the different nature of the transactions.

This meant that respondents considered that the scope and definitions needed to be further clarified to avoid confusion.

The IPSASB agreed to clarify the boundary by defining social benefits as cash transfers in IPSAS 42.

General Approach: Recognition

The General Approach in IPSAS 42 includes a single recognition point for all social benefits.

Under the General Approach, a liability for a social benefit is recognized when the eligibility criteria to receive the next social benefit have been satisfied.

The General Approach does not include requirements for social contributions (revenue received in relation to a social benefit scheme). Social contributions are accounted for in accordance with IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*.

Recognition

A liability is a present obligation for an outflow of resources that results from a past event.

The key factor in determining when a liability for a social benefit arises is identifying the past event.

Under the General Approach, the past event that gives rise to a liability is the satisfaction by the beneficiary of all eligibility criteria for the provision of the next social benefit.

The satisfaction of eligibility criteria for each social benefit payment is a separate past event.

Being alive at the point at which the eligibility criteria are required to be satisfied may be an eligibility criterion, whether explicitly stated or implicit. This depends on the characteristics of each individual social benefit scheme.

Recognition Examples

Examples of when a beneficiary may first satisfy all the eligibility criteria for the provision of the next social benefit include:

- Reaching retirement age (in the case of a retirement pension);
- The death of a partner (in the case of a survivor benefit);
- Becoming unemployed (in the case of an unemployment benefit without a waiting period);
- Being unemployed for a specified period (in the case of an unemployment benefit with a waiting period).

Changes since ED 63

Some respondents to ED 63 were concerned that 'being alive' had been over-emphasized. They considered that there were circumstances where reliance on being alive would be inappropriate.

The IPSASB considered that being alive would often be an eligibility criterion, and, in such cases, would therefore affect recognition of a liability. The IPSASB acknowledged, however, that this might not always be the case, and that IPSAS 42 should reflect this.

Review of IPSAS 42

The IPSASB noted that experience of applying IPSAS 42 may provide further evidence of the extent to which the approach meets users' needs. Given the importance of the area, it concluded that a post-implementation review of IPSAS 42 may be appropriate at some point in the future.

General Approach: Measurement

Under the General Approach, expenses are measured at an amount equivalent to the amount of the liability.

The liability for a social benefit scheme is measured at the best estimate of the costs that the entity will incur in fulfilling the present obligations represented by the liability.

Measurement of Expense

An entity recognizes an expense for a social benefit scheme, measured at the amount of the next payment following satisfaction of the eligibility criteria; discounting of the expense will not be required for most social benefits.

Where the entity makes a social benefit payment prior to all eligibility criteria for the next payment being satisfied, it measures the payment in advance (or expense recognized where the payment is irrecoverable) at the amount of the cash transferred.

Measurement of Liability

Under IPSAS 42, the liability for a social benefit scheme is measured at the best estimate of the costs that the entity will incur in fulfilling the present obligations represented by the liability.

In this context, "costs" means the social benefit payments to be made (i.e., the cash transfers). The costs do not include other elements such as administrative costs and bank charges.

Because the satisfaction of eligibility criteria for each social benefit payment is a separate past event, the liability is for the next payment only. Consequently, liabilities in respect of social benefits will usually be short-term liabilities. As a result, an entity will often know the amounts involved without needing to make estimates. Similarly, because liabilities in respect of social benefits will usually be short-term liabilities, discounting will not be required for most social benefits.

Subsequent Measurement

The liability is reduced as social benefit payments are made. Any difference between the cost of making the social benefit payments and the carrying amount of the liability is recognized in surplus or deficit in the period in which the liability is settled.

Where a liability is discounted the liability is increased and interest expense recognized in each reporting period to reflect the unwinding of the discount.

Where a liability has yet to be settled, the liability is reviewed at each reporting date, and adjusted to reflect the current best estimate of the social benefit payment required to fulfill the liability.

General Approach: Disclosures

The General Approach requires entities to disclose information that:

(a) Explains the characteristics of its social benefit schemes; and

(b) Explains the demographic, economic and other external factors that may affect its social benefit schemes

Paragraphs 45–47 of IPSAS 1, *Presentation of Financial Statements*, provide guidance on materiality and aggregation. Entities may wish to consider these paragraphs when preparing their disclosures.

Characteristics of social benefit schemes

- The nature of the social benefits provided by the schemes (for example, retirement benefits, unemployment benefits, child benefits).
- Key features of the social benefit schemes, such as a description of the legislative framework governing the schemes, and a summary of the main eligibility criteria that must be satisfied to receive the social benefits.
- A description of how the schemes are funded, including whether the funding for the schemes is provided by means of a budget appropriation, a transfer from another public sector entity, or by other means.
- Where a scheme is funded by social contributions:
  - A cross reference to the location of information about those social contributions and any dedicated assets (where included in the entity's financial statements); or
  - A statement regarding the availability of information on those social contributions and any dedicated assets in another entity's financial statements.

Demographic, economic and other external factors

- A description of the key demographic, economic and other external factors that influence the level of expenditure under the social benefit schemes.

Other Disclosure Requirements

- The total expenditure on social benefits recognized in the statement of financial performance, analyzed by social benefit scheme.
- A description of any significant amendments to the social benefit schemes made during the reporting period, along with a description of the expected effect of the amendments. Amendments to a social benefit scheme include:
  - Changes to the level of social benefits provided; and
  - Changes to the eligibility criteria, including the individuals and/or households covered by the social benefit scheme.
- If a social benefit scheme satisfies the criteria to permit the use of the insurance approach, a statement to that effect.

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Alternative Insurance Approach

IPSAS 42 includes the insurance approach as a possible alternative approach. Entities are permitted, *but not required*, to use this approach where a social benefit scheme meets certain criteria.

IPSAS 42 does not include requirements for the insurance approach, but directs entities to apply relevant international or national accounting standards by analogy.

Criteria for Using the Insurance Approach

IPSAS 42 permits entities to use the insurance approach where:

- The social benefit scheme is intended to be fully funded from contributions; and
- There is evidence that the entity manages the scheme in the same way as an issuer of insurance contracts, including assessing the financial performance and financial position of the scheme on a regular basis.

IPSAS 42 includes guidance on how to determine whether a social benefit scheme is intended to be fully funded from contributions.

IPSAS 42 also includes indicators to assist entities in determining whether they are managing a scheme in the same way as an issuer of insurance contracts.

Which Insurance Standards?

Within the insurance approach section of IPSAS 42, the term "the relevant international or national accounting standard dealing with insurance contracts" refers to IFRS 17, *Insurance Contracts*, and national standards that have adopted substantially the same principles as IFRS 17.

IFRS 17 has adopted principles for accounting for insurance contracts that, when applied by analogy to social benefit schemes, will provide information that meets users' needs and satisfies the qualitative characteristics.

This may not be the case for other accounting standards dealing with insurance contracts. Consequently, IPSAS 42 does not allow an entity to apply by analogy an insurance standard that has not adopted substantially the same principles as IFRS 17.

Disclosures

Where an entity has elected to use the insurance approach, IPSAS 42 requires the entity to make the following disclosures:

- The basis for determining that the insurance approach is appropriate;
- The information required by the international or national accounting standard dealing with insurance contracts;
- Information about the characteristics of its social benefit schemes; and
- A description of any significant amendments to the social benefit scheme made during the reporting period.

Effective Date, Project History and Changes since ED 63, *Social Benefits*

The effective date of IPSAS 42 is January 1, 2022.

Effective Date

The effective date of IPSAS 42 is January 1, 2022, with earlier adoption encouraged.

The IPSASB selected this effective date in part because it expects to be able to finalize the proposed amendments included in ED 67, *Collective and Individual Services and Emergency Relief* (Amendments to IPSAS 19) in time for those amendments to have the same effective date.

Governments and other public sector entities that provide social benefits, individual services and collective services will, therefore, be able to introduce new accounting policies for these transactions at the same time. This responds to concerns raised by stakeholders commenting on the proposals in ED 63.

Project History

To learn more about the project history, and to view the consultation documents and responses, please visit: [http://www.ipsasb.org/projects/social-benefits.](http://www.ipsasb.org/projects/social-benefits)

Changes since ED 63, *Social Benefits*

The most notable changes between ED 63 and IPSAS 42 are summarized in the table below:

Section	Changes
Definitions	• The definition of **Social Benefits** was clarified to focus on cash transfers. • The definition of **Universally Accessible Services** was removed.
General Approach	• The **Obligating Event Approach** was renamed. • The emphasis on **being alive** was reduced; but being alive is still seen as important. • The wording has been amended to clarify that the liability is for the **next social benefit payment**. • The disclosure requirements in respect of the **reconciliation of the social benefit liability** and the **best estimate of the undiscounted projected cash outflows** were removed.

IPSASB

Summary—*Collective and Individual Services* (Amendments to IPSAS 19)

This summary provides an overview of *Collective and Individual Services* (Amendments to IPSAS 19).

Project objective:

Collective and Individual Services (Amendments to IPSAS 19) addresses transactions for collective and individual services. Transfers such as grants and contributions will be addressed in a subsequent ED.

Approved

The International Public Sector Accounting Standards Board® (IPSASB®) approved *Collective and Individual Services* (Amendments to IPSAS 19) in September 2019. It was issued in January 2020

Project History

The IPSASB initiated a project on social benefits in 2002, and issued the Invitation to Comment (ITC), *Accounting for Social Policies of Governments* in 2004. This ITC covered collective and individual services as well as social benefits.

The IPSASB subsequently agreed to narrow the scope of its work on social benefits. Collective and individual services were next addressed as part of the IPSASB's Consultation Paper (CP), *Accounting for Revenue and Non-Exchange Expenses*, issued in August 2017.

The IPSASB issued Exposure Draft (ED) 67, *Collective and Individual Services and Emergency Relief* (Amendments to IPSAS 19) in January 2019.

Collective and Individual Services (Amendments to IPSAS 19) is based on ED 67, but responds to comments received to that consultation, principally by excluding requirements in respect of emergency relief.

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Why the IPSASB Undertook this Project

The purpose of the IPSASB's project on non-exchange expenses is to develop new or amended standards that provide recognition and measurement requirements applicable to providers of non-exchange transactions, except for social benefits.

Collective and Individual Services (Amendments to IPSAS 19) includes requirements for collective and individual services, a significant subset of those transactions.

Collective and Individual Services (Amendments to IPSAS 19) forms part of the IPSASB's broader non-exchange expenses project.

While a number of IPSAS provide guidance on the recognition of specific exchange expenses and liabilities, there is very little guidance on the recognition of expenses and liabilities arising from non-exchange transactions; and no equivalent to IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*, which deals with non-exchange revenue. As a consequence, there is ambiguity and inconsistency in developing accounting policies in a highly significant area of expenditure, including the provision of major services to the community and transfers between different levels of government.

The objective of the non-exchange expenses project is to develop new or amended standards, in order to provide accounting requirements that result in consistent accounting for non-exchange expense transactions.

The first step in the development of accounting requirements for non-exchange expenses was the publication of the CP, *Accounting for Revenue and Non-Exchange Expenses*, issued in August 2017.

In the CP, the IPSASB explained the drivers behind the development of the revenue and non-exchange expenses projects. For the non-exchange expenses project, these included:

- The operationalization of the exchange versus non-exchange distinction; and consideration of whether to replace this with a focus on whether transactions include a performance obligation.
- The gap in the current IPSASB literature on accounting for non-exchange expenses which may lead to ambiguity and inconsistency of accounting policies in a highly significant area of expenditure.
- The scope for ensuring consistency of approaches between resource providers (for non-exchange expense transactions) and resource recipients (for revenue transactions).

The CP also noted that the IPSASB's definition of social benefits excludes areas such as the universal provision of healthcare and education, therefore making the development of requirements and guidance for these areas and others not within the scope of IPSAS 42, *Social Benefits,* more pressing. For this reason, the IPSASB has now issued specific guidance on these issues in *Collective and Individual Services* (Amendments to IPSAS 19).

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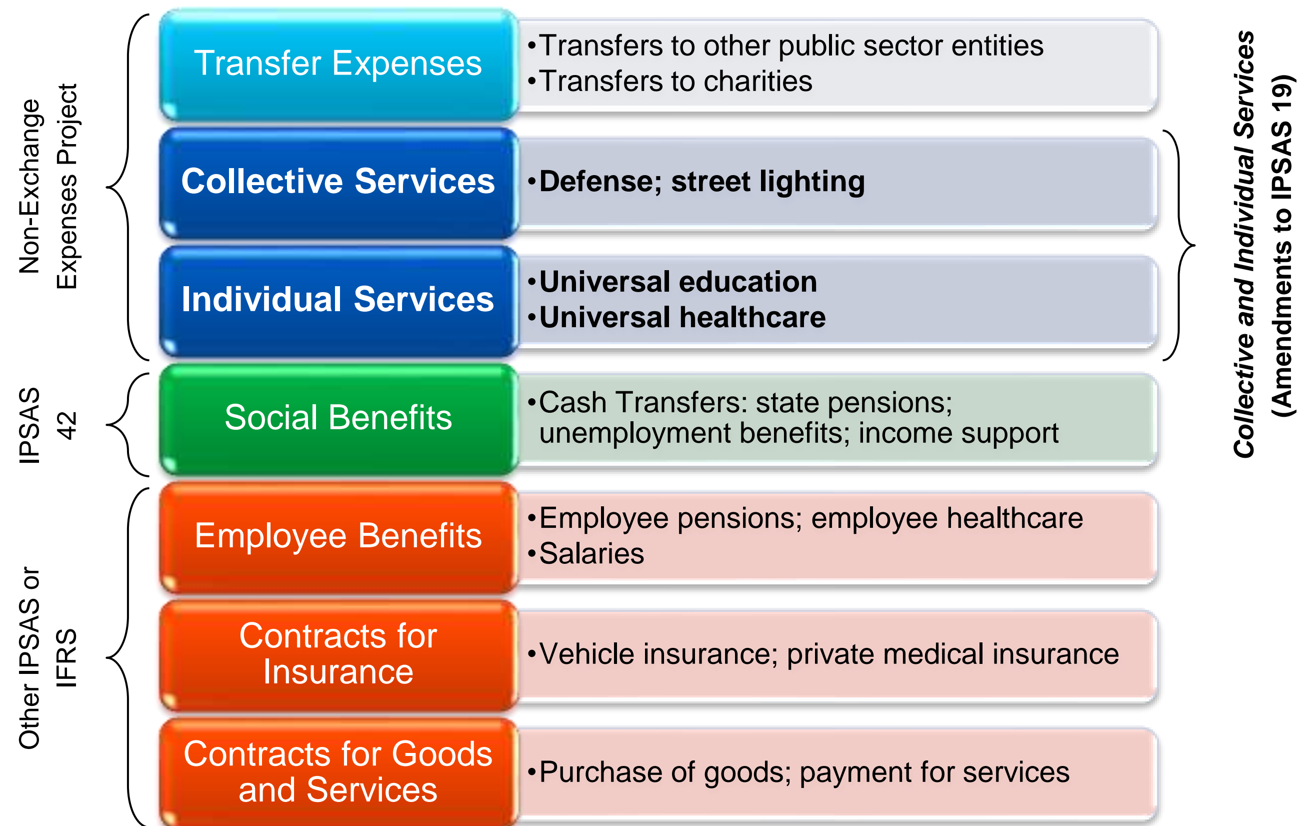
Scope of *Collective and Individual Services* (Amendments to IPSAS 19)

Figure 1 illustrates the scope of *Collective and Individual Services* (Amendments to IPSAS 19) and the boundaries between collective and individual services and other transactions.

Collective and Individual Services (Amendments to IPSAS 19) complements IPSAS 42, *Social Benefits*.

Transfers such as grants and contributions will be addressed in ED 72, *Transfer Expenses*, which the IPSASB approved in December 2019.

Figure 1: Scope of *Collective and Individual Services* (Amendments to IPSAS 19)



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Definitions

Collective and Individual Services (Amendments to IPSAS 19) provides definitions for collective and individual services.

Figure 2 illustrates the relationship between collective services, individual services and social benefits. All these transactions address the needs of society as a whole.

Definitions of Collective Services and Individual Services

Collective services are services provided by a public sector entity simultaneously to all members of the community that are intended to address the needs of society as a whole.

Individual services are goods and services provided to individuals and/or households by a public sector entity that are intended to address the needs of society as a whole.

Figure 2:
Relationship between collective services, individual services and social benefits

	Social Benefits	Individual Services	Collective Services
Involves a cash transfer to eligible beneficiaries?	✓	✗	✗
Provided to individuals and/or households, rather than to a community?	✓	✓	✗
Intended to address the needs of society as a whole?	✓	✓	✓

IPSASB

Accounting for Collective Services and Individual Services

Under *Collective and Individual Services* (Amendments to IPSAS 19), no provision is recognized for a government's intention to provide collective services or individual services.

Information about collective services and individual services is presented and disclosed in accordance with other IPSAS.

Accounting for Collective Services

Under *Collective and Individual Services* (Amendments to IPSAS 19), collective services are considered to be ongoing activities of the public sector entity that delivers the services.

In accordance with IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*, "no provision is recognized for costs that need to be incurred to continue an entity's ongoing activities in the future".

Consequently, under *Collective and Individual Services* (Amendments to IPSAS 19), no provision is recognized for the intention to deliver collective services.

In delivering collective services, a public sector entity acquires resources and incurs expenses through contractual and other binding arrangements. Examples include the salaries paid to defense staff, the electricity used in delivering street lighting, the acquisition of non-current assets used in delivering those services, and the purchase of collective services from a third-party provider.

Under *Collective and Individual Services* (Amendments to IPSAS 19), these contractual and other binding arrangements would be accounted for in accordance with other IPSAS.

Accounting for Individual Services

Collective and Individual Services (Amendments to IPSAS 19) similarly considers that the delivery of individual services is an ongoing activity of the public sector entity that provides the services. The delivery of individual services results in the public sector entity acquiring resources and incurring expenses through contractual and other binding arrangements. Under *Collective and Individual Services* (Amendments to IPSAS 19), these contractual and other binding arrangements would be accounted for in accordance with other IPSAS.

