ACCOUNTING STANDARDS BOARD

THE CONCEPTUAL FRAMEWORK FOR GENERAL PURPOSE FINANCIAL REPORTING

Issued by the

Accounting Standards Board

Acknowledgement

The *Conceptual Framework for General Purpose Financial Reporting* is based on the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* from the *Handbook of International Public Sector Accounting Pronouncements* of the International Public Sector Accounting Standards Board (IPSASB), published by the International Federation of Accountants (IFAC) and is used with the permission of the IFAC.

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International Federation of Accountants

529 Fifth Avenue, 6th Floor

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Internet: http://www.ifac.org

THE CONCEPTUAL FRAMEWORK FOR GENERAL PURPOSE FINANCIAL REPORTING

This Conceptual Framework for General Purpose Financial Reporting (Conceptual Framework) has been approved for issue by the Accounting Standards Board (Board), the body which has as its principal function to set generally recognised accounting practice as required by section 216(1) of the Constitution of the Republic of South Africa (Act 108 of 1996). In the development of this Conceptual Framework, reference was made to:

- *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* developed and issued by the International Public Sector Accounting Standards Board (IPSASB) during October 2014; and
- extracts of the revised *Conceptual Framework for Financial Reporting* issued by the International Accounting Standards Board (IASB®).

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THE PREFACE TO THE CONCEPTUAL FRAMEWORK FOR GENERAL PURPOSE FINANCIAL REPORTING

Introduction

1. The *Conceptual Framework for General Purpose Financial Reporting* (the Conceptual Framework) establishes the concepts that are to be applied in developing Standards of Generally Recognised Accounting Practice (GRAP) applicable to the preparation and presentation of general purpose financial statements (GPFSs) of public sector entities.

2. The Conceptual Framework also establishes concepts for the presentation of general purpose financial reports (GPFRs) which are reported outside the financial statements, and which complement and supplement the information in the financial statements.

3. The primary objective of most public sector entities is to deliver services to the public, rather than to make profits and generate a return on equity to investors. Consequently the performance of such entities can be only partially evaluated by examination of financial position, financial performance and cash flows. GPFRs provide information to users for accountability and decision-making purposes. Therefore, users of the GPFRs of public sector entities need information to support assessments of such matters as:

   - whether the entity provided its services to constituents in an efficient and effective manner;
   - the resources currently available for future expenditures, and to what extent there are restrictions or conditions attached to their use;
   - to what extent the burden on future-year taxpayers of paying for current services has changed; and
   - whether the entity's ability to provide services has improved or deteriorated compared with the previous year.

4. Government generally has broad powers, including the ability to establish and enforce legal requirements, and to change those requirements. Governance in the public sector generally involves the holding to account of the executive by a legislative body (or equivalent).

5. The following sections highlight characteristics of the public sector that the Board has considered in the development of the Conceptual Framework.

The volume and financial significance of non-exchange transactions

6. In a non-exchange transaction, an entity receives value from another party without directly giving approximately equal value in exchange. Such transactions are common in the public sector. The level and quality of services received by an individual, or group of individuals, is not normally directly related to the level of taxes assessed. An individual or group may have to pay a charge or fee and/or may have had to make specified contributions to access certain

services. However, such transactions are, generally, of a non-exchange nature, because the amount that an individual or group of individuals obtains in benefits will not be approximately equal to the amount of any fees paid or contributions made by the individual or group. The nature of non-exchange transactions may have an impact on how they are recognised, measured, and presented to best support assessments of the entity by service recipients and resource providers.

7. Taxation is a legally mandated, compulsory non-exchange transaction between individuals or entities and the government. Tax-raising powers can vary considerably, dependent upon the relationship between the powers of the national government and those of provincial and local governments and public sector entities as outlined in legislation.

8. Government and public sector entities are accountable to resource providers, particularly to those that provide resources through taxes and other compulsory transactions. Chapter 2, *Objectives and Users of General Purpose Financial Reporting,* discusses the accountability objective of financial reporting.

The importance of the approved budget

9. Public sector entities, through the budget process, are appropriated funds by Parliament, the legislatures, municipal councils or other relevant authority, which are to be spent in accordance with certain priorities. Some entities may be required to prepare and make publicly available a budget approved by Parliament, the legislatures, municipal councils or other relevant authorities. Legislation often defines the contents of that documentation. Parliament, the legislatures, municipal councils or other relevant authorities exercise oversight, and constituents and their elected representatives hold the entity's management financially accountable through the budget and other mechanisms. The approved budget is often the basis for setting taxation levels, and is part of the process for obtaining legislative approval for spending.

10. Because of the approved budget's significance, information that enables users to compare financial results with the budget facilitates an assessment of the extent to which a public sector entity has met its financial objectives. Such information promotes accountability and informs decision making in subsequent budgets. Reporting against budget is the mechanism for demonstrating compliance with legal requirements relating to the public finances. The needs of users for budget information are discussed in Chapter 2.

The nature of public sector programmes and the longevity of the public sector

11. Many public sector programmes are long term and the ability to meet commitments depends upon future taxation and contributions. Many commitments arising from public sector programmes and powers to levy future taxation do not meet the definitions of a liability and an asset in Chapter 5, *Elements in Financial Statements*. Therefore, such commitments and powers are not recognised in the financial statements.

12. Consequently, the statement of financial position and statement of financial performance

cannot provide all the information that users need on long-term programmes, particularly those delivering social benefits. The financial consequences of many decisions will have an impact many years or even decades into the future, so GPFRs containing prospective financial information on the long-term sustainability of an entity's finances and key programmes are necessary for accountability and decision-making purposes as discussed in Chapter 2.

13. Although political control may change regularly, governments generally have very long existences. While they may encounter severe financial difficulties and may default on sovereign debt obligations, governments continue to exist. If public sector entities get into financial difficulties, government might act as a lender of last resort or provide large scale guarantees. The main service delivery commitments of public sector entities may continue to be funded by a higher level of government. In other cases public sector entities that are unable to meet their liabilities as they fall due may continue to exist by restructuring their operations.

14. The going concern principle underpins the preparation of the financial statements. Interpretation of the principle needs to reflect the issues discussed in paragraphs 11 to 13.

The nature and purpose of assets and liabilities in the public sector

15. In the public sector, the primary reason for holding property, plant, and equipment and other assets is for their service potential rather than their ability to generate cash flows[1]. Because of the types of services provided, a significant proportion of assets used by public sector entities are specialised—for example, roads and military assets. There may be a limited market for such assets and, even then, they may need considerable adaptation in order to be used by other operators. These factors have implications for the measurement of such assets. Chapter 7, *Measurement of Assets and Liabilities in Financial Statements*, discusses measurement bases for assets.

16. Public sector entities may hold items that contribute to the historical and cultural character of a nation—for example, art treasures, historical buildings, and other artifacts. They may also be responsible for national parks and other areas of natural significance with native flora and fauna. Such items and areas are not generally held for sale, even if markets exist. Rather, public sector entities have a responsibility to preserve and maintain them for current and future generations.

17. Government often has powers over natural and other resources such as mineral reserves, water, fishing grounds, forests and the electromagnetic spectrum. These powers allow government to grant licenses for the use of such resources or to obtain royalties and taxes from their use. The definition of an asset and recognition criteria are discussed in Chapter 5 *Elements in Financial Statements,* and Chapter 6, *Recognition in Financial Statements* respectively.

[1] Many public sector assets will generate cash flows, but this is often not the main reason for holding them.

18. Government and public sector entities incur liabilities related to their service delivery objectives. Many liabilities arise from non-exchange transactions and include those related to programmes that operate to deliver social benefits. Liabilities may also arise from government's role as a lender of last resort and from any obligations to transfer resources to those affected by disasters. In addition government has obligations that arise from monetary activities such as currency in circulation. The definition of a liability and recognition criteria are discussed in Chapters 5 and 6.

The regulatory role of public sector entities

19. Governments and public sector entities have powers to regulate entities operating in certain sectors of the economy, either directly or through specifically created public entities. The underlying public policy rationale for regulation is to safeguard the public interest in accordance with specified public policy objectives. Regulatory intervention can also occur where there are market imperfections or market failure for particular services, or to mitigate against factors such as pollution, the impact of which is not transmitted through pricing. Such regulatory activities are carried out in accordance with legal processes.

20. Government may also regulate itself and public sector entities. Judgement may be necessary to determine whether such regulations create rights of, and obligations on, public sector entities that require recognition as assets and liabilities, or whether the public sector entity's ability to amend such regulations has an impact on how such rights and obligations are accounted for. Chapter 5 considers rights and obligations.

CHAPTER 1: ROLE AND AUTHORITY OF THE CONCEPTUAL FRAMEWORK

Role of the Conceptual Framework

1.1 The *Conceptual Framework for General Purpose Financial Reporting* (the Conceptual Framework) establishes the concepts that underpin general purpose financial reporting (financial reporting) by public sector entities that adopt the accrual basis of accounting.

1.2 The role of the Conceptual Framework is to:

(a) provide the Accounting Standards Board (the Board) with a conceptual basis for developing Standards of Generally Recognised Accounting Practice (GRAP) applicable to the preparation and presentation of general purpose financial statements (GPFSs) of public sector entities;

(b) promote the advancement of financial reporting so that the preparation and presentation of general purpose financial reports (GPFRs) is comprehensive, cohesive and consistent with the concepts used to prepare and present GPFSs;

(c) assist preparers of GPFSs in applying Standards of GRAP and in dealing with topics that may not form the subject of a Standard of GRAP;

(d) provide users of GPFSs prepared in accordance with Standards of GRAP such as Parliament, the legislatures, municipal councils or other relevant authorities, with information on the basis on which such GPFSs are prepared and to assist them to hold entities accountable and make decisions;

(e) assist users of GPFSs in interpreting the information contained in GPFSs prepared in conformity with the Standards of GRAP; and

(f) provide auditors with a framework to form an opinion as to whether financial statements conform with Standards of GRAP.

General Purpose Financial Reports

1.3 GPFRs are a central component of, and support and enhance, transparent financial reporting by government and public sector entities. GPFRs are financial reports intended to meet the information needs of users who are unable to require the preparation of financial reports tailored to meet their specific information needs.

1.4 Some users of financial information may have the authority to require the preparation of reports tailored to meet their specific information needs. While such parties may find the information provided by GPFRs useful for their purposes, GPFRs are not developed to specifically respond to their particular information needs.

1.5 GPFRs are likely to comprise multiple reports, each responding more directly to certain aspects of the objectives of financial reporting and matters included within the scope of financial reporting. GPFRs encompass financial statements including their notes (hereafter referred to as financial statements, unless specified otherwise), as well as the presentation of information in other reports that enhances, complements and supplements the financial statements.

1.6 The scope of financial reporting establishes the boundary around the transactions, other events and activities that may be reported in GPFRs. The scope of financial reporting is determined by the information needs of the primary users of GPFRs and the objectives of financial reporting. The factors that determine what may be encompassed within the scope of financial reporting are outlined in the next chapter.

Authority of the Conceptual Framework

1.7 The Conceptual Framework does not establish authoritative requirements for financial reporting by public sector entities that adopt Standards of GRAP, nor does it override the requirements of any specific Standard of GRAP. Authoritative requirements relating to the recognition, measurement and presentation of transactions and other events and activities that are reported in the financial statements are specified in the Standards of GRAP.

1.8 The Conceptual Framework can provide guidance in dealing with financial reporting issues not dealt with by Standards of GRAP. In these circumstances, preparers and other users can refer to and consider the applicability of the definitions, recognition criteria, measurement principles, and other concepts identified in the Conceptual Framework.

1.9 The Conceptual Framework does not establish the requirements for what information should be included in financial reports outside the financial statements. Instead, the Conceptual Framework sets out broad principles that indicate how the information in these financial reports can be prepared and presented. The Conceptual Framework does not override any existing legislative requirements, frameworks or similar documents issued by other organisations that prescribe requirements for the preparation and presentation of information in these reports.

Applicability of the Conceptual Framework

1.10 The Conceptual Framework applies to financial reporting by public sector entities that apply Standards of GRAP. Legislation determines which public sector entities should apply Standards of GRAP. In the absence of such a legislative requirement, public sector entities may apply Standards of GRAP if they have these characteristics:

- they are responsible for the delivery of services to benefit the public and/or to redistribute income and wealth;
- mainly finance their activities, directly or indirectly, by means of taxes and/or transfers from other spheres of government, social contributions, debt or fees; and
- do not have a primary objective to make profits.

CHAPTER 2: OBJECTIVES AND USERS OF GENERAL PURPOSE FINANCIAL REPORTING

Objectives of financial reporting

2.1 The objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of GPFRs for accountability purposes and for decision-making purposes (hereafter referred to as "useful for accountability and decision-making purposes").

2.2 Financial reporting is not an end in itself. Its purpose is to provide information that is useful to users of GPFRs. The objectives of financial reporting are therefore determined by reference to the users of GPFRs, and their information needs.

Users of General Purpose Financial Reports

2.3 Public sector entities raise resources from taxpayers, donors, lenders and other resource providers for use in the provision of services to citizens and other service recipients. These entities are accountable for their management and use of resources to those that provide them with resources, and to those that depend on them to use those resources to deliver necessary services. Those that provide the resources and receive, or expect to receive, the services also require information as input for decision-making purposes.

2.4 Consequently, GPFRs of public sector entities are developed primarily to respond to the information needs of service recipients and resource providers who do not possess the authority to require a public sector entity to disclose the information they need for accountability and decision-making purposes. Parliament, the legislatures, municipal councils or other relevant authorities are also primary users of GPFRs, and make extensive and ongoing use of GPFRs when acting in their capacity as representatives of the interests of service recipients and resource providers. Therefore, for the purposes of the Conceptual Framework, the primary users of GPFRs are service recipients and their representatives and resource providers and their representatives (hereafter referred to as "service recipients and resource providers", unless identified otherwise).

2.5 Citizens receive services from, and provide resources to, the government and public sector entities. Therefore, citizens are primary users of GPFRs. Some service recipients and some resource providers that rely on GPFRs for the information they need for accountability and decision-making purposes may not be citizens—for example, residents who pay taxes and/or receive benefits but are not citizens; multilateral or bilateral donor agencies and many lenders and corporations that provide resources to, and transact with, government; and those that fund, and/or benefit from, the services provided by international governmental organisations. Where government provides resources to international governmental organisations it is dependent on GPFRs of those organisations for information for accountability and decision-making purposes.

2.6 GPFRs prepared to respond to the information needs of service recipients and resource providers for accountability and decision-making purposes may also provide information useful to other parties and for other purposes. For example, statisticians, analysts, the media, financial advisors, public interest and lobby groups and others may find the information provided by GPFRs useful for their own purposes. Organisations that have the authority to require the preparation of financial reports tailored to meet their own specific information needs may also use the information provided by GPFRs for their own purposes—for example, regulatory and oversight bodies, the Auditor-General of South Africa, subcommittees of Parliament, the legislatures, municipal councils or other relevant authorities , central agencies and budget controllers, entity management, rating agencies and, in some cases, lending institutions and providers of development and other assistance. While these other parties may find the information provided by GPFRs useful, they are not the primary users of GPFRs. Therefore, GPFRs are not developed to specifically respond to their particular information needs.

Accountability and decision making

2.7 The primary objective of government and public sector entities is to provide services that enhance or maintain the well-being of citizens and other eligible residents. Those services include, for example, welfare programmes and policing, public education, national security and defense services. In most cases, these services are provided as a result of a non-exchange transaction[2] and in a non-competitive environment.

2.8 Accountability is the cornerstone of financial reporting in government, and the term *accountability* is used throughout this Conceptual Framework. Accountability is based on the belief that the citizens have a “right to know”, a right to receive openly declared facts that may lead to a public debate by the citizens and their elected representatives. Financial reporting plays a major role in fulfiling government’s duty to be publicly accountable in a democratic society.

