UNITED NATIONS SYSTEM **SYSTEME DES NATIONS UNIES**

Chief Executives Board for Coordination

Conseil des chefs de secrétariat des organismes des Nations Unies pour la coordination

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

30 April 2013

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

Dear Stephenie,

Conceptual Framework Exposure Draft 2

1 Thank you for the opportunity to comment on Conceptual Framework Exposure Draft 2 (CF–ED2), *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Elements and Recognition in Financial Statements*.

United Nations System Task Force on Accounting Standards

2 The United Nations System Task Force on Accounting Standards (Task Force) appreciates the work that the IPSASB is carrying out in developing accounting standards for public sector entities, including international organizations such as those making up the United Nations system. The Task Force is an inter-agency group consisting of directors of accounting, chief accountants and chief financial officers from United Nations System organizations. The comments below represent the views of Members of the Task Force. The individual organizations that provided comments on this submission and concurred with its submission to the IPSASB are listed in Appendix 1. Where an individual organization disagreed with a particular recommendation but agreed to the recommendation going forward to the IPSASB, this has been noted against the individual responses in Appendix 2.

General Comments

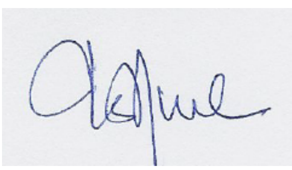
3 We support IPSASB's efforts in developing the Conceptual Framework, which establishes parameters for financial reporting under IPSAS and clarifies concepts not previously explicitly covered by the Standards. We note, however, that discussion in the CF-ED2, including majority of examples, focuses mainly on specific attributes and challenges of governments, making it less useful and applicable for use by other public sector entities.

Specific Matters for Comments

4 Our detailed comments on the specific matters for comment identified in CF-ED2 are attached in Appendix 2.

5 Should you have any queries on our comments, please contact Ms. Dinara Alieva, Financial Analyst, System-wide IPSAS Project Team at alievad@un.org.

Yours sincerely,



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APPENDIX 1: UNITED NATIONS SYSTEM TASK FORCE ON ACCOUNTING STANDARDS

Task Force Members from the following organizations reviewed this submission and concurred with its contents.

Organisation	Agree (Disagree)
1. FAO	Agree
2. IAEA	Agree
3. ICAO	Agree
4. ILO	Agree
5. IMO	Agree
6. ISA	Agree
7. ITU	Agree
8. PAHO	Agree
9. UN	Agree
10. UNAIDS	Agree
11. UNDP	Agree
12. UNESCO	Agree
13. UNFPA	Agree
14. UNHCR	Agree
15. UNICEF	Agree
16. UNIDO	Agree
17. UNOPS	Agree
18. UNRWA	Agree
19. UPU	Agree
20. WFP	Agree
21. WHO	Agree
22. WIPO	Agree
23. WMO	Agree
24. WTO (Tourism)	Agree
25. UNWomen	Agree

APPENDIX 2 - CONCEPTUAL FRAMEWORK FOR GENERAL PURSPOSE FINANCIAL REPORTING BY PUBLIC SECTOR ENTITIES: ELEMENTS AND RECOGNTION IN FINANCIAL STATEMENTS (CF-ED2 or Exposure Draft)

In response to the IPSASB's request for comments on these Specific Matters please find below comments of the Task Force:

Specific Matter for Comment 1

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

Response:

The Task Force agrees with the proposed definition of an asset and notes that it is generally in line with definition of an asset included in IPSAS 1 as well as Task Force comments previously provided on definition of an asset proposed by the Conceptual Framework Phase 2 Consultation Paper (CF-CP2).

The discussion on an asset being a resource appears to cover more ground than the definition of an asset and includes, among other dimensions, benefits that arise directly from the resource itself or from the rights to the resource (para. 2.2). Basis for Conclusions (BC) refers to current rights as a type of intangible asset (para. BC3). It also includes an example of the "right to require other parties to perform in a certain way, by, for example, making payments or providing goods and services in a manner specified by the entity" (para. BC4). A sovereign government has rights to require various parties operating within its jurisdiction to act in a certain way, which may or may not meet definition of benefits related to an asset. However there are also other scenarios in the public sector which are not considered in CF-ED2. For example, UN system organizations routinely engage external partners with specific expertise in implementing projects in various locations around the world. Agreements with implementing partners typically prescribe a manner in which goods and/or services should be provided to beneficiaries. When CF-ED2 describes the concept of the right to require other parties to perform in certain way it draws no distinction between sovereign rights of governments and a right to require other parties to perform in a certain way through routine contractual engagements. However the latter scenario may not give rise to a benefit and hence should be clearly differentiated in the CF-ED2.