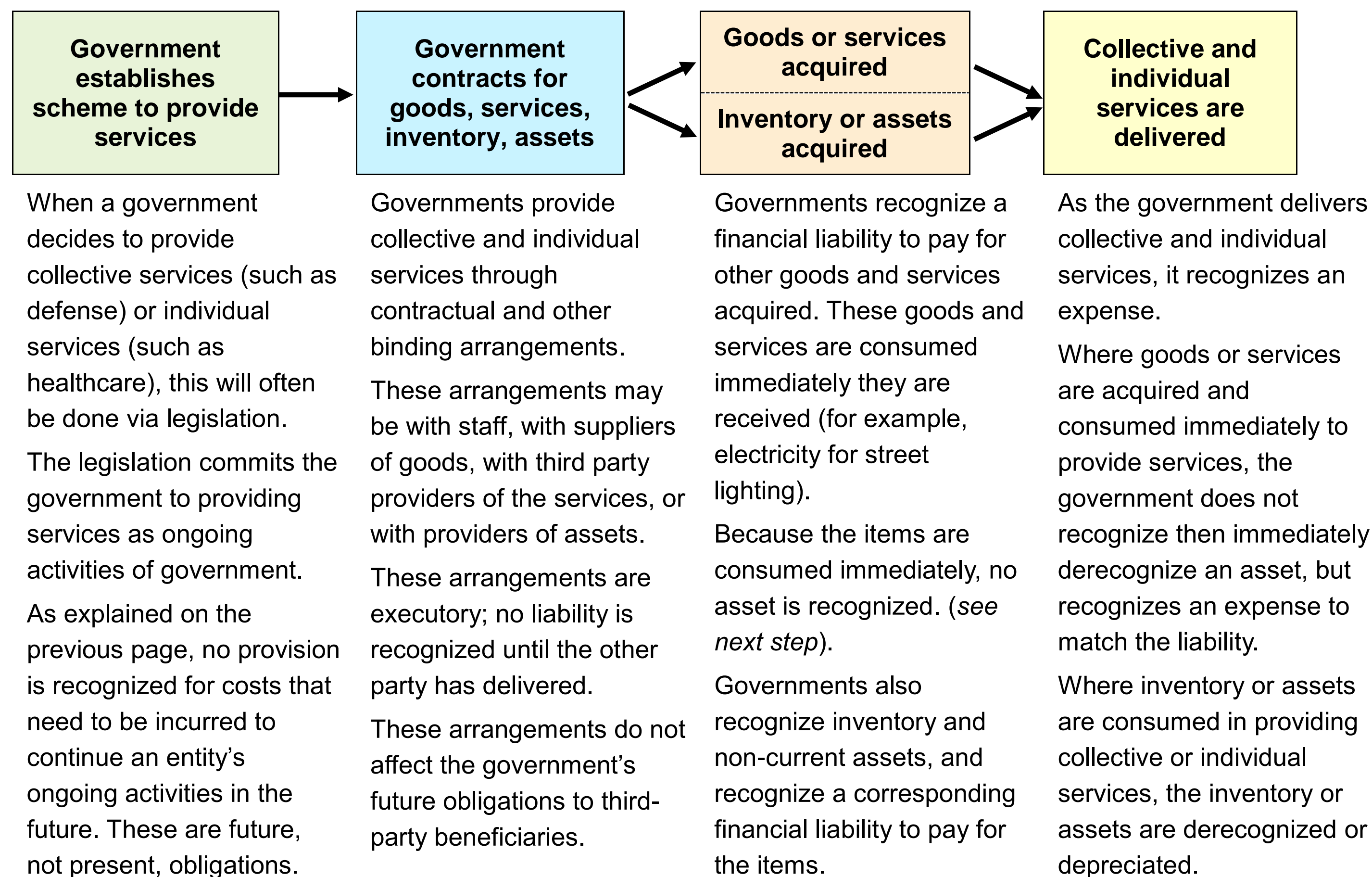
The public sector entity uses the resources acquired to deliver individual services. Where individuals access these services, the entity may have a number of future obligations relating to the delivery of these individual services. However, these obligations are not present obligations and do not give rise to a liability.

As with collective services, no provision is recognized for the intention to deliver individual services prior to individuals and/or households accessing the services.

Interaction of Provisions and Contractual and Other Binding Arrangements in Accounting for Collective and Individual Services

Figure 3 illustrates the interaction of provisions and contractual and other binding arrangements in accounting for collective and individual services, and explains why *Collective and Individual Services* (Amendments to IPSAS 19) states that no provision is recognized for collective services or individual services.

Figure 3: Interaction of Provisions and Contractual and Other Binding Arrangements



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Effective Date, Project History and Exclusion of Emergency Relief

The effective date of *Collective and Individual Services* (Amendments to IPSAS 19) is January 1, 2022.

Early application is permitted, provided IPSAS 42, *Social Benefits*, is applied at the same time.

Effective Date

The effective date of *Collective and Individual Services* (Amendments to IPSAS 19) is January 1, 2022, with earlier adoption encouraged, provided IPSAS 42, *Social Benefits* is applied at the same time.

The IPSASB selected this effective date so that these amendments have the same effective date as IPSAS 42.

Governments and other public sector entities that provide social benefits, individual services and collective services will, therefore, be able to introduce new accounting policies for these transactions at the same time. This responds to concerns raised by stakeholders.

Project History

To learn more about the project history, and to view the consultation documents and responses, please visit: http://www.ipsasb.org/projects/non-exchange-expenses.

Exclusion of Emergency Relief

ED 67, *Collective and Individual Services and Emergency Relief* (Amendments to IPSAS 19), included proposals for accounting for emergency relief. While many respondents were supportive of providing such guidance, several issues were raised. Respondents considered that a definition of emergency relief would be required, notwithstanding the fact that the diverse practices across jurisdictions makes this difficult. Respondents also questioned whether the proposed distinction between emergency relief that is an ongoing activity of government and emergency relief provided in response to specific emergencies was appropriate, and whether it could be applied consistently. Respondents further questioned how other assistance that did not fall within the scope of emergency relief should be accounted for.

In light of these concerns, the IPSASB decided not to proceed with the guidance on emergency relief proposed in ED 67. The IPSASB decided to consider the topic in developing its Mid-Term Work Program Consultation 2021.

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EXTERNAL REPORTING BOARD

Agenda Item 4.1

Memorandum

Date:	16 June 2023
To:	NZASB Members
From:	Gali Slyuzberg and Charis Halliday
Subject:	**IPSASB Measurement: Project update**

COVER SHEET

Project priority and complexity

Project priority	**Medium** IPSAS 46 *Measurement* and the related new pronouncements: • align the fair value measurement requirements in IPSAS with IFRS 13 *Fair Value Measurement;* and • introduce a new public sector-specific measurement basis, current operational value (COV). The impact of the above changes for New Zealand PBEs is expected to depend mainly on the extent of the difference in practice between measurement using 'depreciated replacement cost' as per the existing PBE IPSAS 17, and measurement at COV.
Complexity of Board decision-making at this meeting	**Low** This item is a project update – the Board is not being asked to make decisions at this stage.

Overview of agenda item

Project status	• Pre-project update
Project purpose	• The IPSASB's objectives in issuing IPSAS 46 *Measurement* and related pronouncements was to improve measurement guidance across IPSAS, by providing detailed guidance on commonly used measurement bases and the circumstances in which they should be used. This resulted in the alignment of fair value measurement with the requirements of IFRS 13, and the introduction of COV as a new measurement basis. • As PBE Standards are primarily based on IPSAS, we are considering the incorporation of these standards into PBE Standards.
Board action required at this meeting	The Board is asked to NOTE the project update. If Board Members are aware of issues that could arise in practice from the application of COV in New Zealand, please let staff know.

Purpose and introduction[1]

1. In May 2023, the IPSASB issued IPSAS 46 *Measurement*, which defines and provides guidance of key measurement bases in the public sector. The key changes introduced by IPSAS 46 is the alignment of fair value measurement requirements in IPSAS with those in IFRS 13 *Fair Value Measurement*, and the introduction of a new public sector-specific measurement basis: current operational value (COV).

2. At the same time, the IPSASB also issued updates to the measurement-related chapter of its Conceptual Framework, as well as an updated standard on property, plant and equipment – to reflect the introduction of COV and the changes to fair value measurement.

3. The purpose of this project is to update the Board on the New Zealand project relating to the new measurement-related IPSASB pronouncements.

Recommendation

4. We recommend that the Board NOTES this project update.

Background

5. The IPSASB's *Measurement* project began in 2017, with the rationale that measurement requirements in IPSAS should be amended to better align them with the Conceptual Framework's measurement concepts. The project's objectives were to:

   (a) Provide more detailed guidance on the implementation of commonly used measurement bases, and the circumstances under which these measurement bases will be used;

   (b) Address transaction costs and borrowing costs; and

   (c) Where necessary, issue amended IPSAS with revised requirements for measurement at initial recognition, subsequent measurement, and measurement-related disclosure.

6. As part of its Measurement project, in 2019 the IPSASB consulted on the Consultation Paper *Measurement*. Following this consultation, in 2021 the IPSASB consulted on a group of measurement-related Exposure Drafts (EDs).

7. The IPSASB received the following feedback on the above consultations:

   (a) Respondents to the *Measurement* Consultation Paper and *Measurement* Exposure Draft strongly supported adding an exit-based definition of fair value as a measurement basis to the Conceptual Framework and aligning fair value in IPSAS with the concepts in IFRS 13 *Fair Value Measurement*.

   (b) However, respondents identified challenges in applying fair value as aligned with IFRS 13 in the public sector – particularly for assets that are held for their operational capacity (i.e. to provide a service), as is often the case in the public sector. Stakeholders noted that

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for such assets, the following IFRS 13-based fair value measurement concepts would cause challenges:

(i) The requirement to measure fair value based on the asset's *highest and best use*; and

(ii) The requirement to measure fair value based on *market participants' assumptions* and maximise the use of market participant data.

8. The IPSASB responded to this concern by aligning fair value measurement requirements with IFRS 13, and developing current operational value (COV) – a public sector specific measurement basis, for measuring assets that are held for their operational capacity.

9. The project culminated in the issuance of the following pronouncements in May 2023:

(a) Updated Conceptual Framework: Chapter 7, Measurement of Assets and Liabilities in Financial Statements;

(b) IPSAS 45 *Property, Plant, and Equipment*, and

(c) IPSAS 46 *Measurement*.

10. IPSAS 45 and IPSAS 46 are required to be applied for periods beginning on or after 1 January 2025. Given that the IPSAS Conceptual Framework does not establish authoritative requirements for financial reporting by entities that apply IPSAS, the updates to the Measurement chapter of the Conceptual Framework do not have an 'effective date' – but the IPSASB started applying this updated chapter immediately upon issue.

Summary of IPSAS 46 Measurement and related pronouncements

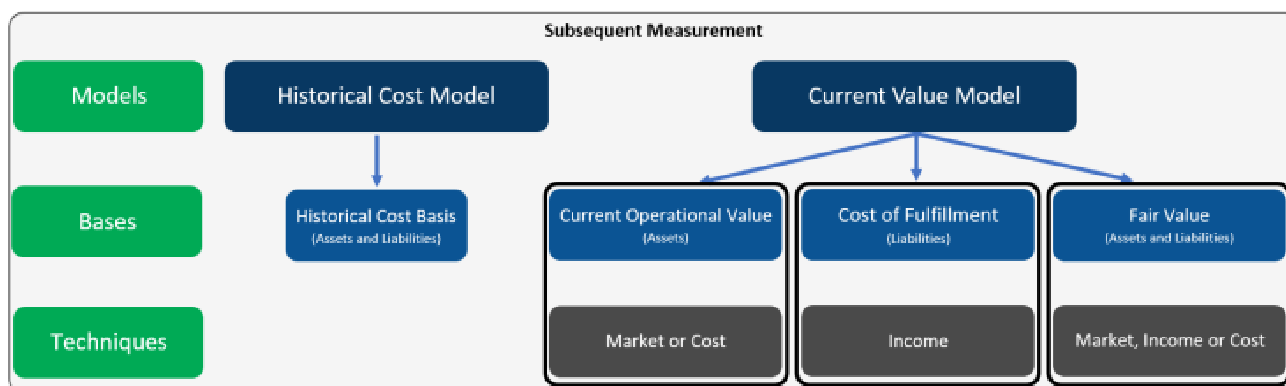
Updated Chapter 7 of the Conceptual Framework

11. The updated Chapter 7 of the IPSASB Conceptual Framework includes a subsequent measurement framework, which clarifies the approach to the measurement of assets and liabilities subsequent to initial recognition in IPSAS. The Conceptual Framework explains the relationship between different aspects of measurement – measurement models, measurement bases and measurement techniques.

12. The subsequent measurement guidance in the Conceptual Framework focuses on four key measurement bases: historical cost, cost of fulfilment, fair value – and the newly-introduced COV. The Conceptual Framework includes the definition of these bases and discusses when it is appropriate to apply these bases.

13. The subsequent measurement framework is shown on the next page.

Figure 1 Subsequent measurement framework



IPSAS 46 Measurement

14. The objective of IPSAS 46 *Measurement* is "to define measurement bases that assist in reflecting fairly the cost of services, operational capacity and financial capacity of assets and liabilities". IPSAS 46 "identifies approaches under those measurement bases to be applied through individual IPSAS to achieve the objectives of financial reporting".

15. IPSAS 46 defines the measurement bases shown in Figure 1 above and provides guidance on the application of these measurement bases – including in relation to the measurement techniques that are appropriate to use under each measurement basis.

16. The definition of the measurement bases covered by IPSAS 46 are shown below.

Measurement basis	Definition
Historical cost	The consideration given to acquire, construct, or develop an asset plus transaction costs, or the consideration received to assume a liability minus transaction costs, at the time the asset is acquired, constructed or developed, or the liability is incurred.
Cost of fulfilment	The costs that the entity will incur in fulfilling the obligations represented by the liability, assuming that it does so in the least costly manner.
Current operational value	The amount the entity would pay for the remaining service potential of an asset at the measurement date.
Fair value	The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

17. It is useful to note the following key aspects of COV measurement:

(a) COV is an *entity-specific* measurement basis – as opposed to fair value, which explicitly requires consideration of market participants' assumptions;

(b) COV is an *entry price* – as opposed to fair value, which is now explicitly an exit price.

(c) COV is based on the asset's *existing use* – as opposed to fair value, which is based on an asset's highest and best use.

IPSAS 45 Property, Plant and Equipment

18. IPSAS 45 replaces IPSAS 17 *Property, Plant and Equipment*, and reflects the introduction of the COV measurement basis.

19. Under IPSAS 45, an entity may choose either the cost model or the current value model (previously known as 'revaluation model') for measuring an item of property, plant and equipment (PP&E) after initial recognition. When the current value model is chosen, an entity uses COV for assets that are held for their operational capacity, and fair value for assets that are held for their financial capacity.

IPSASB 'at a glance' summaries

20. The IPSASB's summaries of the abovementioned pronouncements are available through the links below:

    (a) Summary of IPSAS 46 *Measurement* and Chapter 7 of the Conceptual Framework

    (b) Summary of IPSAS 45 *Property, Plant and Equipment*

Current measurement-related developments

21. We note that the IPSASB is currently undertaking 'Phase 2' of the Measurement project – whereby the IPSASB is considering the applicability of COV to individual IPSAS (other than IPSAS 45, which already refers to COV). This project will also include limited-scope projects on IPSAS 21 *Impairment of Non-Cash-Generating Assets* and IPSAS 31 *Intangible Assets*, with respect to measurement-related matters. An IPSASB ED is expected in December 2023, with a final pronouncement expected in December 2024.

Plans relating to the application of the PBE Policy Approach

22. Now that the IPSASB has issued IPSAS 46 and IPSAS 45 (and the measurement-related updates to the Conceptual Framework), the Board will need to decide whether to propose the incorporation of these standards into PBE Standards (and the PBE Conceptual Framework) in New Zealand.

23. The PBE Policy Approach notes the following: "There is a rebuttable presumption that the NZASB will adopt a new or amended IPSAS". The PBE Policy Approach also includes factors to consider when deciding on whether to amend the requirements of an IPSAS when adopting these requirements into PBE Standards.

24. Before asking the Board to decide whether the rebuttable presumption should apply to the IPSASB's newly-issued measurement-related pronouncements, and the extent to which

amendments to the IPSAS requirements should be considered, we think it is important to first ascertain the extent of the difference in practice between:

(a) Measurement using the new COV basis, and;

(b) Measurement using 'depreciated replacement cost' under the existing PBE IPSAS 17 *Property, Plant and Equipment* – which we understand is commonly used by New Zealand PBEs.

25. We think it is important to understand the above because we expect this to be a key driver of the extent of the impact of incorporating the IPSASB's measurement-related pronouncements into PBE Standards.

26. We plan to discuss the above matter with valuers at a high level, and to inform the Board of the results of our discussion at the August meeting. Further work with valuers following this discussion may be required. We think that a comparison between COV and 'depreciated replacement cost' would be important for informing the Board's decision on the application of the PBE Policy Approach.

27. Consequently, we plan to ask the Board to consider the application of the PBE Policy Approach to the IPSASB's measurement-related pronouncements at the August 2023 meeting. We note that one of the options when considering the application of the PBE Policy Approach would be to defer the decision on whether to incorporate the pronouncements into PBE Standards until Phase 2 of the IPSASB Measurement project is completed.

28. We welcome any feedback Board Members have in the meantime regarding expected practical challenges, if any, relating to the application of COV if this were to be required in New Zealand.

Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Agenda Item 6A.1

Memorandum

Date: 16 June 2023

To: NZASB Members

From: Jamie Cattell

Subject: **Board memo – Supplier Finance Arrangements**

COVER SHEET

Project priority and complexity

Project priority	**Low** This is a narrow scope, disclosure-only amending standard which is likely to have limited applicability.
Complexity of Board decision-making at this meeting	**Low** *Supplier Finance Arrangements* amends NZ IAS 7 and NZ IFRS 7 and is identical in substance to *Supplier Finance Arrangements (Amendments to IAS 7 and IFRS 7)* issued by the International Accounting Standards Board (IASB). The Board is also being asked to agree to further consideration of RDR concessions for the new disclosures established in *Supplier Finance Arrangements* and whether to commence development of equivalent amendments to the PBE Standards.

Overview of agenda item

Project status	Approval – we are seeking approval to issue *Supplier Finance Arrangements*
Project purpose	To increase transparency of supplier finance arrangements and their effects on an entity's liabilities, cash flows and exposure to liquidity risk.
Board action required at this meeting	APPROVAL to issue *Supplier Finance Arrangements* which amends NZ IAS 7 and NZ IFRS 7 AGREEMENT to consider further whether to develop an exposure draft proposing RDR concessions AGREEMENT to defer development of equivalent amendments to the PBE Standards.

Purpose and introduction[1]

1. The purpose of this paper is to:

   (a) seek the Board's approval to issue the amending standard *Supplier Finance Arrangements* which amends NZ IAS 7 *Statement of Cash Flows* and NZ IFRS 7 *Financial Instruments: Disclosures*;

   (b) seek agreement to consider further whether to develop an exposure draft proposing RDR concessions for Tier 2 for-profit entities; and

   (c) consider whether the Board should propose equivalent amendments to the PBE Standards in accordance with the *Policy Approach to Developing the Suite of PBE Standards* (PBE Policy Approach).

Recommendations

2. We recommend that the Board:

   (a) APPROVES for issue *Supplier Finance Arrangements*, which amends NZ IAS 7 and NZ IFRS 7;

   (b) APPROVES the signing memorandum from the Chair of the NZASB to the Chair of the XRB Board requesting approval to issue *Supplier Finance Arrangements;*

   (c) AGREES to further consider RDR concessions for Tier 2 for-profit entities in respect of the disclosures established by *Supplier Finance Arrangements* and whether to develop a New Zealand ED proposing RDR concessions for these disclosures;

   (d) CONSIDERS the application of the PBE Policy Approach to *Supplier Finance Arrangements*; and

   (e) AGREES to defer the decision to develop a PBE Standard based on *Supplier Finance Arrangements* until the IPSASB has completed their related alignment project.

Background

3. The project was initiated following a decision by the IFRS Interpretations Committee in December 2020. The Committee considered a question about the information an entity is required to provide in its financial statements about supply chain finance (reverse factoring) arrangements. The credit rating agency that submitted the question said, based on its experience, entities provide little information in their financial statements about those arrangements. The Committee decided not to add the matter to its standard-setting agenda because it concluded that IFRS Standards provide an adequate basis for an entity to account for supplier finance arrangements.

4. However, in response to the Interpretations Committee's decision, the IASB decided in June 2021 to add a narrow-scope, disclosure-only, standard-setting project to its work plan related

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to supplier finance arrangements. The IASB recognised the need for improved transparency and comparability in the reporting of these arrangements in financial statements.

