IPSASB Exposure Draft *Elements and Recognition in Financial Statements*: Update of Proposals in IPSASB Consultation Paper (CP) and Related Comments in AASB Submission on that CP

This table sets out the issues raised in the Specific Matters for Comment on the IPSASB Conceptual Framework Consultation Paper (CP) *Elements and Recognition in Financial Statements* (December 2010). In the left column are the issues raised in the CP[1] and the AASB's main comments on those issues. The right column updates each issue for its proposed treatment in the IPSASB Conceptual Framework Exposure Draft (ED) *Elements and Recognition in Financial Statements*, and sets out the AASB staff recommendation on:

(a) whether to support the ED's proposed treatment of the issue; and, if not

(b) the nature of the comments on the issue that should be made in the Board's submission on the ED.

Issues giving rise to key concerns of AASB staff are shaded.

Issue in IPSASB CP, and AASB comments thereon	**Treatment of issue in IPSASB ED, and AASB staff comments thereon**
<u>Issue 1:</u> IPSASB's proposal to identify 'deferred outflows' and 'deferred inflows' as elements of financial statements (under a so-called 'revenue and expense-led approach' for identifying revenues and expenses) The AASB supports the 'asset and liability-led approach' for identifying revenues and expenses. The AASB is of the view that assets and liabilities should be defined in relation to economic resources and economic obligations, that revenues and expenses should reflect changes in those economic resources and economic obligations, and that (apart from net assets/equity) the statement of financial position should report only assets and liabilities. An important reason why the AASB does not support the 'revenue and expense-led approach', as articulated in the CP, is because that approach appears to mix economic phenomena and accounting devices ('deferred outflows' and 'deferred inflows') as elements of the financial statements. Assets and liabilities are economic phenomena that have a dimension that is external to the entity. Deferred outflows and deferred inflows do not possess that quality.	The IPSASB ED retained the 'revenue and expense-led approach' (without calling it that) – that is, it still proposes identifying 'deferred outflows' and 'deferred inflows' as elements of financial statements. See Agenda Paper 13.3 for proposed Board comments on this key concern.

[1] The numbering scheme used for issues in this paper does not correspond to the numbering of the Specific Matters for Comment on the IPSASB CP. Some questions in the IPSASB CP had multiple parts and some questions have been grouped in this paper for simplicity.

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The AASB is concerned that the discussion in paragraphs 4.4, 4.6 and 4.22 of the CP about the 'revenue and expense-led approach' implies it is the only approach concerned with reporting current period financial performance. That approach defines revenues and expenses as "flows that relate to efforts of the current period" (paragraph 4.6). The logical implication is that the 'asset and liability-led approach' is concerned predominantly with reporting financial position, with reported financial performance being a by-product of that emphasis. However, the AASB considers that revenues and expenses comprise the financial effects of an entity's current period accomplishments and that the 'asset and liability-led approach' gives equal importance to the reporting of financial position and financial performance.	The IPSASB ED effectively retained the notion of defining revenues and expenses as flows that relate to efforts of the current period, in paragraph 4.3.
The AASB is also concerned with the focus of the 'revenue and expense-led approach' on achieving 'inter-period equity', and its adoption of the view that "the principle that taxpayers pay only for the services they receive, and not pass on obligations to future taxpayers, should underlie any measure of financial performance" (paragraph 4.21). The AASB is particularly concerned that this approach is based on a value judgement about who should pay for services rendered in a particular period and its direct link between funding decisions and recognition. If a decision were made that taxpayers of a different period should pay for current period services, should the recognition principles change accordingly? The AASB thinks the recognition principles should not change, but is concerned that adopting the 'inter-period equity concept' may create a precedent for public policy decisions to determine recognition principles.	The IPSASB CP's discussion of the notion of inter-period equity was not repeated in the IPSASB ED.
Whilst the AASB does not support the 'revenue and expense-led approach', as articulated in the CP, it does not consider the 'revenue and expense-led approach' to be articulated clearly enough to enable proper comparison of the two approaches. Whilst the AASB supports an 'asset and liability-led approach', if the other approach were articulated more clearly, it may be feasible to identify the conceptual differences between the approaches and reduce the risk of disagreements based on misunderstandings about what each	As is noted in Agenda Paper 13.3, unfortunately, the approach involving deferrals is not fleshed out in the IPSASB ED, which includes less explanation of the proposed approach and its implications than in the CP.

