

30 April 2013

Ms Stephenie Fox
The Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street West
Toronto, Ontario M5V 3H2 CANADA

Dear Ms Fox

**IPSASB Conceptual Framework Exposure Draft 2:
Elements and Recognition in Financial Statements**

Please find attached comments from the Australasian Council of Auditors-General (ACAG) on the IPSASB Exposure Draft referred to above.

The views expressed in this submission represent those of the Australian members of ACAG. While all Australian members of ACAG hold a common view on some aspects of this Exposure Draft, there exist different views amongst the members in connection with the proposed definition of deferred inflows and deferred outflows as separate elements, and the proposed treatment of increases/decreases therein.

While the different views relate principally to Specific Matter for Comment 5 and have been outlined within that area, these differences also impact Specific Matters for Comment 3, 4 and 6. The comments set out in this submission which reflect the view of the majority of the Australian members of ACAG are titled 'Main view', with a 'Divergent view' within Specific Matter for Comment 5 reflecting the view of two members.

The opportunity to comment is appreciated and I trust you will find the attached comments useful.

Yours sincerely



Simon O'Neill
Chairman
ACAG Financial Reporting and Auditing Committee

Specific Matter for Comment 1

Do you agree with the definition of an asset? If not, how would you modify it?

ACAG suggests amending the definition of an asset for the use the term “future economic benefits” instead of “economic benefits” in order to be consistent with the IASB Conceptual Framework;

Specific Matter for Comment 2

(a) Do you agree with the definition of a liability? If not, how would you modify it?

ACAG agrees with the definition of a liability.

However, ACAG does not agree with the view expressed in paragraph BC22 of the Basis for Conclusions that “distinguishing between conditional and unconditional obligations is not useful for the purpose of defining a liability because it is possible for conditional obligations to give rise to liabilities”. Unconditional stand-ready obligations (which are liabilities) and conditional obligations (which may be liabilities in certain situations) are useful concepts, at least as guidance in determining whether a liability exists. The IPSASB’s concern that obligations to stand ready to provide social benefits might be inappropriately recognised as liabilities in the statement of financial position is a recognition issue, which can then be addressed in the recognition section of the Framework (ideally) or at a standards level.

Similarly, ACAG does not agree with paragraph BC26 that it would not be appropriate to use the term “performance obligation” in the Framework. The concept of performance obligations is fundamental to the upcoming IFRS on revenue recognition and therefore should also be discussed by the IPSASB in the context of the definition of a liability.

(b) Do you agree with the description of non-legal binding obligations? If not, how would you modify it?

ACAG agrees with the description of non-legal binding obligations. We agree that liabilities can arise from non-legal binding obligations as explained in paragraph 3.10 of the Exposure Draft.

Specific Matter for Comment 3

Do you agree with the definition of revenue? If not, how would you modify it?

Main view

Most Australian members of ACAG suggest amending the definition of revenue for the following:

- Exclude inflows that result from decreases in deferred inflows from the definition of revenue in accordance with the Alternative View of Prof. Mariano D’Amore. Please refer to our response to SMC 5(a) below.
- Modify the phrase ‘inflows during the current reporting period’ as inflows are generally associated with cash-based reporting. We recommend that the term ‘increases in economic resources or benefits’ replaces the term ‘inflows’ as this is consistent with IFRS terminology, and better reflects the concept of accrual accounting.

ACAG view

In addition, paragraph 4.7 of the ED states that “the difference between revenue and expenses is the entity’s surplus or deficit for the period, which is the primary indicator of financial performance”. We are not sure whether this will be addressed in Phase 4 of the Framework on Presentation in General Purpose Financial Reports, but it should be made clear that surplus or deficit in the Exposure Draft is different from surplus or deficit in the existing standards which excludes items like revaluation surpluses/losses (i.e. items of other comprehensive income (OCI) under IFRSs). We believe that the IPSASB should discuss the concept of OCI items as part of the Framework (as is being proposed by the IASB in its Conceptual Framework project).

Specific Matter for Comment 4

Do you agree with the definition of expenses? If not, how would you modify it?

Main view

Most Australian members of ACAG suggest amending the definition of expenses for the following:

- Exclude outflows that result from decreases in deferred outflows from the definition of expenses in accordance with the Alternative View of Prof. Mariano D’Amore. Please refer to our response to SMC 5(a) below.
- Consistently with the comment in SMC 3 above, replace the term ‘outflows’ with the term ‘decreases in economic resources or benefits’ as this is consistent with IFRS terminology, and better reflects the concept of accrual accounting.

ACAG view

Please also refer to our comment in SMC 3 above on OCI items.

Specific Matter for Comment 5

(a) Do you agree with the decision to define deferred inflows and deferred outflows as elements? If not, why not?

Main view

Most Australian members of ACAG support the decision to define deferred inflows and deferred outflows as elements. They agree with the rationale set out in paragraphs BC35 and BC40 of the Basis for Conclusions. However, they do not support the proposed treatment of increases/decreases in deferred inflows and deferred outflows because this substantially modifies the generally understood concepts of revenue and expenses as changes in net assets. They support the Alternative View of Prof. Mariano D’Amore that increases/decreases in deferred inflows and deferred outflows should be considered as separate elements from revenue and expenses.