5. To address the identified issues the IASB developed ED/2021/10 *Supplier Finance Arrangements* (the ED). The ED proposed amendments to IAS 7 and IFRS 7 which would require entities to provide more detailed disclosures about their Supplier Finance Arrangements including:

   (a) the nature and extent of the arrangements;

   (b) the risks associated with the arrangements; and

   (c) the effects of the arrangements on an entity's liquidity and cash flows.

6. The IASB issued the ED in November 2021 with comments due by 28 March 2022. The XRB also published the ED on our website at this time with comments due by 2 February 2022.

7. The XRB received no comment letters on the ED from its New Zealand constituents and did not comment on the ED. The IASB received 94 comment letters from its world-wide constituents, including a joint comment letter from CA ANZ and CPA Australia and from the AASB.

8. On 25 May 2023, the IASB published the final pronouncement *Supplier Finance Arrangements (Amendments to IAS 7 and IFRS 7)*.

Feedback received and the IASB's response

9. Many of the 94 respondents agreed with the proposals, while some suggested changes. The key feedback received from these respondents included:

   (a) requests for clarifications to aspects of the description of a supplier finance arrangement;

   (b) suggestions to require entities to disclose the effect of supplier finance arrangements on operating cash flows;

   (c) suggestions to add a specific requirement for non-cash transactions or the component of trade payables that is similar to bank debt;

   (d) concerns that the proposed changes to IFRS 7 would result in no change in disclosure practices because of the way the proposed changes are worded; and

   (e) requests for a broader project to address classification and presentation of liabilities and cash flows associated with supplier finance arrangements or a broader review of IAS 7.

10. In response to the feedback, the IASB decided to proceed with the project, with some changes to the proposals. The changes between the proposals in the ED and the final standard are summarised in Table 1 below.

Table 1 – summary of changes between the ED and the amending standard

Paragraph reference	Changes from the ED
IAS 7	

Paragraph reference	Changes from the ED
44B(da)	Deleted in response to feedback from constituents that including the example in paragraph 44B which is specifically related to financing activities makes it unclear whether non-cash changes arising from operating activities are also captured. Instead, guidance has been added to new paragraph 44H.
44F	Added liquidity risk to the disclosure objective in paragraph 44F for clarity.
44G	Added clarification that the following are not supplier finance arrangements as described in the amendments. • Arrangements such as financial guarantees that are solely credit enhancements for the entity such as financial guarantees • Instruments used by the entity to settle directly with a supplier such as credit cards.
44H	Amended the paragraph to require disclosure of terms and conditions of the entity's supplier finance arrangements in aggregate, with aggregations of arrangements on dissimilar terms and conditions from each other separately disclosed. In effect this captures the guidance of paragraph 44I below which has now been deleted. Incorporated clarification in relation to non-cash changes from ED paragraph 44B(da) above which has been removed in the final standard.
44I	This paragraph has been deleted as guidance on disclosing terms and conditions in aggregate has now been reflected in Paragraph 44H.
Guidance on implementing IFRS 7	
IG18	Removed the wording related to identifying concentrations of other risks (including supplier finance arrangements) which has instead been included and expanded on in new paragraph IG18A
IG18A	Added new paragraph to include and expand on the concentrations of other risks including liquidity and market risks that was removed from IG18 above. This new paragraph includes specific reference to supplier finance arrangements as described in IAS 7.

Final IASB amendments introduced

11. The amending standard increases transparency of supplier finance arrangements and their effects on an entity's liabilities, cash flows and exposure to liquidity risk. To achieve this the amending standard supplements other requirements within IFRS by adding requirements for entities to disclose in relation to their supplier finance arrangements:

    (a) the terms and conditions;

    (b) the amount of the liabilities that are part of the arrangements, breaking out the amounts for which the suppliers have already received payment from the finance providers, and stating where the liabilities sit on the balance sheet;

    (c) ranges of payment due dates; and

    (d) liquidity risk information.

12. The amending standard does not make any changes to recognition and measurement requirements for supplier finance arrangements.

Due process

13. Following its consideration of comments from constituents, the IASB reviewed the due process steps that it had taken since the publication of the ED and concluded that the applicable due process steps had been completed. This review of due process occurred at the IASB's February 2023 meeting.[2]

14. In accordance with the Accounting Standards Framework, the XRB Board is committed to adopting international standards in the for-profit sector and ensuring that Tier 1 for-profit entities in New Zealand can assert compliance with IFRS. This means that the Board will seek to adopt all IFRS Standards (including amendments) into our For-Profit Standards as soon as possible after an IASB final pronouncement is issued.

15. The due process followed by the NZASB complied with the due process requirements established by the XRB Board and, in our view, meets the requirements of section 22 of the Financial Reporting Act 2013.

16. In accordance with section 22(2) of the Financial Reporting Act 2013 we have considered whether the amending standard is likely to require the disclosure of personal information. In our view the amending standard does not include requirements that would result in the disclosure of personal information, and therefore no consultation with the Privacy Commissioner is required.

RDR concessions

17. The amending standard establishes new requirements for an entity to disclose information about its supplier finance arrangements that enables users to assess the effects of those arrangements on the entity's liabilities and cash flows and on the entity's exposure to liquidity risk.

18. To meet this objective the amendments require an entity to disclose in aggregate:

    (a) the terms and conditions of the arrangements. However, an entity shall disclose separately the terms and conditions of arrangements that have dissimilar terms and conditions; and

    (b) as at the beginning and end of the reporting period:

        (i) the carrying amounts and associated line items presented in the entity's statement of financial position of the financial liabilities that are part of a supplier finance arrangement;

        (ii) the carrying amounts and associated line items of the financial liabilities disclosed under (i) for which suppliers have already received payment from the finance providers;

[2] A summary of the IASB's February 2023 meeting is available here

(iii) the range of payment due dates for both the financial liabilities disclosed under (i) and comparable trade payables that are not part of a supplier finance arrangement; and

(c) the type and effect of non-cash changes in the carrying amounts of the financial liabilities disclosed under (b)(i).

19. In considering whether to grant RDR concessions for these disclosures, we have first looked for relevant analogies within the for-profit standards. We have identified the following two relevant analogies.

(a) Changes in liabilities arising from financing activities in NZ IAS 7[3] - we consider that this is a relevant analogy on the basis that the disclosures in *Supplier Finance Arrangements* primarily relate to the effect of supplier finance arrangements on an entity's financial liabilities.

(b) Liquidity risk disclosures in NZ IFRS 7[4] – we consider that this is a relevant analogy on the basis that an explicit objective of the proposals is to provide information about an entity's exposure to liquidity risk.

20. For both of these topics we note that RDR concessions have been granted in relation to the disclosures which may indicate that concessions for the disclosures introduced by supplier finance arrangements are appropriate. However, as the AASB and the IASB are expected to consider providing concessions for these disclosures in AASB 1060 and the new standard expected under the *Subsidiaries without Public Accountability Project* respectively, we intend to observe these decisions before making a final recommendation on RDR concessions for Board consideration at a future meeting.

21. As per paragraph 23 of EG A2 *Overview of the Accounting Standard-setting Process,* if the NZASB considers that disclosure concessions are warranted, it consults separately on the proposed concessions. We will therefore present any future ED for approval at a future Board meeting. As we have recently issued several standards which introduce new disclosure requirements, we intend to address all concessions the Board agrees to propose for these disclosures within a single, combined ED.

Question for the Board
Q1. Does the Board AGREE to consider RDR concessions for the disclosures introduced by *Supplier Finance Arrangements* at a future meeting as discussed above?

Draft amending standard and signing memorandum

22. Attached as agenda item 6A.2 is the draft for-profit amending standard *Supplier Finance Arrangements. Supplier Finance Arrangements* is identical to *Supplier Finance Arrangements (Amendments to IAS 7 and IFRS 7)* issued by the IASB except for the New Zealand-specific introduction and numbering, a scope paragraph limiting the application of the amending

[3] These disclosures are found in paragraphs 44A – 44E of NZ IAS 7.

[4] This disclosure is found in paragraph 39 of NZ IFRS 7

standard to Tier 1 and Tier 2 for-profit entities, and New Zealand specific wording for commencement and application of the amending standard.

23. Attached as agenda item 6A.3 is a draft signing memorandum from the Chair of the NZASB to the Chair of the XRB Board.

Commencement and Application

24. Section 28 of the Financial Reporting Act 2013 states that:

    (1) A standard, an authoritative notice, an amendment, or a revocation commences to apply in relation to the accounting periods or interim accounting periods that the Board specifies in the standard, notice, amendment, or revocation.

    (2) Those periods—

    (a) may be accounting periods or interim accounting periods that have commenced or that commence before the date on which the standard, authoritative notice, amendment, or revocation takes effect; but

    (b) must not be accounting periods or interim accounting periods that have ended or that end before the standard, authoritative notice, amendment, or revocation takes effect.

25. Further, we note that the Legislation Act 2019 does not allow legislation to have retrospective effect in New Zealand and we have considered whether this amending standard requires any amendments to comply with this restriction.

26. We note that in its basis for conclusions the IASB states the following:

> "BC 41 In reaching its decisions, the IASB considered:
>
> ...
>
> (b) the time needed by entities to develop processes and controls to collect and validate information to be disclosed and the time needed by audit firms to audit the information—particularly for the information required by paragraph 44H(b)(ii)–(iii) of IAS 7. Entities will need time to develop processes and controls to collect and validate information by the beginning of the annual reporting period in which an entity first applies the amendments. If an entity were to develop such processes and controls after the beginning of the first annual reporting period, it might not be possible to use those processes and controls, with the necessary reliability, on a retrospective basis."

27. The use of the word 'retrospective' in this context does not pose a risk that the amending standard would contravene the requirements of the Financial Reporting Act 2013 or the Legislation Act 2019. It is simply explaining why the IASB decided on an application date of 2024 without requiring comparative information. We therefore do not consider that a NZ BC is required for this matter.

Mandatory date

28. *Supplier Finance Arrangements* will be applicable for annual reporting periods beginning on or after 1 January 2024 with earlier application permitted for accounting periods that begin before this date, but which do not end before it takes effect. This is consistent with the effective date established by the IASB to the extent permitted under section 28 of the Financial Reporting Act 2013.

Questions for the Board
Q2. Does the Board APPROVE for issue *Supplier Finance Arrangements* which amends NZ IAS 7 and NZ IFRS 7?
Q3. Does the Board APPROVE the signing memorandum from the Chair of the NZASB to the Chair of the XRB Board, requesting approval to issue the amending standard?

PBE Policy Approach

29. As *Supplier Finance Arrangements* amends IAS 7 and IFRS 7, which are used as the basis for IPSAS 2 *Cash Flow Statements* and IPSAS 30 *Financial Instruments: Disclosures* respectively, we are required to apply the PBE Policy Approach to determine whether to propose amendments to the PBE Standards.

30. The PBE Policy Approach (paragraph 31) establishes a rebuttable presumption that, in the case of limited-scope amendments or amendments to an NZ IFRS that the NZASB considers are minor, the NZASB should not incorporate the change into the equivalent PBE Standard in advance of the IPSASB.

31. Table 2 below considers the factors in the development principle as it applies to *Supplier Finance Arrangements.*

Table 2 – Application of the PBE Policy Approach to *Supplier Finance Arrangements*

Are the amendments minor?
Yes. The amendments are only to introduce additional disclosures related to supplier finance arrangements and do not change recognition and measurement requirements.
Will the IPSASB consider these amendments in an acceptable timeframe?
Yes. The IPSASB is monitoring *Supplier Finance Arrangements* on their IPSAS–IFRS Alignment Dashboard and is reflected as an active maintenance project.
Will the potential development lead to higher quality financial reporting?
Yes. The amending standard will increase transparency over the nature, extent, and risks associated with an entity's supplier finance arrangements. However, we do not expect

that these arrangements are prevalent in the PBE sector in New Zealand and therefore the extent of improvement will likely be limited.
Will the benefits outweigh the costs?
No. *Relevant to the PBE sector as a whole?* We don't have any indication that supplier finance arrangements are common for the PBE sector in New Zealand. Accordingly we expect that the amendments will be relevant only in limited circumstances for the PBE sector as a whole. *Whether the benefits will outweigh the costs* As the amendments are minor, have limited applicability to the PBE sector, and are already reflected in an IPSASB maintenance project we do not consider the benefits of incorporating them into the PBE Standards would outweigh the costs of doing so ahead of the IPSASB. *Coherence of the suite of PBE Standards* The amendments would affect only IPSAS 2 and IPSAS 30. There are no consequential amendments to other PBE Standards so the coherence of the suite of PBE Standards would be maintained. *Impact on mixed groups* Should a PBE have supplier finance arrangements, developing amendments to the PBE Standards would promote a consistent approach and could have a positive impact on mixed groups. However, as the amendments only add disclosure requirements, the impact of not introducing them to the PBE Standards at this time is likely to be exceptionally limited.

Staff recommendation

32. We do not consider there is sufficient evidence to rebut the presumption that the NZASB will not incorporate the amendments into the equivalent PBE Standards in advance of the IPSASB. Therefore, our recommendation is to defer the decision to develop a PBE Standard based on *Supplier Finance Arrangements* until the IPSASB has developed their amendments.

Question for the Board

Q4. Does the Board AGREE to defer the decision to develop a PBE Standard based on *Supplier Finance Arrangements* until the IPSASB has completed its equivalent alignment project?

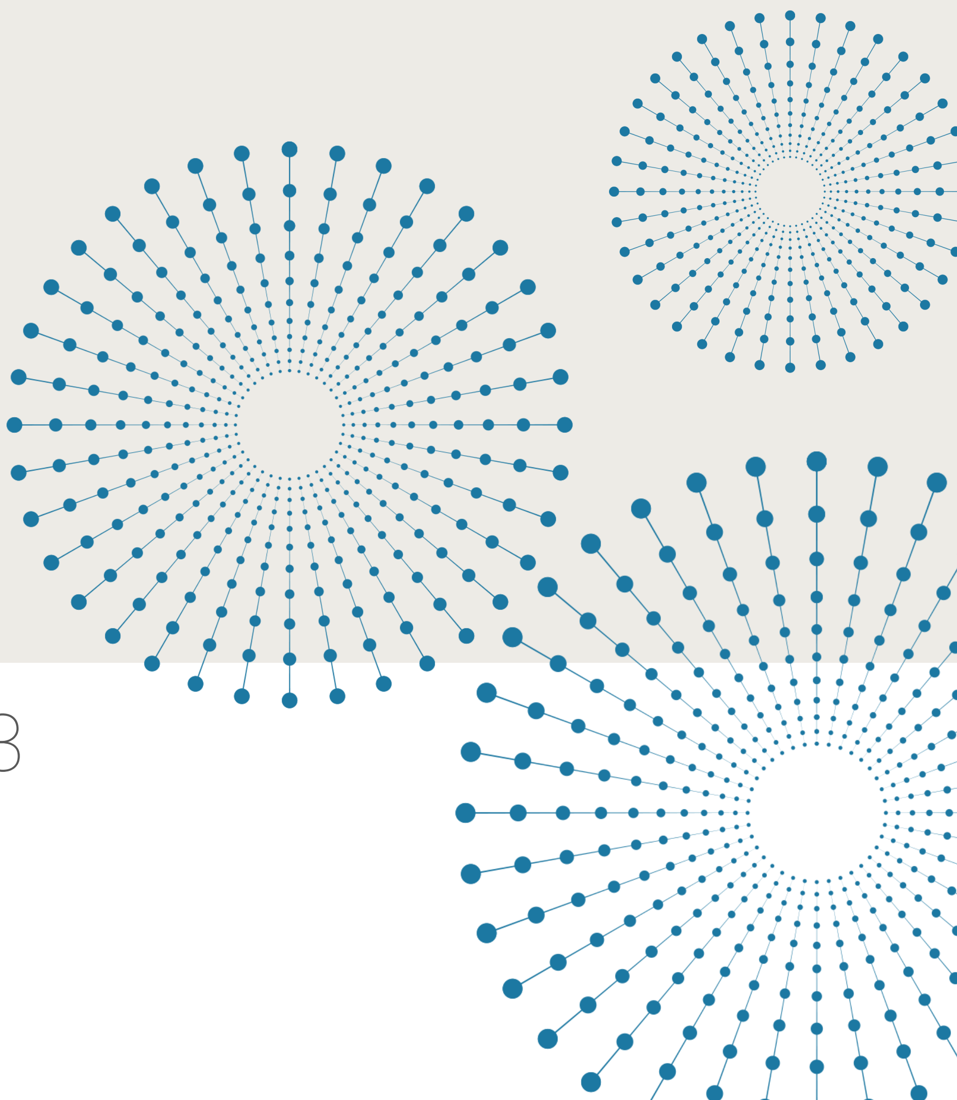
Attachments

Agenda item 6A.2: Draft *Supplier Finance Arrangements*

Agenda item 6A.3: Draft signing memorandum

Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Supplier Finance Arrangements



Issued July 2023

Supplier Finance Arrangements

Issued July 2023

This Tier 1 and Tier 2 for-profit amending Standard is based on *Supplier Finance Arrangements*, issued by the International Accounting Standards Board, which amended IAS 7 *Statement of Cash Flows* and IFRS 7 *Financial Instruments: Disclosures*. This amending Standard introduces disclosures to enhance transparency of an entity's supplier finance arrangements and their effects on its liabilities, cash flows and exposure to liquidity risk.

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

Legal status of amending Standard

This amending Standard was issued on XX July 2023 by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This amending Standard is secondary legislation for the purposes of the Legislation Act 2019.

The amending Standard, pursuant to section 27(1) of the Financial Reporting Act 2013, takes effect on the 28th day after the date of its publication. The amending Standard was published under the Legislation Act 2019 on XX July 2023 and takes effect on XX xxxx 2023.

Commencement and application

The amending Standard has a mandatory date of 1 January 2024, meaning it must be applied by Tier 1 and Tier 2 for-profit entities for accounting periods that begin on or after this date.

Application to an earlier accounting period is permitted for accounting periods that end after this amending Standard takes effect – refer to paragraphs 62 – 63.3 of this amending Standard.

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

APPROVAL BY THE IASB OF *SUPPLIER FINANCE ARRANGEMENTS* ISSUED IN MAY 2023

AMENDMENTS TO THE BASIS FOR CONCLUSIONS ON IAS 7 *STATEMENT OF CASH FLOWS*

AMENDMENTS TO THE BASIS FOR CONCLUSIONS ON IFRS 7 *FINANCIAL INSTRUMENTS: DISCLOSURES*

Part A – Introduction

This amending Standard sets out amendments to NZ IAS 7 *Statement of Cash Flows* and NZ IFRS 7 *Financial Instruments: Disclosures*. The amendments introduce additional disclosures to enhance transparency over an entity's supplier finance arrangements and their effect on the entity's liabilities, cash flows and exposure to liquidity risk.

Tier 2 entities are required to comply with all the requirements in this amending Standard.

Part B – Scope

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

Part C – Amendments to NZ IAS 7 *Statement of Cash Flows*

Paragraphs 44F–44H and their related heading and paragraphs 62–63 are added. For ease of reading, these paragraphs and their headings have not been underlined. The heading of the section which includes paragraph 62–63.3 is amended. New text in that heading is underlined.