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approach entails. A ‘revenue and expense-led approach’, properly developed and in a form the AASB would find acceptable, might complement an ‘asset and liability-led approach’.	
The AASB notes that the main objectives of the ‘revenue and expense-led approach’ are described as: (a) attributing the costs of services to the period in which the services are provided; and (b) attributing tax and other revenue to the period in which they were intended to finance the related costs (paragraph 4.8).	The main objectives for identifying ‘deferred outflows’ and ‘deferred inflows’ as elements of financial statements, set out in the IPSASB CP, have been retained in paragraphs BC35 and BC40 of the IPSASB ED.
However, the AASB notes other unrelated notions are implicit in the CP’s discussion of the ‘revenue and expense-led approach’. For example, a ‘likely realisation’ notion seems to be applied to the recognition of gains and losses on assets [paragraph 4.31(d)].	The other unrelated notions implicit in the IPSASB CP’s discussion, such as ‘likely realisation’, were not retained in the IPSASB ED.
When inflows of resources are not stipulated to be used to finance particular costs of services, attributing those inflows to particular costs of services would involve arbitrary allocations. For example, inflows of resources from general purpose taxes and grants without stipulations can be applied to meet costs of current period services, repay debts incurred in providing services in previous periods or meet the costs of providing services in future periods. Because cash is fungible, any allocation of those inflows to particular outflows would be arbitrary and intent-driven. Another illustration of this concern is Example 1 in paragraphs 4.13 – 4.15 of the CP. In that example, retention of the grant is conditional on construction of the library—that is, the inflow is required to finance an expenditure rather than an expense. However, under the revenue and expense-led approach, the grant revenue is recognised when the library is depreciated. Furthermore, it is unclear how the revenue and expense-led approach would be applied if a grant were stipulated as financing the purchase of a non-depreciable asset (e.g., land) or was in the form of ‘seed money’ for the acquisition of an asset that must be maintained and refurbished for an indefinite period. In these cases, would a deferred inflow be recognised indefinitely?	The AASB’s concern with arbitrary allocations, in its comments on the IPSASB CP, would still seem warranted in relation to the IPSASB ED. This is despite the example in paragraphs 4.13 – 4.15 of the IPSASB CP not being retained in the IPSASB ED.

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<u>**Issue 2:**</u> **Role of association with the entity: definitions or recognition criteria?** The AASB suggests defining assets and liabilities generically, without requiring them to have an association with the entity. The AASB considers that it is useful to focus on the nature of economic phenomena (economic benefits and claims to economic benefits) that affect various entities, without restricting definitions of assets and liabilities to only phenomena that affect the reporting entity. It considers that criteria for associating those particular phenomena with the reporting entity should be included in recognition criteria. This approach has the advantages of: (a) keeping the definitions relatively simple and readily understandable; and (b) helping minimise the risk that standard setters and others will 'peek ahead' to consider whether consequences of the definitions for the recognition of assets and liabilities will be desirable and/or consistent with existing conventions. Developing definitions that do not necessarily affect reporting entities should help in focusing on the economic phenomena to be identified as the elements of financial position (and, by derivation, the elements of financial performance). Consistent with this view, the AASB recommends that assets and liabilities should not be limited to items that would necessarily be recognised in financial statements. Accordingly, a government's rights/powers to tax and levy fees and social benefit obligations should be identified as assets and liabilities respectively, although these elements might not qualify for recognition in the financial statements.	The IPSASB did not accept the AASB's recommendation. The IPSASB ED retains the approach in the CP of treating factors that associate a resource or an obligation with an entity as part of the definitions of an asset and a liability. AASB staff recommend re-iterating the Board's comment on the CP in the Board's submission.
<u>**Issue 3:**</u> **Relevance of 'exchange' / 'non-exchange distinction** In various places the CP analyses the implications of transactions for the definition and recognition of elements of financial statements by reference to whether the transactions are 'exchange' or 'non-exchange'. In some of these cases the nature of the transaction potentially determines whether, or when, an element can arise (for example, paragraphs 2.49, 3.33 – 3.34,	The 'exchange' / 'non-exchange' distinction has been retained in the IPSASB ED. In most cases, references to either 'exchange' or 'non-exchange' transactions provides context for discussion of an issue but the distinction does not determine the treatment of the transaction. The noteworthy exception that AASB staff have identified is the proposal to limit the scope of 'deferred outflows' and 'deferred inflows' to non-