2.9 Public sector entities are accountable to those that provide them with resources, and to those that depend on them to use those resources to deliver services during the reporting period and over the longer term. The discharge of accountability obligations requires the provision of information about the entity’s management of the resources entrusted to it for the delivery of services to constituents and others, and its compliance with legislation, regulation, or other authority that governs its service delivery and other operations. Given the way in which the services provided by public sector entities are funded (primarily by

[2] Exchange transactions are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equally value to another entity in exchange. Non-exchange transactions are transactions in which an entity receives value from another entity without directly giving approximately equal value in exchange.

taxation revenues or other non-exchange transactions) and the dependency of service recipients on the provision of those services over the long term, the discharge of accountability obligations will also require the provision of information about such matters as the entity's service delivery achievements during the reporting period, and its capacity to continue to provide services in future periods.

2.10 Service recipients and resource providers will also require information as input for making decisions. For example:

- lenders, creditors, donors and others that provide resources on a voluntary basis, including in an exchange transaction, make decisions about whether to provide resources to support the current and future activities of the government or public sector entity. In some circumstances, Parliament, the legislatures, municipal councils or other relevant authorities who depend on GPFRs for the information they need, can make or influence decisions about the service delivery objectives of public sector entities and the resources allocated to support their achievement; and
- taxpayers do not usually provide funds to the government or public sector entities on a voluntary basis or as a result of an exchange transaction as they cannot choose whether or not to pay taxes. In addition, in many cases, they do not have the discretion to choose whether or not to accept the services provided by a public sector entity or to choose an alternative service provider. Consequently, they have little direct or immediate capacity to make decisions about whether to provide resources to the government, the resources to be allocated for the provision of services by a particular public sector entity or whether to purchase or consume the services provided. However, service recipients and resource providers can make decisions about their voting preferences, and representations they make to elected officials or other representative bodies—these decisions may have resource allocation consequences for certain public sector entities.

2.11 Information provided in GPFRs for accountability purposes will contribute to, and inform, decision making. For example, information about the costs, efficiency and effectiveness of past service delivery activities, the amount and sources of cost recovery, and the resources available to support future activities will be necessary for the discharge of accountability. This information will also be useful for decision making by users of GPFRs, including decisions that donors and other financial supporters make about providing resources to the entity.

Information needs of service recipients and resource providers

2.12 For accountability and decision-making purposes, service recipients and resource providers will need information that supports the assessments of such matters as:

- the performance of the entity during the reporting period in, for example:
  - meeting its service delivery and other operating and financial objectives;
  - managing the resources it is responsible for;
  - complying with relevant budgetary, legislative, and other authority regulating the raising and use of resources;
- the liquidity (for example, ability to meet current obligations) and solvency (for example, ability to meet obligations over the long term) of the entity;
- the sustainability of the entity's service delivery and other operations over the long term, and changes therein as a result of the activities of the entity during the reporting period including, for example:
  - the capacity of the entity to continue to fund its activities and to meet its operational objectives in the future (its financial capacity), including the likely sources of funding and the extent to which the entity is dependent on, and therefore vulnerable to, funding or demand pressures outside its control;
  - the physical and other resources currently available to support the provision of services in future periods (its operational capacity); and
- the capacity of the entity to adapt to changing circumstances, whether changes in demographics or changes in domestic or global economic conditions which are likely to impact the nature or composition of the activities it undertakes and the services it provides.

2.13 The information service recipients and resource providers need for these purposes is likely to overlap in many respects. For example, service recipients will require information as input to assessments of such matters as whether:

- the entity is using resources economically, efficiently, effectively and as intended, and whether such use is in their interest;
- the range, volume and cost of services provided during the reporting period are appropriate, and the amounts and sources of their cost recoveries; and
- current levels of taxes or other resources raised are sufficient to maintain the volume and quality of services currently provided.

Service recipients will also require information about the consequences of decisions made, and activities undertaken, by the entity during the reporting period on the resources available to support the provision of services in future periods, the entity's anticipated future service delivery activities and objectives, and the amounts and sources of cost recoveries necessary to support those activities.

2.14 Resource providers will require information as input to assessments of such matters as whether the entity:

- is achieving the objectives established as the justification for the resources raised during the reporting period;
- funded current operations from funds raised in the current period from taxpayers or from borrowings or other sources; and
- is likely to need additional (or less) resources in the future, and the likely sources of those resources.

Lenders and creditors will require information as input to assessments of the liquidity of the entity and, therefore, whether the amount and timing of repayment will be as agreed. Donors will require information to support assessments of whether the entity is using resources economically, efficiently, effectively and as intended. They will also require information about the entity's anticipated future service delivery activities and resource needs.

The scope of General Purpose Financial Reports

2.15 The scope of financial reporting establishes the boundary around the transactions, other events and activities that may be reported in GPFRs. To respond to the information needs of users, the Conceptual Framework reflects a scope for financial reporting that is more comprehensive than that encompassed by financial statements. It provides for the presentation within GPFRs of additional information that enhances, complements, and supplements those statements.

2.16 While the Conceptual Framework reflects a scope of financial reporting that is more comprehensive than that encompassed by financial statements, information presented in financial statements remains at the core of financial reporting. How the elements of financial statements are defined, recognised and measured, and forms of presentation and communication that might be adopted for information included within GPFRs, is considered in other chapters of the Conceptual Framework and in the development of individual Standards of GRAP, as appropriate.

Information provided by General Purpose Financial Reports

Financial position, financial performance, and cash flows

2.17 Information about the financial performance of a government or public sector entity will inform assessments of matters such as whether the entity has acquired resources economically, and used them efficiently and effectively to achieve its service delivery objectives. Information about the costs of service delivery and the amounts and sources of cost recovery during the reporting period will assist users to determine whether operating costs were recovered from, for example, taxes, user charges, contributions and transfers, or were financed by increasing the level of indebtedness of the government or entity.

2.18 Information about the cash flows of a government or public sector entity contributes to assessments of financial performance and the entity's liquidity and solvency. It indicates how the entity raised and used cash during the period, including its borrowing and repayment of borrowing and its acquisition and sale of, for example, property, plant, and equipment. It also identifies the cash received from, for example, taxes and investments and the cash transfers made to, and received from, other governments, government agencies or international organisations. Information about cash flows can also support assessments of the entity's compliance with spending mandates expressed in cash flow terms, and inform assessments of the likely amounts and sources of cash inflows needed in future periods to support service delivery objectives.

2.19 Information about financial position, financial performance, and cash flows are typically presented in financial statements. To assist users to better understand, interpret and place in context the information presented in the financial statements, GPFRs may also provide financial and non-financial information that enhances, complements and supplements the financial statements, including information about such matters as the government's or public sector entity's:

- compliance with approved budgets and other authority governing its operations;
- service delivery activities and achievements during the reporting period; and
- expectations regarding service delivery and other activities in future periods, and the long term consequences of decisions made and activities undertaken during the reporting period, including those that may impact expectations about the future.

Depending upon the level of detail and purpose of this additional information it may be presented in the notes to the financial statements, or as a separate part of the GPFR containing the financial statements or in a separate GPFR.

Budget information and compliance with legislation governing the raising and use of resources

2.20 Some public sector entities are required to make their approved budgets publicly available. The approved budget provides interested parties with financial information about the entity's operational plans for the forthcoming period and its capital needs. It is used to justify the raising of resources from taxpayers and other resource providers, and establishes the authority for expenditure of resources.

2.21 Some resources to support the activities of public sector entities may be received from donors, lenders or as a result of exchange transactions. However, resources to support the activities of public sector entities are predominantly provided in non-exchange transactions by taxpayers and others, consistent with the expectations reflected in an approved budget.

2.22 GPFRs provide information about the financial results described as “surplus or deficit”, performance and cash flows of the entity during the reporting period, its assets and liabilities at the reporting date and the change therein during the reporting period, and its service delivery achievements.

2.23 The inclusion within GPFRs of information that assists users in assessing the extent to which revenues, expenses, cash flows and financial results of the entity comply with the estimates reflected in approved budgets, and the entity’s adherence to relevant legislation, supporting regulations or similar means governing the raising and use of resources, is important in determining how well a public sector entity has met its financial objectives. Such information is necessary for the discharge of a public sector entity’s accountability to its constituents, enhances the assessment of the financial performance of the entity and will inform decision making.

Service delivery achievements

2.24 The primary objective of government and most public sector entities is to provide needed services to constituents. Consequently, the performance of government and public sector entities will not be fully or adequately reflected in any measure of financial results. Therefore, their financial results will need to be assessed in the context of the achievement of service delivery objectives in the GPFRs.

2.25 In some cases, quantitative measures of the outputs and outcomes of the entity’s service delivery activities during the reporting period will provide relevant information about the achievement of service delivery objectives—for example, information about the cost, volume, and frequency of service delivery, and the relationship of services provided to the resource base of the entity. In other cases, the achievement of service delivery objectives may need to be communicated by an explanation of the quality of particular services provided or the outcome of certain programmes.

2.26 Reporting non-financial as well as financial information about service delivery activities, achievements and/or outcomes during the reporting period will provide input to assessments of the economy, efficiency, and effectiveness of the entity’s operations. Reporting such information is necessary for the government or public sector entity to discharge its obligation to be accountable—that is, to account for, and justify the use of, the resources raised from, or on behalf of, constituents. Decisions that donors make about the allocation of resources to particular entities and programmes are also made, at least in part, in response to information about service delivery achievements during the reporting period, and future service delivery objectives.

Prospective financial and non-financial information

2.27 Given the longevity of government and many government programmes, the financial consequences of many decisions made in the reporting period may only become clear many years into the future. Financial statements which present information about financial position at a point in time and financial performance and cash flows over the reporting period will then need to be assessed in the context of the long term.

2.28 Decisions made by a government or public sector entity in a particular period about programmes for delivering and funding services in the future can have significant consequences for:

- constituents who will be dependent on those services in the future; and
- current and future generations of taxpayers and other involuntary resource providers who will provide the taxes and levies to fund the planned service delivery activities and related financial commitments.

2.29 Information about the entity's anticipated future service delivery activities and objectives, their likely impact on the future resource needs of the entity and the likely sources of funding for such resources, will be necessary as input to any assessment of the ability of the government or public sector entity to meet its service delivery and financial commitments in the future. The disclosure of such information in GPFRs will support assessments of the sustainability of service delivery by the government or public sector entity, enhance the accountability of the entity and provide additional information useful for decision-making purposes.

Explanatory information

2.30 Information about the major factors underlying the financial and service delivery performance of the entity during the reporting period and the assumptions that underpin expectations about, and factors that are likely to influence, the entity's future performance may be presented in GPFRs in notes to the financial statements or in separate reports. Such information will assist users to better understand and place in context the financial and non-financial information included in GPFRs, and enhance the role of GPFRs in providing information useful for accountability and decision-making purposes.

Other sources of information

2.31 GPFRs play a significant role in communicating information necessary to support the discharge of a government's or public sector entity's obligation to be accountable, as well as providing information useful as input for decision-making purposes. However, it is unlikely that GPFRs will provide all the information users need for accountability and decision-making purposes. For example, while comparison of actual with budget information for the reporting period may be included in GPFRs, the budgets and financial forecasts issued by government provide more detailed financial and non-financial information about the financial characteristics of the plans of governments and public sector entities over the short and medium terms. Government, public sector entities and independent agencies also issue reports on the need for, and sustainability of, existing service delivery initiatives and anticipated economic conditions and changes in the demographics over the medium and longer term that will influence budgets and service delivery needs in the future. Consequently, service recipients and resource providers may also need to consider information from other sources, including reports on current and anticipated economic conditions, budgets and forecasts, and information about policy initiatives not reported in GPFRs.

CHAPTER 3: QUALITATIVE CHARACTERISTICS

Introduction

3.1 GPFRs present financial and non-financial information about economic and other phenomena, i.e. an occurrence that has economic consequences. The qualitative characteristics of information included in GPFRs are the attributes that make that information useful to users and support the achievement of the objectives of financial reporting. The objectives of financial reporting are to provide information useful for accountability and decision-making purposes.

3.2 The qualitative characteristics of information included in GPFRs of public sector entities are relevance, faithful representation, understandability, timeliness, comparability, and verifiability.

3.3 Pervasive constraints on information included in GPFRs are cost-benefit, and achieving an appropriate balance between the qualitative characteristics.

3.4 Each of the qualitative characteristics is integral to, and works with, the other characteristics to provide in GPFRs information useful for achieving the objectives of financial reporting. However, in practice, all qualitative characteristics may not be fully achieved, and a balance or trade-off between certain of them may be necessary.

3.5 The qualitative characteristics apply to all financial and non-financial information reported in GPFRs, including historic and prospective information, and explanatory information. However, the extent to which the qualitative characteristics can be achieved may differ depending on the degree of uncertainty and subjective assessment or opinion involved in compiling the financial and non-financial information.

3.6 The need for additional guidance on interpreting and applying the qualitative characteristics to information in the financial statements will be considered in the development of any Standard of GRAP that deals with such matters.

Relevance

3.7 Financial and non-financial information is relevant if it is capable of making a difference in achieving the objectives of financial reporting. Financial and non-financial information is capable of making a difference when it has confirmatory value, predictive value, or both. It may be capable of making a difference, and thus be relevant, even if some users choose not to take advantage of it or are already aware of it.

3.8 Financial and non-financial information has confirmatory value if it confirms or changes past (or present) expectations. For example, information will be relevant for accountability and decision-making purposes if it confirms expectations about such matters as the extent to which managers have discharged their responsibilities for the efficient and effective use of resources, the achievement of specified service delivery objectives, and compliance with relevant budgetary, legislative and other requirements.

3.9 GPFRs may present information about an entity's anticipated future service delivery activities, objectives and costs, and the amount and sources of the resources that are intended to be allocated to providing services in the future. Such future oriented information will have predictive value and be relevant for accountability and decision-making purposes. Information about economic and other phenomena that exist or have already occurred can also have predictive value in helping form expectations about the future. For example, information that confirms or disproves past expectations can reinforce or change expectations about financial results and service delivery outcomes that may occur in the future.

3.10 The confirmatory and predictive roles of information are interrelated—for example, information about the current level and structure of an entity's resources and claims to those resources helps users to confirm the outcome of resource management strategies during the period, and to predict an entity's ability to respond to changing circumstances and anticipated future service delivery needs. The same information helps to confirm or correct users' past expectations and predictions about the entity's ability to respond to such changes. It also helps to confirm or correct prospective financial information included in previous GPFRs.

Materiality

3.11 The relevance of information is affected by its nature and materiality. In some cases, the nature of information alone is sufficient to determine its relevance. For example, the reporting of a new programme or service segment may affect the assessment of the risks and opportunities facing the entity irrespective of the materiality of the results achieved by the new segment in the reporting period. In other cases, both the nature and materiality are important, for example, the amounts of inventories held in each of the main categories that are appropriate to the entity.

3.12 Information is material if its omission or misstatement could influence the discharge of accountability by the entity, or the decisions that users make on the basis of the entity's GPFRs prepared for that reporting period. Materiality depends on both the nature and amount of the item judged in the particular circumstances of each entity. GPFRs may encompass qualitative and quantitative information about service delivery achievements during the reporting period, and expectations about service delivery and financial outcomes in the future. Consequently, it is not possible to specify a uniform quantitative threshold at which a particular type of information becomes material.

3.13 Assessments of materiality will be made in the context of the legislative, institutional and operating environment within which the entity operates and, in respect of prospective financial and non-financial information, the preparer's knowledge and expectations about the future. Disclosure of information about compliance or non-compliance with legislation, supporting regulations or similar means may be material because of its nature, irrespective of the magnitude of any amounts involved. In determining whether an item is material in these circumstances, consideration will be given to such matters as the nature, legality, sensitivity and consequences of past or anticipated transactions and events, the parties involved in any such transactions and the circumstances giving rise to them.