The CF-ED2 also refers to entity's rights to benefits, including use of an external party's resource to provide services, for example, leases (para. 2.2). The Task Force is of the view that a more detailed discussion of a resource which embodies an entity's rights to a benefit would be helpful. More specifically in terms of leases, a decision of whether or not an asset exists for a lessee on the reporting date should be determined based on whether or not a lessee controls the asset at that date rather than on the fact that a lessee has a right to benefits associated with use of a leased resource. In this regard, it is noted that CF-ED2 refers to control of individual benefits from use of the resource as opposed to control over the resource in its entirety for determining whether an asset exists. This proposed concept is discussed further in the following section of the submission on control of an asset.

In addition, while governments typically have rights to a wide range of resources, use of external resources by other public sector entities are usually based on contractual arrangements between two willing parties. Such arrangements may be of non-exchange nature and/or involve nominal fees, but they may not necessarily constitute a right (or entitlement) to receive benefits from external resources.

On a closely related matter, the Task Force submission on CF-CP2 raised a question of recognition and measurement of donated rights to use assets and peppercorn rent, an area not yet covered by an IPSAS standard. The Task Force believes that IPSASB should consider reviewing these types of arrangements in detail in light of the proposed recognition of leases in CF-ED2.

Control of an asset

CF-ED2 builds on definition of control as the ability to exclude or regulate the access of others to the benefits of an asset (IPSAS 23) by listing three additional indicators. While (a) legal ownership has always been a traditional indicator, indicators (c) and (d) (para. 2.7) represent a much more defined version of the previously used concept that control of an asset "arises when the entity can use or otherwise benefit from the asset in pursuit of its objectives" (IPSASB Handbook 2012, Glossary of Defined Terms). CF-ED2 states that the entity should have "means to ensure that the resources are used to achieve its objectives" and should have an "enforceable right to service potential or economic benefits arsing from a resource". However it was noted that while the Basis for Conclusions discusses indicators (a) and (b) in detail it does not analyse indicators (c) and (d) and the impact which this more defined approach is expected to have on determining controlled assets in public sector. The Task Force is of the view that these indicators are important and that the Board should be is in a position to provide some principles-based guidance thereon.

It is important to note that the Basis for Conclusions considers ability to access a resource to be a solid indicator of control only if accompanied by the ability to deny or restrict the access of others to the resource (para. BC 14).

The Basis for Conclusions also warns against erroneous application of control to a "resource in its entirety and not to individual benefits that accrue from the resource" (para. BC 11). It is imperative that the Board expands discussion of this proposed concept in interpretation of control of an asset and its practical application and relocates it to the main body of the CF-ED2 due to its significance. It is also anticipated that recognition and measurement of assets based on the proposed approach would be very complex, especially in absence of clear guidance in CF-ED2, while benefits of the proposed approach are not indentified in the Exposure Draft. Due to these reasons the Task Force is not able to support this proposal at this time.

Past event

The discussion acknowledges a newly introduced concept that a right to a resource can give rise to a benefit and through it to an asset. However it then goes on to refer to the power to tax or to issue licenses as an example of “powers and rights that other non-public sector entities do not have” (para. 2.8). This new dimension of having ‘exclusive rights’ to regulate a process or an activity and its implications for definitions of past event and of an asset in general should be further discussed in CF-ED2.

There also appears to be an inconsistency between discussion in IPSAS 23 (para. 34) which states that “transactions or events expected to occur in the future do not in themselves give rise to assets – hence for example, an intention to levy taxation is not a past event that gives rise to an asset in the form of a claim against a taxpayer”, whereas CF ED-2 in its main body of text proposes that “general ability to tax” or “establishment of a power through a statute” can be considered as past events for recognition of an asset (para 2.8). At the same time, the Basis for Conclusions (para. BC 20) clarifies that “the IPSASB considered that a government’s inherent powers do not give rise to assets until these powers are exercised”. This clarification has to be included in the main body of the CF-ED2 to correct the above highlighted inconsistency.

Specific Matter for Comment 2

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

Response:

The Task Force notes that the proposed definition of a liability generally falls in line with definition of liabilities promulgated by IPSAS 1 as well Task Force comments on proposed definition of a liability in the CF-CP2, hence it is acceptable to the Task Force.

