



To:	AASB members	Date:	15 April 2010
From:	Emma O'Brien	Agenda Item:	6.1
Subject:	Impairment of Statutory Receivables	File:	

1 Action

Consider the letter from the Australasian Council of Auditors-General (ACAG) Financial Reporting and Auditing Committee Chairman, Simon O'Neill (agenda paper 6.2), and decide:

- whether a clarifying Aus paragraph in AASB 136 *Impairment of Assets* is warranted, having regard to the Board's *Process for Modifying IFRS for PBE/NFP*, and, if so:
 - the content of such a paragraph; and
 - the process to be followed in incorporating the paragraph into AASB 136; or
- whether to issue a formal Board Agenda Decision; or
- whether to take no further action.

2 Background

'Impairment of Statutory Receivables' was addressed at the December 2009 AASB meeting. At that meeting the Board considered a staff issues paper that included a comparison of the impairment-related requirements under AASB 136 and AASB 139 *Financial Instruments: Recognition and Measurement*. The approved minutes of the December 2009 meeting state:

The Board considered agenda paper 19.2, noting that it addresses one of the 'gaps in GAAP' that public sector constituent groups asked the Board to consider. The Board also noted that the issue is not limited to not-for-profit public sector entities.

The Board expressed the preliminary view that the impairment requirements in AASB 136 *Impairment of Assets* apply to non-contractual assets, because paragraph AG12 of AASB 132 *Financial Instruments: Presentation* says non-contractual assets "such as income taxes that are created as a result of statutory requirements" are not financial assets.

The Board noted that, in accounting for the impairment of non-contractual assets, professional judgement needs to be applied, including in relation to assessing materiality and using estimates, averages and computational short cuts referred to in paragraph 23 of AASB 136.

The Board decided that the Chairman should write to the ACAG, with a copy to the HoTARAC, conveying the Board's preliminary view and seeking further input from the ACAG should they wish to see the issue pursued.

Consistent with the minutes, the AASB Chairman wrote to ACAG, with a copy to HoTARAC (agenda paper 6.3). ACAG's response (agenda paper 6.2) expresses the view "that a clarifying Aus paragraph in AASB 136 would benefit preparers of financial reports applying this standard."

3 A possible clarifying Aus paragraph

In developing a possible clarifying Aus paragraph, consideration needs to be given to its scope (eg statutory receivables vs non-contractual receivables; and not-for-profit entities vs not-for-profit public sector entities) and the extent of guidance (eg whether to address the relationship of a portfolio approach to paragraph 23 of AASB 136; and whether to acknowledge that disclosures under AASB 7 *Financial Instruments: Disclosures* could be made).

In drafting the following alternative possible clarifying Aus paragraphs, consistent with the *Process*, we considered how IPSASB has dealt with or intends dealing with the issue. We noted that, in undertaking its recently concluded Financial Instruments Convergence project, the IPSASB recognised that issues predominantly relating to the public sector (such as statutory receivables) exist and chose to address those issues in a separate project, Financial Instruments – Public Sector. The IPSASB draft agenda schedule 2010-2012 shows that, whilst the IPSASB is committed to this project, with a Consultation Paper potentially being issued by the end of 2011, a timeframe for its completion is yet to be developed. As such, specific guidance from the IPSASB in relation to statutory receivables is not expected to be available for several years. Accordingly, the IPSASB's work to-date does not provide material that is relevant to the issue under consideration.

Based on the Board's December 2009 discussions and the ACAG response, consideration could be given to including a clarifying Aus paragraph along either of the following lines in AASB 136:

(a) perhaps in the scope section as paragraph Aus5.1:

In respect of not-for-profit public sector entities, this Standard applies to non-contractual receivables that are created as a result of transactions or events subject to statutory requirements imposed by governments (termed 'statutory receivables'). Adoption of a portfolio approach for impairment testing of statutory receivables is consistent with paragraph 23 of this Standard. Disclosures compatible with AASB 7 *Financial Instruments: Disclosures* for statutory receivables could also be made.

(b) perhaps in the measuring recoverable amount section as paragraph Aus23.1:

Adoption of a portfolio approach for impairment testing of statutory receivables is consistent with paragraph 23 of this Standard.

Staff view

The majority of staff prefer alternative 3(a) as the basis for a clarifying Aus paragraph (or a formal Board Agenda Decision) as it explicitly constrains the paragraph to not-for-profit public sector entities and explicitly acknowledges the potential relevance of information compatible with AASB 7.

4 Process for modifying IFRSs for PBE/NFP

The *Process for Modifying IFRSs for PBE/NFPs* states that the purpose of modifying IFRSs for PBE/NFP is to reflect differences between the PBE/NFP and for-profit sectors, including differences in user information needs, that warrant a different accounting treatment or guidance. The *Process* outlines factors (examined below) to be considered before modifying an IFRS for PBE/NFP.

(a) Are there issues that might warrant modifying an IFRS for PBE/NFP?

(i) Nature of transactions, events and circumstances and their impact on PBE/NFP

Factors that suggest the nature of impairment of statutory receivables might warrant a clarifying Aus paragraph

- Depending on how they are defined, statutory receivables predominantly arise in a public sector context.
- Preparers might find the requirements of AASB 136 difficult to apply to statutory receivables as the focus of AASB 136 is predominantly on property, plant and equipment, intangible assets and goodwill, rather than monetary items. For example, AASB 136 does not explicitly mention a portfolio approach.
- Even though AASB 132 effectively scopes out the impairment of non-contractual receivables from AASB 139, statutory receivables are more in the nature of financial instruments than the kind of assets for which AASB 136 was written. Therefore, a clarifying Aus paragraph might help preparers by confirming that AASB 136 is applicable.