3.14 In developing Standards of GRAP, the Board will consider the materiality of the consequences of applying a particular accounting policy, basis of preparation or presentation of a particular item or type of information. Subject to the requirements of any Standard of GRAP, entities preparing GPFRs will also consider the materiality of, for example, the application of a particular basis of preparation or presentation of particular items of information.

Faithful representation

3.15 To be useful in financial reporting, information must be a faithful representation of the economic and other phenomena that it purports to represent. Faithful representation is attained when the depiction of the phenomenon is complete, neutral, and free from material error. Information that faithfully represents an economic or other phenomenon depicts the substance of the underlying transaction, other event, activity or circumstance—which is not necessarily always the same as its legal form.

3.16 In practice, it may not be possible to know or confirm whether information presented in GPFRs is complete, neutral, and free from material error. However, information should be as complete, neutral, and free from material error as is possible.

3.17 An omission of some information can cause the representation of an economic or other phenomenon to be false or misleading, and thus not useful to users of GPFRs. For example, a complete depiction of the item "plant and equipment" in GPFRs will include a numeric representation of the aggregate amount of plant and equipment together with other quantitative, descriptive and explanatory information necessary to faithfully represent that class of assets. In some cases, this may include the disclosure of information about such matters as the major classes of plant and equipment, factors that have affected their use in the past or might impact on their use in the future, and the basis and process for determining their numeric representation. Similarly, prospective financial and non- financial information and information about the achievement of service delivery objectives and outcomes included in GPFRs will need to be presented with the key assumptions that underlie that information and any explanations that are necessary to ensure that its depiction is complete and useful to users.

3.18 Neutrality in financial reporting is the absence of bias. It means that the selection and presentation of financial and non-financial information is not made with the intention of attaining a particular predetermined result—for example, to influence in a particular way users' assessment of the discharge of accountability by the entity or a decision or judgement that is to be made, or to induce particular behaviour.

3.19 Neutral information faithfully represents the economic and other phenomena that it purports to represent. However, to require information included in GPFRs to be neutral does not mean that it is not without purpose or that it will not influence behaviour. Relevance is a qualitative characteristic and, by definition, relevant information is capable of influencing users' assessments and decisions.

3.20 The economic and other phenomena represented in GPFRs generally occur under conditions of uncertainty. Information included in GPFRs will therefore often include estimates that incorporate management's judgement. To faithfully represent an economic or other phenomenon, an estimate must be based on appropriate inputs, and each input must reflect the best available information. Caution will need to be exercised when dealing with uncertainty. It may sometimes be necessary to explicitly disclose the degree of uncertainty in financial and non-financial information to faithfully represent economic and other phenomena.

3.21 Free from material error does not mean complete accuracy in all respects. Free from material error means there are no errors or omissions that are individually or collectively material in the description of the phenomenon, and the process used to produce the reported information has been applied as described. In some cases, it may be possible to determine the accuracy of some information included in GPFRs—for example, the amount of a cash transfer to another level of government, the volume of services delivered or the price paid for the acquisition of plant and equipment. However, in other cases it may not—for example, the accuracy of an estimate of the value or cost of an item or the effectiveness of a service delivery programme may not be able to be determined. In these cases, the estimate will be free from material error if the amount is clearly described as an estimate, the nature and limitations of the estimation process are explained, and no material errors have been identified in selecting and applying an appropriate process for developing the estimate.

Understandability

3.22 Understandability is the quality of information that enables users to comprehend its meaning. GPFRs of public sector entities should present information in a manner that responds to the needs and knowledge base of users, and to the nature of the information presented. For example, explanations of financial and non-financial information and commentary on service delivery and other achievements during the reporting period and expectations for future periods should be written in plain language, and presented in a manner that is readily understandable by users. Understandability is enhanced when information is classified, characterised, and presented clearly and concisely. Comparability also can enhance understandability.

3.23 Users of GPFRs are assumed to have a reasonable knowledge of the entity's activities and the environment in which it operates, to be able and prepared to read GPFRs, and to review and analyse the information presented with reasonable diligence. Some economic and other phenomena are particularly complex and difficult to represent in GPFRs, and some users may need to seek the aid of an advisor to assist in their understanding of them. All efforts should be undertaken to represent economic and other phenomena included in GPFRs in a manner that is understandable to a wide range of users. However, information should not be excluded from GPFRs solely because it may be too complex or difficult for some users to understand without assistance.

Timeliness

3.24 Timeliness means having information available for users before it loses its capacity to be useful for accountability and decision-making purposes. Having relevant information available sooner can enhance its usefulness as input to assessments of accountability and its capacity to inform and influence decisions that need to be made. A lack of timeliness can render information less useful.

3.25 Some items of information may continue to be useful long after the reporting period or reporting date. For example, for accountability and decision-making purposes, users of GPFRs may need to assess trends in the financial and service delivery performance of the entity and its compliance with budgets over a number of reporting periods. In addition, the outcome and effects of some service delivery programmes may not be determinable until future periods—for example, this may occur in respect of programmes intended to enhance the economic well-being of constituents, reduce the incidence of a particular disease, or increase literacy levels of certain age groups.

Comparability

3.26 Comparability is the quality of information that enables users to identify similarities in, and differences between, two sets of phenomena. Comparability is not a quality of an individual item of information, but rather a quality of the relationship between two or more items of information.

3.27 Comparability differs from consistency. Consistency refers to the use of the same accounting principles or policies and basis of preparation, either from period to period within an entity or in a single period across more than one entity. Comparability is the goal, and consistency helps in achieving that goal. In some cases, the accounting principles or policies adopted by an entity may be revised to better represent a particular transaction or event in GPFRs. In these cases, the inclusion of additional disclosures or explanation may be necessary to satisfy the characteristics of comparability.

3.28 Comparability also differs from uniformity. For information to be comparable, like things must look alike and different things must look different. An over-emphasis on uniformity may reduce comparability by making unlike things look alike. Comparability of information in GPFRs is not enhanced by making unlike things look alike, any more than it is by making like things look different.

3.29 Information about the entity's financial position, financial performance, cash flows, compliance with approved budgets and relevant legislation or other authority governing the raising and use of resources, service delivery achievements, and its future plans is necessary for accountability purposes and useful as input for decision-making purposes. The usefulness of such information is enhanced if it can be compared with, for example:

- prospective financial and non-financial information previously presented for that reporting period or reporting date;
- similar information about the same entity for some other period or some other point in time; and
- similar information about other entities (for example, public sector entities providing similar services in different sectors) for the same reporting period.

3.30 Consistent application of accounting principles, policies and basis of preparation to prospective financial and non-financial information and actual outcomes will enhance the usefulness of any comparison of projected and actual results. Comparability with other entities may be less significant for explanations of management's perception or opinion of the factors underlying the entity's current performance.

Verifiability

3.31 Verifiability is the quality of information that helps assure users that information in GPFRs faithfully represents the economic and other phenomena that it purports to represent. Supportability is sometimes used to describe this quality when applied in respect of explanatory information and prospective financial and non-financial quantitative information disclosed in GPFRs—that is, the quality of information that helps assure users that explanatory or prospective financial and non- financial quantitative information faithfully represents the economic and other phenomena that it purports to represent. Whether referred to as verifiability or supportability, the characteristic implies that different knowledgeable and independent observers could reach general consensus, although not necessarily complete agreement, that either:

- the information represents the economic and other phenomena that it purports to represent without material error or bias; or
- an appropriate recognition, measurement, or representation method has been applied without material error or bias.

3.32 To be verifiable, information need not be a single point estimate. A range of possible amounts and the related probabilities also can be verified.

3.33 Verification may be direct or indirect. With direct verification, an amount or other representation is itself verified, such as by (a) counting cash, (b) observing marketable securities and their quoted prices, or (c) confirming that the factors identified as influencing past service delivery performance were present and operated with the effect identified. With indirect verification, the amount or other representation is verified by checking the inputs and recalculating the outputs using the same accounting convention or methodology. An example is verifying the carrying amount of inventory by checking the inputs (quantities and costs) and recalculating the ending inventory using the same cost flow assumption (for example, average cost or first-in-first-out).

3.34 The quality of verifiability (or supportability if such term is used to describe this characteristic) is not an absolute—some information may be more or less capable of verification than other information. However, the more verifiable is the information included in GPFRs, the more it will assure users that the information faithfully represents the economic and other phenomena that it purports to represent.

3.35 GPFRs of public sector entities may include financial and other quantitative information and explanations about (a) key influences on the entity's performance during the period, (b) the anticipated future effects or outcomes of service delivery programmes undertaken during the reporting period, and (c) prospective financial and non-financial information. It may not be possible to verify the accuracy of all quantitative representations and explanations of such information until a future period, if at all.

3.36 To help assure users that prospective financial and non-financial quantitative information and explanations included in GPFRs faithfully represents the economic and other phenomena that they purport to represent, the assumptions that underlie the information disclosed, the methodologies adopted in compiling that information, and the factors and circumstances that support any opinions expressed or disclosures made should be transparent. This will enable users to form judgements about the appropriateness of those assumptions and the method of compilation, measurement, representation and interpretation of the information.

Constraints on information included in General Purpose Financial Reports

Cost-benefit

3.37 Financial reporting imposes costs. The benefits of financial reporting should justify those costs. Assessing whether the benefits of providing information justify the related costs is often a matter of judgement, because it is often not possible to identify and/or quantify all the costs and all the benefits of information included in GPFRs.

3.38 The costs of providing information include the costs of collecting and processing the information, the costs of verifying it and/or presenting the assumptions and methodologies that support it, and the costs of disseminating it. Users incur the costs of analysis and interpretation. Omission of useful information also imposes costs, including the costs that users incur to obtain needed information from other sources and the costs that result from making decisions using incomplete data provided by GPFRs.

3.39 Preparers expend the majority of the effort to provide information in GPFRs. However, service recipients and resource providers ultimately bear the cost of those efforts—because resources are redirected from service delivery activities to preparation of information for inclusion in GPFRs.

3.40 Users reap the majority of benefits from the information provided by GPFRs. However, information prepared for GPFRs may also be used internally by management and result in better decision making by management. The disclosure of information in GPFRs consistent with the concepts identified in the Conceptual Framework and Standards of GRAP derived from them will enhance and reinforce perceptions of the transparency of financial reporting by government and public sector entities and contribute to the more accurate pricing of public sector debt. Therefore, public sector entities may also benefit in a number of ways from the information provided by GPFRs.

3.41 Application of the cost-benefit constraint involves assessing whether the benefits of reporting information are likely to justify the costs incurred to provide and use the information. When making this assessment, it is necessary to consider whether one or more qualitative characteristics might be sacrificed to some degree to reduce cost.

3.42 In developing Standards of GRAP, the Board considers information from preparers, users, academics, and others about the expected nature and quantity of the benefits and costs of the proposed requirements. Disclosure and other requirements which result in the presentation of information useful to users of GPFRs for accountability and decision-making purposes and satisfy the qualitative characteristics are prescribed by Standards of GRAP when the benefits of compliance with those disclosures and other requirements are assessed by the Board to justify their costs.

Balance between the qualitative characteristics

3.43 The qualitative characteristics work together to contribute to the usefulness of information. For example, neither a depiction that faithfully represents an irrelevant phenomenon, nor a depiction that unfaithfully represents a relevant phenomenon, results in useful information. Similarly, to be relevant, information must be timely and understandable. The relative importance of the characteristics in different cases is a matter of professional judgement.

3.44 In some cases, a balancing or trade-off between qualitative characteristics may be necessary to achieve the objectives of financial reporting. The relative importance of the qualitative characteristics in each situation is a matter of professional judgement. The aim is to achieve an appropriate balance among the characteristics in order to meet the objectives of financial reporting.

CHAPTER 4: REPORTING ENTITY

Introduction

4.1 The reporting entity concept is used to identify when an entity should prepare GPFRs.

4.2 A public sector reporting entity is a government or public sector organisation, programme or identifiable area of activity (hereafter referred to as an entity or public sector entity) that chooses, or is required, to prepare GPFRs.

4.3 A public sector reporting entity is not necessarily a legal entity. It may comprise a portion of an entity or two or more separate entities that present GPFRs as if they are a single entity—such a reporting entity is referred to as a group reporting entity.

4.4 GPFRs are sometimes prepared for two or more portions of entities or separate entities that usually have no control relationship with each other. These GPFRs are presented as if they are a single entity. Such a reporting entity is referred to as a group reporting entity.

4.5 In applying the reporting entity concept, a distinction should be made between the preparation of GPFRs by a reporting entity and the preparation of GPFSs by entities in order to meet the requirements of specific Standards of GRAP. In particular, when one entity (the controlling entity) has control over another entity (the controlled entity), the term "economic entity" is used to define, for financial statement purposes, the group of entities comprising the controlling entity and any controlled entities. A group reporting entity is not limited to an economic entity (or any other type of entity that may be defined in Standards of GRAP), because an economic entity only exists if one entity has control over another entity. In contrast, the boundary of a group reporting entity is determined using the characteristics outlined in paragraphs 4.6 to 4.14 below.

Key characteristics of a reporting entity

4.6 Key characteristics of a public sector reporting entity are that:

- it is an entity that raises resources from, or on behalf of, constituents and/or uses resources to undertake activities for the benefit of, or on behalf of, those constituents; and
- there are service recipients or resource providers dependent on GPFRs of the entity for information for accountability or decision-making purposes.

4.7 A government may establish and/or operate through administrative units such as ministries or departments. It may also operate through trusts, statutory authorities, government corporations and other entities with a separate legal identity or operational autonomy to undertake or otherwise support the provision of services to constituents. Public sector organisations, including municipalities, may also undertake certain activities through, and may benefit from and be exposed to a financial burden or loss as a result of, the activities of entities with a separate legal identity or operational autonomy.

4.8 GPFRs are prepared to report information useful to users for accountability and decision-making purposes. Service recipients and resource providers are the primary users of GPFRs. Consequently, a key characteristic of a reporting entity, including a group reporting entity, is the existence of service recipients or resource providers who are dependent on GPFRs of that entity or group of entities for information for accountability or decision-making purposes.

4.9 GPFRs encompass financial statements and information that enhances, complements and supplements the financial statements. Financial statements present information about the resources of the reporting entity or group reporting entity and claims to those resources at the reporting date, and changes to those resources and claims and cash flows during the reporting period. Therefore, to enable the preparation of financial statements, a reporting entity will raise resources and/or use resources previously raised to undertake activities for the benefit of, or on behalf of, its constituents.

4.10 The factors that are likely to signal the existence of users of GPFRs of a public sector entity or group of entities include an entity having the responsibility or capacity to raise or deploy resources, acquire or manage public assets, incur liabilities, or undertake activities to achieve service delivery objectives. The greater the resources that a public sector entity raises, manages and/or has the capacity to deploy, the greater the liabilities it incurs and the greater the economic or social impact of its activities, the more likely it is that there will exist service recipients or resource providers who are dependent on GPFRs for information about it for accountability and decision-making purposes. In the absence of these factors, or where they are not significant, it is unlikely that users of GPFRs of these entities will exist.

4.11 The preparation of GPFRs is not a cost-free process. Therefore, if the imposition of financial reporting requirements is to be efficient and effective, it is important that only those public sector entities for which such users exist are required to prepare GPFRs.

4.12 In many cases, it will be clear whether or not there exists service recipients or resource providers that are dependent on GPFRs of a public sector entity for information for accountability and decision-making purposes. For example, such users are likely to exist for GPFRs of a government at the national, provincial or local government level. This is because these spheres of government and organisations generally have the capacity to raise substantial resources from and/or deploy substantial resources on behalf of their constituents, to incur liabilities, and to impact the economic and/or social well-being of the communities that depend on them for the provision of services.