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3.55 – 3.58, 4.32 and 4.42 – 4.45). The AASB notes that 'exchange transactions' and 'non-exchange transactions' are not defined in the CP and that the discussion of these terms presumes that, at a conceptual level, the distinction between exchange and non-exchange transactions is important (without explaining that presumption). The AASB considers that the issue of whether to distinguish exchange and non-exchange transactions is a standards-level issue only, and that the terms 'exchange' and 'non-exchange' should not (and need not) be used in the IPSASB Conceptual Framework.	exchange transactions (see paragraphs 5.1, 5.2 and 5.6 of the IPSASB ED). Specific comments on this scope limitation are set out in Agenda Paper 13.3 dealing generally with 'deferred outflows' and 'deferred inflows'. AASB staff do not recommend raising the 'exchange' / 'non-exchange' distinction elsewhere in the Board's submission.
<u>Issue 4:</u> **Which benefits compose an asset?** *The IPSASB CP asked whether the definition of an asset should cover all of the following types of benefits: (i) service potential; (ii) net cash inflows; and (iii) unconditional rights to receive resources.* *AASB response:* The AASB supports a definition of an asset that covers service potential, net cash inflows and unconditional rights to receive resources. Assets held by not-for-profit entities to provide services (and which are explained in paragraph 2.16 as possessing 'service potential') would generally also be held to generate net cash inflows, either directly through user charges (as noted in paragraph 2.19) or indirectly in the form of transfers from government and/or taxes. Sometimes a cash inflow may be in the form of an explicit subsidy of the cost of services provided, or implicit in the raising of revenue at an entity-wide level (for example, in the form of some taxes). The fact that some net cash inflows are more difficult than others to relate to particular assets does not necessarily mean the assets are not cash-generating. The AASB observes that unconditional rights to receive resources embody service potential and a capacity to generate net cash inflows, as they will be converted into other assets also possessing those benefits or attributes.	The definition of an asset in paragraph 2.1 of the IPSASB ED refers to "service potential or economic benefits". AASB staff recommend noting in the Board's submission that '*future* economic benefits' is a more appropriate term for the counterpart to 'service potential'. The first two sentences of paragraph BC6 of the Basis for Conclusions on the IPSASB ED indicate that unconditional rights "may give rise to assets, if the entity has paid for them or if the unconditional right has acquired an identifiable value in an open, active and orderly market". AASB staff recommend disagreeing with this statement in the Board's submission because: • all unconditional rights should be identified as assets (whether recognised or not); and • having a cost or strong market evidence of its value is not an essential characteristic of assets, either for assets generally in the IPSASB ED or in the IASB *Framework*.
<u>Issue 5:</u> **Should the definition of assets refer to economic benefits and service potential, or just economic benefits?** The AASB would prefer using the term 'economic benefits' in the definition of an asset,	The definition of an asset in paragraph 2.1 of the IPSASB ED refers to economic benefits and service potential. AASB staff recommend saying in the Board's submission that the AASB would prefer using the

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with clarifying guidance that service potential is a sub-set of economic benefits.	term 'future economic benefits' in the definition of an asset, with clarifying guidance that service potential is a sub-set of future economic benefits. AASB staff also recommend noting in the Board's submission that the relationship between service potential and economic benefits seems unclear from paragraphs 2.3 – 2.4 of the IPSASB ED. Paragraph 2.3 describes service potential so broadly as to be likely to encompass all assets; whilst economic benefits, being equated with an ability to generate net cash inflows (see second sentence of paragraph BC8), seems to be a subset of service potential. However, the last sentence of paragraph 2.4 refers to "many assets that embody service potential", which implies economic benefits complement service potential. Related to this issue, AASB staff disagree with the implication in paragraph BC9 of the Basis for Conclusions on the IPSASB ED that an asset may generate net cash inflows without providing goods or services. 'Goods and services' have been used with a very broad meaning in IFRSs, and there is no apparent public-sector-specific reason to regard them differently in the IPSASB Conceptual Framework.
<u>Issue 6:</u> Associating an asset with a specific entity [*Background note:* As noted in Issue 2, the AASB considers that factors associating an element (whether an asset or a liability) with an entity should be treated as recognition criteria rather than aspects of the element's definition.] *The IPSASB CP asked which approach should be used to associate an asset with a specific entity: (i) control; (ii) risks and rewards; and (iii) access to rights, including the right to restrict or deny others' access to rights:* *AASB response:* It may be difficult, in some circumstances, to associate an asset with an entity without considering the notion of control. Sometimes a resource is only a right (e.g., an amount receivable) and sometimes a resource is an object (e.g., owned property) that gives rise to various rights of its holder. This can cause different interpretations of 'rights' in relation to the identification of assets – for example, some argue that if a resource is a right, there is no obvious reason why it is preferable to say an entity *has access to that right* than to say an entity	Paragraph 2.6 of the IPSASB ED indicates that an entity must control a resource if it is to qualify as an asset. Paragraph 2.7 notes that "access to or, conversely, the ability to deny or restrict access to the resource" is an indicator of control. The fifth and sixth sentences of paragraph BC16 of the Basis for Conclusions on the IPSASB ED say the IPSASB decided exposure to the risks and rewards of ownership should not be an indicator of control "because it is not compatible with the control approach". AASB staff recommend that the Board's submission on the IPSASB ED: • disagrees with that comment because it is too categorical; and • suggests that the IPSASB Framework says that, in some instances, the risks and rewards of ownership might not be clearly identifiable or might be a less appropriate indicator of control than other indicators.