Structure and content

…

Supplier finance arrangements

44F **An entity shall disclose information about its supplier finance arrangements (as described in paragraph 44G) that enables users of financial statements to assess the effects of those arrangements on the entity's liabilities and cash flows and on the entity's exposure to liquidity risk.**

44G Supplier finance arrangements are characterised by one or more finance providers offering to pay amounts an entity owes its suppliers and the entity agreeing to pay according to the terms and conditions of the arrangements at the same date as, or a date later than, suppliers are paid. These arrangements provide the entity with extended payment terms, or the entity's suppliers with early payment terms, compared to the related invoice payment due date. Supplier finance arrangements are often referred to as supply chain finance, payables finance or reverse factoring arrangements. Arrangements that are solely credit enhancements for the entity (for example, financial guarantees including letters of credit used as guarantees) or instruments used by the entity to settle directly with a supplier the amounts owed (for example, credit cards) are not supplier finance arrangements.

44H To meet the objectives in paragraph 44F, an entity shall disclose in aggregate for its supplier finance arrangements:

(a) the terms and conditions of the arrangements (for example, extended payment terms and security or guarantees provided). However, an entity shall disclose separately the terms and conditions of arrangements that have dissimilar terms and conditions.

(b) as at the beginning and end of the reporting period:

(i) the carrying amounts, and associated line items presented in the entity's statement of financial position, of the financial liabilities that are part of a supplier finance arrangement.

(ii) the carrying amounts, and associated line items, of the financial liabilities disclosed under (i) for which suppliers have already received payment from the finance providers.

(iii) the range of payment due dates (for example, 30–40 days after the invoice date) for both the financial liabilities disclosed under (i) and comparable trade payables that are not part of a supplier finance arrangement. Comparable trade payables are, for example, trade payables of the entity within the same line of business or jurisdiction as the financial liabilities disclosed under (i). If ranges of payment due dates are wide, an entity

shall disclose explanatory information about those ranges or disclose additional ranges (for example, stratified ranges).

(c) the type and effect of non-cash changes in the carrying amounts of the financial liabilities disclosed under (b)(i). Examples of non-cash changes include the effect of business combinations, exchange differences or other transactions that do not require the use of cash or cash equivalents (see paragraph 43).

...

~~Effective date and transition~~ Commencement and application

...

62 The amending Standard *Supplier Finance Arrangements*, published in May 2023, added paragraphs 44F–44H. An entity shall apply those amendments in accordance with the commencement and application date provisions in paragraphs NZ 63.1–NZ 63.3. An entity that applies those amendments to an 'early adoption accounting period' shall disclose that fact.

63 In applying *Supplier Finance Arrangements*, an entity is not required to disclose:

(a) comparative information for any reporting periods presented before the beginning of the annual reporting period in which the entity first applies those amendments.

(b) the information otherwise required by paragraph 44H(b)(ii)–(iii) as at the beginning of the annual reporting period in which the entity first applies those amendments.

(c) the information otherwise required by paragraphs 44F–44H for any interim period presented within the annual reporting period in which the entity first applies those amendments.

When amending Standard takes effect (section 27 Financial Reporting Act 2013)

63.1 The amending Standard takes effect on the 28th day after the date of its publication under the Legislation Act 2019. The amending Standard was published on xx July 2023 and takes effect on xx August 2023

Accounting period in relation to which standards commence to apply (section 28 Financial Reporting Act)

63.2 The accounting periods in relation to which this amending Standard commences to apply are:

(a) for an **early adopter**, those accounting periods following and including, the **early adoption accounting period**.

(b) for any other reporting entity, those accounting periods following, and including, the first accounting period for the entity that begins on or after the **mandatory date.**

63.3 In paragraph 63.2:

early adopter means a reporting entity that applies this amending Standard for an early adoption accounting period

early adoption accounting period means an accounting period of the early adopter:

(a) that begins before the mandatory date but has not ended or does not end before this amending Standard takes effect (and to avoid doubt, that period may have begun before this amending Standard takes effect); and

(b) for which the early adopter:

(i) first applies this amending Standard in preparing its financial statements; and

(ii) discloses in its financial statements for that accounting period that this amending Standard has been applied for that period.

mandatory date means 1 January 2024.

Part D – Amendments to NZ IFRS 7 *Financial Instruments: Disclosures*

Paragraph 44JJ is added. In Appendix B, paragraph B11F is amended. Deleted text is struck through and new text is underlined.

Structure and content

…

~~Effective date and transition~~ Commencement and application

...

44JJ *Supplier Finance Arrangements*, issued in July 2023, which also amended NZ IAS 7, amended paragraph B11F. An entity shall apply that amendment when it applies the amendments to NZ IAS 7.

...

Appendix B
Application guidance

...

Nature and extent of risks arising from financial instruments (paragraphs 31–42)

...

Quantitative liquidity risk disclosures (paragraphs 34(a) and 39(a) and (b))

...

B11F Other factors that an entity might consider in providing the disclosure required in paragraph 39(c) include, but are not limited to, whether the entity:

(a) has committed borrowing facilities (eg commercial paper facilities) or other lines of credit (eg stand-by credit facilities) that it can access to meet liquidity needs;

(b) holds deposits at central banks to meet liquidity needs;

(c) has very diverse funding sources;

(d) has significant concentrations of liquidity risk in either its assets or its funding sources;

(e) has internal control processes and contingency plans for managing liquidity risk;

(f) has instruments that include accelerated repayment terms (eg on the downgrade of the entity's credit rating);

(g) has instruments that could require the posting of collateral (eg margin calls for derivatives);

(h) has instruments that allow the entity to choose whether it settles its financial liabilities by delivering cash (or another financial asset) or by delivering its own shares; ~~or~~

(i) has instruments that are subject to master netting agreements; or

(j) has accessed, or has access to, facilities under supplier finance arrangements (as described in paragraph 44G of IAS 7) that provide the entity with extended payment terms or the entity's suppliers with early payment terms.

...

Agenda Item 6A.3

XRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Memorandum

Date:	XX July 2023
To:	Michele Embling, Chair External Reporting Board
From:	Carolyn Cordery, Chair NZASB
Subject:	***Supplier Finance Arrangements***

Introduction[1]

1. In accordance with the protocols established by the XRB Board, NZASB seeks your approval to issue *Supplier Finance Arrangements* which amends NZ IAS 7 *Statement of Cash Flows* and NZ IFRS 7 *Financial Instruments: Disclosures*.

2. This amending standard is aligned with *Supplier Finance Arrangements*, issued by the International Accounting Standards Board (IASB) in May 2023, which amended IAS 7 *Statement of Cash Flows* and IFRS 7 *Financial Instruments: Disclosures*.

3. The IASB's objective in issuing this amending standard is to enhance transparency of an entity's supplier finance arrangements and their effects on the entity's liabilities, cash flows and exposure to liquidity risk. The amendments arose in response to an IFRS Interpretations Committee decision in December 2020 about the information an entity is required to provide in its financial statements about supplier finance arrangements. While the Interpretations Committee concluded that IFRS provide an adequate basis for accounting for these arrangements and therefore did not add the matter to its standard-setting agenda, the IASB considered there was a need to enhance transparency of supplier finance arrangements. The IASB decided to add a narrow-scope, disclosure-only, standard-setting project to its work plan in June 2021.

4. The amending standard introduces requirements to disclose the terms and conditions of an entity's supplier finance arrangements and how they are reflected in the financial liabilities presented in an entity's statement of financial position.

Due process

5. The IASB issued Exposure Draft ED/2021/10 *Supplier Finance Arrangements* (ED/2021/10) in November 2021.

6. The NZASB issued the ED for comment in New Zealand around the same time. Comments were due to the NZASB on 2 February 2022 and to the IASB on 22 March 2022.

7. The NZASB did not comment on ED/2021/10 and received no comment letters from New Zealand constituents.

8. The IASB received 94 comment letters from its world-wide constituents, including a joint comment letter from CA ANZ and CPA Australia.

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

9. Following its consideration of comments from constituents, the IASB reviewed the due process steps that it had taken since the publication of ED/2021/10 and concluded that the applicable due process steps had been completed. This review of due process occurred at the IASB meeting in February 2023.[2]

10. The IASB issued *Supplier Finance Arrangements* in May 2023. This amending standard is effective for annual periods beginning on or after 1 January 2024 with early application permitted.

11. The NZASB has approved *Supplier Finance Arrangements*. The due process followed by the NZASB complied with the due process requirements established by the XRB Board and, in the NZASB's view, meets the requirements of section 22 of the Financial Reporting Act 2013.

12. In accordance with section 22(2) of the Financial Reporting Act 2013 the NZASB has considered whether the amending standard is likely to require the disclosure of personal information. In the NZASB's view the amending standard does not include requirements that would result in the disclosure of personal information and therefore no consultation with the Privacy Commissioner is required.

Consistency with XRB Financial Reporting Strategy

13. The amending standard is a standard in its own right. The amending standard is identical to *Supplier Finance Arrangements* issued by the IASB, except for the following inclusions:

    (a) A New Zealand specific introduction, formatting and numbering;

    (b) a scope paragraph explaining that the standard applies to Tier 1 and Tier 2 for-profit entities; and

    (c) New Zealand specific wording for the commencement and application of the amending standard.

14. The amending standard establishes some new disclosure requirements. On the basis that concessions have already been provided for similar disclosures we intend to deliberate further whether to propose RDR concessions in respect of these new disclosure requirements. This deliberation will consider decisions made by:

    (a) the IASB regarding disclosure requirements for subsidiaries without public accountability; and

    (b) the AASB regarding Tier 2 reporting requirements made at its June meeting.

15. The Australian Accounting Standards Board (AASB) is expected to approve the equivalent Australian Accounting Standard in June 2023.

16. In 2020 the AASB issued a stand-alone disclosure standard, AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities*. Prior to this New Zealand and Australia had equivalent RDR regimes and New Zealand's Tier 1 and Tier 2 for-profit reporting requirements were aligned with those in Australia. The AASB now considers whether to add new disclosure requirements to AASB 1060 on a case by case

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[2] An update on the IASB meeting in February 2023 is available here

basis. The AASB is expected to consider the effect of the new amending standard on AASB 1060 in June 2023.

17. In June 2022, as part of its Disclosure Initiative—Subsidiaries without Public Accountability project the IASB tentatively decided to incorporate the disclosure requirements of IFRS Accounting Standards issued up until 28 February 2021. For disclosures introduced after February 2021, the IASB decided to review and consider these in the context of the new standard, only after it has been issued. Therefore the IASB is expected to issue an ED proposing amendments to the new standard for the disclosures introduced by *Supplier Finance Arrangements* in the near future.

18. The issue of this amending standard is consistent with all three elements of the Financial Reporting Strategy: it adopts the international standard, retains a harmonised position with Australia for Tier 1 for-profit entities and is consistent with the Accounting Standards Framework.

Commencement and application date

19. The commencement and application date requirements for the amending standard is included in Appendix A of this memo. An entity that is not an early adopter is required to apply the amending standard for accounting periods beginning on or after 1 January 2024. Application is permitted for an 'early adoption accounting period' when that period begins before the mandatory date but has not ended or does not end before this amending standard takes effect (as defined in Appendix A).

Other matters

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

Recommendation

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

Attachments

Supplier Finance Arrangements

Certificate of determination

Carolyn Cordery
Chair NZASB

Appendix A: Commencement and application

A1. The commencement and application provisions below will apply to the amending standard once it is published.

When standard takes effect (section 27 Financial Reporting Act 2013)

A2. This standard takes effect on the 28th day after the date of its publication under the Legislation Act 2019. The standard is expected to be published on XX July 2023 and take effect on XX August 2023.

Accounting periods in relation to which standards commence to apply (section 28 Financial Reporting Act 2013)

A3. The accounting periods in relation to which this standard commences to apply are:

(a) for an early adopter, those accounting periods following, and including, the early adoption accounting period; and

(b) for any other reporting entity, those accounting periods following, and including, the first accounting period for the entity that begins on or after the mandatory date.

A4. In applying paragraph A3:

early adopter means a reporting entity that applies the standard for an early adoption accounting period.

early adoption accounting period means an accounting period of the early adopter:

(a) that begins before the mandatory date but has not ended or does not end before this standard takes effect (and to avoid doubt, that period may have begun before this standard takes effect); and

(b) for which the early adopter:

(i) first applies this standard in preparing its financial statements; and

(ii) discloses in its financial statements for that accounting period that the standard has been applied for that period.

mandatory date means 1 January 2024.

EXRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Agenda Item 6B.1

Memorandum

Date:	16 June 2023
To:	NZASB Members
From:	Tereza Bublikova and Charis Halliday
Subject:	***International Tax Reform – Pillar Two Model Rules***

COVER SHEET

Project priority and complexity

Project priority	**Medium** Some jurisdictions have already enacted new tax legislation to implement the Pillar Two rules and others are expected to do so shortly. This legislation affects multi-national entities and their subsidiaries operating and reporting in New Zealand. Any standard-setting has to be completed urgently for the new disclosures and temporary relief from recognising Pillar Two related deferred tax to be effective.
Complexity of Board decision-making at this meeting	**Low** *International Tax Reform—Pillar Two Model Rules*, amends NZ IAS 12 *Income Taxes* and is identical in substance to *International Tax Reform—Pillar Two Model Rules (Amendments to IAS 12)* issued by the International Accounting Standards Board (IASB).

Overview of agenda item

Project status	Standard approval stage: seeking approval to issue *International Tax Reform—Pillar Two Model Rules*, which amends NZ IAS 12.
Project purpose	• Provide temporary relief for affected entities from determining how to apply the deferred tax accounting requirements in NZ IAS 12 to a complex new Pilar Two tax regime in a short period of time; • avoid different interpretations of NZ IAS 12 developing in practice that might result in inconsistent application of the Standard; and • allow time for jurisdictions to enact new tax laws and for stakeholders to assess how the rules have been implemented by those jurisdictions.
Board action required at this meeting	APPROVAL to issue *International Tax Reform—Pillar Two Model Rules,* which amends NZ IAS 12. AGREEMENT not to provide any RDR concessions with respect to the disclosure requirements in the amending standard at this time. AGREEMENT to develop equivalent amendments to the PBE Standard.

Purpose and introduction[1]

1. The purpose of this paper is to:

   (a) Seek the Board's approval to issue the amending standard *International Tax Reform—Pillar Two Model Rules* which amends NZ IAS 12 *Income Taxes*;

   (b) seek the Board's agreement not to develop an exposure draft proposing RDR concessions for Tier 2 for-profit entities at this time; and

   (c) consider whether the Board should propose equivalent amendments to the PBE Standards in accordance with the *Policy Approach to Developing the Suite of PBE Standards* (PBE Policy Approach).

Recommendation

2. We recommend that the Board:

   (a) APPROVES for issue *International Tax Reform—Pillar Two Model Rules*, which amends NZ IAS 12;

   (b) AGREES that no RDR concessions should be given with respect to the disclosure requirements in the amending standard at this time;

   (c) APPROVES the signing memorandum from the Chair of the NZASB to the Chair of the XRB Board requesting approval to issue *International Tax Reform—Pillar Two Model Rules*; and

   (d) CONSIDERS the application of the PBE Policy Approach to *International Tax Reform—Pillar Two Model Rules*.

Background

3. The IASB issued Exposure Draft ED/2023/1 *International Tax Reform—Pillar Two Model Rules* (ED/2023/1) in January 2023, with comments due on 10 March 2023. At its February 2023 the NZASB agreed not to comment on the ED/2023/1.

4. The NZASB issued ED/2023/1 for comment in New Zealand around the same time that it was issued internationally. Comments were due to the NZASB on 15 February 2023. The NZASB received one comment letter from Cantin Consulting which was sent directly to IASB as well.

5. The IASB received 98 comment letters from its world-wide constituents, including the Cantin Consulting submission and a joint submission from CPA Australia and CA ANZ (CPA/CAANZ).

6. The IASB issued *International Tax Reform—Pillar Two Model Rules* in May 2023. The exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes and the corresponding disclosure requirement are effective immediately upon the issue of these amendments. The rest of the amending standard is

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

effective for annual periods beginning on or after 1 January 2023, and for interim periods ending after 31 December 2023.

Reason for amendments

7. In October 2021, more than 135 countries and jurisdictions agreed to a major international tax reform that introduces a global minimum tax for large multinational enterprises (MNEs). These countries and jurisdictions joined the Organisation for Economic Co-operation and Development (OECD)/G20 Inclusive Framework on Base Erosion and Profit Shifting statement on a Two-Pillar Solution to address the tax challenges arising from the digitalisation of the economy. The two-pillar solution comprises:

   (a) Pillar One—which aims to ensure a fairer distribution of profits and taxing rights among countries for the largest MNEs; and

   (b) Pillar Two—which aims to put a floor on tax competition by introducing a global minimum corporate tax rate set at 15% for large MNEs.

8. In December 2021, the OECD released the Pillar Two Model Rules (the Rules) which provide a template that jurisdictions can translate into domestic tax law.[2]

9. Stakeholders informed the IASB of concerns about the potential implications for income tax accounting resulting from jurisdictions implementing the Pillar Two Model Rules. In particular, stakeholders were concerned about:

   (a) the scope of IAS 12 where it was unclear whether the Rules top-up tax is an income tax in the financial statements of a group's subsidiaries — for example, when an entity is liable to pay such tax with respect to profits of entities that are not part of its reporting group (such as with respect to a fellow subsidiary's profits);

   (b) uncertainty over the accounting for deferred taxes arising from the Rules; and

   (c) urgent need for clarity given the imminent implementation of the Rules in some jurisdictions. As this lack of clarity could result in diversity in the accounting applied by affected entities and information that is potentially not useful.

IASB amendments introduced and stakeholders' response to the IASB ED

Temporary exception to deferred tax accounting

10. After considering stakeholders' concerns, the IASB agreed that entities need time to determine how to apply the principles and requirements in IAS 12 to account for deferred taxes related to Pillar Two income taxes. The IASB also needs time to engage further with stakeholders and to consider whether any action is needed to support the consistent application of IAS 12. The IASB concluded that it was not feasible to complete these activities before jurisdictions enact new tax laws and thus before entities are required to reflect those laws in accounting for deferred taxes.

[2] For the details about the Pillar Two Model Rules please refer to February 2023 agenda item 5A.1.

11. The IASB therefore decided to introduce a temporary exception to the requirements in IAS 12 to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes. The IASB concluded that doing so would:

    (a) provide affected entities with relief from accounting for deferred tax assets and liabilities in relation to complex new tax legislation to be enacted by multiple jurisdictions in a short period of time;

    (b) avoid the development of diverse interpretations of IAS 12 and the resulting inconsistent application of the Standard; and

    (c) allow time for stakeholders to assess how the Rules have been implemented in different jurisdictions, for entities to assess how they are affected and for the IASB to consider whether to do further work.

12. As some entities are unaffected by the Rules and therefore, would not apply the exception, the IASB decided to require an entity to disclose that it has applied the temporary exception. This disclosure will make the exception's application transparent to users of financial statements during the periods in which it is applied.

13. The IASB also decided to make the application of the temporary exception mandatory because doing so would:

    (a) result in greater comparability between entities' financial statements and, therefore, more useful information for users of financial statements; and

    (b) eliminate the risk of entities inadvertently developing accounting policies that are inconsistent with the principles and requirements in IAS 12.

14. The IASB concluded that it was not possible to determine how much time would be required for the activities described in paragraph 10 because they would depend on how and when jurisdictions implement the Rules. Therefore, the IASB decided not to specify how long the temporary exception will be in place.

15. Respondents to the ED/2023/1, including respondents from New Zealand and Australia, showed strong support of the IASB's proposal to introduce this mandatory temporary exception as a pragmatic approach to addresses stakeholders' concerns. The related disclosures were in general considered to be reasonable.