4.13 However, it may not always be clear whether there are service recipients or resource providers that are dependent on GPFRs of, for example, individual programmes or identifiable areas of activity for information for accountability and decision-making purposes. Determining whether these organisations, programmes or activities should be identified as reporting entities and, consequently, be required to prepare GPFRs will involve the exercise of professional judgement.

4.14 The government and public sector entities have a separate identity or standing in law (a legal identity). However, public sector organisations, programmes and activities without a separate legal identity may also raise or deploy resources, acquire or manage public assets, incur liabilities, undertake activities to achieve service delivery objectives or otherwise implement government policy. Service recipients and resource providers may depend on GPFRs of these organisations, programmes and activities for information for accountability and decision-making purposes. Consequently, a public sector reporting entity may have a separate legal identity or be, for example, an organisation, administrative arrangement or programme without a separate legal identity.

Identification of a reporting entity

4.15 A reporting entity, or group reporting entity is an entity or group of entities that:

(a) where a legislative or similar requirement exists:

i. is required to prepare GPFRs; and/or

ii. elects to present GPFRs for a portion, programme or identifiable area of activity of that entity or group of entities and meets the characteristics outlined in paragraph 4.6 and the objectives of financial reporting; or

(b) in the absence of legislative or similar requirements to prepare GPFRs, determines that it is a reporting entity because it meets the characteristics outlined in paragraph 4.6 and the objectives of financial reporting.

4.16 Where an entity elects to prepare GPFRs in accordance with paragraph 4.15(a), the financial statements prepared in accordance with legislation or similar means, or that an entity elects to prepare, are prepared in accordance with the applicable Standards of GRAP. When an entity elects to prepare financial statements for the portion, programme or identifiable area of activity of an entity, this does not imply that the entity can exclude the revenue, expenses, assets and liabilities of the portion, programme or identifiable area of activity of that entity from the financial statements prepared in accordance with legislation or similar means. Consequently, the entity applies the applicable Standards of GRAP to ensure that all the relevant revenue, expenses, assets and liabilities of the portion, programme or identifiable area of activity of that entity are included in the financial statements prepared in accordance with legislation or similar means.

CHAPTER 5: ELEMENTS IN FINANCIAL STATEMENTS

Introduction

Purpose of this chapter

5.1 This Chapter defines the elements used in financial statements and provides further explanation about those definitions.

Elements and their importance

5.2 Financial statements portray the financial effects of transactions and other events by grouping them into broad classes which share common economic characteristics. These broad classes are termed the elements of financial statements. Elements are the building blocks from which financial statements are constructed. These building blocks provide an initial point for recording, classifying and aggregating economic data and activity in a way that provides users with information that meets the objectives of financial reporting and achieves the qualitative characteristics of financial reporting while taking into account the constraints on information included in GPFRs.

5.3 The elements defined in this Chapter do not refer to the individual items that are recognised as a result of transactions and events. Sub-classifications of individual items within an element and aggregations of items are used to enhance the understandability of the financial statements. Presentation is addressed in Chapter 8, *Presentation in General Purpose Financial Reports.*

Elements defined

5.4 The elements that are defined in this Chapter are:

- assets;
- liabilities;
- revenue;
- expense;
- ownership contributions; and
- ownership distributions.

Assets

Definition

5.5 An asset is:

A resource presently controlled by the entity as a result of a past event.

A resource

5.6 A resource is an item with service potential or the ability to generate economic benefits. Physical form is not a necessary condition of a resource. The service potential or ability to generate economic benefits can arise directly from the resource itself, from the rights to use the resource or the entity's ability to direct how it may be used by denying or restricting access to that resource. Some resources embody an entity's rights to a variety of benefits including, for example, the right to:

- use the resource to provide services;
- use an external party's resources to provide services, for example, leases;
- convert the resource into cash through its disposal;
- benefit from the resource's appreciation in value; or
- receive a stream of cash flows.

5.7 Service potential is the capacity to provide services that contribute to achieving the entity's objectives. Service potential enables an entity to achieve its objectives without necessarily generating net cash inflows.

5.8 Public sector assets that embody service potential may include recreational, heritage, community, defense and other assets which are held by governments and public sector entities, and which are used to provide services to third parties. Such services may be for collective or individual consumption. Many services may be provided in areas where there is no market competition or limited market competition. The use and disposal of such assets may be restricted as many assets that embody service potential are specialised in nature.

5.9 Economic benefits are cash inflows or a reduction in cash outflows. Cash inflows (or reduced cash outflows) may be derived from, for example:

- an asset's use in the production and sale of services; or
- the direct exchange of an asset for cash or other resources.

Presently controlled by the entity

5.10 An entity must have control of the resource. Control of the resource entails the ability of the entity to use the resource (or direct other parties on its use) so as to derive the benefit of the service potential or economic benefits embodied in the resource in the achievement of its service delivery or other objectives.

5.11 In assessing whether it presently controls a resource, an entity assesses whether the following indicators of control exist:

- legal ownership;
- access to the resource, or the ability to deny or restrict access to the resource;
- the means to ensure that the resource is used to achieve its objectives; and
- the existence of an enforceable right to service potential or the ability to generate economic benefits arising from a resource.

While these indicators are not conclusive determinants of whether control exists, identification and analysis of them can inform that decision.

Past event

5.12 The definition of an asset requires that a resource that an entity presently controls must have arisen from a past transaction or other past event. The past transactions or other events that result in an entity gaining control of a resource and therefore an asset may differ. Entities can obtain assets by purchasing them in an exchange transaction or developing them. Assets may also arise through non-exchange transactions, including through the exercising of sovereign powers. The power to tax or to issue licenses and to access or restrict or deny access to the benefits embodied in intangible resources, like the electromagnetic spectrum, are examples of public sector-specific powers and rights that may give rise to assets. In assessing when an entity's control of rights to resources arise the following events may be considered:

- a general ability to establish a power,
- establishment of a power through a statute,
- exercising the power to create a right, and
- the event which gives rise to the right to receive resources from an external party. An asset arises when the power is exercised and the rights exist to receive resources.

Liabilities

Definition

5.13 A liability is:

A present obligation of the entity for an outflow of resources[3] that results from a past event.

A present obligation

5.14 Public sector entities can have a number of obligations. A present obligation is a legally binding obligation (legal obligation) or non-legally binding obligation, which an entity has little or no realistic alternative to avoid. Obligations are not present obligations unless they are binding and there is little or no realistic alternative to avoid an outflow of resources.

An outflow of resources from the entity

5.15 A liability must involve an outflow of resources from the entity for it to be settled. An obligation that can be settled without an outflow of resources from the entity is not a liability.

Past event

5.16 To satisfy the definition of a liability, it is necessary that a present obligation arises as a result of a past transaction or other event and requires an outflow of resources from the entity. The complexity of public sector programmes and activities means that a number of events in the development, implementation and operation of a particular programme may give rise to obligations. For financial reporting purposes it is necessary to determine whether such commitments and obligations, including binding obligations that the entity has little or no realistic alternative to avoid but are not legally enforceable (non-legally binding obligations) are present obligations and satisfy the definition of a liability. Where an arrangement has a legal form and is binding, such as a contract, the past event may be straightforward to identify. In other cases, it may be more difficult to identify the past event and identification involves an assessment of when an entity has little or no realistic alternative to avoid an outflow of resources from the entity. In making such an assessment an entity considers all the relevant factors.

Legal and non-legally binding obligations

5.17 Binding obligations can be legal obligations or non-legally binding obligations. Binding obligations can arise from both exchange and non-exchange transactions. An obligation must be to an external party in order to give rise to a liability. An entity cannot be obligated to itself, even where it has publicly communicated an intention to behave in a particular way. Identification of an external party is an indication of the existence of an obligation giving rise to a liability. However, it is not essential to know the identity of the external party before the

[3] A resource is an item with service potential or the ability to generate economic benefits (see paragraph 5.6).

time of settlement in order for a present obligation and a liability to exist.

5.18 Many arrangements that give rise to an obligation include settlement dates. The inclusion of a settlement date may provide an indication that an obligation involves an outflow of resources and gives rise to a liability. However, there are many agreements that do not contain settlement dates. The absence of a settlement date does not preclude an obligation giving rise to a liability.

Legal obligations

5.19 A legal obligation is enforceable in law. Such enforceable obligations may arise from a variety of legal constructs. Exchange transactions are usually contractual in nature and therefore enforceable through the laws of contract or equivalent authority or arrangements. For some types of non-exchange transactions, judgement will be necessary to determine whether an obligation is enforceable in law. Where it is determined that an obligation is enforceable in law there can be no doubt that an entity has no realistic alternative to avoid the obligation and that a liability exists.

5.20 Some obligations related to exchange transactions are not strictly enforceable by an external party at the reporting date, but will be enforceable with the passage of time without the external party having to meet further conditions— or having to take any further action— prior to settlement. Claims that are unconditionally enforceable subject to the passage of time are enforceable obligations in the context of the definition of a liability.

5.21 Sovereign power is the ultimate authority of government to make, amend and repeal legal provisions. Sovereign power is not a rationale for concluding that an obligation does not meet the definition of a liability in this Conceptual Framework. The legal position should be assessed at each reporting date to consider if an obligation is no longer binding and does not meet the definition of a liability.

Non-legally binding obligations

5.22 Liabilities can arise from non-legally binding obligations. Non-legally binding obligations differ from legal obligations in that the party to whom the obligation exists cannot take legal (or equivalent) action to enforce settlement. Non-legally binding obligations that give rise to liabilities have the following attributes:

- 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;
- 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
- the entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities.

5.23 In the public sector, obligations may arise at a number of points. For example, in implementing a programme or service:

- making a political promise such as an electoral pledge;
- announcement of a policy;
- introduction (and approval) of the budget (which may be two distinct points); and
- the budget becoming effective.

The early stages of implementation are unlikely to give rise to present obligations that meet the definition of a liability. Later stages, such as claimants meeting the eligibility criteria for the service to be provided, may give rise to obligations that meet the definition of a liability.

5.24 The point at which an obligation gives rise to a liability depends on the nature of the obligation. Factors that are likely to impact on judgements whether other parties can validly conclude that the obligation is such that the entity has little or no realistic alternative to avoid an outflow of resources include:

- the nature of the past event or events that give rise to the obligation. For example, a promise made in an election is unlikely to give rise to a present obligation because an electoral pledge very rarely creates a valid expectation on the part of external parties that the entity has an obligation that it has little or no realistic alternative to avoid settling. However, an announcement in relation to an event or circumstance that has occurred may have such political support that the government has little option to withdraw. Where the government has committed to introduce and secure passage of the necessary budgetary provision such an announcement may give rise to a non-legally binding obligation; and
- the ability of the entity to modify or change the obligation before it crystallises. For example, the announcement of policy will generally not give rise to a non-legally binding obligation, if it can be modified before being implemented. Similarly, if an obligation is contingent on future events occurring, there may be discretion to avoid an outflow of resources before those events occur.

5.25 “Economic coercion”, “political necessity” or other circumstances may give rise to situations where, although the public sector entity is not legally obliged to incur an outflow of resources, the economic or political consequences of refusing to do so are such that the entity may have little or no realistic alternative to avoid an outflow of resources. Economic coercion, political necessity or other circumstances may lead to a liability arising from a non-legally binding obligation.

Net financial position

5.26 Net financial position is the difference between assets and liabilities recognised in the statement of financial position. Net financial position can be a positive or negative residual amount.

Revenue and expense

Definitions

5.27 Revenue is:

Increases in the net financial position of the entity, other than increases arising from ownership contributions.

5.28 Expense is:

Decreases in the net financial position of the entity, other than decreases arising from ownership distributions.

5.29 Revenue and expense arise from exchange and non-exchange transactions, other events such as unrealised increases and decreases in the value of assets and liabilities, and the consumption of assets through depreciation and erosion of service potential and ability to generate economic benefits through impairments. Revenue and expense may arise from individual transactions or groups of transactions.

Surplus or deficit for the period

5.30 The entity's surplus or deficit for the period is the difference between revenue and expense reported on the statement of financial performance.

Ownership contributions and ownership distributions

Definitions

5.31 Ownership contributions are:

Inflows of resources to an entity, contributed by external parties in their capacity as owners, which establish, maintain or increase an interest in the net financial position of the entity.

5.32 Ownership distributions are:

Outflows of resources from the entity, distributed to external parties in their capacity as owners, which return or reduce an interest in the net financial position of the entity.

5.33 It is important to distinguish inflows of resources from owners, including those inflows that initially establish the ownership interest on creation of the entity as well as those made subsequently and outflows of resources to owners in their capacity as owners from revenue and expense. An entity is required to first identify who the owners of the entity are before it can distinguish the nature of the inflows and outflows relating to the owners. In addition to the injections of resources and the payment of dividends or similar distributions that may occur it is relatively common for assets and liabilities to be transferred between public sector entities. Where such transfers satisfy the definitions of ownership contributions or ownership distributions they will be accounted for as such.

5.34 Ownership interests may arise on the creation of an entity when another entity contributes resources to provide the new entity with the capacity to commence operational activities. In the public sector, contributions to, and distributions from, entities are sometimes linked to the restructuring of government and will take the form of transfers of assets and liabilities rather than cash transactions. Ownership interests may take different forms, which may not be evidenced by an equity instrument.

5.35 Ownership contributions may take the form of an initial injection of resources at the creation of an entity or a subsequent injection of resources, including those where an entity is restructured. Ownership distributions may be:

- a return on investment;
- a full or partial return of investment; or
- in the event of the entity being wound up or restructured, a return of any residual resources.

CHAPTER 6: RECOGNITION IN FINANCIAL STATEMENTS

Recognition criteria and their relationship to disclosure

6.1 This chapter identifies the criteria that must be satisfied in order for an element to be recognised in the financial statements. Recognition is the process of incorporating and including in amounts displayed on the face of the appropriate financial statement an item that meets the definition of an element and can be measured in a way that achieves the qualitative characteristics and takes account of the constraints on information included in GPFRs.

6.2 The recognition criteria are that:

- an item satisfies the definition of an element; and
- can be measured in a way that achieves the qualitative characteristics and takes account of constraints on information in GPFRs.

6.3 All items that satisfy the recognition criteria are recognised in the financial statements.

6.4 Recognition involves an assessment of uncertainty related to the existence and measurement of the element. The conditions that give rise to uncertainty, if any, can change. Therefore, it is important that uncertainty is assessed at each reporting date.

Definition of an element

6.5 In order to be recognised as an element an item must meet the definition of one of the elements in Chapter 5. Uncertainty about the existence of an element is addressed by considering the available evidence in order to make a neutral judgement about whether an item satisfies all essential characteristics of the definition of that element, taking into account all available facts and circumstances at the reporting date.

6.6 If it is determined that an element exists, uncertainty about the amount of service potential or ability to generate economic benefits represented by that element is taken into account in the measurement of that element (see paragraphs 6.7 and 6.8). Preparers review and assess all available evidence in determining whether an element exists and is recognised, whether that element continues to qualify for recognition (see paragraph 6.9), or whether there has been a change to an existing element.

Measurement uncertainty

6.7 In order to recognise an item in the financial statements, it is necessary to attach a monetary value to the item. This entails choosing an appropriate measurement basis and determining whether the measurement of the item achieves the qualitative characteristics, taking into account the constraints on information in GPFRs, including that the measurement is sufficiently relevant and faithfully representative for the item to be recognised in the financial statements. The selection of an appropriate measurement basis is considered in Chapter 7, *Measurement of Assets and Liabilities in Financial Statements.*

6.8 There may be uncertainty associated with the measurement of many amounts presented in the financial statements. The use of estimates is an essential part of the accrual basis of accounting. A decision about the relevance and faithful representativeness of measurement involves the consideration of techniques, such as using ranges of outcomes and point estimates, and whether additional evidence is available about economic circumstances that existed at the reporting date. Disclosures can provide useful information on estimation techniques employed. There may be rare instances in which the level of uncertainty in a single point estimate is so large that the relevance and faithful representativeness of the measure is questionable even if disclosures are provided to explain estimation techniques. Under these circumstances the item is not recognised.