It was noted that the Basis for Conclusions (paras. BC 21-26) discusses such types of obligations as conditional and unconditional obligations, stand-ready obligations and performance obligations, but these are considered by the IPSASB to fall outside the scope of the Conceptual Framework. The Task Force concurs with this approach. The Task force refers to its comments on CF-CP2 where it recommended to the IPSASB to take a conservative approach while exploring the possibility of expanding types of obligations which can be classified as liabilities. The Task Force submission stated that “many public sector organizations carry out tasks that directly impact lives of millions of people in various regions of the world, and hence they are subjected to increased level of scrutiny from donors, recipients and general public. These organizations also often have to divert their activities and resources from initial plan to address people’s needs triggered by unexpected events and problems, like natural disasters or new areas of military conflict. It will not be possible or practical to have a comprehensive list of all obligations of organizations of such scale while recognizing and measuring these liabilities completely and reliably, with reasonable cost/benefit balance. Therefore, the position of the Task Force is that IPSASB should only consider introduction of new or expanded concepts to this element of financial statements if there is an intention to supplement them with in-depth analysis for all preparers of GPFSs who wish to conform to the Conceptual Framework".

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

Response:

IPSASB considers the term "constructive obligation" used in standard setting literature globally, including IPSAS, to be "difficult to interpret and apply in the public sector context" (BC 21). Therefore the Board proposes to focus on defining legal and non-legal binding obligations as a more straightforward approach.

Legal obligation is a well established concept which, according to IPSAS 19, "is an obligation that derives from:

(a) A contract (through its explicit or implicit terms);
(b) Legislation; or
(c) Other operation of law.

It was noted that the CF-ED2 also proposes to treat as legal those binding obligations which are created in jurisdictions where government and public sector entities cannot have legal obligations but where there are alternative processes with equivalent effect.

Constructive obligation, as defined by IPSAS 19, "is an obligation that derives from an entity's actions where:

(a) By an established pattern of past practice, published policies, or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and
(b) As a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities" (para.18).

In defining non-legal binding obligation the CF-ED2 borrowed above definition of the constructive obligation from IPSAS 19 and added a third attribute, as follows:

"(c) The entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities" (para. 3.10)

As IPSASB acknowledged that the term "constructive obligation" was difficult to interpret and apply in a public sector, the Task Force is not convinced that by adding a third attribute to the definition the CF-ED2 resolved the problem with the application of the term "constructive obligation" or "non-legal binding obligation" in public sector. In addition, the dimension of having 'no realistic alternative to avoid settling the obligation' is not completely new and is currently used in the Glossary of Defined Terms as well as in IPSAS 19 to define the "obligating event" (para. 18). The same dimension is also part of the new definition of a liability proposed by the CF-ED2 and appears to be the only rephrased part of both definitions when compared to existing IPSASs. This increases the importance of understanding the augmented role of this dimension in the Conceptual Framework and its application in the public sector.

CF-ED 2 attempts to include indicators that are likely to impact on decision whether or not the entity has little or no realistic alternative to avoid outflow of service potential or economic benefit, but the discussion is mainly focused on examples applicable to governments and remains at a highly theoretical level, which brings preparers of the GPFSs back to the same problem as encountered with the use of the term "constructive obligation".

The Task Force notes that assessment of enforceability of legal and non-legal binding obligations has not been sufficiently addressed by the CF-ED2 and recommends that this issue be rectified. The CF-ED2 would also benefit from inclusion of examples of legal and non-legal binding obligations applicable to public sector entities other than governments.

Specific Matter for Comment 3

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

Response:

The Task Force acknowledges similarities between the definition proposed by CF-ED2 as compared to the definition of revenue used in IPSAS 1 and notes that main difference between the definitions relates to the concept of changes in deferred inflows and outflows. New definition also excludes reference to inflow of economic benefits or service potential as attribute of the revenue, which broadens the definition and does not limit it to specific types of activities associated with main operations of an entity. As further discussed in the Basis for Conclusions, the IPSASB took the view that inflows and outflows related to activities outside of ordinary course of operations (for example, gains and losses) "do not differ from other forms of revenue and expenses, because they both involve net increases or decreases of assets and/or liabilities" (para. BC 38).

The Task Force agrees with the proposed definition of revenue, but would like to reserve the right to present other types of revenue and expenses on the face of financial statements as well as in the notes thereto should organizations consider that such disclosure would provide useful information to users of their financial statements. The IPSASB is requested to consider surrendering the decision on presentation of other types of revenue and expenses to preparers of the GPFSs while formulating views for Phase 4 of the Conceptual Framework "Presentation in General Purpose Financial Reports".

Although definition of revenue has not been significantly altered, it is clear that introduction of concept of deferred inflows and outflows in definition of the revenue is likely to have a significant impact on recognition and presentation of revenues and expenses in financial statements of entities which currently conform to requirements of IPSAS 23 which does not provide for recognition of inflows based on the period to which they relate.