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controls that right. In addition, if an asset is a right of access, using 'access to rights' would be confusing, because one would then say an entity has access to a right of access. Here, control would be more understandable. Therefore, the AASB supports an approach that includes either or both of the notions of control and access to rights, including the right to restrict or deny others' access to rights. The AASB also considers that the risks and rewards notion may be a useful indicator of control and access to rights.	
<u>Issue 7:</u> Associating an asset with a specific entity (continued) *The IPSASB CP asked whether an entity's enforceable claim to benefits or ability to deny, restrict or otherwise regulate others' access link a resource to a specific entity.* *AASB response:* The AASB considers that, depending on the nature of the item, either an enforceable claim to benefits or the ability to deny, restrict or otherwise regulate others' access would be necessary to link an asset with an entity.	Paragraph 2.7 of the IPSASB ED says indicators of control are: • "access to or, conversely, the ability to deny or restrict access to the resource"; and • "the existence of an enforceable right to service potential or economic benefits arising from a resource". AASB staff broadly support these comments in the ED.
<u>Issue 8:</u> Is a past event a necessary component of the definition of an asset or a liability? The AASB considers that every asset or liability of a reporting entity that qualifies for recognition is the result of a past transaction or other past event. However, the AASB considers that *identification* of a past transaction or other past event of the reporting entity should not be necessary for an asset or a liability to qualify for recognition. Nevertheless, the AASB supports: (a) emphasising the importance of a past transaction or other past event of the reporting entity as an indicator that an asset or a liability of the reporting entity would, subject to meeting other recognition criteria, qualify for recognition; while (b) noting that the existence of a past transaction or other past event does not guarantee that an asset or a liability continues to qualify for recognition.	The IPSASB ED retained the CP's proposal that the definitions of an asset and a liability require these elements to arise from a past event (see ED paragraphs 2.1, 2.8, 3.1 and 3.3). AASB staff recommend that the Board's submission repeats the comments in its submission on the CP, as shown adjacently in the left column.

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<u>Issue 9:</u> Whether, and if so when, public sector entity rights and powers (such as the power to tax) are assets *The IPSASB CP asked whether public sector entity rights and powers, such as those associated with the power to tax and levy fees, are (i) inherent assets of that entity; (ii) assets only when those powers are exercised; or (iii) assets when a more relevant intermediate event occurs.* *AASB response:* The AASB's view is that assets should be defined without limiting them to items that would necessarily be recognised in financial statements. In addition, the AASB is of the view that the recognition criteria should be separate from definitions of the elements of financial statements. The same applies to the definition of a liability. Accordingly, a government's rights/powers to tax and levy fees should be identified as assets, although assets associated with a government's rights/powers to tax and levy fees might not qualify for recognition in the financial statements until an event (such as the exercise of the rights/powers) occurs. The AASB does not support depicting a right to tax as a 'perpetual asset' because the levying of some taxes constrains the government's ability to levy further taxes—therefore, some of the future economic benefits embodied in the right to tax are consumed by the levying of the tax (and therefore the right is not perpetual).	In relation to the power to tax or to issue licences, and to access or restrict or deny access to the benefits embodied in intangible resources, the IPSASB ED proposes that an asset arises when the power is exercised and the rights exist to receive service potential or economic benefits (paragraph 2.8). The IPSASB ED did not refer to depicting a right to tax as a 'perpetual asset'. AASB staff recommend that the Board's submission repeats the comments on this issue in its submission on the CP, except for the now-inapplicable comment on 'perpetual assets'. In particular, AASB staff recommend arguing that the above-mentioned powers of governments should be identified as assets, although assets associated with those powers might not qualify for recognition until an event (such as the exercise of the powers) occurs.
<u>Issue 10:</u> Other characteristics of an asset An idea of the stock of an entity's wealth (or capital) is important for defining the elements of its financial statements. This is because assets and liabilities are stores of wealth and claims to those stores of wealth. This point is reiterated here as a reminder of the link between the measurement and elements components of a Conceptual Framework. The AASB also recommends that the definitions of assets and liabilities be symmetrical, or at least that any asymmetry is explained.	The AASB's comment on the IPSASB CP in the first adjacent paragraph in the left column was not addressed in the IPSASB ED. AASB staff recommend that the Board's submission on the ED reiterates that previous comment. Regarding the AASB's comment on the IPSASB CP in the second adjacent paragraph in the left column, AASB staff have not identified asymmetry between the definitions of assets and liabilities. As the IASB's work on defining assets and liabilities progresses, AASB staff will explore this issue further in light of that work.