Disclosure and recognition

6.9 The failure to recognise items that meet the definition of an element and the recognition criteria is not rectified by the disclosure of accounting policies, notes or other explanatory detail. However, disclosure can provide information about items that meet many, but not all the characteristics of the definition of an element. Disclosure can also provide information on items that meet the definition of an element but cannot be measured in a manner that achieves the qualitative characteristics sufficiently to meet the objectives of financial reporting. Disclosure is appropriate when knowledge of the item is considered to be relevant to the evaluation of the net financial position of the entity and therefore meets the objectives of financial reporting.

Unit of account

6.10 The unit of account is the group of rights, the group of obligations or the group of rights and obligations, to which recognition and measurement requirements are applied.

6.11 A unit of account is selected for an asset or a liability after considering how recognition and measurement will apply, not only to that asset or liability, but also to the related revenue and expenses. The selected unit of account may need to be aggregated or disaggregated for display or disclosure purposes.

6.12 In some circumstances, it may be appropriate to select one unit of account for recognition and a different unit of account for measurement (for example, contracts may sometimes be recognised individually but measured as part of a portfolio of contracts).

Derecognition

6.13 Derecognition is the process of evaluating whether changes have occurred since the previous reporting date that warrant removing an element that has been previously recognised from the financial statements, and removing the item if such changes have occurred. In evaluating uncertainty about the existence of an element the same criteria are used for derecognition as at initial recognition.

CHAPTER 7: MEASUREMENT OF ASSETS AND LIABILITIES IN FINANCIAL STATEMENTS

Introduction

7.1 This Chapter identifies the measurement concepts in the selection of measurement bases for assets and liabilities where there are no requirements in Standards of GRAP.

The objective of measurement

7.2 The objective of measurement is:

To select those measurement bases that most fairly reflect the cost of services, operational capacity and financial capacity of the entity in a manner that is useful in holding the entity to account, and for decision-making purposes.

7.3 The selection of a measurement basis for assets and liabilities contributes to meeting the objectives of financial reporting in the public sector by providing information that enables users to assess:

- the cost of services provided in the period in historical or current terms;
- operational capacity—the capacity of the entity to support the provision of services in future periods through physical and other resources; and
- financial capacity—the capacity of the entity to fund its activities.

7.4 The selection of a measurement basis also includes an evaluation of the extent to which the information provided achieves the qualitative characteristics while taking into account the constraints on information in financial reports.

Measurement bases and their selection

7.5 It is not possible to identify a single measurement basis that best meets the measurement objective at a Conceptual Framework level. Therefore, the Conceptual Framework does not propose a single measurement basis (or combination of bases) for all transactions, events and conditions. It provides guidance on the selection of a measurement basis for assets and liabilities in order to meet the measurement objective.

7.6 The following measurement bases for assets are identified and discussed in terms of the information they provide about the cost of services delivered by an entity, the operating capacity of an entity and the financial capacity of an entity, and the extent to which they provide information that meets the qualitative characteristics:

Historical cost measurement

- historical cost;

Current value measurements

- market value;
- replacement cost;
- net selling price; and
- value in use.

Table 1 summarises these measurement bases in terms of whether they (a) provide entry or exit values; (b) are observable in a market; and (c) whether or not they are entity-specific.[4]

Table 1: Summary of measurement bases for assets

Measurement Basis	Entry or Exit	Observable or Unobservable in a Market	Entity or Non-entity Specific
Historical cost	Entry	Generally observable	Entity-specific
Market value in open, active and orderly market	Entry and exit	Observable	Non-entity-specific
Market value in inactive market	Exit	Dependent on valuation technique	Dependent on valuation technique
Replacement cost	Entry	Observable	Entity-specific
Net selling price	Exit	Observable	Entity-specific
Value in use	Exit[5]	Unobservable	Entity-specific

[4] In some cases a judgement has been made in classifying a particular measurement basis as observable or unobservable in a market and/or as entity or non-entity specific.
[5] As pointed out in paragraph 7.67, for non-cash-generating assets the calculation of value in use may require the use of replacement cost as surrogate.

7.7 The following measurement bases for liabilities are identified and discussed in terms of (a) the information they provide about the cost of services delivered by an entity, the operating capacity of an entity and the financial capacity of an entity; and (b) the extent to which they provide information that meets the qualitative characteristics:

Historical cost measurement

- historical cost;

Current value measurements

- cost of fulfilment;
- market value;
- cost of release; and
- assumption price.

Table 2 summarises these measurement bases in terms of whether they (a) provide entry or exit values; (b) are observable in a market; and (c) whether or not they are entity-specific.

Table 2: Summary of measurement bases for liabilities

Measurement Basis	**Entry or Exit**	**Observable or Unobservable in a Market**	**Entity or Non-entity Specific**
Historical cost	Entry	Generally observable	Entity-specific
Cost of fulfilment	Exit	Unobservable	Entity-specific
Market value in open, active and orderly market	Entry and exit	Observable	Non-entity specific
Market value in inactive market	Exit	Dependent on valuation technique	Dependent on valuation technique
Cost of release	Exit	Observable	Entity-specific
Assumption price	Entry	Observable	Entity-specific

Entry and exit values

7.8 Measurement bases may provide either entry or exit values. For assets, entry values reflect the cost of purchase. Historical cost and replacement cost are entry values. Exit values reflect the economic benefits from sale. An exit value also reflects the amount that will be derived from use of the asset. In a diversified economy entry and exit prices differ as entities typically:

- acquire assets tailored to the entity's particular operating requirements for which other market participants would be unwilling to pay a similar price; and
- incur transaction costs on acquisition.

7.9 Measurement bases for liabilities may also be classified in terms of whether they are entry or exit values. Entry values relate to the transaction under which an obligation is received or the amount that an entity would accept to assume a liability. Exit values reflect the amount required to fulfil an obligation or the amount required to release the entity from an obligation.

Observable and unobservable measures

7.10 Certain measures may be classified according to whether they are observable in an open, active and orderly market.[6] Measures that are observable in a market are likely to be more understandable and verifiable than measures that are not observable. They may also be more faithfully representative of the phenomena they are measuring.

Entity-specific and non-entity specific measures

7.11 Measures may also be classified according to whether they are "entity-specific" or "non-entity-specific". Measurement bases that are entity-specific reflect the economic and current policy constraints that affect the possible uses of an asset and the settlement of a liability by an entity. Entity-specific measures may reflect economic opportunities that are not available to other entities and risks that are not experienced by other entities. Non-entity-specific measures reflect general market opportunities and risks. The decision on whether to use an entity-specific or non-entity-specific measure is taken by reference to the measurement objective and the qualitative characteristics.

[6] The term "open, active and orderly markets" was developed by Dr. J. Alex Milburn. For example, see *Toward a Measurement Framework for Profit-oriented Entities*, published by the Canadian Institute of Chartered Accountants in 2012.

Measurement bases for assets

Historical cost

7.12 Historical cost for an asset is:

The consideration given to acquire or develop an asset, which is the cash or cash equivalents or the value of the other consideration given, at the time of its acquisition or development.

7.13 Historical cost is an entry, entity-specific value.[7] Under the historical cost model assets are initially reported at the cost incurred on their acquisition. Subsequent to initial recognition, this cost may be allocated as an expense to reporting periods in the form of depreciation or amortisation for certain assets, as the service potential or ability to generate economic benefits provided by such assets are consumed over their useful lives. Following initial recognition, the measurement of an asset is not changed to reflect changes in prices or increases in the value of the asset.

7.14 Where the time value of an asset is material—for example, where the length of time before the asset is realised is significant— the amount of the future receipt is discounted so that, at the time an asset is first recognised, it represents the value of the amount received. The difference between the amount of the future receipt and the present value of the asset is amortised over the life of the asset, so that the asset is stated at the amount of the required receipt when it is realised.

7.15 Under the historical cost model the amount of an asset may be reduced by recognising impairments. Impairment is the extent to which the service potential or ability to generate economic benefits provided by an asset have diminished due to changes in economic or other conditions, as distinct to their consumption. This involves assessments of recoverability. Conversely, the amount of an asset may be increased to reflect the cost of additions and enhancements (excluding price increases for unimproved assets) or other events, such as the accrual of interest on a financial asset.

Costs of services

7.16 Where historical cost is used, the cost of services reflects the amount of the resources expended to acquire or develop assets consumed in the provision of services. Historical cost generally provides a direct link to the transactions actually undertaken by the entity. Because the costs used are those carried forward from an earlier period without adjustment for price changes, they do not reflect the cost of assets when the assets are consumed. As the cost of services is reported using past prices, historical cost information will not facilitate the assessment of the future cost of providing services if cumulative price changes since

[7] The term “historical cost” may also be referred to as the “cost model” or generically as “cost-based measures.”

acquisition are significant. Where budgets are prepared on the historical cost basis, historical cost information demonstrates the extent to which the budget has been executed.

Operational capacity

7.17 If an asset has been acquired in an exchange transaction, historical cost provides information on the resources available to provide services in future periods, based on their acquisition cost. At the time an asset is purchased or developed, it can be assumed that the value to the entity of its service potential is at least as great as the cost of purchase.[8] When depreciation or amortisation is recognised it reflects the extent to which the service potential of an asset has been consumed. Historical cost information shows that the resources available for future services are at least as great as the amount at which they are stated. Increases in the value of an asset are not reflected under the historical cost model. If an asset has been acquired in a non-exchange transaction the transaction price will not provide information on operating capacity.

Financial capacity

7.18 The amount at which assets are stated in financial statements assists in an assessment of financial capacity. Historical cost can provide information on the amount of assets that may be used as effective security for borrowings. An assessment of financial capacity also requires information on the amount that could be received on sale of an asset, and reinvested in assets to provide different services. Historical cost does not provide this information when significantly different from current exit values.

Application of the qualitative characteristics

7.19 Paragraphs 7.16 to 7.18 explain the areas where historical cost provides relevant information in terms of its confirmatory or predictive value. Application of historical cost is often straightforward, because transaction information is usually readily available. As a result amounts derived from the historical cost model are generally representationally faithful in that they represent what they purport to represent—that is, the cost to acquire or develop an asset based on actual transactions. Estimates of depreciation and impairment used in the historical cost model, particularly for non-cash-generating assets, can affect representational faithfulness. Because application of historical cost generally reflects resources consumed by reference to actual transactions, historical cost measures are verifiable, understandable and can be prepared on a timely basis.

7.20 Historical cost information is comparable to the extent that assets have the same or similar acquisition dates. Because historical cost does not reflect the impact of price changes, it is not possible to compare the amounts of assets that were acquired at different times when prices differed in a meaningful way.

[8] Where this is not the case the initial historical cost measurement will be reduced by the amount of the impairment.

7.21 In certain circumstances the application of historical cost necessitates the use of allocations—for example where:

- several assets are acquired in a single transaction;
- assets are constructed by the entity itself and overheads and other costs have to be attributed; and
- the use of a flow assumption, such as first-in-first-out, is necessary when many similar assets are held. To the extent such allocations are arbitrary they reduce the extent to which the resulting measurement achieves the qualitative characteristics.

Current value measurements

7.22 Current value measurements reflect the economic environment prevailing at the reporting date.

7.23 There are four current value measurement bases for assets:

- market value;
- replacement cost;
- net selling price; and
- value in use.

Market value

7.24 Market value for assets is:

The amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

7.25 At acquisition market value and historical cost will be the same, if transaction costs are ignored and the transaction is an exchange transaction. The extent to which market value meets the objectives of financial reporting and the information needs of users partially depends on the quality of the market evidence. Market evidence, in turn, depends upon the characteristics of the market in which the asset is traded. Market value is particularly appropriate where it is judged that the difference between entry and exit values is unlikely to be significant or the asset is being held with a view to sale.

7.26 In principle, market values provide useful information because they fairly reflect the value of the asset to the entity. In an open, active and orderly market (see paragraph 7.28), the asset cannot be worth less than market value as the entity can obtain that amount by selling the asset, and cannot be worth more than market value, as the entity can obtain equivalent service potential or the ability to generate economic benefits by purchasing the same asset.

7.27 The usefulness of market values is more questionable when the assumption that markets are open, active and orderly does not hold. In such circumstances it cannot be assumed that the asset may be sold for the same price as that at which it can be acquired and it is necessary to determine whether an exit price or an entry price is the more useful measure. Exit-based market values are useful for assets that are held for trading, such as certain financial instruments, but may not be useful for specialised operational assets. Furthermore, while the purchase of an asset provides evidence that the value of the asset to the entity is at least as great as its purchase price, operational factors may mean that the value to the entity may be greater. Hence market values may not reflect the value to the entity of the asset, represented by its operational capacity.

Market values in open, active and orderly markets

7.28 Open, active and orderly markets have the following characteristics:

- there are no barriers that prevent the entity from transacting in the market;
- they are active so there is sufficient frequency and volume of transactions to provide price information; and
- they are orderly, with many well-informed buyers and sellers acting without compulsion, so there is assurance of "fairness" in determining current prices—including that prices do not represent distress sales.

An orderly market is one that is run in a reliable, secure, accurate and efficient manner. Such markets deal in assets that are identical and therefore mutually interchangeable, such as commodities, currencies and securities where prices are publicly available. In practice few, if any, markets fully exhibit all of these characteristics, but some may approach an orderly market as described.

Market values where it cannot be assumed that markets are open, active and orderly

7.29 Markets for assets that are unique and rarely traded are not open, active and orderly: any purchases and sales are individually negotiated, and there may be a large range of prices at which a transaction might be agreed. Therefore, participants will incur significant costs to purchase or to sell an asset. In such circumstances it is necessary to use an estimation technique to estimate the price at which an orderly transaction to sell the asset would take place between market participants at the measurement date under current market conditions.

Costs of services

7.30 Revenue from services reported in financial statements is measured on the basis of prices current in the reporting period. If assets used to provide services are measured at market value, the allocation of the cost of assets to reflect their consumption in the current reporting period is based on the current market value of the asset.

7.31 The use of market values permits a return on assets to be determined. However, public sector entities do not generally carry out activities with the primary objective of generating profits, and services are often provided in non-exchange transactions or on subsidised terms. Consequently there may be limited relevance in a reported return derived from exit-based market prices.

7.32 As noted above, revenue from providing services reported in financial statements is measured on the basis of prices current in the reporting period. Thus the surplus or deficit for a period includes price movements that take place over the period during which assets and liabilities are held, and no profit or loss is reported on the sale of an asset. Where the asset is traded on an open, active and orderly market, the existence of the market provides assurance that the entity would be able to realise the market value (and no more) at the reporting date: it is therefore unnecessary to postpone recognition of changes in value until a surplus is realised on sale. However, where assets used to provide services are not traded on open, active and orderly markets, or a close approximation to such markets, the relevance of revenue and expense related to changes in market value is more questionable.

Operational capacity

7.33 Information on the market value of assets held to provide services in future periods is useful if it reflects the value that the entity is capable of deriving from assets by using them in providing or delivering services. However, if an exit-based market value is significantly lower than historical cost, market value is likely to be less relevant than the historical cost of such assets in providing information on operational capacity—such a market value is also likely to be less relevant than entry value-based current measures.

Financial capacity

7.34 An assessment of financial capacity requires information on the amount that would be received on sale of an asset. This information is provided by market value.

Application of the qualitative characteristics

7.35 Values determined in open, active and orderly markets can be readily used for financial reporting purposes. The information will meet the qualitative characteristics—that is it will be relevant, representationally faithful, understandable, comparable, and verifiable. Under such market conditions entry and exit values can be assumed to be the same or very similar. Because it can be prepared quickly, such information is also likely to be timely.