Disclosures when the Pillar Two tax legislation is enacted or substantively enacted but not yet in effect

16. In periods when the Pillar Two tax legislation is enacted or substantively enacted but not yet in effect the legislation could create exposures that are not yet reflected in the entity's income tax expense. As users of financial statements need to understand such exposure, the IASB proposed requiring an entity to disclose specific items of information based on the requirements in IAS 12.

17. However, feedback (including responses from New Zealand) suggested the proposed disclosure requirements may not provide useful information for users as information based on

the requirements in IAS 12 differs from that based on the requirements of the Rules and that in general the benefits of disclosing such information would not outweigh the costs of preparing it.

18. Respondents also pointed out that those disclosure requirements are expected to apply to only a few reporting periods and suggested the IASB maintain a principle-based approach rather than developing specific requirements for the Pillar Two tax.

19. In considering stakeholders' feedback, the IASB decided to set a disclosure objective and require an entity to disclose information that meets the disclosure objective (paragraph 88C of the amending Standard), but not to specify the items of information an entity is required to disclose or the basis on which the entity prepares that information. This approach would allow an entity to disclose information that is available from its assessments of Pillar Two tax impacts and that reflects its circumstances, which will vary from entity to entity.

20. Furthermore, the IASB clarified that the information an entity is required to disclose to meet the disclosure objective:

    (a) does not have to reflect all the specific requirements of the Pillar Two legislation and can be provided in the form of an indicative range; and

    (b) should be based on an entity's circumstances at the end of the reporting period, i.e. that an entity would not have to disclose information about possible future transactions and other possible future events (forward-looking information), such as forecast future profits or planned mitigation actions.

21. The IASB also considered feedback from users of financial statements that indicated that they need both qualitative and quantitative information to understand an entity's exposure to Pillar Two income taxes and require an entity to disclose information that is both qualitative and quantitative in nature (paragraph 88D).

22. The IASB included examples of qualitative and quantitative information to help an entity understand the type of information it can provide to meet the disclosure objective.

23. Also, please note that one IASB member, Mr Zach Gast, voted against issuing *International Tax Reform—Pillar Two Model Rules* on the basis that the above-mentioned temporary exemption will result in a significant loss of information for users of financial statements and that the disclosure requirements in IAS 12, including those introduced by the amending Standard, provide insufficient information for users to analyse the impact of Pillar Two income taxes. In his opinion, the disclosure objective is not sufficiently stringent without requiring entities to provide alternative quantitative information (a backstop) when information is deemed not known or reasonably estimable.

Disclosures when the Pillar Two tax legislation is in effect

24. The IASB decided to require an entity to disclose separately the current tax expense related to Pillar Two income taxes. The IASB concluded that this information:

    (a) would help users of financial statements understand the magnitude of Pillar Two income taxes relative to an entity's overall tax expense; and

(b) would not be costly to prepare because an entity would already be required to recognise current tax related to Pillar Two income taxes.

25. Respondents to the ED/2023/1, including respondents from New Zealand, found this disclosure requirement useful as even though entities can be expected over time to build compliance systems which produce better estimates of Pillar Two income taxes, it is unlikely that those systems will be fully complete or robust particularly in the first years of applying the Rules and adjustments to prior year Pillar Two income taxes will be likely.

Application date

26. The IASB concluded that:

    (a) for the temporary exception to be effective, it needs to be available to entities immediately upon the issue of the amendments; and

    (b) requiring an entity to apply the disclosure requirements in paragraphs 88B–88D for annual reporting periods beginning on or after 1 January 2023—but not for interim periods ending on or before 31 December 2023 — provides an entity with enough time to prepare the required information.

27. Respondents to the ED/2023/1, including respondents from New Zealand and Australia, showed strong support of enacting this amending standard as soon as possible.

28. The IASB decided to require an entity to apply the temporary exception immediately with retrospective effect. This could result in an entity applying the exception for periods that have ended before the amending standard takes effect.

29. Section 28 of the Financial Reporting Act 2013 states that:

    (1) A standard, an authoritative notice, an amendment, or a revocation commences to apply in relation to the accounting periods or interim accounting periods that the Board specifies in the standard, notice, amendment, or revocation.

    (2) Those periods—

    (a) may be accounting periods or interim accounting periods that have commenced or that commence before the date on which the standard, authoritative notice, amendment, or revocation takes effect; but

    (b) must not be accounting periods or interim accounting periods that have ended or that end before the standard, authoritative notice, amendment, or revocation takes effect.

30. Further, we note that the Legislation Act 2019 does not allow legislation to have retrospective effect in New Zealand.

31. Therefore, we propose to limit the commencement and application of:

    (a) the temporary exception and related disclosure requirements (paragraphs 4A and 88A of the amending Standard) to annual reporting periods that have not ended or do not end before the date that the amending Standard takes effect (i.e. 28 days after being gazetted); and

(b) the other disclosure requirements (paragraphs 88B–88D of the amending Standard) to annual reporting periods beginning on or after 1 January 2023 but which have not ended or do not end before this amending Standard takes effect.

32. For clarity, we propose to add following New Zealand specific Basis for Conclusions:

> **International Tax Reform—Pillar Two Model Rules July 2023**
>
> NZ BC1 The IASB's *International Tax Reform – Pillar Two Model* Rules Basis for Conclusions states "BC117 The IASB decided to require an entity to apply the temporary exception retrospectively. This requirement would result in an entity applying the exception from the date Pillar Two legislation is enacted or substantively enacted—even if that date is before the date of issuing the amendments—and would not result in additional costs." The NZASB considered whether this would be appropriate in accordance with the requirements in the Legislation Act 2019, which does not allow legislation to have retrospective effect in New Zealand. The NZASB noted that application for periods that have ended before this amending Standard takes effect would be inappropriate. However, for annual reporting periods that have not ended or do not end before this amending Standard takes effect, entities may apply the requirements of the amending Standard in accordance with the commencement and application provisions. The NZASB has amended the commencement and application provisions to reflect the legislative requirements in New Zealand.

Due process

33. Following its consideration of comments from constituents, the IASB reviewed the due process steps that it had taken since the publication of the ED and concluded that the applicable due process steps had been completed. This review of due process occurred at the IASB's supplementary April 2023 meeting.[3]

34. In accordance with the Accounting Standards Framework, the XRB Board is committed to adopting international standards in the for-profit sector and ensuring that Tier 1 for-profit entities in New Zealand can assert compliance with IFRS. This means that the Board will seek to adopt all IFRS Standards (including amendments) into our For-Profit Standards as soon as possible after an IASB final pronouncement is issued.

35. The due process followed by the NZASB complied with the due process requirements established by the XRB Board and, in our view, meets the requirements of section 22 of the Financial Reporting Act 2013.

36. In accordance with section 22(2) of the Financial Reporting Act 2013 we have considered whether the amending standard is likely to require the disclosure of personal information. In our view the amending standard does not include requirements that would result in the disclosure of personal information, and therefore no consultation with the Privacy Commissioner is required.

Reduce Disclosure Requirements (RDR) concessions considerations

37. On 1 June 2023 the IASB issued IASB/ED/2023/3 *Amendments to the IFRS for SMEs Accounting Standard—International Tax Reform—Pillar Two Model Rules* which proposes narrow-scope amendments to Section 29 of the *IFRS for SMEs* Accounting Standard ('Income Tax'). The proposed amendments are in substance identical to *International Tax Reform—Pillar Two*

[3] A summary of the supplementary IASB's April 2023 meeting is available here.

Model Rules (amending IAS 12) with the exception of the disclosure requirements when the Pillar Two tax legislation is enacted or substantively enacted but not yet in effect.

38. The IASB hasn't proposed those disclosures on the basis that the paragraph 29.38 of the Section 29 of the *IFRS for SMEs* already includes overarching disclosure requirements to "*disclose information that enables users of its financial statements to evaluate the nature and financial effect of the current and deferred tax consequences of recognised transactions and other events*". However, the IASB clarified that 'other events' in this disclosure objective include enacted or substantively enacted Pillar Two legislation.

39. In light of this decisions and considering feedback from New Zealand constituents we believe that the disclosure requirements in paragraphs 88A - 88C of the *International Tax Reform—Pillar Two Model Rules* are relevant to both Tier 1 and Tier 2 entities – this means the requirements to disclose:

    (a) separately its current tax expense (income) related to Pillar Two income taxes (in periods when Pillar Two legislation is in effect);

    (b) known or reasonably estimable information that helps users of financial statements understand the entity's exposure to Pillar Two income taxes arising from Pillar Two legislation that is enacted or substantively enacted but not yet in effect; and

    (c) that entity applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes.

40. Providing RDR concession in respect of paragraph 88D would release Tier 2 entities from the requirement to disclose both qualitative and quantitative information about their exposure to Pillar Two income taxes. In other words this would give them more flexibility to decide how to meet the disclosure objective of providing information that helps users of financial statements understand the entity's exposure to Pillar Two income taxes.

41. However, as per discussion with IRD, it's likely that the Rules will be included in a Bill that gets introduced in the Parliament in Q2 2023 and is enacted by March 2024. The Rules will provide for the application date to be determined by Order in Council, which means the application date hasn't been decided yet. At this stage, it's likely that the application date will be for income years beginning on or after 1 January 2024. This means the period when the Pillar Two tax legislation is enacted or substantively enacted but not yet in effect in New Zealand is very short, if any.

42. Moreover, there are circa one thousand foreign owned MNEs operating in NZ which can be subject to the Rules enacted in other jurisdictions[4]. The foreign owned MNEs operate in a broad range of industries including tech, food & beverage, manufacturing, mining, oil & gas, pharmaceuticals, finance, air transport, motor vehicles, etc. Therefore, any standard-setting has to be completed urgently. Whereas per paragraph 23 of EG A2 *Overview of the Accounting Standard-setting Process,* if the NZASB considers that disclosure concessions are warranted, it

[4] We note that as of 31 March 2023, Japan's 2023 Tax Reform legislation (that includes the OECD Income Inclusion Rule (IIR)) was finalised, with effect from 1 April 2023. Japan's IIR will apply to fiscal years beginning on or after 1 April 2024 (aligned with the fiscal years of the vast majority of Japanese MNCs). Japan's IIR is generally in line with the OECD's Model Rules.

consults separately on the proposed concessions, which would significantly prolong the standard-setting process.

43. We also note that the IASB will be considering whether to propose *International Tax Reform—Pillar Two Model Rules* amendments to its Standard on *Disclosure Initiative—Subsidiaries without Public Accountability: Disclosures.*

44. Further we note that the AASB will discuss the amending Standard *International Tax Reform—Pillar Two Model Rules* at its 21-22 June meeting. The AASB staff is recommending developing an Exposure Draft proposing adding specific disclosures to AASB 1060 for circumstances where a Tier 2 entity is affected by the Rules and applies the mandatory temporary exception. If approved, the AASB will issue this Exposure Draft on 6 July 2023 with shortened comment period of 45-days.

45. Considering the imminent enactment of Pillar Two tax law in some jurisdictions and urgent need for the amendments to NZ IAS 12 as well as cost benefit of developing a New Zealand ED proposing RDR concessions for Tier 2 for-profit entities in respect of the disclosures established by paragraph 88D of the *International Tax Reform—Pillar Two Model Rules* we propose at this time not to provide any RDR concessions with respect to the disclosure requirements in the amending Standard.

46. The staff will keep monitoring the development of the IASB's projects on *Disclosure Initiative—Subsidiaries without Public Accountability: Disclosures* and on *Amendments to the IFRS for SMEs Accounting Standard—International Tax Reform—Pillar Two Model Rules* as well as development in Australia. If relevant we will bring the RDR concession for Board consideration at its coming meetings.

Draft amending standard and signing memorandum

47. Attached as agenda item 6B.2 is the draft for-profit amending standard *International Tax Reform—Pillar Two Model Rules (Amendments to NZ IAS 12)* identical to *International Tax Reform—Pillar Two Model Rules (Amendments to IAS 12)* issued by the IASB except for the New Zealand-specific introduction and a scope paragraph limiting the application of the amending standard to Tier 1 and Tier 2 for-profit entities. We have also modified the commencement and application paragraphs to comply with legislative requirements in New Zealand and added New Zealand specific Basis for Conclusion (see paragraphs 28-32 above).

48. Attached as agenda item 6B.3 is a draft signing memorandum from the Chair of the NZASB to the Chair of the XRB Board.

Questions for the Board

Q1. Does the Board have any questions or comments on the draft amending standard?

Q2. Does the Board AGREE that at this stage there should not be any RDR concessions with respect to the disclosure requirements in the amending standard?

Q3. Does the Board APPROVE for issue the amending Standard *International Tax Reform—Pillar Two Model Rules (Amendments to NZ IAS 12)*?

Q4.	Does the Board APPROVE the signing memorandum from the Chair of the NZASB to the Chair of the XRB Board, requesting approval to issue the amending standard?

Attachments

Agenda item 6B.2: Draft *International Tax Reform—Pillar Two Model Rules (Amendments to NZ IAS 12)*

Agenda item 6B.3: Draft signing memorandum

PBE Policy Approach

49. As *International Tax Reform—Pillar Two Model Rules*

    (a) relates to a new topic; and

    (b) amends IAS 12, which is the basis for PBE IAS 12 *Income Taxes*,

    we are required to apply the PBE Policy Approach to determine whether to propose amendments to the PBE Standards.

50. Table 1 below considers the factors in the development principle as it applies to *International Tax Reform—Pillar Two Model Rules.*

Table 1 – Application of the PBE Policy Approach to International Tax Reform—Pillar Two Model Rules

Are the amendments minor?
No. The amendments introduce temporary mandatory exception to the requirements in NZ IAS 12 to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes.
Will the IPSASB consider these amendments in an acceptable timeframe?
No. There is no equivalent IPSASB Standard to IAS 12 *Income Taxes* as entities reporting on IPSAS basis generally do not pay income taxes.
Will the potential development lead to higher quality financial reporting?
Yes. The amending standard will introduce temporary mandatory exception to the requirements in NZ IAS 12 to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes which will prevent developing different interpretations of NZ IAS 12 in practice that might result in inconsistent application of the Standard and misleading information to users of financial statements.

The amending standard also require to disclose known or reasonably estimable information that helps users of financial statements understand the entity's exposure to Pillar Two income taxes. However, we do not expect that many (if any) New Zealand PBE entities will be subject to Pillar Two income taxes and therefore the extent of improvement will likely be limited.
Will the benefits outweigh the costs?
Yes. *Relevant to the PBE sector as a whole?* The Rules apply to entities that are members of MNE Group that have consolidated annual revenues of at least EUR 750 million in at least two of the last four fiscal years. The Rules exclude governmental entities, international entities and non-for-profit organisations[5] unless such organisation carry on a trade or business. The Rules also exclude taxpayers who have no foreign presence. This means that a PBE can be in scope of Pillar Two tax if it carries on a trade or business, its turnover is greater the 750m Euro, and it has operations in more than one country. In theory, there could be NZ PBE within the scope of the Rules, but based on the discussion with IRD and based on review of the Charities Register we are not aware of any such entity. *Whether the benefits will outweigh the costs* Should a PBE be subject to the Pilar Two income tax it should be granted the exception to the requirements in NZ IAS 12 to recognise and disclose information about deferred tax assets and liabilities related to this tax. As discussed previously, providing this information would be costly and potentially wouldn't bring benefits to the users of financial statements. *Coherence of the suite of PBE Standards* The amendments would affect only PBE IAS 12. There are no consequential amendments to other PBE Standards so the coherence of the suite of PBE Standards would be maintained. *Impact on mixed groups* Should a PBE be subject to the Pilar Two income tax, developing amendments to the PBE Standards would promote a consistent approach and could have a positive impact on mixed groups. However, we do not expect that many (if any) New Zealand PBE entities will be subject to Pillar Two income taxes and therefore the extent of benefits will likely be limited.

Staff recommendation

51. Based on the analysis in the Table 1 above we consider that NZASB should incorporate the amending standard *International Tax Reform—Pillar Two Model Rules* into the equivalent PBE Standards.

[5] For the detail definition of non-for-profit entity please refer to paragraphs 69-75 of the chapter 10 of the GloBE Rules Commentary.

52. Considering that we are not aware of any New Zealand PBE that is subject to Pillar Two income taxes we believe there is no urgency to develop the equivalent amendments to the PBE Standard and we recommend consulting those amendment together with the *2023 Omnibus Amendments to PBE Standards* which we plan to issue in New Zealand in June 2024 with mandatory application date 1 January 2025.

Questions for the Board

Q5. Does the Board AGREE to develop amendments to PBE IAS 12 based on *International Tax Reform—Pillar Two Model Rules*?

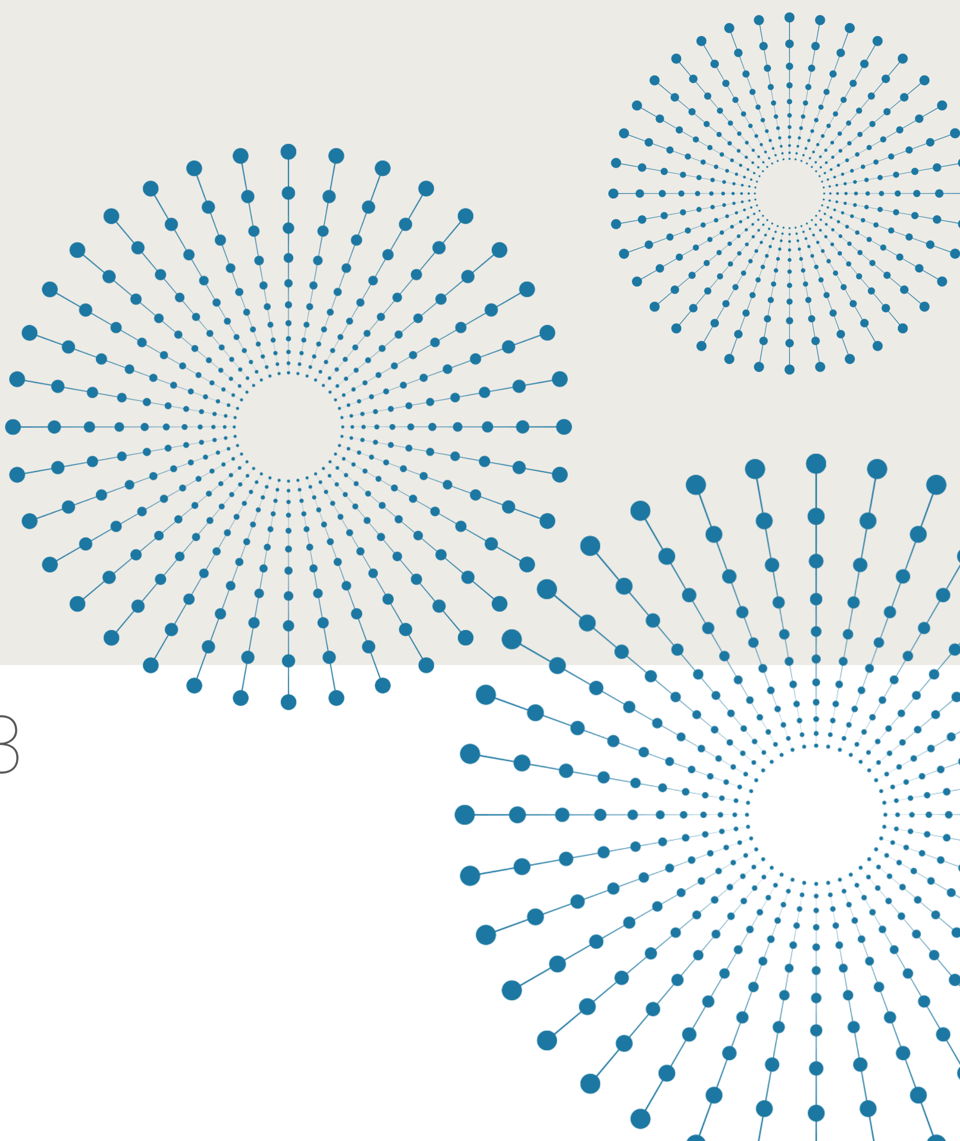
Q6. Does the Board AGREE to consult those amendments together with *2023 Omnibus Amendments* to PBE Standards?