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<u>Issue 11:</u> Which obligations compose a liability? *The IPSASB CP asked whether the definition of a liability should cover all of the following types of obligations: (i) obligations to transfer benefits, including goods and services; (ii) unconditional obligations, including such obligations to stand ready to insure against loss; (iii) performance obligations; and (iv) obligations to provide access to or forego future resources.* *AASB response:* The AASB agrees that all of these types of obligations are liabilities.	The body of the IPSASB ED does not discuss the types of obligations discussed in the IPSASB CP, as mentioned in italics in the left adjacent column. The Basis for Conclusions on the IPSASB ED says "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" (paragraph BC 22, second sentence). AASB staff recommend that the Board's submission disagrees with that view. Unconditional stand-ready obligations (which are liabilities) are accompanied by conditional obligations (which are not liabilities). The IASB's work to date in its Conceptual Framework project treats the distinction between conditional and unconditional rights and obligations as fundamental to identifying whether assets and liabilities exist. AASB staff are unaware of a public-sector-specific reason to differ from that principle. Furthermore, applying the notions of conditional and unconditional obligations avoids the need to think about whether a contract is 'executory'; AASB staff think the discussion of executory contracts in paragraph BC7 is unnecessary and unhelpful. Paragraph BC 24 (third, fourth and sixth sentences) of the Basis for Conclusions on the IPSASB ED says: • "… the notion of a stand-ready obligation does not work well in a public sector non-exchange context where it is very difficult to distinguish a stand-ready obligation from other conditional obligations"; • "… use of the term stand-ready obligations could give rise to assumptions about the recognition of liabilities related to the ongoing provision of social benefits"; and • "use of the term stand-ready obligations … would not provide a sound basis for future standard setting". AASB staff recommend that the Board's submission disagrees with this argument. The existence of obligations to stand ready to transfer economic benefits if uncertain future events occur does not depend on whether those events occur,

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	as is implied by the IPSASB's comments in the first bullet point above. Concerns about recognising social benefit 'obligations' at inappropriate points could be addressed by saying that not all items that are potentially considered 'stand-ready obligations' would necessarily qualify as liabilities, and that guidance on when social benefit 'obligations' qualify as liabilities will be developed at a standards level (or, if the AASB staff recommendation in Issue 16 below were adopted, elsewhere in the Conceptual Framework). In relation to performance obligations, the last sentence of paragraph BC26 says "because performance obligations are normally conditional obligations and because the issues in determining whether such obligations give rise to liabilities is dependent upon the terms of particular binding agreements and may vary between jurisdictions, it would not be appropriate to use the term 'performance obligation' in the Framework". AASB staff recommend disagreeing with this view in the Board's submission on the ED. The IPSASB's conclusion (quoted above) is based on the mistaken presumption that performance obligations are normally conditional obligations. In addition, performance obligations are fundamental to the upcoming IFRS on revenue recognition, and this aspect will confront the IPSASB if and when it revises its Standards in light of that IFRS. AASB staff recommend further that the Board's submission on the ED expresses a significant concern that, in view of the problems described above, the discussion of liabilities generally needs considerable revision.
<u>Issue 12:</u> Is a settlement date an essential characteristic of a liability? The AASB does not consider that a particular settlement date is an essential characteristic of a liability. Although a settlement date may be relevant in the context of a contract, it is not always necessary.	Paragraph 3.5 of the IPSASB ED says a settlement date is not an essential characteristic of a liability. This is consistent with the Board's response to the IPSASB CP on this issue.
<u>Issue 13:</u> Is the ability to identify a specific external party (or parties) to whom the entity is obligated an essential characteristic of a liability? The AASB is of the view that the definition of a	The fifth sentence of paragraph 3.4 of the ED says it is not essential to know the identity of the external party to whom an obligation is owed in order for a liability to exist. This is consistent with the Board's response to the IPSASB CP on