7.36 The extent to which market values meet the qualitative characteristics will decrease as the quality of market evidence diminishes and the determination of such values relies on estimation techniques. As indicated above, exit-based market values are only likely to be relevant to assessments of financial capacity and not to assessments of the cost of services and operational capacity.

Replacement cost

7.37 Replacement cost[9] is:

The most economic cost required for the entity to replace the service potential of an asset (including the amount that the entity will receive from its disposal at the end of its useful life) at the reporting date.

7.38 Replacement cost differs from market value because:

- in a public sector context it is explicitly an entry value that reflects the cost of replacing the service potential of an asset;
- it includes all the costs that would necessarily be incurred in the replacement of the service potential of an asset; and
- it is entity specific and therefore reflects the economic position of the entity, rather than the position prevailing in a hypothetical market. For example, the replacement cost of a vehicle is less for an entity that usually acquires a large number of vehicles in a single transaction and is regularly able to negotiate discounts than for an entity that purchases vehicles individually.

7.39 Because entities usually acquire their assets by the most economic means available, replacement cost reflects the procurement or construction process that an entity generally follows. Replacement cost reflects the replacement of service potential in the normal course of operations, and not the costs that might be incurred if an urgent necessity arose as a result of some unforeseeable event, such as a fire.

7.40 Replacement cost is the cost to the entity of replacing an asset's service potential rather than determining the cost of acquiring an identical asset. Replacement cost adopts an optimised approach and differs from reproduction cost, which is the cost of acquiring an identical asset.[10] Although in many cases the most economic replacement of the service potential will be by purchasing an asset that is similar to that which is controlled, replacement cost is based on an alternative asset if that alternative would provide the same service potential more cheaply. For financial reporting purposes, it is therefore necessary to reflect the difference in service potential between the existing and replacement asset.

7.41 The appropriate service potential is that which the entity is capable of using or expects to use, having regard to the need to hold sufficient service capacity to deal with contingencies.

[9] The full term is "optimised depreciated replacement cost" to denote that it refers to the replacement of the service potential embodied in an asset and not the asset itself (see paragraph 7.40). The term "replacement cost" is used for economy of expression in the Conceptual Framework.

[10] There may be cases where replacement cost equates to reproduction cost. This is where the most economical way of replacing service potential is to reproduce the asset.

Therefore, the replacement cost of an asset reflects reductions in required service capacity. For example, if an entity owns a school that accommodates 500 pupils but, because of demographic changes since its construction, a school for 100 pupils would be adequate for current and reasonably foreseeable requirements, the replacement cost of the asset is that of a school for 100 pupils.

7.42 In some cases the value that will be derived from an asset will be greater than its replacement cost. However, it would not be appropriate to measure the asset at that value, as it includes benefits from future activities, rather than service potential at the reporting date. Replacement cost represents the highest potential value of an asset, as, by definition, the entity is able to secure equivalent service potential by incurring replacement cost.

Costs of services

7.43 Replacement cost provides a relevant measure of the cost of the provision of services. The cost of consuming an asset is equivalent to the amount of the sacrifice of service potential incurred by that use. That amount is its replacement cost—the entity is able to restore its position to that prevailing immediately before the consumption of the asset by an outlay equal to replacement cost.

7.44 The costs of services are reported in current terms when based on replacement cost. Thus the amount of assets consumed is stated at the value of the assets at the time they are consumed—and not, as with historical cost, at the time they were acquired. This provides a valid basis for a comparison between the cost of services and the amount of taxes and other revenue received in the period—which are generally transactions of the current period and measured in current prices— and for assessing whether resources have been used economically and efficiently. It also provides a useful basis for comparison with other entities that report on the same basis, as asset values will not be affected by different acquisition dates, and for assessing the cost of providing services in the future and future resource needs, as future costs are more likely to resemble current costs than those incurred in the past, when prices were different (see also paragraph 7.48).

Operational capacity

7.45 In principle, replacement cost provides a useful measure of the resources available to provide services in future periods, as it is focused on the current value of assets and their service potential to the entity.

Financial capacity

7.46 Replacement cost does not provide information on the amounts that would be received on the sale of assets. It therefore does not facilitate an assessment of financial capacity.

Application of the qualitative characteristics

7.47 As noted above, replacement cost is relevant to assessments of the cost of services and operational capacity. It is not relevant to assessments of financial capacity. In some circumstances calculation of replacement cost is complex, and subjective judgements are required. These factors may reduce the representational faithfulness of replacement cost. In these circumstances the timeliness, comparability and verifiability of information prepared on a replacement cost basis may be affected, and replacement cost may be more costly than some alternatives. Replacement cost information may also not be straightforward to understand, particularly when that information reflects a reduction in required service capacity (see paragraph 7.41).

7.48 Replacement cost information is comparable within an entity as assets that provide equivalent service potential are stated at similar amounts, regardless of when those assets were acquired. In principle different entities may report similar assets at different amounts, because replacement cost is an entity-specific measure that reflects the opportunities for replacement that are available to the entity. The opportunities for replacement may be the same or similar for different public sector entities. Where they are different, the economic advantage of an entity that is able to acquire assets more cheaply is reported in financial statements through lower asset values and a lower cost of services in order to be representationally faithful.

Net selling price

7.49 Net selling price is:

The amount that the entity can obtain from sale of the asset, after deducting the costs of sale.

7.50 Net selling price differs from market value in that it does not require an open, active and orderly market or the estimation of a price in such a market and that it includes the entity's costs of sale. Net selling price therefore reflects constraints on sale. It is entity-specific.

7.51 The potential usefulness of measuring assets at net selling price is that an asset cannot be worth less to the entity than the amount it could obtain on sale of the asset. However, it is not appropriate as a measurement basis if the entity is able to use its resources more efficiently by employing the asset in another way, for example by using it in the delivery of services.

7.52 Net selling price is therefore useful where the most resource-efficient course available to the entity is to sell the asset. This is the case where the asset cannot provide service potential or the ability to generate economic benefits at least as valuable as net selling price. Net selling price may provide useful information where an entity is contractually obligated to sell an asset at below market value. There may be cases where net selling price can indicate a development opportunity.

Costs of services

7.53 It is not appropriate to quantify the cost of the provision of services at net selling prices. Such an approach would involve the use of an exit value as the basis of the expense reported.

Operational capacity

7.54 Stating assets held for use in the provision of services at net selling price does not provide information useful to an assessment of operating capacity. Net selling price shows the amount that could be derived from an asset's sale, rather than the value of the service potential that could be derived from that asset.

Financial capacity

7.55 As noted above, an assessment of financial capacity requires information on the amount that would be received on sale of an asset. Such information is provided by the use of net selling price. However, such a measure is not relevant for assets that may yield more valuable service potential by continuing to use them to deliver services.

Application of the qualitative characteristics

7.56 As indicated in paragraph 7.52 net selling price provides relevant information only where the most resource-efficient course available to the entity is to sell the asset. Assessments of net selling price may be made by reference to active markets where they exist. For major assets it may be possible and cost-effective to obtain professional appraisals. Net selling price will generally provide understandable information.

7.57 In most cases where net selling price is relevant, it will achieve the qualitative characteristics of faithful representation, verifiability, and timeliness.

Value in use

7.58 Value in use is:

The present value to the entity of the asset's remaining service potential or ability to generate economic benefits if it continues to be used, and of the net amount that the entity will receive from its disposal at the end of its useful life.

Suitability of value in use

7.59 Value in use is an entity-specific value that reflects the amount that can be derived from an asset through its operation and its disposal at the end of its useful life. As noted in paragraph 7.42 above, the value that will be derived from an asset is often greater than its replacement cost—it is also usually greater than its historical cost. Where this is the case, reporting an asset at its value in use is of limited usefulness, as by definition, the entity is able to secure equivalent service potential at replacement cost.

7.60 Value in use is also not an appropriate measurement basis when net selling price is greater than value in use, as in this case the most resource-efficient use of the asset is to sell it, rather than continue to use it.

7.61 Therefore, value in use is appropriate where it is less than replacement cost and greater than net selling price. This occurs where an asset is not worth replacing, but the value of its service potential or ability to generate economic benefits is greater than its net selling price. In such circumstances value in use represents the value of the asset to the entity.

7.62 Value in use is an appropriate measurement basis for the assessment of certain impairments, because it is used in the determination of the recoverable amount for an asset or group of assets.

Costs of services, operational capacity, financial capacity

7.63 Because of its potential complexity[11], its limited applicability and the fact that its operationalisation in a public sector context for non-cash-generating assets involves the use of replacement cost as a surrogate, value in use is generally inappropriate for determining the cost of services. Its usefulness to assessments of operational capacity is limited, and is only likely to be significant in the atypical circumstances where entities have a large number of assets that are not worth replacing, but their value in use is greater than their net selling price. This may be the case if, for example, an entity will discontinue provision of a service in the future, but the proceeds of immediate sale are less than the service potential embodied in the assets. Value in use does involve an estimate of the net amount that an entity will receive from disposal of the asset. However, its limited applicability reduces its relevance for assessments of financial capacity.

Application of the qualitative characteristics

7.64 While value in use may be used in assessments of certain impairments its relevance for financial reporting purposes is limited to the circumstances outlined in paragraph 7.61.

7.65 The extent to which value in use meets the other qualitative characteristics depends on how it is determined. In some cases, an asset's value in use can be quantified by calculating the value that the entity will derive from the asset assuming its continued use. This may be based on the future cash inflows related to the asset, or on cost savings that will accrue to the entity through its control of the asset. The calculation of value in use takes into account the time value of money and, in principle, the risk of variations in the amount and timing of cash flows.

7.66 The calculation of value in use can be complex. Assets that are employed in cash-generating activities often provide cash flows jointly with other assets. In such cases value

[11] See paragraph 7.66.

in use can be estimated only by calculating the present value of the cash flows of a group of assets and then making an allocation to individual assets.

7.67 In the public sector, most assets are held with the primary objective of contributing to the provision of services, rather than to the generation of a commercial return: such assets are referred to as "non-cash-generating assets". Because value in use is usually derived from expected cash flows, its operationalisation in such a context can be difficult. It may be inappropriate to calculate value in use on the basis of expected cash flows, because such a measure would not be faithfully representative of the value in use of such an asset to the entity. Therefore, it would be necessary to use replacement cost as a surrogate for financial reporting purposes.

7.68 The method of determining value in use reduces its representational faithfulness in many cases. It also affects the timeliness, comparability, understandability and verifiability of information prepared on a value in use basis.

Measurement bases for liabilities

7.69 This section discusses the measurement bases for liabilities. This section does not repeat all the discussion in the section on assets. It considers the following measurement bases:

- historical cost;
- cost of fulfilment;
- market value;
- cost of release; and
- assumption price.

Historical cost

7.70 Historical cost for a liability is:

The consideration received to assume an obligation, which is the cash or cash equivalents, or the value of the other consideration received at the time the liability is incurred.

7.71 Under the historical cost model initial measures may be adjusted to reflect factors such as the accrual of interest, the accretion of discount or amortisation of a premium.

7.72 Where the time value of a liability is material—for example, where the length of time before settlement falls due is significant— the amount of the future payment is discounted so that, at the time a liability is first recognised, it represents the value of the amount received. The difference between the amount of the future payment and the present value of the liability is amortised over the life of the liability, so that the liability is stated at the amount of the required payment when it falls due.

7.73 The advantages and drawbacks of using the historical cost basis for liabilities are similar to those that apply in relation to assets. Historical cost is appropriate where liabilities are likely to be settled at stated terms. However, historical cost cannot be applied for liabilities that do not arise from a transaction, such as a liability to pay damages for a delictor civil damages. It is also unlikely to provide relevant information where the liability has been incurred in a non-exchange transaction, because it does not provide a faithful representation of the claims against the resources of the entity. It is also difficult to apply historical cost to liabilities that may vary in amount, such as those related to defined benefit pension liabilities.

Cost of fulfilment

7.74 Cost of fulfilment is:

The costs that the entity will incur in fulfiling the obligations represented by the liability, assuming that it does so in the least costly manner.

7.75 Where the cost of fulfilment depends on uncertain future events, all possible outcomes are taken into account in the estimated cost of fulfilment, which aims to reflect all those possible outcomes in an unbiased manner.

7.76 Where fulfilment requires work to be done—for example, where the liability is to rectify environmental damage—the relevant costs are those that the entity will incur. This may be the cost to the entity of doing the remedial work itself, or of contracting with an external party to carry out the work. However, the costs of contracting with an external party are only relevant where employing a contractor is the least costly means of fulfiling the obligation.

7.77 Where fulfilment will be made by the entity itself, the fulfilment cost does not include any surplus, because any such surplus does not represent a use of the entity's resources. Where fulfilment amount is based on the cost of employing a contractor, the amount will implicitly include the profit required by the contractor, as the total amount charged by the contractor will be a claim on the entity's resources—this is consistent with the approach for assets, where replacement cost would include the profit required by a supplier, but no profit would be included in the replacement cost for assets that the entity would replace through self-construction.

7.78 Where fulfilment will not take place for an extended period, the cash flows need to be discounted to reflect the value of the liability at the reporting date.

7.79 Cost of fulfilment is generally relevant for measuring liabilities except in the following circumstances:

- where the entity can obtain release from an obligation at a lower amount than cost of fulfilment, then cost of release is a more relevant measure of the current burden of a liability, just as, for an asset, net selling price is more relevant when it is higher than value in use; and
- in the case of liabilities assumed for a consideration, assumption price (see paragraphs 7.88 to 7.93) is more relevant when assumption price is higher than both cost of fulfilment and cost of release.

Market value

7.80 Market value for liabilities is:

The amount for which a liability could be settled between knowledgeable, willing parties in an arm's length transaction.

7.81 The advantages and disadvantages of market value for liabilities are the same as those for assets. Such a measurement basis may be appropriate, for example, where the liability is attributable to changes in a specified rate, price or index quoted in an open, active and orderly market. However, in cases where the ability to transfer a liability is restricted and the terms on which such a transfer might be made are unclear the case for market values, even if they exist, is significantly weaker. This is particularly the case for liabilities arising from obligations in non-exchange transactions, because it is unlikely that there will be an open, active and orderly market for such liabilities.

Cost of release

7.82 Cost of release is:

The amount of an immediate exit from the obligation.

7.83 Cost of release is the term used in the context of liabilities to refer to the same concept as "net selling price" in the context of assets. Cost of release is the amount that either the creditor will accept in settlement of its claim, or a third party would charge to accept the transfer of the liability from the obligor. Where there is more than one way of securing release from the liability, the cost of release is that of the lowest amount—this is consistent with the approach for assets, where net selling price would not reflect the amount that would be received on sale to a scrap dealer, if a higher price could be obtained from sale to a purchaser who would use the asset.

7.84 For some liabilities, particularly in the public sector, transfer of a liability is not practically possible and cost of release will therefore be the amount that the creditor will accept in settlement of its claim. This amount will be known if it is specified in the agreement with the creditor—for example, where a contract includes a specific cancellation clause.

7.85 In some cases there may be evidence of the price at which a liability may be transferred—for example, in the case of some pension liabilities. Transferring a liability may be distinguished from entering into an agreement with another party that will fulfil the entity's obligation or bear all the costs stemming from a liability. For a liability to be transferred it is necessary that all of the creditor's rights against the entity are extinguished. If this is not the effect of an arrangement, the liability remains a liability of the entity.

7.86 In assessing whether cost of release is appropriate for measuring liabilities it is necessary to consider whether release in the envisaged manner is an option that is open to the entity in practice, having regard to any consequences of obtaining release, such as damage to the entity's reputation.