Agenda Item 6B.2

XRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

International Tax Reform—Pillar Two Model Rules

(Amendments to NZ IAS 12)



Issued July 2023

International Tax Reform—Pillar Two Model Rules

Issued July 2023

This Tier 1 and Tier 2 for-profit amending Standard is based on *International Tax Reform—Pillar Two Model Rules*, issued by the International Accounting Standards Board, which amended IAS 12 *Income Taxes*. This amending Standard give entities temporary relief from accounting for deferred taxes arising from the Organisation for Economic Co-operation and Development's (OECD) international tax reform.

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

Legal status of amending Standard

This amending Standard was issued on XX July 2023 by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This amending Standard is secondary legislation for the purposes of the Legislation Act 2019.

The amending Standard, pursuant to section 27(1) of the Financial Reporting Act 2013, takes effect on the 28th day after the date of its publication. The amending Standard was published under the Legislation Act 2019 on XX July 2023 and takes effect on XX August 2023.

Commencement and application

The amending Standard has a mandatory date of 1 January 2023, meaning it must be applied by Tier 1 and Tier 2 for-profit entities for accounting periods that begin on or after 1 January 2023 but have not ended or do not end before this amending Standard takes effect (see paragraph NZ 98M.2).

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

APPROVAL BY THE IASB OF *INTERNATIONAL TAX REFORM – PILLAR TWO MODEL RULES* IN MAY 2023

AMENDMENTS TO THE IASB BASIS FOR CONCLUSIONS ON IAS 12 *INCOME TAXES*

IASB DISSENTING OPINION

Part A – Introduction

This amending Standard sets out amendments to NZ IAS 12 Income Taxes. The amendments give entities a temporary exception to the requirements to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes, i.e., taxes arising from the Organisation for Economic Co-operation and Development's (OECD) international tax reform. The amendments further introduce targeted disclosure requirements for entities affected by the Pillar Two income taxes.

Tier 2 entities are required to comply with all the requirements in this amending Standard.

Part B – Scope

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

Part C – Amendments to NZ IAS 12 *Income Taxes*

Paragraphs 4A, 88A – 88D and NZ 98M.1 – NZ 98M.2 are added including their related heading and the box after paragraph 88D. For ease of reading, new text is not underlined.

Scope

…

4A This Standard applies to income taxes arising from tax law enacted or substantively enacted to implement the Pillar Two model rules published by the Organisation for Economic Co-operation and Development (OECD), including tax law that implements qualified domestic minimum top-up taxes described in those rules. Such tax law, and the income taxes arising from it, are hereafter referred to as 'Pillar Two legislation' and 'Pillar Two income taxes'. As an exception to the requirements in this Standard, an entity shall neither recognise nor disclose information about deferred tax assets and liabilities related to Pillar Two income taxes.

…

Disclosure

…

International tax reform—Pillar Two model rules

88A An entity shall disclose that it has applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes (see paragraph 4A).

88B An entity shall disclose separately its current tax expense (income) related to Pillar Two income taxes.

88C In periods in which Pillar Two legislation is enacted or substantively enacted but not yet in effect, an entity shall disclose known or reasonably estimable information that helps users of financial statements understand the entity's exposure to Pillar Two income taxes arising from that legislation.

88D To meet the disclosure objective in paragraph 88C, an entity shall disclose qualitative and quantitative information about its exposure to Pillar Two income taxes at the end of the reporting period. This information does not have to reflect all the specific requirements of the Pillar Two legislation and can be provided in the form of an indicative range. To the extent information is not known or reasonably estimable, an entity shall instead disclose a statement to that effect and disclose information about the entity's progress in assessing its exposure.

Examples illustrating paragraphs 88C–88D

Examples of information an entity could disclose to meet the objective and requirements in paragraphs 88C–88D include:

(a) qualitative information such as information about how an entity is affected by Pillar Two legislation and the main jurisdictions in which exposures to Pillar Two income taxes might exist; and

(b) quantitative information such as:

(i) an indication of the proportion of an entity's profits that might be subject to Pillar Two income taxes and the average effective tax rate applicable to those profits; or

(ii) an indication of how the entity's average effective tax rate would have changed if Pillar Two legislation had been in effect.

…

~~Effective date~~ Commencement and application

…

International Tax Reform—Pillar Two Model Rules

NZ 98M.1 *International Tax Reform—Pillar Two Model Rules*, published in July 2023, added paragraphs 4A and 88A–88D. An entity shall:

(a) apply paragraphs 4A and 88A on the date that this amending Standard takes effect (see paragraph NZ 98M.2) and for annual reporting periods that have not ended or do not end before that date. An entity shall apply those paragraphs as if they had always been applied, in accordance with NZ IAS 8; and

(b) apply paragraphs 88B–88D for annual reporting periods beginning on or after 1 January 2023 but have not ended or do not end before this amending Standard takes effect (see paragraph NZ 98M.2). An entity is not required to disclose the information required by these paragraphs for any interim period ending on or before 31 December 2023.

When amending Standard takes effect (section 27 Financial Reporting Act 2013)

NZ 98M.2 The amending Standard takes effect on the 28th day after the date of its publication under the Legislation Act 2019. The amending Standard was published on XX July 2023 and takes effect on XX August 2023.

…

Basis for Conclusions on NZ IAS 12

Paragraph NZ BC1 and the related heading are added. For ease of reading, new text is not underlined.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, NZ IAS 12.

International Tax Reform—Pillar Two Model Rules July 2023

NZ BC1 The IASB's *International Tax Reform – Pillar Two Model* Rules Basis for Conclusions states "BC117 The IASB decided to require an entity to apply the temporary exception retrospectively. This requirement would result in an entity applying the exception from the date Pillar Two legislation is enacted or substantively enacted—even if that date is before the date of issuing the amendments—and would not result in additional

costs." The NZASB considered whether this would be appropriate in accordance with the requirements in the Legislation Act 2019, which does not allow legislation to have retrospective effect in New Zealand. The NZASB noted that application for periods that have ended before this amending Standard takes effect would be inappropriate. However, for annual reporting periods that have not ended or do not end before this amending Standard takes effect, entities may apply the requirements of the amending Standard in accordance with the commencement and application provisions. The NZASB has amended the commencement and application provisions to reflect the legislative requirements in New Zealand.

XRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Memorandum

Date:	XX July 2023
To:	Michele Embling, Chair External Reporting Board
From:	Carolyn Cordery, Chair NZASB
Subject:	***International Tax Reform—Pillar Two Model Rules***

Introduction[1]

1. In accordance with the protocols established by the XRB Board, the NZASB seeks your approval to issue *International Tax Reform—Pillar Two Model Rules* which amends NZ IAS 12 *Income Taxes.*

2. This amending standard is aligned with *International Tax Reform—Pillar Two Model Rules*, issued by the International Accounting Standards Board (IASB) in May 2023, which amended IAS 12 *Income Taxes*.

3. The IASB's issued those amendments in response to stakeholders' concerns about the potential implications for income tax accounting resulting from jurisdictions implementing the Pillar Two Model Rules which arise from the OECD international tax reform.

4. The IASB decided to introduce a temporary exception to the requirements in IAS 12 to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes. The IASB concluded that doing so would:

   (a) provide affected entities with relief from accounting for deferred tax assets and liabilities in relation to complex new tax legislation to be enacted by multiple jurisdictions in a short period of time;

   (b) avoid the development of diverse interpretations of IAS 12 and the resulting inconsistent application of the standard; and

   (c) allow time for stakeholders to assess how the Pillar Two Model Rules have been implemented in different jurisdictions, for entities to assess how they are affected and for the IASB to consider whether to do further work.

5. The amending standard also introduces requirements to disclose:

   (a) that the entity has applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes;

   (b) known or reasonably estimable information that helps users of financial statements understand the entity's exposure to Pillar Two income taxes in periods in which Pillar Two legislation is enacted or substantively enacted but not yet in effect; and

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

(c) information about current tax expense (income) related to Pillar Two income taxes separately from other income taxes.

Due process

6. The IASB issued Exposure Draft ED/2023/1 *International Tax Reform—Pillar Two Model Rules* (ED/2023/1) in January 2023.

7. The NZASB issued the ED for comment in New Zealand around the same time. Comments were due to the NZASB on 15 February 2023 and to the IASB on 10 March 2023.

8. The NZASB did not comment on ED/2023/1 and received one comment letter from Cantin Consulting which was sent directly to IASB as well.

9. The IASB received 98 comment letters from its world-wide constituents, including the Cantin Consulting submission and a joint submission from CPA Australia and CA ANZ (CPA/CAANZ).

10. Following its consideration of comments from constituents, the IASB reviewed the due process steps that it had taken since the publication of ED/2023/1 and concluded that the applicable due process steps had been completed. This review of due process occurred at the IASB supplementary meeting in April 2023.[2]

11. The IASB issued *International Tax Reform—Pillar Two Model Rules* in May 2023. This amending standard is effective for annual periods beginning on or after 1 January 2023 and the temporary mandatory exception to the requirements in IAS 12 to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes is effective immediately upon the issue of these amendments.

12. The NZASB has approved *International Tax Reform—Pillar Two Model Rules*. The due process followed by the NZASB complied with the due process requirements established by the XRB Board and, in the NZASB's view, meets the requirements of section 22 of the Financial Reporting Act 2013.

13. In accordance with section 22(2) of the Financial Reporting Act 2013 the NZASB has considered whether the amending standard is likely to require the disclosure of personal information. In the NZASB's view the amending standard does not include requirements that would result in the disclosure of personal information and therefore no consultation with the Privacy Commissioner is required.

Consistency with XRB Financial Reporting Strategy

14. The amending standard is a standard in its own right. The amending standard is identical to *International Tax Reform—Pillar Two Model Rules* issued by the IASB, except for the following inclusions:

    (a) A New Zealand specific introduction, formatting and numbering;

    (b) a scope paragraph explaining that the standard applies to Tier 1 and Tier 2 for-profit entities; and

[2] An update on the IASB meeting in April 2023 is available here.

(c) New Zealand-specific commencement and application date provisions (refer to paragraphs 20-22 and Appendix A).

15. The amending standard establishes some new disclosure requirements. The NZASB noted that there is a basis for providing RDR concessions in respect of some of the disclosures required in periods in which Pillar Two legislation is enacted or substantively enacted but not yet in effect. However, at this stage the NZASB decided not to not propose any RDR concessions considering:

    (a) the urgent need for amendments to NZ IAS 12 given the imminent implementation of the Pillar Two Model Rules in some jurisdictions;

    (b) the time needed to develop a domestic ED to seek feedback on the RDR concessions; and

    (c) the relatively short period in which Pillar Two legislation is enacted or substantively enacted but not yet in effect in New Zealand.

16. The NZASB will deliberate whether to develop a domestic ED on the RDR concessions. This deliberation will consider decisions made by

    (a) the IASB regarding disclosure requirements about impacts of Pillar Two income taxes for SMEs and subsidiaries without public accountability; and

    (b) the AASB regarding Tier 2 reporting requirements made at its June meeting.

17. The Australian Accounting Standards Board (AASB) is expected to approve/approved the equivalent Australian Accounting Standard in June 2023.

18. In 2020 the AASB issued a stand-alone disclosure standard, AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities*. Prior to this New Zealand and Australia had equivalent RDR regimes and New Zealand's Tier 1 and Tier 2 for-profit reporting requirements were aligned with those in Australia. The AASB now considers whether to add new disclosure requirements to AASB 1060 on a case by case basis. The AASB is expected to consider/considered the effect of the new amending standard on AASB 1060 in June 2023.

19. The issue of this amending standard is consistent with all three elements of the Financial Reporting Strategy: it adopts the international standard, retains a harmonised position with Australia for Tier 1 for-profit entities and is consistent with the Accounting Standards Framework.

Commencement and application date

20. The commencement and application date requirements for the amending standard is included in Appendix A of this memo. An entity is required to apply the amending standard for accounting periods beginning on or after 1 January 2023, but which do not end before the amending standard takes effect.

21. The temporary mandatory exception to the requirements in NZ IAS 12 to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes will be applicable on the date that this amending Standard takes effect, for periods not

ended before that date. The date when the amending standard takes effect is defined in Appendix A.

22. For any interim period ending on or before 31 December 2023, an entity is not required to provide disclosure requirements other than the information that it has applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes.

Other matters

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

Recommendation

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

Attachments

International Tax Reform—Pillar Two Model Rules

Certificate of determination

Carolyn Cordery
Chair NZASB

Appendix A: Commencement and application

A1. The commencement and application provisions below will apply to the amending standard once it is published.

When standard takes effect (section 27 Financial Reporting Act 2013)

A2. The amending Standard takes effect on the 28th day after the date of its publication under the Legislation Act 2019. The amending Standard was published on XX July 2023 and takes effect on XX August 2023.

Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Agenda Item 7.1

Memorandum

Date:	16 June 2023
To:	NZASB Members
From:	Gali Slyuzberg and Charis Halliday
Subject:	**IASB ED *Amendments to the Classification and Measurement of Financial Instruments***

COVER SHEET

Project priority and complexity

Project priority	**Medium** The proposed amendments to IFRS 9 in the ED are generally narrow in scope, but some of the proposals relate to transactions that are prevalent in New Zealand and/or are of importance to New Zealand stakeholders.
Complexity of Board decision-making at this meeting	**Low** The Board is being asked to approve the comment letter, which is broadly supportive of the IASB's proposals but recommends improvements in certain specific areas.

Overview of agenda item

Project status	• Review and approval of comment letter to the IASB
Project purpose	• The ED proposes amendments to IFRS 9 *Financial Instruments* to address matters raised during the first stage of the PIR of IFRS 9.
Board action required at this meeting	APPROVE the comment letter on the IASB ED *Amendments to the Classification and Measurement of Financial Instruments*. We encourage any editorial comments to be sent directly to staff - gali.slyuzberg@xrb.govt.nz

Purpose and introduction[1]

1. In March 2023, the International Accounting Standards Board (IASB) issued the Exposure Draft *Amendments to the Classification and Measurement of Financial Instruments* (ED). The ED proposes narrow-scope amendments to IFRS 9 *Financial Instruments* and IFRS 7 *Financial Instruments: Disclosures*, in response to:

   (a) feedback received on the Request for Information *Post-implementation Review of IFRS 9—Classification and Measurement* (RFI); and

   (b) a recent IFRS Interpretation Committee discussion relating to the recognition of cash received via an electronic transfer system as settlement for a financial asset.

2. At its April 2023 meeting, the Board agreed to comment on the ED. Comments are due to the IASB by 19 July 2023.

3. The purpose of this memo is to seek the Board's approval of the comment letter on the ED, subject to updating the letter for any comments identified by the Board at this meeting.

Recommendation

4. We recommend that the Board:

   (a) PROVIDES FEEDBACK on the draft comment letter on IASB ED *Amendments to the Classification and Measurement of Financial Instruments* (Agenda Item 7.3); and

   (b) APPROVES the comment letter, subject to staff processing any changes identified by Board Members at this meeting.

Structure of this memo

5. This memo includes the following sections.

   (a) Background

   (a) Approach to responding to the ED and outreach

   (b) ED questions that we have addressed in the comment letter

      i. Settling financial liabilities using an electronic payment system

      ii. Classification of financial assets: contractual terms that are consistent with a basic lending arrangement – and related disclosures

   (c) ED questions that we recommend not to address in the comment letter

   (d) Approval of the comment letter

   (e) Next steps

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

Background

6. In 2021, as part of its post-implementation review (PIR) of IFRS 9, the IASB consulted on the RFI *Post-implementation Review of IFRS 9 – Classification and Measurement*. The RFI sought feedback on whether the classification and measurement requirements in IFRS 9 are operating as intended – i.e. whether these requirements are meeting their objectives and resulting in useful information, whether entities are able to apply these requirements consistently, and whether the costs of applying these requirements are as expected.

7. Based on the feedback from PIR participants, the IASB concluded that:

   (a) In general, entities are able to apply the classification and measurement requirements of IFRS 9 consistently, and the requirements are resulting in useful information being provided in the financial statements;

   (b) However, the requirements on some matters should be clarified to improve their understandability.

8. A key matter raised by PIR participants internationally related to the classification and measurement of financial assets with features linked to environmental, social and governance (ESG) matters. Specifically, PIR participants asked the IASB to clarify how the assessment of contractual cash flow characteristics – also known as the 'solely payments of principal and interest' test (SPPI test) – applies to such financial assets. PIR participants noted that, because such financial assets are rapidly becoming more prevalent, clarification is required to avoid diversity in practice becoming established. We note that similar comments were raised in New Zealand when we consulted on the PIR of IFRS 9 with New Zealand stakeholders.

9. International PIR participants also asked the IASB to clarify the application of the SPPI test to non-recourse loans and contractually linked instruments. Some PIR participants expressed concerns about the 'non-recycling' of gains on equity investments measured at fair value through other comprehensive revenue and expense (OCI).

10. To address the matters raised by RFI respondents, the IASB issued the ED *Amendments to the Classification and Measurement of Financial Instruments* – which includes:

    (a) proposals to clarify the application of the 'SPPI test', including with respect to financial assets with ESG-linked features, non-recourse loans and contractually-linked instruments; and

    (b) proposed additional disclosure requirements with respect to equity investments classified and measured at fair value through OCI.

11. Furthermore, in response to feedback received on a recent tentative agenda decision, the ED also proposes to allow financial liabilities settled via electronic transfer to be de-recognised before the settlement date, if specific criteria are met.

12. The ED is available here (and is attached as Agenda Item 7.4 in the Supporting Papers), and the IASB's 'snapshot' summary of the ED is available here.

Approach to responding to the ED and outreach

General comments on the approach to the comment letter

13. When the Board agreed to comment on the ED at its April 2023 meeting, the Board envisaged a brief comment letter that is:

    (a) broadly supportive – given that the ED aims to addresses concerns raised by New Zealand constituents during the PIR of IFRS 9, and given that the ED proposals generally seemed sensible based on staff's preliminary review; and

    (b) includes any comments or concerns that we hear from stakeholders.

Outreach and feedback

14. As per our usual consultation process, the ED was published on the XRB website and publicised through our newsletters. The Board also agreed that staff should carry out targeted outreach to inform the comment letter.

15. As part of the abovementioned targeted outreach, we have discussed the ED with the Accounting TRG in May 2023. We reflected the TRG's feedback in the draft comment letter. More information on the TRG discussion is included further below.

16. Staff also attended a roundtable organised by professional accounting bodies. The points raised at the roundtable event were broadly consistent with the TRG discussion, with some additional matters being raised. While staff did not make significant changes to the comment letter to reflect all points raised at the roundtable (noting that these comments will be raised in others' submissions to the IASB), staff updated the draft letter for certain points made at the roundtable discussion when they further elaborated on points raised by the TRG.