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liability should not require the identification of a specific party or parties outside the reporting entity to whom the entity is obligated. A liability for environmental remediation might not involve an identified external party.	this issue.
<u>**Issue 14:**</u> **Is the absence of a realistic alternative to avoid an obligation an essential characteristic of a liability?** The AASB considers that the absence of a realistic ability to avoid the obligation should not be identified as an essential characteristic of a liability. The AASB considers that this is a factor associating a liability with an entity, and therefore should be treated as a possible recognition criterion.	Having "little or no realistic alternative to avoid an outflow of service potential or economic benefits" was included in the definition of a liability in paragraph 3.1 of the IPSASB ED. This conflicts with the Board's comment on this issue in its submission on the IPSASB CP. AASB staff recommend that the Board's submission on the ED repeats the comments in its submission on the CP, as shown adjacently in the left column.
<u>**Issue 15:**</u> **Possible approaches to determining whether an entity has no realistic alternative to avoid an obligation** *The IPSASB CP asked which of the following sets of obligations would meet the characteristic of having no realistic alternative to be avoided: (i) enforceable contractual, constructive, and equitable obligations; (ii) the obligations in (i) plus other constructive and equitable obligations associated with exchange transactions; and (iii) the obligations in (i) plus all other constructive and equitable obligations from which the entity cannot realistically withdraw.* *AASB response:* The AASB commented that: (a) it considers that the definition of a liability should be applicable to all types of obligations, with no distinction between obligations arising from exchange and non-exchange transactions; and (b) whether a 'cannot realistically avoid' principle should be adopted is a recognition issue (because it associates an obligation with an entity). The AASB does not have a view on whether any and, if so, which of the three sets of obligations identified should be preferred. The AASB notes that there is considerable overlap between the three sets of obligations identified and suggests that, if discussion of them is retained in the IPSASB's ED on Elements and Recognition, the ED should contrast the approaches more clearly.	The IPSASB ED identifies the following obligations as those that would meet the characteristic of having little or no realistic alternative to be avoided: • 'obligations enforceable in law' (paragraph 3.6); and • 'non-legal binding obligations' with the following attributes [the first two of which are consistent with two of the criteria for a constructive obligation in paragraph 12 of the IASB's Working Draft IFRS *Liabilities* (19 February 2010) and broadly consistent with the tentative views of the IASB at its March 2013 meeting (see page 20 of Agenda Paper 12.2)]: o The entity has indicated to other parties by an established pattern of past practice, published policies, or a sufficiently specific current statement that it will accept certain responsibilities; o As a result of such an indication, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities; and o The entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities. AASB staff tentatively lean toward supporting those characteristics of a liability, subject to the