7.87 Just as net selling price is relevant only when the most resource-efficient course available to the entity is to sell the asset, so cost of release is relevant only when the most resource-efficient course is to seek immediate release from an obligation. In particular, where cost of fulfilment is lower than cost of release, cost of fulfilment provides more relevant information than cost of release, even if it is feasible to negotiate a release from the obligation in accordance with the methods for transferring a liability in paragraph 7.84.

Assumption price

7.88 Assumption price is:

The amount which the entity would rationally be willing to accept in exchange for assuming an existing liability.

7.89 "Assumption price" is the term used in the context of liabilities to refer to the same concept as replacement cost for assets. Exchange transactions carried out on arms-length terms will provide evidence of assumption price—this is not the case for non- exchange transactions.

7.90 In the context of an activity that is carried out with a view to profit, an entity will assume a liability only if the amount it is paid to assume the liability is greater than the cost of fulfilment or release— i.e. the settlement amount. Once that assumption price has been received by the entity, the entity has an obligation to its creditor.

7.91 At the time a liability is first incurred in an exchange transaction, assumption price represents the amount that was accepted by the entity for assuming the liability—it is therefore usually reasonable to assume that assumption price is the price that the entity would rationally accept for assuming a similar liability. It would charge a higher amount, if competitive pressures allowed it to do so, but it might be unwilling to accept a lower price. Just as replacement cost is a current value so, conceptually, is assumption price. There are, however, practical problems in reflecting changes in prices in obligations that are stated at assumption price.

7.92 A consequence of stating performance obligations at the assumption price is that no surplus is reported at the time the obligation is taken on. A surplus or deficit is reported in the financial statements in the period when fulfilment (or release) takes place, as it is the difference between the revenue arising from satisfaction of the liability and the cost of settlement.

7.93 An entity may have a potential obligation that is larger than assumption price. If the entity has to seek release from a contract, the other party to the contract may be able to claim recompense for losses that it will sustain, as well as the return of any amounts paid. However, provided that the entity can settle the obligation by fulfilment, it can avoid such additional obligations and it is representationally faithful to report the obligation at no more than assumption price—this is analogous to the position where an asset will yield greater benefits than replacement cost. Under such circumstances, as explained in paragraph 7.42, replacement cost rather than value in use is the most relevant measurement basis.

CHAPTER 8: PRESENTATION IN GENERAL PURPOSE FINANCIAL REPORTS

Introduction

8.1 This Chapter sets out the concepts applicable to the presentation of information in GPFRs, including financial statements.

8.2 Presentation is linked to Chapters 1 to 4—the objectives of financial reporting, users' needs, the qualitative characteristics, constraints on information included in GPFRs and the reporting entity all influence presentation decisions. For information reported in the financial statements, presentation is also linked to the definitions of the elements, recognition criteria and measurement bases identified in Chapters 5 to 7—for example:

- the definition of the elements affect the items that can be presented in the financial statements;
- application of the recognition criteria affects the location of information; and
- the selection of measurement bases impacts the information presented on measurement methodologies.

Language in which financial statement and other GPFRs are issued

8.3 The language (or languages) in which financial statements and other GPFRs are issued supports achievement of the objectives of financial reporting and the qualitative characteristics. All translated versions need to be faithful to the original language version. The translated version is made available to meet the needs of users with reference to:

- legal requirements; and
- translation costs and benefits.

Presentation

8.4 Presentation is the selection, location and organisation of information that is reported in the GPFRs.

8.5 Presentation aims to provide information that contributes towards the objectives of financial reporting and achieves the qualitative characteristics while taking into account the constraints on information included in GPFRs. Decisions on selection, location and organisation of information are made in response to the needs of users for information about economic or other phenomena.

8.6 Chapter 1 explains that GPFRs are likely to comprise multiple reports, each responding more directly to certain aspects of the objectives of financial reporting and matters included within the scope of financial reporting. In addition to the financial statements, GPFRs provide information relevant to, for example, assessments of an entity's service performance and the sustainability of its finances. The objectives of financial reporting, applied to the area covered by a particular report, guide presentation decisions for that report.

8.7 Presentation decisions may:

- result in the development of a new GPFR, the movement of information between reports, or the amalgamation of existing reports; or
- be detailed decisions on information selection, location and organisation within a GPFR.

Presentation decisions are interlinked

8.8 Decisions on information selection, location and organisation are interlinked and, in practice, are likely to be considered together. The amount or type of information selected could have implications on whether it is included in a separate report or organised into tables or separate schedules. The following three sections separately focus on each presentation decision.

Information selection

8.9 Decisions on information selection address what information is reported:

- in the financial statements; and
- in GPFRs outside the financial statements (other GPFRs).

8.10 As Chapter 2 explains, the objectives of financial reporting are to provide information about the entity that is useful to users of GPFRs for accountability and decision-making purposes. Chapter 2 describes the types of information that users need to meet the objectives of financial reporting. That description guides decisions on whether particular types of reports are needed. This Chapter focuses on the selection of information to be presented in GPFRs, including financial statements and other reports.

Presentation and disclosure objectives and principles

8.11 When the Board develops standard-level requirements it will consider including specific presentation and disclosure objectives that enable entities to identify relevant information and decide how to communicate that information in the most efficient and effective manner.

8.12 In setting presentation and disclosure requirements, an appropriate balance is needed between:

(a) giving entities the flexibility to provide relevant information that faithfully represents the entity's assets and liabilities, and the transactions and other events of the period; and

(b) requiring information that is comparable among entities and across reporting periods.

8.13 Efficient and effective communication of information also requires consideration of the following principles:

(a) entity-specific information is more useful than 'boilerplate' language and is more useful than information that is readily available outside the financial statements; and

(b) duplication of information in different parts of the financial statements is usually unnecessary and makes financial statements less understandable.

Information selection—nature of information

Nature of information in financial statements

8.14 Users' information needs identified in Chapter 2 underpin information selection for the financial statements. Those needs include information about the financial position, financial performance and cash flows of an entity in order to:

- enable users to identify the resources of the entity and claims on those resources at the reporting date;
- inform assessments of matters such as whether the entity has acquired resources economically, and used them efficiently and effectively to achieve its service delivery objectives; and
- inform assessments of financial performance and the entity's liquidity and solvency.

8.15 The financial statements may also provide information that assists users in assessing the extent to which:

- an entity has met its financial objectives;
- revenues, expenses, cash flows and financial results of the entity comply with approved budgets; and
- an entity has adhered to relevant legislation, supporting regulations or similar means governing the raising and use of public monies.

8.16 The financial statements do not report comprehensively on an entity's service performance. However information in the financial statements may provide information relevant to the financial aspects of service performance such as information about:

- revenue, expenses and cash flows related to services; and
- the assets and liabilities that inform users' evaluations of, for example, an entity's operational capacity or financial risks that could impact on service provision.

8.17 Other reports in GPFRs present information additional to the financial statements. Such information could, for example, include:

- information on the sustainability of an entity's public finances, where relevant;
- financial statement discussion and analysis; or
- service performance information.

Information selected for display or disclosure

8.18 Information is selected for display or disclosure in GPFRs. Information selected for display communicates key messages in a GPFR, while information selected for disclosure makes displayed information more useful by providing detail that will help users to understand the displayed information. Disclosure is not a substitute for display.

8.19 Repetition of information in a GPFR needs to generally be avoided. However, the same information may be both displayed and disclosed. For example, a total displayed on the face of the financial statements may be repeated in the notes, where the notes provide a disaggregation of the displayed total. Similarly the same information may be presented in different GPFRs in order to address their different aims.

Information selected for display

8.20 Every GPFR contains key messages that are communicated, so every GPFR contains displayed information. Displayed information is kept to a concise, understandable level, so that users can focus on the key messages presented and not be distracted by detail that could otherwise obscure those messages. Displayed information is presented prominently, using appropriate presentation techniques such as clear labeling, borders, tables and graphs.

8.21 The items displayed on the face of the financial statements provide information about such matters as the reporting entity's financial position, financial performance and cash flows.

8.22 Assessment of whether an item satisfies the recognition criteria is one of the key mechanisms in determining whether information is displayed on the face of the statement of financial position or statement of financial performance and/or disclosed either in the notes or elsewhere in the GPFRs. In other cases, for example a statement of cash flows, displayed information will also support achievement of the objectives of financial reporting.

8.23 Developing requirements for the display of line items and totals involves balancing the standardisation of displayed information, which facilitates understandability, with information that is tailored for entity-specific factors. The aim of both standardised display requirements and entity- specific information is to ensure that information necessary to meet the objectives of financial reporting is available for all entities, while allowing information to be displayed in a manner that reflects the nature and operations of specific entities.

Information selected for disclosure

8.24 Disclosed information is likely to include:

- the basis for the displayed information, such as applicable policies or methodologies;
- disaggregation of displayed information; and
- items that share some but not all of the aspects of displayed information—for example disclosures on items that meet some, but not all, of the characteristics of the definition of an element or disclosures on items that meet the definition of an element, but not the recognition criterion.

8.25 The level of detail provided by disclosed information contributes to achievement of the objectives of financial reporting, without being excessive. Disclosed information, like displayed information, is necessary for achievement of the objectives of financial reporting.

8.26 Information disclosed in the notes to the financial statements:

- is necessary to a user's understanding of the financial statements;
- provides information that presents the financial statements in the context of the entity and its operating environment; and
- generally will have a clear and demonstrable relationship to information displayed on the face of the financial statement(s) to which it pertains.

8.27 Information disclosed in the notes may also include:

- entity-related factors that could influence judgements about reported information (for example, information about related parties and controlled entities or interests in other entities);
- the basis for what is displayed (for example, information on accounting policies and measurement, including measurement methods and measurement uncertainties where applicable);

- disaggregation of amounts displayed on the face of the statements (for example, a break-down of property, plant and equipment into different classes);
- items that do not meet the definition of an element or the recognition criteria, but are important to an understanding of the entity's finances and ability to deliver services—for example, information about events and conditions, that might affect future cash flows or service potential, including their natures, possible effects on cash flows or service potential, probabilities of occurrence, and sensitivities to changes in conditions; and
- information that may explain underlying trends affecting displayed totals.

Principles applicable to information selection

8.28 Decisions about what information needs to be displayed and disclosed involve consideration of:

- the objectives of financial reporting;
- the qualitative characteristics and constraints on information included in GPFRs; and
- the relevant economic or other phenomena about which information may be necessary.

8.29 Information selection results in information that contributes to meeting the objectives of financial reporting, as applied to the area covered by a particular report, and provides the appropriate level of detail. Decisions on information selection involve information prioritisation and summarisation. Information selection avoids information overload that reduces understandability. Too much information may make it difficult for users to understand the key messages, and, consequently undermines achievement of the objectives of financial reporting.

8.30 Preparers, applying pronouncements and their professional judgement, are responsible for ensuring that information that meets the objectives of financial reporting and achieves the qualitative characteristics is provided in the GPFRs that they prepare.

8.31 Decisions on information selection require continuing and critical review. Information identified for possible selection is reviewed as it is developed and considered for presentation, with particular reference to its relevance, materiality and cost-benefit, although all the qualitative characteristics and constraints are applied to decisions on information selection. Past decisions may require reconsideration because new information may make existing information requirements redundant with the result that those items no longer achieve the qualitative characteristics and/or the constraints.

8.32 All material transactions, events, and other items reported are presented in a manner that conveys their substance rather than their legal or other form so that the qualitative characteristics of relevance and representational faithfulness are achieved.

8.33 The benefits to users of receiving information need to justify the costs to entities of collecting and presenting that information. In making this assessment it is important to consider how individual items impact on the overall view presented and the nature of the information presented. Items that may appear to have little benefit when viewed in isolation could have much greater benefit in contributing to the complete set of information presented.

8.34 Information needs to be presented on a sufficiently timely basis to enable users to hold management accountable and to inform users' decisions.

8.35 GPFRs may include additional information derived from sources other than the financial information system. The qualitative characteristics apply to such information. The date of delivery of any such additional information needs to be as close as possible to the financial statements' reporting date, so that reported information will be timely.

Principles for selection of information for display and disclosure

8.36 Decisions about display or disclosure apply to both the financial statements and other GPFRs. The objectives of financial reporting are applied to the area covered by a particular report to guide the identification of information for display or disclosure. The identification of information for display and disclosure in a particular GPFR may involve the development of:

- classification principles;
- a list of broad types of information that are displayed and a similar list of broad types of information that are disclosed; and/or
- lists of specific information that preparers must display or disclose.

8.37 Decisions about selection of information to be displayed and disclosed are made:

- with reference to each other rather than in isolation; and
- to effectively communicate an integrated set of information.

8.38 Selection decisions with respect to information in other GPFRs are made after carefully considering the relationship of the other GPFRs to the financial statements.

Information location

8.39 Decisions on information location are made about which:

- report information is located within; and
- component of a report information is located.

8.40 The location of information has an impact on information's contribution to achievement of the objectives of financial reporting and the qualitative characteristics. Location may affect the way that users interpret information and the comparability of information. Location may be used to:

- convey the relative importance of information and its connections with other items of information;
- convey the nature of information;
- link different items of information that combine to meet a particular user need; and
- distinguish between information selected for display and information selected for disclosure.

Principles for allocation of information between different reports

8.41 Factors relevant to decisions about allocating information between the financial statements and another GPFR include:

- *nature*: whether the nature of the information, for example historical versus prospective, supports including the information either in the same or a different GPFR, because of considerations related to, for example, comparability and/or understandability;
- *legislative requirement:* whether legislative requirements, such as legal provisions, specify requirements on information location; and
- *linkage:* whether or not the additional information envisaged needs to link very closely to information already included in an existing report. The linkages between all information need to be assessed, not only linkages between new and existing information.

8.42 The factors above, which are expressed from the perspective of adding information to an existing set of information, also apply to considerations of whether the grouping of existing information could be improved, which is discussed in the section on information organisation.

8.43 A separate GPFR may be necessary when:

- additional user information needs, not satisfied by an existing report, are identified; and
- a separate GPFR to meet those needs is more likely to achieve the objectives of financial reporting and the qualitative characteristics than including information in an existing report.

Principles for location of information within a report

8.44 Paragraph 8.17 states that displayed information is presented prominently, using appropriate presentation techniques—location is one way to achieve this. Information location within a report ensures that displayed information is given appropriate prominence and is not obscured by more detailed and extensive disclosed information.

8.45 The location of information in the financial statements contributes to communicating a comprehensive financial picture of an entity.

8.46 For the financial statements, displayed information is shown on the face of the appropriate statement, while disclosures are in the notes. Distinguishing displayed information and disclosed information through location ensures that those items that directly relate to communicating matters, such as an entity's financial position, financial performance and cash flows, can be highlighted, with further more detailed information provided through disclosure in the notes.

8.47 For other GPFRs, displayed information may either be located separately from disclosed information or located in the same area, but distinguished from disclosed information and given prominence through the use of another presentation technique.

Information organisation

8.48 Information organisation addresses the arrangement, grouping and ordering of information, which includes decisions on:

- how information is arranged within a GPFR; and
- the overall structure of a GPFR.

8.49 Information organisation involves a range of decisions including decisions on the use of cross-referencing, tables, graphs, headings, numbering, and the arrangement of items within a particular component of a report, including decisions on item order. How information is organised can affect its interpretation by users.

Nature of information relevant to organisation

8.50 Decisions about the organisation of information take into account:

- important relationships between information; and
- whether information is for display or disclosure.

Types of relationships

8.51 Important relationships include, but are not restricted to:

- enhancement;
- similarity; and
- shared purpose.

8.52 *Enhancement*: Information in one place in a GPFR may be enhanced through information provided elsewhere. For example, budget, prospective and service performance information enhances information in the financial statements. Tables and graphs may be used to enhance the understanding of narrative information. Links to information reported outside the GPFRs may enhance the understandability of information reported in GPFRs.