17. Comments on the ED were due to the XRB by 7 June 2023. At the time of writing, we have received a submission from one constituent – please see agenda item 7.2. The comments relate to the ED proposals on financial instruments with ESG-linked features. We have incorporated these comments into the draft comment letter.

18. We are aware of New Zealand constituents that plan to submit a comment directly to the IASB. In our understanding, the content of their comment letter is expected to be broadly consistent with our draft comment letter, except that their letter will also include additional comments and cover more of the ED questions.

Selection of ED questions to respond to

19. In selecting the ED questions to respond to, staff considered that the following topics should be covered in the comment letter:

    (a) topics specifically mentioned by New Zealand constituents during our consultation on the first stage of the PIR of IFRS 9 in 2021; and

    (b) topics dealing with transactions that have high prevalence among New Zealand entities.

20. On this basis, staff selected the following topics to cover in the comment letter:

    (a) De-recognition of a financial liability settled through electronic transfer [ED Question 1]: We expect that most, if not all, New Zealand reporting entities settle financial liabilities via electronic transfer. New Zealand electronic cash transfer systems are efficient and settlement times via these systems tends to be short. However, we understand that it is still possible that an electronic payment initiated on balance date might be completed on the following date (e.g. if the payment was initiated late in the day, etc.). Therefore, requirements relating to timing of financial liabilities settlements and derecognition can be relevant to New Zealand constituents.

    (b) Classification of financial assets – contractual terms that are consistent with a basic lending arrangement, and related disclosures [ED Questions 2 and 6]: These proposals were driven by requests to clarify the accounting for financial instruments with ESG-linked features – and we have heard similar comments from New Zealand stakeholders during the PIR of IFRS 9, indicating that this topic is of relevance in New Zealand.

21. The sections that follow summarise the proposals on the above two topics, as well as our discussion with the TRG on those topics and how it was reflected in the comment letter.

22. For those ED topics that we did not cover in the comment letter, we have checked with TRG Members the assumption that the ED proposals on these topics are unlikely to cause significant concerns in New Zealand.

ED questions that we have addressed in the comment letter

Settling financial liabilities using an electronic payment system [ED Question 1]

Summary of the proposals and rationale

Rationale for the proposals

23. In 2021, the IFRS Interpretations Committee issued the tentative agenda decision Cash Received via Electronic Transfer as Settlement for a Financial Asset. The tentative agenda related to a receivable that is settled via an electronic transfer of cash, which is initiated before year end but completed after year end. The tentative decision noted that under the existing requirements of IFRS 9 (including the 'settlement date accounting' requirements), the cash is recognised only once it is received in the entity's bank account, and not before – and the receivable is derecognised when the contractual rights to the receivable expire.

24. Respondents to the tentative agenda decision generally agreed with the Committee's technical analysis. However, they expressed concerns about the implications that this agenda decision would have on the accounting for financial liabilities settled via electronic cash transfers (as well as on the accounting for payments via cheque, credit card, etc.) – and that the agenda decision would cause a significant change to established accounting practice.

Proposed requirements on derecognition of financial liabilities settled via electronic transfer

25. The IASB acknowledged stakeholders' concerns regarding the tentative agenda decision, and decided to address them together with other matters arising from the PIR of IFRS 9. To address these concerns, the IASB ED includes proposals that:

    (a) clarify that an entity uses settlement date accounting when recognising or derecognising financial assets and financial liabilities – except as permitted under (b) below; and

    (b) permit an entity to deem a financial liability that is settled using an electronic payment system to be discharged before the settlement date if specified criteria are met.

26. Under the proposals, an entity would be permitted to derecognise a financial liability before the settlement date if and only if the entity has initiated the payment instruction and:

    (a) the entity has no ability to withdraw, stop or cancel the payment instruction;

    (b) the entity has no practical ability to access the cash to be used for settlement as a result of the payment instruction; and

    (c) the settlement risk associated with the electronic payment system is insignificant.

27. An entity derecognising a financial liability before the settlement date in line with the requirements in the paragraph 17 above shall apply those requirements to all settlements made through the same electronic payment system.

28. Please refer to the ED paragraphs B3.1.2A and B3.3.8 – B3.3.10 of the draft amendments to IFRS 9 for the proposed wording. Paragraphs BC5–BC34 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Scope of the proposed requirements

29. The scope of the proposed derecognition option is limited to settling financial liabilities using an electronic payment system, and will not include other types of disbursements, nor does it include the financial asset side.

30. The IASB considered whether the proposed requirements could be applied to a wider population of cash payments, but decided to limit the scope to cash settlements using electronic payment systems that meet the specified criteria, without otherwise changing the application of the derecognition requirements in IFRS 9.

31. The IASB noted that widening the scope of the proposed derecognition option to other types of settlements could give rise to a number of conceptual and practical challenges, including the risk that cash could be seen as being treated differently from other financial assets for the purposes of the derecognition requirements in IFRS 9.

32. Paragraphs BC35–BC38 of the Basis for Conclusions explain the IASB's rationale for these decisions.

Preliminary staff views and TRG discussion

33. Staff's preliminary views was that the ED proposals to allow financial liabilities settled via electronic transfer to be derecognised generally seemed sensible. That is, it makes sense to allow an entity to derecognise a financial liability on the date of the initiating the payment instruction (provided that the 'settlement risk' is low) – as opposed to requiring entities to wait until the settlement date before the liability can be derecognised.

34. TRG Members broadly agreed that the proposals were reasonable, but they noted the following concerns.

    (a) The amendments introduce an asymmetry between the treatment of financial liabilities that are settled via an electronic payment system and financial assets that are settled via the same method. Under the amendments, settlement date accounting must still be applied to the de-recognition of financial assets settled via electronic transfer – whereas financial liabilities settled via electronic transfer can be de-recognised before the settlement date when certain conditions are met.

    (b) To be able to de-recognise a liability before the settlement date, entities would need to find out how much time they have to withdraw or cancel the electronic payment (even if they do not intend to cancel the payment). Entities may find it challenging and/or time-consuming to collect this information, particularly when entities make payments using the systems of various banks in various countries.

    (c) It would be useful if the IASB clarified what it means by 'electronic payment system', to clarify what types of payments are in the scope of the proposed accounting policy choice.

Comments from other stakeholders – external roundtable

35. We note that at the external roundtable we attended, certain additional comments were raised which are somewhat related to the TRG's point regarding the challenge of determining when an electronic payment cannot be cancelled or withdrawn.

36. The comments related to two of the proposed criteria for de-recognising a financial liability before the settlement date: (a) the entity has no ability to withdraw, stop or cancel the payment instruction, and; (b) that the entity has no practical ability to access the cash to be used for settlement as a result of the payment instruction [paragraph B.3.38 of the ED]. In this regard, roundtable attendees noted the following:

    (a) An entity would usually meet criterion (a) and criterion (b) at the same time, i.e. it is unlikely for one criterion to be met and the other not to be met.

    (b) Criterion (a) requires the entity to have *no ability* to withdraw, stop or cancel the payment, whereas criterion (b) requires having *no practical* ability to access the cash to be used for settlement. It is not clear why criterion (a) is subject to a higher threshold of ability than criterion (b).

Comment letter

37. We have reflected the comments above in our draft comment letter – except for the comment about the asymmetric treatment of financial assets and financial liabilities that are settled via electronic payment systems.

38. We did not include comments about asymmetry in the comment letter for the following reasons.

    (a) In our understanding, a key practical issue arising from the abovementioned asymmetric de-recognition requirements for financial assets and financial liabilities is that in case of intercompany loans/receivables, it is possible that the creditor entity would de-recognise an intercompany loan/payable before the settlement date, whereas the debtor entity would be required to wait until the settlement date before de-recognising the related intercompany financial asset. If settlement date is after year end, this can create an issue upon consolidation. However, we note that the de-recognition of financial liabilities before settlement date would be an accounting policy choice. Therefore, if the abovementioned asymmetry results in a consolidation issue, it is possible to choose not to apply the early derecognition accounting policy.

    (b) We also note that when the IASB was considering possible standard-setting actions in relation to financial assets and financial liabilities settled via electronic transfer, the staff paper from the IASB's October 2022 meeting noted the following regarding asymmetry between the recognition and derecognition of financial assets and financial liabilities: "The recognition and derecognition requirements in IFRS 9 are generally symmetrical—in other words, if one entity has a financial asset, another entity will have a financial liability (or equity instrument). However, there is not necessarily symmetry in the timing of recognition and derecognition. An entity assesses its rights to receive cash and obligation to pay cash from its own perspective, based on the information it has at the reporting date; it does not base its accounting on what the counterparty has done."

    (c) We also note that the concerns raised by respondents to the tentative agenda decision on electronic transfers mainly related to the settlement of financial liabilities, rather than financial assets -- therefore, we think it is sensible not to amend the de-recognition requirements for financial assets at this time, while still addressing stakeholders' concerns in relation to financial liabilities.

39. Our draft response to Question 1 is included in paragraphs 1–3 of the comment letter in agenda item 7.3.

Question for the Board

Q1. Does the Board agree with our response to Question 1 of the ED in Agenda Item 7.3 – which relates to the ED proposals on the derecognition of financial liabilities settled via electronic transfer?

Classification of financial assets: contractual terms that are consistent with a basic lending arrangement – and related disclosures [Questions 2 and 6]

Summary of the proposals and rationale

40. For a financial asset to be classified and measured at amortised cost, one of the conditions is that the contractual cash flows from the asset must be 'solely payments of principal and interests on the principal amounts outstanding' – known as the 'SPPI test'. For the SPPI test to be met, the principal and interest need to be consistent with a 'basic lending arrangement'.

41. Respondents to the PIR of IFRS 9 noted difficulties in applying the SPPI test for financial assets with ESG-linked or similar features. They noted that amortised cost would be the most relevant method for measuring such financial assets. However, due to changes in the interest rate being dependent on ESG-related targets, etc., such instruments might fail the SPPI test under the current requirements – resulting in measurement at fair value through profit or loss. Similar comments about financial assets with ESG-linked features had been made by New Zealand constituents.

42. The IASB considered that the SPPI test is as relevant to financial assets with ESG-linked features as to other financial assets. To address respondents' concerns, the IASB ED proposes:

    (a) To clarify in general how to determine whether the contractual cash flows from a financial asset – including changes in contractual cash flows that depend on a contingent event – are consistent with a 'basic lending arrangement';

    (b) To provides examples of the application of the SPPI test, including the 'basic lending arrangement' requirements, to financial assets with ESG-linked features; and

    (c) To require additional disclosures in relation to financial assets where there are contractual terms that can change the timing or amount of contractual cash flows based on the occurrence/non-occurrence of a contingent event.

43. The IASB's proposals are outlined below.

Table 1 Summary of proposals relating to ED Question 2 and Question 6

Topic	Summary of proposals	ED ref
Clarifications on how to assess consistency with 'basic lending arrangement' **[ED Question 2]**	The ED proposes to clarify that: (a) when assessing whether contractual cash flows are consistent with interest in a basic lending arrangement, the assessment of interest focuses on what an entity is being compensated for, rather than how much compensation an entity receives; and (b) contractual cash flows are inconsistent with a basic lending arrangement if: (i) the cash flows include compensation for risks or market factors not typically considered basic lending risks or costs, even if such terms are common in the market; and (ii) the cash flows change in a way that is not aligned with the direction and magnitude of changes in lending risks or costs.	Amendments to IFRS 9, para B4.1.8A;

Topic	Summary of proposals	ED ref
	The ED also proposes to clarify the following when financial assets contain contractual terms that could change the timing or amount of contractual cash flows following the occurrence (or non-occurrence) of a contingent event: (a) an entity shall assess whether the contractually specified change would meet the SPPI requirement irrespective of the probability of the contingent event occurring; (b) a change in contractual cash flows is consistent with a basic lending arrangement if the occurrence (or non-occurrence) of the contingent event is specific to the debtor; and (c) the resulting contractual cash flows should represent neither an investment in the debtor nor an exposure to the performance of specified assets.	Amendments to IFRS 9, para B4.1.10A
Example relating to financial instruments with ESG-linked features **[ED Question 2]**	The ED includes the following example: "Instrument EA is a loan with an interest rate that is periodically adjusted by a specified number of basis points if the debtor achieves a contractually specified reduction in greenhouse gas emissions during the preceding reporting period." The ED says that this instrument meets the SPPI test: "The contractual cash flows are solely payments of principal and interest on the principal amount outstanding. The occurrence of the contingent event (achieving a contractually specified reduction in greenhouse gas emissions) is specific to the debtor. The contractual cash flows arising from the occurrence (or non-occurrence) of the contingent event are in all circumstances solely payments of principal and interest on the principal amount outstanding. […]."	Amendments to IFRS 9, para B4.1.13
	The ED also includes another example (Instrument I), where the interest rate on a loan is adjusted when the market-determined carbon price index reaches a contractually-defined threshold. The ED notes that in this example, the loan fails the SPPI test – because the contractual payments are based on a market factor that is not a basic lending risk or cost.	Amendments to IFRS 9, para B4.1.14
Disclosures relating to contractual terms that change the timing and amount of cash flows from a financial asset **[ED Question 6]**	An entity would be required to disclose: (a) a qualitative description of the nature of the contingent event; (b) quantitative information about the range of changes to contractual cash flows that could result from the contractual terms; and (c) the gross carrying amount of financial assets and the amortised cost of financial liabilities subject to those contractual terms. An entity would disclose the information above separately for each class of financial assets measured at amortised cost or fair value through OCI and for each class of financial liabilities measured at amortised cost. This information would be required irrespective of the likelihood of the contingent events.	Amendments to IFRS 7, para 20B and 20C

44. Paragraphs BC98–BC104 of the Basis for Conclusions explain the IASB's rationale for the proposed requirements and examples above, and paragraphs BC98–BC104 of the Basis for Conclusions explain the IASB's rationale for the proposed disclosures.

Preliminary staff views

45. While staff considered the proposals on this topic to be sensible, staff were concerned that it is not clear from the ED *how and why* contractual cash flows that vary based on the achievement of ESG-related targets are consistent with a 'basic lending arrangement' as described in IFRS 9. Further details are provided below.

    (a) IFRS 9 currently states that in a basic lending arrangement, typical elements of interest include compensation for the time value of money, credit risk, other basic lending risks (such as liquidity risk), and costs associated with holding the financial asset—as well as a profit margin.

    (b) The ED does not change the above description of a 'basic lending arrangement' – it only adds further guidance – including that when contractual cash flows can change based on a contingent event, the cash flows must meet the SPPI requirements regardless of whether the contingent event occurs, and that the contingent event must be specific to the debtor for the SPPI test to be met.

    (c) In the example relating to 'Instrument EA' (see above), it is clear that "the occurrence of the contingent event (achieving a contractually specified reduction in greenhouse gas emissions) is specific to the debtor".

    (d) However, it is not clear how and why "the contractual cash flows arising from the occurrence (or non-occurrence) of the contingent event are in all circumstances solely payments of principal and interest on the principal amount outstanding". That is, it is not clear how changes in the interest rate and related cash flows based on the debtor's achievement of greenhouse gas emission targets is consistent with a 'basic lending arrangement' and the basic lending risks and costs as described in IFRS 9.

TRG discussion

46. TRG Members noted the following regarding the prevalence of financial assets with ESG-linked features in New Zealand.

    (a) TRG Members have not seen many loans with ESG-linked features yet, they expect the prevalence of such loans to grow in the future. Also, at the moment, contractually specified changes in interest that are based on ESG-related targets tend to be 'de minimis', and therefore do not tend to affect the SPPI assessment.

    (b) However, TRG Members expect loans with ESG-linked features to become more prevalent in the future. Also, TRG Members expect that in the future, the impact of ESG-linked features on interest would be more than 'de-minimis', when such instruments become more prevalent and market participants gain more experience with such instruments. It can be challenging to prove that a loan is 'green' if the ESG-linked features have a 'de-minimis' impact on the interest.

47. Therefore, TRG Members thought it was important to clarify the accounting for financial assets with ESG-linked features, and to achieve an appropriate outcome in relation to their classification. Classification and measurement of such loans at amortised cost, rather than fair value, was seen as an appropriate outcome.

48. However: TRG Members agree with staff that that the IASB should clarify how contractual cash flows that vary based on the achievement of ESG-related targets are consistent with a 'basic lending arrangement' – as this is currently unclear from the ED. A TRG Member noted that the amount of greenhouse gas emissions produced by the debtor could be linked to the debtor's credit risk – but this link needs to be clarified.

49. In addition, a TRG Member noted a concern regarding the proposed requirement: "For a change in contractual cash flows to be consistent with a basic lending arrangement, the occurrence (or non-occurrence) of the contingent event must be specific to the debtor". The Member noted that this requirement could cause financial assets that are not consistent with a 'basic lending arrangement' to meet the SPPI test, which would not be appropriate.

50. Staff also discussed with the TRG the proposed disclosures in the ED in relation to financial assets that have contractually specified changes in cash flows that depend on the occurrence of a specified event.

51. TRG Members did not note concerns about proposed disclosures. Comments on the disclosures included the following.

    (a) Given the current level of interest in ESG-related matters, some preparers would welcome the opportunity to provide disclosures on the topic of ESG as per the proposed disclosure requirements (although this may not be the case when the ESG-based targets are not being achieved).

    (b) The disclosure would help address 'greenwashing', as they would help identify loans where the ESG-linked features are substantive.

Additional comments from external roundtable

52. The discussion at the external roundtable highlighted the importance of being clear around the *principles* that are relevant in assessing whether a financial instruments with ESG-linked features is consistent with a basic lending arrangements – to ensure that these principles can be applied to other types of instruments – rather than adding ad-hoc guidance and examples.

53. Regarding the proposed disclosures about financial assets where there are contractual terms that can contractual cash flows based on the occurrence of a contingent event, it was noted that the scope of the disclosures was broad, and that there was some overlap between the proposed disclosure requirements and existing disclosure requirements in IFRS 7.

Comments from submission received

54. We have received comments on the ED from one respondent – see Agenda Item 7.2. The respondent recommended that the IASB should provide more detailed guidance on the topic of financial instruments with ESG-linked features, particularly given the current international focus on climate change and the development of related financial products.

55. Specifically, the respondent recommends clarifying the application of the SPPI test – particularly, the proposal that to meet the SPPI test, contingent events that change

contractual cash flows must be specific to the debtor – to loans with ESG-linked targets of the types mentioned below.

(a) For a loan contract where interest is adjusted based on whether the debtor is in the top 20% of sustainability leaders for a particular industry or group, it is not clear from the ED whether the condition of meeting the 'top 20%' target qualify as a contingent event that is specific to the debtor. Meeting this target is partially dependent on the debtor's actions, but it is also dependent on the actions of other entities.

(b) In some loans with ESG-linked features, the ESG-based target relates to the *group* that the debtor is part of, rather than debtor entity itself. For example, the interest on a loan may be adjusted based on whether the debtor's parent entity achieves certain ESG-based targets. It is not clear whether such a target constitutes a contingent event that is specific to the debtor.

56. The respondent recommended adding examples to cover the above situations and other common types of ESG-linked targets.

Comment letter

57. We have reflected the comments above in our response to ED Questions 2 and 6 in the draft comment letter – please refer to paragraphs 4–16 of Agenda Item 7.3.

Question for the Board

Q2. Does the Board agree with our response to Questions 2 and 6 of the ED in Agenda Item 7.3 – which relate to the ED proposals to clarify the assessment of whether cash flows are consistent with a 'basic lending arrangement' for the purpose of the SPPI test, and the proposed disclosures relating to cash flows that can change based on a contingent event?