Divergent view

Two Australian members of ACAG do not support the decision to define deferred inflows and deferred outflows as elements. They are not convinced by paragraphs BC40-43 of the Basis for Conclusions that there is a need for new elements in financial statements to deal with specific non-exchange transactions. A new element for a specific group of transactions is not required, when it can be addressed through the definitions and recognition criteria of other elements, e.g. revenue, liability. Users will be further confused when deferred inflows and deferred outflows, and net financial position are defined, recognised and measured separately

from existing elements. The Exposure Draft will lead to two measures of financial performance and two measures of financial position.

These two Australian members of ACAG support the Alternative View of Ms Jeanine Poggiolini. As outlined in paragraph AV8, Ms Poggiolini disagrees with the identification and recognition of separate elements for deferred inflows and outflows, and believes that these flows should be included in the definitions of revenues and expenses. As a consequence these members also do not support the need to separately define net financial position (refer SMC 6 below), as it would result in the same figure net assets under the approach outlined in paragraph AV8.

(b) If you agree with the decision to define deferred inflows and deferred outflows as elements, do you agree with the:

- (i) Decision to restrict those definitions to non-exchange transactions? If not, why not?**
- (ii) Definitions of deferred inflows and deferred outflows? If not, how would you modify them?**

Main view

- (i) Most Australian members of ACAG agree with the decision to restrict the definitions to non-exchange transactions. They believe that the prevalence of non-exchange transactions in the public sector is a key distinguishing factor from the private sector and is a sufficiently strong rationale for creating the concepts of deferred inflows and deferred outflows (and hence not aligning with the IASB Conceptual Framework).
- (ii) Most Australian members of ACAG suggest amending the definition of deferred inflows and deferred outflows for the following:
 - Reference to “a specified future reporting period” should be changed to “a future reporting period”. These members of ACAG believe that limiting deferred inflows and deferred outflows to situations where the future period over which the resources can be used is specified (specifically documented) in an agreement is too restrictive and would not achieve the objective that revenue and expenses (and increases/decreases in deferred inflows and deferred outflows, if these are defined as separate elements as suggested in our response to SMC 5(a) above) are flows that relate to the current period. For example:
 - where an entity receives a grant;
 - the grant agreement states that the grant will fund a particular research project but does not specify a period; and
 - the research project will only be performed in the future,it would appear to be appropriate to defer the revenue.
 - Should the IPSASB decide to adopt a restrictive approach and continue to require a specified future reporting period:
 - the definition of “deferred inflow” should refer to “use in a future reporting period specified by an external party”; and
 - The definition of “deferred outflow” should refer to “use by that other entity or party in a future reporting period specified by the reporting entity”.

Specific Matter for Comment 6

- (a) **Do you agree with the terms net assets and net financial position and the definitions? If not, how would you modify the terms and/or definitions?**

Main view

Most Australian members of ACAG agree with the terms net assets and net financial position and the definitions.

- (b) **Do you agree with the decision to define ownership contributions and ownership distributions as elements? If not, why not?**

ACAG agrees with the decision to define ownership contributions and ownership distributions as elements.

- (c) **If you agree with the decision to define ownership contributions and ownership distributions as elements, do you agree with the definitions of ownership contributions and ownership distributions? If not, how would you modify them?**

ACAG agrees with the definitions of ownership contributions and ownership distributions.

- (d) **Ownership interests have not been defined in this Conceptual Framework. Do you think they should be?**

ACAG believes that the term ownership interests should be defined as it has economic substance, being ownership claims on the public sector entity's assets. This would ensure users are aware of any of the Government's net assets which may be attributable to outside third parties.

Specific Matter for Comment 7

Do you agree with the discussion on recognition? If not, how would you modify it?

ACAG agrees that recognition is a distinct stage in the accounting process so that the definitions of the elements do not include recognition criteria. However, we do not agree with the fact that, although there is a discussion of existence uncertainty and measurement uncertainty, there is an absence of any explicit recognition criteria or principles in the draft Framework. We believe this section of the Framework could be improved by:

- The inclusion of specific recognition criteria for elements, to be applied once all available evidence has been assessed in determining whether an element exists. Elements should be recognised where:
 - In the entity's judgement, the element exists; and
 - The cost or value of the element can be reliably measured.
- As mentioned in our response to SMC 2(a) above, it would be useful if recognition criteria or principles for social benefits obligations as liabilities in the statement of financial position are addressed in the Framework.

Other Matters

ACAG recommends that the Conceptual Framework provide additional emphasis on the significance of materiality based on the context and nature of an item because this is likely to be of particular importance for public sector entities.

In order to assist preparers, auditors and end-users, ACAG suggests that further discussion, examples and/or guidance be included in the Conceptual Framework on each of the elements of the financial statements.

ACAG supports the IPSASB's strategy of maintaining the alignment of IPSASs with IFRSs where appropriate for the public sector. The IPSASB should monitor closely the developments in the IASB Conceptual Framework project to see if these can be applied or adapted in the IPSASB project. We note that various bodies such as the European Financial Reporting Advisory Group (EFRAG) are actively contributing on the subject by issuing bulletins on various topics. Therefore, we believe that the IPSASB should not finalise its Framework until the IASB Conceptual Framework project has been completed.