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	point made in Issue 14 that 'having little or no realistic alternative to be avoided' should be a recognition criterion. The IPSASB ED is consistent with the Board's comment on the CP that the distinction between obligations arising from exchange and non-exchange transactions should not determine whether the obligations are liabilities. However, AASB staff recommend that the Board's submission on the ED disagrees with the comment in the sixth sentence of paragraph BC32 that: "In assessing whether a non-legal obligation gives rise to a liability the availability of funding to settle the obligation may be a persuasive indicator." In some contracts, the receipt of payment in respect of a promise to perform can be the event that makes that promise unconditional (even in such cases, there is no need to focus on funding, but, rather, one would focus simply on whether an unconditional promise exists). However, for 'non-legal obligations', which need not involve an identified counterparty, it is not clear why funding would be a persuasive indicator of a liability's existence. (Paragraph 3.12(c) of the IPSASB ED also discusses the relationship between funding and present obligations, but seems much more equivocal than paragraph BC32 on this issue.)
<u>Issue 16:</u> If and when obligations to provide social benefits, and similar obligations, are liabilities *The IPSASB CP asked whether public sector entity obligations such as those associated with its duties and responsibilities as a government: (i) perpetual obligations; (ii) obligations only when they are enforceable claims; or (iii) obligations when a more relevant intermediate event occurs?* *AASB response:* The AASB: (a) considers that obligations to provide social benefits are liabilities that may qualify for recognition; but (b) does not support depicting such obligations as 'perpetual obligations' because those obligations are continually settled and replaced with new obligations. Whilst those obligations may appear to be perpetual, in substance they are not. Another example of what might,	It seems that the key factor that would determine whether public sector entity obligations such as those associated with its duties and responsibilities as a government (e.g. social benefit 'obligations') would qualify as liabilities is whether the entity has "little or no realistic alternative to avoid settling the obligation" (see paragraphs 3.1, 3.10 and 3.12 of the IPSASB ED). The issue is not categorically resolved in the ED. The fifth sentence of paragraph BC24 says the issue of liabilities arising from social benefits should be considered at the standards level. The Board's submission on the CP argued that liabilities should be defined broadly and the association of those liabilities with the entity should be addressed through the recognition criteria. AASB staff think the recognition of social benefits is such an important and pervasive public

Issue in IPSASB CP, and AASB comments thereon	Treatment of issue in IPSASB ED, and AASB staff comments thereon
inappropriately, be termed a perpetual obligation is the balance of employees' holiday leave entitlements.	sector issue that it should be addressed in the IPSASB Conceptual Framework. In particular, AASB staff think addressing social benefits in the Framework would be an important test of the robustness of the key notion of having "little or no realistic alternative to avoid settling the obligation". Therefore, AASB staff recommend that the Board's submission disagrees with treating the recognition of social benefit 'obligations' as only a standards-level issue.
<u>Issue 17:</u> Is enforceability of an obligation an essential characteristic of a liability? The AASB is of the view that the significance of whether an obligation is enforceable is a recognition issue rather than an issue affecting the definition of a liability. A similar liability recognition issue the AASB recommends addressing is whether obligations should be unconditional in order to qualify for recognition. Whether an obligation is unconditional is a factor associating a liability with an entity, and therefore the AASB does not consider it to be an issue affecting the definition of a liability.	The IPSASB ED conflicts with the Board's comment in its submission on the CP that the significance of whether an obligation is enforceable is a recognition issue rather than an issue affecting the definition of a liability. AASB staff recommend that the Board reiterates that point in its submission on the ED. Paragraph BC31 of the Basis for Conclusions on the IPSASB ED does not directly answer the question of whether enforceability is an essential characteristic of a liability. As noted in the comments above on Issue 16, the definition of a liability in paragraph 3.1 of the ED says "there is little or no realistic alternative to avoid an outflow" in settling the obligation. Potentially, this characteristic is not much broader than 'enforceability'. A key test of whether that is the case would be social benefits; however, as noted above in the comments on Issue 16, social benefits are treated in the ED as a standards-level issue.
<u>Issue 18:</u> Implications of sovereign power for the definition of a liability *The IPSASB CP asked whether the definition of a liability should include an assumption about the role that sovereign power plays, such as by reference to the legal position at the reporting date.* *AASB response:* The AASB considers that the significance of sovereign powers to cancel or modify obligations to other parties is a recognition issue rather than an issue affecting the definition of a liability. The AASB considers that assessments of whether particular liabilities qualify for recognition should be based on existing legislation.	In relation to sovereign power, the second and third sentences of paragraph 3.9 of the ED and the seventh sentence of paragraph BC33 are consistent with the Board's view, expressed in its submission on the CP, that assessments of whether particular liabilities qualify for recognition should be based on existing legislation.