ED questions that we recommend not to address in the comment letter

58. We recommend not commenting on the following ED topics, for the reasons explained in the table below.

Table 2 ED questions that we recommend not to comment on

Topic	Summary of proposals	ED ref	Reasons not to comment
Financial assets with non-recourse features **[ED Question 3]**	For financial assets with non-recourse features, the IASB proposes to clarify that, for a financial asset to have such features, the entity's contractual right to receive cash flows must be limited to the cash flows from the specified assets both over the life of the financial asset and in the case of default. The entity is therefore primarily exposed to the specified assets' performance risk rather than the debtor's credit risk over the life of the instrument. The entity may also need to consider	Amendments to IFRS 9, paragraphs B4.1.16, B4.1.16A, B4.1.17, and B4.1.17A – and paragraphs BC73-BC79 of the Basis for Conclusions	We have not heard significant concerns about financial assets with non-recourse features and/or investments in contractually linked instruments when we consulted on the IASB's RFI on the first stage of the PIR of IFRS 9. The TRG did not express concerns about the

Topic	Summary of proposals	ED ref	Reasons not to comment
	factors such as the legal and capital structure of the debtor.		proposals on this topic at the May 2023 TRG meeting.
Contractually linked instruments **[ED Question 4]**	To help identify whether the investments in contractually linked instruments meet the SPPI requirement, the IASB proposes to clarify the characteristics of contractually linked instruments through specific reference to the concentrations of credit risk that result in the disproportionate allocation of losses between different tranches. The IASB also proposes to clarify, that transactions involving the creation of Special Purpose Entity (SPE) – i.e., a structured entity that issues multiple debt instruments to facilitate a lending transaction with a single creditor – do not contain contractually linked instruments.	Amendments to IFRS 9, Paragraphs B4.1.20, B4.1.20A, B4.1.21, and B4.1.23 – and paragraphs BC80-BC93 of the Basis for Conclusions.	
Disclosure – investment in equity instruments designated as fair value through other comprehensive income **[ED Question 5]**	the IASB proposed additional disclosure requirements to help users of financial statements to better evaluate the performance of investments in equity instruments for which subsequent changes in fair value are presented in other comprehensive income. An entity would be required to disclose: (a) the change in the fair value of investments in equity instruments during the reporting period, showing separately the amount of that change related to investments derecognised during the reporting period and the amount related to investments held at the end of the reporting period; and (b) the aggregate fair value of investments in equity instruments (rather than the fair value of each investment) at the end of the reporting period.	Amendments to IFRS 7, paragraphs 11A(c) and 11A(f).	While we have heard that investments in equity instruments are sometimes incorrectly classified as fair value through OCI during the first stage of the PIR of IFRS 9, this was identified as an educational matter, rather than a concern with the requirements in IFRS 9. We also understand that investments in equity instruments classified as fair value through OCI is not overly common in the for-profit sector in New Zealand. The TRG did not express concerns about the proposed disclosures on this topic at the May 2023 TRG meeting. A TRG Member noted that the proposed disclosures may not achieve much, but was not concerned.
Transition **[ED Question 7]**	The ED proposes that entities would be required to apply the amendments retrospectively, but not to restate comparative information. The ED also proposes that an entity be required to disclose information about financial assets that changed measurement category as a result of applying these amendments.	Paragraphs 7.2.47–7.2.49	We considered that the transitional requirements were sensible and did not have specific comments on them.

Question for the Board

Q3. Does the Board agree not to respond to ED Questions 3–5 and 7?

Approval of the comment letter

59. The draft comment letter, including a cover page and an appendix with our detailed responses to ED Questions 1, 2 and 6, is included in Agenda Item 7.3. We recommend that the Board approve the letter – subject to staff updating the letter for any changes identified by Board Members at this meeting, and having those changes finalised via review by the Chair.

Question for the Board

Q4. Does the Board have any other comments on the draft comment letter in Agenda Item 7.3?

Q5. Does the Board approve the comment letter, subject to any changes raised by the Board at this meeting being finalised via review by the Chair?

Next steps

60. We will update the draft comment letter for any changes identified by the Board at this meeting. After finalising these changes via review by the Chair, we will send before the due date of 19 July 2023.

Attachments

Agenda item 7.2	Submission
Agenda item 7.3	Draft comment letter
Agenda item 7.4	IASB ED *Amendments to the Classification and Measurement of Financial Instruments* (in the Supporting Papers)

IASB ED *Amendments to the Classification and Measurement of Financial Instruments*
Email from Karl Hickey – received on 14 June 2023

Subject: IFRS 9 - Climate Change Reporting Guidance

Hi Anthony

Hopefully it is not too late to provide the NZASB with comments to Question 2 of the IASB's invitation for comment on the proposed Amendments to the Classification and Measurement of Financial Assets.

1. **Summary**

The proposed amendments to IFRS 9 include guidance on applying the requirements for assessing contractual cash flow characteristics to financial assets with features linked to environmental, social and governance (ESG) concerns. However in my view it would be appropriate for the IASB to include more detailed guidance in this area – particularly given the current international focus on Climate Change reporting and product development.

Below I have detailed several areas that the existing guidance does not seem to cover.

2. **Details**

Paragraph B4.1.10A notes that "for a change in contractual cash flows to be consistent with a basic lending arrangement, the occurrence (or non-occurrence) of the contingent event must be specific to the debtor. The occurrence of a contingent event is specific to the debtor if it depends on the debtor achieving a contractually specified target, even if the same target is included in other contracts for other debtors".

I have some questions about the application of this guidance in the following scenarios and believe the examples in sections B4.1.13 and B4.1.14 could be usefully extended to include these and other common targets which result in amendments to the debtor's interest rate and impact the assessment of whether an instrument's cash flows are solely payments of principal and interest on the principal amount outstanding:

a) Where a contract might provide for a benefit on meeting particular sustainability targets. For example if a loan contract allowed for an interest adjustment if a particular client was in was in the top 20% of sustainability leaders for a particular industry or index.

   It is unclear whether such a target would be considered specific to the debtor since achieving that target is not fully within the debtor's control. That is, inclusion in the index is dependent on what other entities do to improve their CSA ? relative to the debtor.

b) Im aware that in some instances a target may be specific to the Group the debtor forms part of but not specific to the debtor itself (for example if the financing is to a subsidiary of a larger Group). Where the interest adjustment applies to the say, 100% owned subsidiary entity but the target ranking applies to the parent entity, would this satisfy the requirements of B4.1.10A?

Further clarification of how the guidance is intended to apply in such instances would be appropriate.

Please let me know if you would like to discuss these comments further or me to provide any further information.

Kind regards
Karl

Karl Hickey | ANZ | Head of NZ Financial Governance & Policy

Mr Andreas Barckow

XX June 2023

Chairman of the International Accounting Standards Board
IFRS Foundation
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Submitted to: www.ifrs.org

Dear Andreas

IASB/ED/2023/2 *Amendments to the Classification and Measurement of Financial Instruments* (Proposed amendments to IFRS 9 and IFRS 7) *('the ED')*

Thank you for the opportunity to comment the ED, which has been exposed for comment in New Zealand. In developing our responses to the ED, we have focused on those questions that we considered would be of most relevance to New Zealand stakeholders.

While we are generally supportive of the ED proposals, we have the following **recommendations**:

Derecognition of financial liabilities settled via electronic transfer:

- Clarifying the meaning of 'electronic payment system'; and
- Addressing concerns about the challenges of determining when precisely the entity is unable to withdraw or cancel an electronic payment.

Classification of financial assets – clarifications relating to 'basic lending arrangements':

- Explaining in the amendments how and why contractual cash flows that vary based on the achievement of ESG-related targets are consistent with a 'basic lending arrangement'; and
- Clarifying the application of requirements relating to contingent events that are specific to the debtor.

Our recommendations and responses to the specific questions for respondents are provided 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) or me.

Yours sincerely

Carolyn Cordery
Chair – New Zealand Accounting Standards Board

Appendix

Question 1 – Derecognition of a financial liability settled through electronic transfer
Paragraph B3.3.8 of the draft amendments to IFRS 9 proposes that, when specified criteria are met, an entity would be permitted to derecognise a financial liability that is settled using an electronic payment system although cash has yet to be delivered by the entity. Paragraphs BC5–BC38 of the Basis for Conclusions explain the IASB's rationale for this proposal. Do you agree with this proposal? If you disagree, please explain what aspect of the proposal you disagree with. What would you suggest instead and why?

Response to Question 1

1. We agree with the proposals to allow a financial liability that is settled via an electronic payment system to be derecognised on the date of initiating the payment instruction (provided that the 'settlement risk' is low) – as opposed to requiring entities to wait until the settlement date before the liability can be derecognised.

2. However, we recommend that the IASB clarify what constitutes an 'electronic payment system', i.e. what types of electronic payments are within the scope of the proposed policy choice for derecognising a liability before the settlement date. Specifically, it would be useful to clarify whether the proposals only relate to the settlement of liabilities via instructions to the bank to transfer money from one bank account to another, or whether it also includes other methods of settling liabilities electronically, such as payments via debit card (with debit cards being linked directly to bank accounts, and therefore being similar to electronic fund transfer via an instruction to the bank). Furthermore, we think it would be useful to clarify the principle for determining whether a type of electronic payment is within the scope of the accounting policy choice, in order to 'future proof' these requirements for new types of electronic payments.

3. Furthermore, we have heard concerns that it may be challenging and time-consuming for entities to ascertain the exact point at which the criteria in paragraph B3.3.8(a) would be met, i.e. whether and for how long the entity has the ability to cancel or withdraw an electronic payment instruction – particularly when an entity uses the services of various banks in different countries, whose electronic payment systems might operate differently in this regard. We recommend considering the following options for addressing this matter.

   (a) Paragraph B3.3.8(a) could be updated to refer to the *practical* ability to withdraw or cancel the payment instruction – rather than the ability to do so in general. This would make the principle of this requirement consistent with paragraph B3.3.8(b) – which refers to the entity having no *practical ability* to access the cash to be used for settlement of the liability).

   (b) We are aware of feedback that in terms of the de-recognition criteria in paragraphs B3.3.8(a) and B3.3.8(b), it is very unlikely for an entity to meet one criterion and not the

other. That is, the criterion of not being able to stop, cancel or withdraw the payment instruction and the criterion of not being able to access the cash to be used for settling the liability are generally met at the same time. Therefore, to streamline the requirements and to make it easier for entities to determine when they can de-recognise a financial liability before the settlement date, it could be useful to reduce these two criteria into a single criterion, and have this criterion refer to *practical* ability.

(c) Consider providing additional guidance to help entities assess when practical ability to cancel or withdraw the payment and/or access the related cash exists.

We have responded to Questions 2 and Question 6 together:

Question 2 – Classification of financial assets—contractual terms that are consistent with a basic lending arrangement

Paragraphs B4.1.8A and B4.1.10A of the draft amendments to IFRS 9 propose how an entity would be required to assess:

(a) interest for the purposes of applying paragraph B4.1.7A; and

(b) contractual terms that change the timing or amount of contractual cash flows for the purposes of applying paragraph B4.1.10.

The draft amendments to paragraphs B4.1.13 and B4.1.14 of IFRS 9 propose additional examples of financial assets that have, or do not have, contractual cash flows that are solely payments of principal and interest on the principal amount outstanding.

Paragraphs BC39–BC72 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree, please explain what aspect of the proposals you disagree with. What would you suggest instead and why?

Question 6 – Disclosures—contractual terms that could change the timing or amount of contractual cash flows

Paragraph 20B of the draft amendments to IFRS 7 proposes disclosure requirements for contractual terms that could change the timing or amount of contractual cash flows on the occurrence (or non-occurrence) of a contingent event. The proposed requirements would apply to each class of financial asset measured at amortised cost or fair value through other comprehensive income and each class of financial liability measured at amortised cost (paragraph 20C).

Paragraphs BC98–BC104 of the Basis for Conclusions explain the IASB's rationale for this proposal.

Do you agree with this proposal? Why or why not? If you disagree, please explain what aspect of the proposal you disagree with. What would you suggest instead and why?

Response to Questions 2 and 6

4. We support the IASB's initiative to clarify in general the assessment of whether cash flows are consistent with a 'basic lending arrangement' for the purpose of applying the 'solely payments of principal and interest test' ('SPPI test') – and to clarify in particular how to make this assessment for financial assets with ESG-linked features.

5. However, we recommend clarifying the proposals relating to financial assets with ESG-linked features, and considering further the impact of proposals relating to contingent events that are specific to the debtor. More information is provided below.

Support for the initiative to clarify 'basic lending arrangement' and the classification of financial assets with ESG-linked features

6. Our stakeholders have highlighted the importance of clarifying the classification of financial assets with ESG-linked features. The following are comments that stakeholders raised during the PIR of IFRS 9 and/or the current consultation on the ED.

   (a) During the first stage of the PIR of IFRS 9, stakeholders noted that under the current requirements of IFRS 9, it can be unclear whether a loan with ESG-linked features is consistent with a 'basic lending arrangement' and therefore whether it passes or fails the 'SPPI test' (when the ESG-linked features are not 'de minimis' – see below). Stakeholders noted that generally, classification of such loans at amortised cost seems the appropriate outcome and would provide useful information – but without further clarification of the existing requirements in IFRS 9, there is a risk that such loans would fail the SPPI test and would need to be measured at fair value. This could have the unintended consequence of discouraging banks and other financial institutions from offering such loans.

   (b) Stakeholders noted that it is timely to address this matter. They acknowledged that, loans with ESG-linked features are currently not highly prevalent in New Zealand, and that contractually-specified changes in interest rates resulting from ESG-linked features are mostly 'de-minimis' at this stage (and therefore do not materially impact the classification and measurement of such loans). However, they noted that loans with ESG-linked features are likely to become more common in the future. Such loans are already being used in the electricity and agriculture industries in New Zealand. Also, it is expected that when financial assets with ESG-linked feature become more prevalent and as the market gains more experience with such instruments, the impact of ESG-linked features on interest would become more substantial – as it will become more and more challenging to prove that a loan is 'green' if the ESG-linked features have a 'de-minimis' impact on the interest.

Recommendation to clarify <u>how</u> financial assets with ESG-linked features are consistent with a 'basic lending arrangement

7. We note that the ED proposes to include the following example underneath paragraph B4.1.13, in relation to financial assets with ESG-linked features:

   "Instrument EA is a loan with an interest rate that is periodically adjusted by a specified number of basis points if the debtor achieves a contractually specified reduction in greenhouse gas emissions during the preceding reporting period."

8. The ED says that this instrument meets the SPPI test, noting that "the occurrence of the contingent event (achieving a contractually specified reduction in greenhouse gas emissions) is specific to the debtor", and the contractual cash flows are "in all circumstances solely payments of principal and interest on the principal amount outstanding".

9. Based on feedback from stakeholders, it is not clear from the wording of this example (or from the other proposed amendments in the ED) how and why the cash flows of Instrument EA are consistent with a 'basic lending arrangement' and therefore meet the SPPI test – and we recommend clarifying this. Further explanation is provided below.

   (a) In our understanding, the proposed additional requirements about cash flows that are subject to change based on contingent events do not change the fact that such cash flows still need to be consistent with a 'basic lending arrangement', as described in existing paragraph B4.1.7A, in order for the financial asset to pass the SPPI test.

   (b) While it is clear from the 'Instrument EA' example that the changes in the cash flows are specific to the debtor, which is consistent with the new guidance in paragraph B4.1.10A, in our understanding this is not sufficient for meeting the description of 'basic lending arrangement' in paragraph B4.1.7A.

   (c) Existing paragraph B4.1.7A states that in a basic lending arrangement, interest typically reflects the debtor's credit risk and the time value of money, as well as other basic lending risks and costs associated with holding the asset, such as liquidity risk, and a profit margin. We recommend clarifying *to which of these basic lending risks or costs do the changes in cash flows based on the achievement of greenhouse gas emission targets relate*. For example, it may be that the achievement of greenhouse gas emission target is considered to be related to the debtor's credit risk. If that is the case, then we think it is important to explain this.

   (d) It is important that the *principles* driving the decision that 'Instrument EA' is consistent with a basic lending arrangement and meets the SPPI test are clearly articulated. This would be useful for preparers when applying these principles to other types of financial assets with ESG-linked features, and to other types of assets with variable contractual cash flows that depend on a contingent event.

Recommendation to further consider the proposed requirement for a contingent event to be specific to the debtor

10. We have heard concerns with respect to the following proposed requirement in paragraph B4.1.10A: "For a change in contractual cash flows to be consistent with a basic lending arrangement, the occurrence (or non-occurrence) of the contingent event must be specific to the debtor."

11. Stakeholders noted that this proposal could cause financial assets that are not consistent with a 'basic lending arrangement' to meet the 'SPPI test', and to be reclassified from fair value through surplus or deficit to amortised cost, which would not be appropriate. We consider it is important to ensure that the proposed requirement does not unintentionally bring financial assets that are more usefully measured at fair value into the amortised cost category.

12. We recommend clarifying in paragraph B4.1.10A that when the occurrence or non-occurrence of the contingent event is specific to the debtor, this fact on its own does not mean that the change in contractual cash flows is consistent with a basic lending arrangement – and that it is necessary to consider the description of 'basic lending arrangement' in paragraph B4.1.7A

when assessing whether a change in contractual cash flow that is subject to a debtor-specific contingent event is consistent with a basic lending arrangement for the purpose of the SPPI test.

13. We are also aware of certain loans with ESG-linked features where, under the ED proposals, it could be challenging to determine whether an ESG-linked target represents a contingent event that is specific to the debtor. This is the case for the following types of loans.

    (a) *Loans where achievement of the ESG-linked target is partially dependent on the debtor*: For a loan contract where interest is adjusted based on whether the debtor is in the top X% of sustainability leaders for a particular industry or group, it is not clear from the ED whether the condition of meeting the 'top X%' target qualifies as a contingent event that is specific to the debtor. Meeting this target is partially dependent on the debtor's actions, but it is also dependent on the actions of other entities.

    (b) *Loans where the ESG-linked target relates to the group that the debtor is part of*: In some loans with ESG-linked features, the ESG-based target relates to the *group* that the debtor is part of, rather than debtor entity itself. For example, the interest on a loan may be adjusted based on whether the debtor's parent entity achieves certain ESG-based targets. It is not clear whether such a target constitutes a contingent event that is specific to the debtor.

14. We recommend clarifying how the assessment of whether a contingent event is specific to the debtor should be applied to the types of situations above. This could be done by way of examples, similarly to the examples added for 'Instrument EA' and 'Instrument I', taking into account our recommendations above to clearly articulate the principles driving the decisions in the examples. Alternatively, this could be done by adding paragraphs with guidance on contingent events that are dependent partially on the debtor and partially on external factors, and contingent events that are specific to the group that the debtor is part of, but not the debtor itself.

Proposed disclosures on contractual terms that could change the timing or amount of contractual cash flows based on the occurrence of a contingent event

15. We do not have significant concerns about the proposed disclosures, although we are aware of feedback that the scope of the disclosures is relatively broad.

16. One of the benefits of the proposed disclosures highlighted by our stakeholders is that they could help combat 'greenwashing', by making it clear to users of financial statements whether the ESG-linked features of a loan are indeed substantive, i.e. whether they substantively impact the cash flow of the loan or not.

Questions 3–5 and 7

17. We have not commented on these questions.