Factors that suggest the nature of impairment of statutory receivables might not warrant a clarifying Aus paragraph

- Depending on how statutory receivables are defined, the impairment of statutory receivables is not solely a public sector issue. Arguably, statutory receivables arise in a range of for-profit private sector entities such as in the gaming industry and operators of toll roads.
- Even if statutory receivables are defined to arise only in a not-for-profit public sector context, they are a form of non-contractual receivables, which might arise in a broader range of entities. It therefore might be difficult to constrain the clarifying Aus paragraph from being used by analogy by for-profit entities under the AASB 108 *Accounting Policies, changes in Accounting Estimates and Errors* hierarchy.

(ii) Benefits to users of complying with the IFRS

This factor is not relevant to the issue as the clarifying Aus paragraph being contemplated would not adversely affect compliance with the IFRS. Indeed, the clarifying Aus paragraph might improve not-for-profit public sector entities' compliance with the IFRS.

(iii) Costs of complying with the IFRS

Again, this factor is not relevant to the issue as the clarifying Aus paragraph being contemplated would not adversely affect compliance. Indeed, the clarifying Aus paragraph might help reduce the costs of complying with the IFRS to the extent it supports the use of cost-effective methods (such as a portfolio approach) to assessing impairment.

Staff View

On balance, the nature of impairments of statutory receivables, their impact on not-for-profit public sector entities and the potential for a clarifying Aus paragraph to enhance compliance with IFRS in a cost-effective way suggest that a clarifying Aus paragraph might be warranted.

(b) Are the identified issues sufficiently significant to warrant a departure from an IFRS?

Four specific factors (examined individually in the context of statutory receivables below) are identified by the *Process* to be taken into account when deciding whether or not the identified PBE/NFP issue is so significant that a modification to an IFRS is warranted.

(i) An estimate of the significance of any modification on the financial statements

The *Process* states that a modification is warranted where the modification would have a significant impact on financial statements.

Currently, the accounting for impairment of statutory receivables in practice appears to be diverse, with some jurisdictions apparently applying AASB 139 and others applying AASB 136. A clarifying Aus paragraph would help ensure compliance with AASB 136 rather than AASB 139, and thereby have a significant positive impact on financial statements. However, we acknowledge that, depending on circumstances, the outcomes of applying AASB 136 or AASB 139 to the impairment of statutory receivables might not be materially different.

(ii) An estimate of the significance of a transaction, event or circumstance on the financial statements taken as a whole

Given the significance of statutory receivables in the public sector, depending on circumstances, the impairment of statutory receivables might have a significant impact on the financial statements as a whole.

(iii) Whether or not a modification will increase or decrease internal consistency within IFRSs as modified for PBE/NFP entities

A clarifying Aus paragraph to help ensure consistent application of Standards by public sector entities would not affect the consistency of the Standards themselves.

(iv) The costs of the modification

Given that the Aus paragraph would merely clarify the application of AASB 136 to statutory receivables in a not-for-profit public sector context, it is not expected that it would be costly to draft. However, it should be acknowledged that some jurisdictions might incur costs in assessing their existing accounting systems to confirm that they comply with AASB 136. Also, a cost of the modification would be the possible implications for the Board's principles-based approach to writing standards. Some would argue that a clarifying Aus paragraph is unnecessary as the principles in the Standards are already clear and that the Aus paragraph would be tantamount to writing rules.

Staff View

On balance, the majority of staff think the identified issues are sufficiently significant to warrant the inclusion of a clarifying Aus paragraph along the lines of that presented in section 3(a), or at least section 3(b), above. As noted in section 5 below, an alternative, supported by some staff, would be to issue a 'Board Agenda Decision' conveying the same kind of message that a possible clarifying Aus paragraph could convey. However, given the significance of the issue, the majority of staff think a clarifying Aus paragraph is preferable to a 'Board Agenda Decision' (although we acknowledge that doing so may set a precedent for adding further clarifying Aus paragraphs to a range of Standards in response to other 'gaps in GAAP').

5 Due process

If the Board decides that a clarifying Aus paragraph is warranted, we think it should be developed jointly with NZ FRSB. (The advice we have received from the NZ FRSB suggests that, currently, the NZ FRSB is not doing any work on this topic, nor has it formed any view.) We think the clarifying Aus paragraph should be subject to the usual due process for amending Standards. Therefore, an Exposure Draft should be developed and issued for public comment.

6 Alternative response

If, however, the Board is of the opinion that an Aus paragraph is not warranted, a potential action to provide the clarification without amending the Standard would be to issue a 'Board Agenda Decision' following the usual due process of issuing a proposed agenda decision for public comment. The content of the proposed agenda decision could be based on the possible clarifying Aus paragraph in section 3(a) or 3(b) above. As the NZ FRSB does not issue formal Agenda Decisions, this action would not be expected to be undertaken jointly with the FRSB.

Staff View

Staff think issuing a formal Agenda Decision is preferable to taking no further action, as it will enhance the visibility of the Board's decision.

Questions for the Board:

- (a) do you agree that a clarifying Aus paragraph should be incorporated into AASB 136?
- (b) do you agree that the Aus paragraph should be expressed along the lines of the suggestion in section 3(a) above?
- (c) do you agree that the amendments to AASB 136 should be considered in conjunction with NZ FRSB and effected through the usual due process?

7 Attachments

- Agenda paper 6.2: ACAG Financial Reporting and Auditing Committee Chairman's letter in response to AASB Chairman, 1 April 2010
- Agenda paper 6.3: AASB Chairman's letter to ACAG Financial Reporting and Auditing Committee Chairman, 21 December 2009