Issue in IPSASB CP, and AASB comments thereon	Treatment of issue in IPSASB ED, and AASB staff comments thereon
<u>Issue 19:</u> **Should transactions with residual/equity interests be excluded from revenues and expenses?** The AASB considers that transactions with residual/equity interests should be excluded from revenues and expenses.	Paragraphs 4.1 and 4.2 of the IPSASB ED (supported by paragraph BC39) exclude ownership contributions and ownership distributions from the definitions of revenue and expenses, consistent with the view expressed in the Board's submission on the CP.
<u>Issue 20:</u> **Should the definitions of revenue and expense be limited to specific types of activities associated with operations?** The AASB does not support restricting the definitions of revenues and expenses to specific types of activities associated with operations. Instead, the definitions of revenues and expenses should include inflows from all transactions and events other than transactions with residual/equity interests.	The definitions of revenue and expenses in paragraphs 4.1 and 4.2 of the IPSASB ED are not limited to specific types of activities associated with operations (see also paragraphs BC37 and BC38). This is consistent with the Board's response on this issue in the CP.
<u>Issue 21:</u> **Are net assets/net liabilities a residual amount, a residual interest or an ownership interest?** The AASB would prefer that net assets/net liabilities were described as a residual interest rather than a residual amount. The AASB does not support treating net assets/net liabilities as necessarily being an ownership interest because, in some cases, such as local governments in Australia, there may not be an ownership interest in a public sector entity.	Paragraphs BC48 and BC49 of the IPSASB ED indicate net financial position (and, by implication, net assets) is a residual amount that should not be defined. Paragraph 6.1 of the IPSASB ED says neither net assets nor net financial position are elements. AASB staff recommend that the Board disagrees with this view in its submission on the ED, focusing on the nature of net assets/equity rather than net financial position (since the latter notion arises from the IPSASB proposal to recognise deferred outflows and deferred inflows). The proposed reasons for disagreeing are that: • residual interests have economic substance and are not merely a balancing item; • it is inconsistent to define assets and liabilities as elements of financial statements but not net assets; and • it is inconsistent to define ownership contributions and ownership distributions as elements of financial statements (in paragraphs 6.3 and 6.4 of the IPSASB ED) but not the item affected by those transactions with owners.
<u>Issue 22:</u> **Should the concept of ownership interests be incorporated into the definition of net assets/net liabilities?**	Paragraphs BC48 – BC50 of the ED indicate that part of an entity's net financial position can be an ownership interest, which is a sub-classification of net financial position. This is consistent with

Issue in IPSASB CP, and AASB comments thereon	**Treatment of issue in IPSASB ED, and AASB staff comments thereon**
The AASB supports the approach in the CP that treats any specific ownership interest as a sub-classification of net assets/net liabilities.	the Board's comment on this issue in its submission on the IPSASB CP.
<u>**Issue 23:**</u> **Should transactions with residual/equity interests be defined as separate elements?** The AASB is of the view that transactions with residual interest holders could, but would not necessarily, be defined as separate elements. This would depend on the wording of the definitions. However, it is important to define transactions with residual interest holders because reference is made to those transactions in existing definitions of revenues and expenses.	Ownership contributions and ownership distributions are defined as elements of financial statements in paragraphs 6.3 and 6.4 of the IPSASB ED, for the reason discussed in the last two sentences of paragraph BC50. This is compatible with the Board's comment on this issue in its submission on the IPSASB CP.
<u>**Issue 24:**</u> **Recognition criteria** The AASB is of the view that the recognition criteria should be: (a) separate from definitions of the elements of financial statements; and (b) neutral, both in requiring a neutral judgement of whether an element exists at the reporting date and in specifying the same recognition threshold for all assets and liabilities.	The IPSASB ED treats recognition criteria as separate and distinct from the definitions of the elements of financial statements (see Section 7 and paragraph BC51). However, although Section 7 of the ED is headed 'Recognition Criteria', no explicit recognition criteria are set out. In addition, paragraph 7.4 of the ED says 'existence uncertainty' is addressed by making a neutral judgement about whether an element exists, implying a 'probable' threshold. In relation to 'measurement uncertainty', paragraphs 7.5 – 7.6 of the ED do not indicate whether it is possible that no measure of an asset or a liability would result in a sufficiently faithful representation of that element for it to be recognised. (Note also that, to be contemporary with IASB thinking, 'existence uncertainty' and 'outcome uncertainty' should be analysed, and neither of these is concerned with 'measurement uncertainty'.) AASB staff recommend expressing the concerns in this paragraph in the Board's submission on the ED.
<u>**Issue 25:**</u> **Derecognition criteria** The AASB supports the use of the same criteria for derecognition as for initial recognition. A corollary of the AASB's view that recognition criteria should be neutral (see comment above on Specific Matter for Comment 17) is that recognition criteria should apply equally to the initial recognition and subsequent recognition of an element. Derecognition is synonymous with treating an element as failing criteria for subsequent recognition.	Paragraph 7.7 of the IPSASB ED says that, in evaluating existence uncertainty, the same criteria should apply to the initial recognition and derecognition of an element of financial statements. This is compatible with the Board's comment on this issue in its submission on the IPSASB CP.