The IPSASB would need to conceptually bridge the approach to revenue recognition proposed in CF-ED2 with that of IPSAS 23 to support preparers of the GPFS who wish to conform to both pronunciations of the Board.

The United Nations, a member of the Task Force, does not agree with definition of revenue proposed by the CF-ED2 as it does not sufficiently explain significance of deferred inflows to revenue recognition.

Specific Matter for Comment 4

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

The Task Force agrees with the proposed definition. Please see response to SMC 3 for further details.

Similar to the comment on SMC 3 above, the United Nations does not agree with definition of expenses proposed by the CF-ED2 as it does not sufficiently explain significance of deferred outflow to recognition of expenses.

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?

Response:

The Task Force supports in principle the proposal of CF-ED2 to define deferred inflows and outflows as separate elements of financial statements and takes note of the reasons that led the IPSASB to this decision as discussed in the Basis for Conclusions (paras. BC 40-43). However, the concept of deferred inflows and outflows should be explained in more detail, including addition of examples applicable to a wide range of public sector entities.

Some members of the Task Force note with interest alternative view of Ms. Jeanine Poggiolini and are inclined to support the IPSASB member's view that deferred inflows and outflows should be included in the definitions of revenues and expenses.

(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?

Response:

(i) The Task Force takes note of the discussion of risks and benefits of restricting definitions of deferred inflows and outflows to non-exchange transactions presented in the Basis for Conclusions (paras. BC 44-46) and has no reservations against the proposed approach. In addition, revenue from exchange transactions is regulated by IPSAS 9 which addresses 'applicability' of the revenue to the reporting period through its recognition based on the stage of completion of underlying transaction/activity.

(ii) The Task Force agrees with proposed definitions of deferred inflows and outflows. It was noted that although the CF-ED2 states that conditional revenues or expenses cannot be classified as deferred inflows or outflows, the definition of the latter does not include reference to conditionality of revenue or expense.

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?

Response:

The Task Force considers the term 'net assets' and its definition to be clear, customary and acceptable to the majority of preparers and users of GPFS.

The term 'financial position' seems to have emerged only as a result of introducing concept of deferred inflows and outflows and the Task Force is not convinced that it should be defined as a specific term due to its limited applicability. It is noted that the IPSASB is of the view that financial position may be used to assess availability of net resources of the reporting entity in future periods. However this view does not take into account current period revenues and expenses which may represent significant portion of transactions during the reporting period, which is common for public sector organizations other than governments. Such current period revenues may include reclassification of liabilities upon compliance with related conditions in the reporting period. Therefore, except for cases when deferred inflows and outflows constitute majority of transactions of the reporting entity, which is presumably more relevant to governments than to other public sector entities, use of financial position on its own for assessing future economic viability of preparers of the GPFS would not be appropriate.

Members of the Task Force believe that introduction of the term 'financial position', as currently proposed by the CF-ED2, may unnecessarily complicate presentation of the

Statement of Financial Position and is unlikely to enhance usefulness of information presented in the GPFS. It was also noted that the concept of 'financial position', as presented by CF-ED2, is not promulgated by other international financial reporting frameworks.

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

Response:

The Task Force does not object to the decision to define ownership contributions and distributions as separate elements of financial statements.

(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?

Response:

The Task Force has no reservations in relation to the proposed definitions of ownership contributions and distributions. However the related discussion in the CF-ED2 does not seem to cover the broad spectrum of arrangements in the public sector related to injection of resources to the entity as well their subsequent distribution. One example that can be used to illustrate the point is the relationship between the United Nations and the Member States, where annual contributions of the latter are recognized as revenue by the United Nations, but should the United Nations be wound up or get restructured, the Member States are likely to receive its net assets or at least decide on the ultimate distribution of such net assets. Hence it might be useful to include in CF-ED2 more practical examples which would be relevant to international organizations and public sector entities other than governments.

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

Response:

The concept of ownership interest should only be defined if it is expected that it will be applicable to majority of GPFSs preparers.

Specific Matter for Comment 7

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

Response:

It was noted that the CF-ED considers that use of standardized threshold criteria to assess existence uncertainty may not meet some of the qualitative characteristics of GPFS. The IPSASB therefore concluded that “all available evidence should be assessed in determining whether an element exists and that uncertainty about the flows of service potential or economic benefits should be taken into account in measurement” (para. BC 55). The Task Force is of the view that discussion on recognition in the CF-ED2, although interesting and overall useful, addresses recognition mostly on theoretical level and should be supplemented by examples and more practical guidance for each element of the GPFS.