8.53 *Similarity*: A relationship of similarity exists where information reported in one place is based on information reported elsewhere in the GPFRs, and the information either has not been adjusted or has had relatively minor adjustments. For example, if service performance information includes the cost of services, or the value of assets used in different services, then it may be helpful to show how those totals relate to expense and assets reported in the financial statements. Another example is the relationship between the total expense reported against budget and total expense reported in the statement of financial performance. A reconciliation between the two different amounts can enhance users' understanding of an entity's finances.

8.54 *Shared purpose*: A relationship of shared purpose exists where information reported in different places contributes to the same purpose. An example is where different statements and disclosures provide information needed for assessments of accountability for services delivered. Information about (a) the actual and budgeted cost of different services, (b) financial and non-financial resources used in the provision of different services, and (c) future provision of different services may be included in different places. To make the relationship between the information in different places clear, it may be appropriate to organise the information by using techniques such as common headings and referencing.

8.55 Relationships may exist between information in different:

- GPFRs;
- components within a GPFR; and
- parts of a single component.

Grouping of information

8.56 The three factors noted in the section on information selection as being applicable to decisions on information location—linkage, nature of information and legislative requirements—also apply to considerations of whether the grouping of existing information could be improved. Decisions on effective grouping of information consider linkages between information sets, the nature of the different information sets, and, to the extent appropriate, legislative requirements.

Principles applicable to information organisation

8.57 Information organisation:

- supports achievement of the objectives of financial reporting; and
- helps reported information meet the qualitative characteristics.

8.58 Information organisation:

- helps to ensure that key messages are understandable;
- clearly identifies important relationships;
- gives appropriate prominence to information that conveys key messages; and
- facilitates comparisons.

8.59 Related information is linked through the use of consistent headings, presentation order, and/or other methods appropriate to the relationship and type of information. Where links are to information reported outside the GPFRs it is important that:

- links to information from other sources do not undermine a GPFR's achievement of the qualitative characteristics; and
- the issuance date of any such linked information is as close as possible to the financial statements' reporting date so that reported information will be timely.

Comparability

8.60 Information organisation takes into account the benefits of consistent presentation over time. Consistent presentation supports users' ability to understand information and facilitates their access to information. It helps to achieve the qualitative characteristic of comparability.

Principles for information organisation within the financial statements

8.61 Information displayed on the face of the financial statements is usually organised into numeric totals and sub-totals. Its organisation provides a structured overview of such matters as the reporting entity's financial position, financial performance and cash flows.

8.62 For the financial statements, relationships may exist between:

- subsets of displayed amounts or changes in displayed amounts and their impact on an entity's financial position, financial performance and/or cash flows;
- different displayed amounts in different financial statements, which all reflect the impact of a common external event, or contribute together towards an understanding of an aspect of the entity's financial position or financial performance; and
- displayed amounts and related note disclosures that provide information that explains or could otherwise support users' understanding of displayed items.

8.63 The organisation of information in financial statements includes decisions on:

- the type and number of statements;
- disaggregation of totals into meaningful subcategories;
- ordering and grouping of items displayed within each statement;
- identification of aggregates (additive and subtractive); and
- identification of other information for inclusion on the face of the statement.

8.64 Information disclosed in the notes to the financial statements is organised so that relationships to items reported on the face of the financial statements are clear. The notes are an integral part of the financial statements.

Principles for organisation of information within other GPFRs

8.65 As is the case for the financial statements, information organisation in other GPFRs helps to ensure that key messages conveyed by displayed information are understandable. Presentation that clearly identifies important relationships is likely to enhance the extent to which a report:

- meets the objectives of financial reporting; and
- achieves the qualitative characteristics.

8.66 Linking related information helps users to find important information. Some information is more understandable when organised into graphs, charts, tables, ratios or key performance indicators. Other information may be presented more effectively in narrative form. Information organisation supports users' understanding of linkages between information within the same GPFR.

8.67 Information organisation facilitates comparisons such as making clear when items are similar or dissimilar. Inter-period comparability is facilitated by avoiding changes to the way that information is organised for the same entity from year to year unless such changes enhance relevance and understandability. Inter-entity comparisons are facilitated when different reporting entities organise the information they present in similar ways.

Withdrawal of the *Framework for the Preparation and Presentation of Financial Statements* (June 2014)

This Conceptual Framework supersedes the *Framework for the Preparation and Presentation of Financial Statements* (June 2014).

Basis for conclusions

This basis for conclusions gives the Accounting Standards Board's (the Board's) reasons for accepting or rejecting certain solutions related to issues outlined in the Conceptual Framework and departures from the IPSASB's Conceptual Framework. This basis for conclusions accompanies, but is not part of, the Conceptual Framework.

Background

BC1. The Conceptual Framework is based on *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (the IPSASB's Conceptual Framework) developed and issued by the International Public Sector Accounting Standards Board (IPSASB) during October 2014. It also refers to extracts of the revised *Conceptual Framework for Financial Reporting* issued by the International Accounting Standards Board®.

BC2. As the pronouncements issued by the IPSASB are used to develop Standards of GRAP, the issuing of the IPSASB's Conceptual Framework necessitated a review of the Board's existing *Framework for the Preparation and Presentation of Financial Statements* (the Framework).

BC3. In December 2015, the Board considered the appropriateness of the IPSASB's Conceptual Framework in the Research Paper on the *Impact of the IPSASB's Conceptual Framework on the Board's Existing Framework*. This Research Paper discusses the differences identified between the IPSASB's Conceptual Framework and the Framework, as well as the potential implications of those differences for the local environment. Each section in the Research Paper considers a specific chapter in the IPSASB's Conceptual Framework, and discusses how the concepts in those chapters compare with those in the Framework, and what the impact will be if the Board adopts those concepts locally.

BC4. Notwithstanding the differences noted, the Board concluded that the IPSASB's Conceptual Framework has indicated that substantial improvement could be made to the Framework to reflect the current IPSASB's concepts. As such, it was agreed that the IPSASB's Conceptual Framework is appropriate for the local environment, and should be adopted in its entirety, and modified for relevance in the local environment as discussed in this basis for conclusions. The Board developed an Exposure Draft of the proposed *Conceptual Framework for General Purpose Financial Reporting* (ED 149) and issued it for comment during 2016.

Scope of the Conceptual Framework

BC5. The IPSASB's Conceptual Framework established the concepts that are to be applied in developing concepts that the IPSASB will apply in developing the International Public

Sector Accounting Standards (IPSASs) and Recommended Practice Guidelines (RPGs) applicable to the preparation and presentation of general purpose financial reports (GPFRs) of public sector entities; and in dealing with topics that have yet to form the subject of IPSASs. Included in the Preface is a brief discussion on the GPFRs, while a more detailed discussion explaining what are GPFRs, and the type of information that is included in GPFRs is found in Chapters 1 and 2 respectively. In the Research Paper, the Board considered, generally, whether the scope of the IPSASB's Conceptual Framework is appropriate for the local environment.

BC6. The IPSASB distinguished between GPFRs and GPFSs. GPFRs reflect a scope of financial reporting that is broader than that encompassed by the financial statements, as they include information that enhances, complements, and supplements the financial statements. The IPSASB has acknowledged in its Conceptual Framework that information in the GPFSs is insufficient to meet users' needs. As a result, the IPSASB concluded that additional information, reported outside the financial statements, is necessary to provide relevant information to the users of the GPFRs for accountability and decision making purposes.

BC7. Historically, the Board's Framework only dealt with financial statements and did not cover information reported outside the financial statements. The information in the financial statements communicates messages about whether an entity has met its financial objectives by providing information about an entity's financial position, financial performance and cash flows. This information is necessary in understanding what resources an entity has available to fund future service delivery and any debts, how well those resources were used and preserved during the period, and whether revenues were sufficient to fund current activities. The Board noted however, that while financial statements are critical in exercising accountability and decision-making, the information they include is limited as they only provide information about historical financial transactions. As a result, information about an entity's prospects or whether it has achieved its strategic objectives is not communicated in the financial statements.

BC8. While financial statements themselves do not communicate such information, the information in the financial statements can be used in reports outside the financial statements to provide such information. Financial statements and other information reported outside the financial statements are both vitally important and complementary; for example, the information in the financial statements can be used as inputs into assessments of:

- assessing compliance with the budget and strategy;
- the economy, efficiency and effectiveness of services provided; and

- projections of an entity's long term sustainability.

BC9. GPFRs are designed to complement and supplement the financial statements, and therefore exclude certain non-financial areas that are covered by integrated reporting. Reporting outside the financial statements is not only about the preparation of additional information. The Board believed that what matters most is the information that is used to prepare these reports and the way in which the information is reported. These reports must be based on credible financial statements and other information. It is also critical that the information included in these reports is consistent, cohesive and provide an integrated overview of the entity's achievements. It is thus critical that reporting requirements for the financial statements and reports outside the financial statements are developed to create comprehensive, cohesive reporting requirements. The Board noted that while the reporting requirements for financial reports are established by other institutions, the Conceptual Framework's broader scope does not imply that the Board will issue those reporting requirements.

BC10. The Board therefore concluded that there is a need for a broader scope in the Conceptual Framework, and holds the view that while entities have been reporting information outside the financial statements, there is no set of established principles to guide the preparation and presentation of this information. The Board concluded that establishing principles for a more comprehensive scope of financial reporting in the Conceptual Framework will have the following benefits:

- outlining fundamental principles that will guide entities to develop best practice in reporting such information; and
- the communication of information will be enhanced, and will focus on information that is useful to the users for accountability and decision-making purposes.

BC11. In the Exposure Draft, the Board sought views on whether there is a need for a broader scope in the Conceptual Framework. Respondents to the Exposure Draft expressed support for the broader scope of financial reporting.

Preface of the Conceptual Framework

BC12. Included in the IPSASB's Conceptual Framework is the Preface which was developed to provide a discussion of the characteristics of public sector entities that influenced the development of the concepts included in the IPSASB's Conceptual Framework. The Board concluded that these characteristics are an important aspect of the Conceptual Framework as they underpin the established concepts. As such the Board agreed to include the Preface in the Conceptual Framework. However, the discussion on statistical reporting has not been included as the Board was of the view that the discussion is more appropriate for the IPSASB as one of its objectives is to remove differences between IPSASs and the

GFS reporting guidelines.

Chapter 1 – Role and authority of the Conceptual Framework

BC13. While the Board considered the discussion of the role of IPSASB's Conceptual Framework to be broad, the Board agreed to make minor modification to this Chapter to clarify the purpose of the Conceptual Framework to its users locally. When discussing the applicability of the Conceptual Framework, it was noted that the Board should include a broad principle that entities would consider in determining whether they are public sector entities to which Standards of GRAP apply. The Board agreed that the Conceptual Framework should include such a broad principle that identifies the characteristics of a public sector entity, instead of indicating which entities are required or permitted to apply Standards of GRAP. These characteristics are based on the characteristics of a public sector entity that were established in the IPSASB's project on *The Applicability of IPSASs*.

BC14. Respondents to the Exposure Draft questioned the link between the characteristics of a public sector entity and the Directive on *The Selection of an Appropriate Reporting Framework by Public Entities* (Directive 12). Directive 12 outlines criteria for certain public entities to assess whether they should apply International Financial Reporting Standards®. As explained in BC13, the Board considered it necessary to include a broad principle in the Conceptual Framework that identifies the characteristics of a public sector entity. These characteristics complement the criteria in Directive 12. Consequently, the Board agreed to clarify in the Conceptual Framework that the characteristics of a public sector entity should not be interpreted to mean that entities that meet those characteristics should apply Standards of GRAP.

Chapter 2 – Objectives and users of General Purpose Financial Reports

BC15. The Board did not make any significant modifications to Chapter 2 of the IPSASB's Conceptual Framework.

Chapter 3 – Qualitative characteristics

BC16. The IPSASB's qualitative characteristics (QCs) are broadly consistent with those of the Board. However, the IPSASB considered materiality as a pervasive constraint rather than an aspect of relevance. The IPSASB held the view that the materiality has a more pervasive role than would be reflected if it classified as an entity-specific aspect of relevance. When the Board considered the Research Paper, it considered whether it would apply materiality in its Conceptual Framework in the same way as the IPSASB.

BC17. The Board considered how other standard-setting bodies that have not adopted the IPSASB's Conceptual Framework have treated materiality. The Board noted that most standard-setters treat materiality as an aspect of relevance. In the past, there have been standard-setters (for example the Financial Accounting Standards Board (FASB)) that considered materiality a pervasive constraint on financial reporting that can only be considered together with the QCs, especially relevance and faithful representation (historically referred to as reliability). In recent years, the FASB's thinking has changed following the convergence of its Concepts Statements with the IASB's Conceptual Framework.

BC18. The Board considered the description of materiality in the IPSASB's Conceptual Framework, and tried to apply it to all the QCs. Information is considered material if its omission or misstatement could influence the discharge of accountability by the entity, or the decisions that users make on the basis of GPFRs. As such, users need information that is relevant to holding entities accountable and making decisions. As a result, the Board was of the view that although materiality is pervasive, it is not an overall constraint on reporting of information. Based on an analysis of the description of materiality, the Board observed that it could relate materiality to relevance and faithful representation, but it was conceptually and practically impossible to indicate that materiality has a role in relation to the other QCs. From a practical point of view, the Board also noted that preparers are likely to have difficulty in demonstrating how materiality is a constraint on the entity's ability to report information.

BC19. The Board considered the IPSASB's rationale for its approach when it developed its Conceptual Framework. It was noted that during the development of the IPSASB's Conceptual Framework, the discussion at the IPSASB did not involve the actual application of the definition of materiality as a threshold to all the QCs but rather an overall consideration of materiality on standard-setting. The Board concluded that conceptually there may not be differences in either approach, however practically it is difficult to relate materiality to the other QCs.

BC20. Before making a final decision, the Board considered what the implications on standard-setting would be if it deviated from the IPSASB's approach. In developing Standards, the Board takes into account all relevant factors, including best accounting practices both locally and internationally. International best practice includes the pronouncements of both the IPSASB and IASB. Usually the Board follows the IPSASB's approach to maintain alignment with IPSASs unless there is a significant South African public sector issue that warrants a departure. However, in this instance the Board believed that it should follow the IASB's approach to treat materiality as an aspect of relevance as it had done in its existing Framework. Even though this would be a departure from the IPSASB's Conceptual Framework, the Board believed that such a departure is warranted given the Board's observations in applying materiality practically.

BC21. Responses to the Exposure Draft were mixed, with one respondent opposing the Board's proposal to treat materiality as an aspect of relevance. The respondent supported the IPSASB's view that materiality is a constraint on information similar to the cost-benefit constraint. The Board was still not persuaded by the respondent's argument, and believed that it would be inappropriate to apply materiality on the same level as cost-benefit, as this would imply that an entity has already assessed and applied the other QCs to the information to be presented in the GPFRs.

BC22. Based on feedback on the Exposure Draft from stakeholders, the Board considered the impact of legislative requirements that govern the preparation of GPFRs on the achievement of the QCs and/or constraints on information. For example, it was noted that in some instances, legislative requirements may require entities to provide certain information in the GPFRs regardless of whether that information satisfies the QCs. The Board debated whether Chapter 3 should reflect that, in some instances, the QCs and/or constraints on information will not be applied as entities are required to comply with legislative or equivalent requirements. The Board observed that it has already set a principle in Chapter 1 that provides that the Conceptual Framework does not override any existing legislative requirements or frameworks set by other organisations. As such, the Board concluded that no further clarification was necessary in Chapter 3.

Chapter 4 – Reporting entity

BC23. Chapter 4 of the IPSASB's Conceptual Framework was modified to include guidance on the impact of control and the preparation of consolidated financial statements for the economic reporting entity.

BC24. Some respondents to the Exposure Draft raised concerns that it was not clear how the guidance should be applied, particularly as local legislation identifies specific reporting entities. The Board agreed that clarification was necessary to ensure that the concept is interpreted and applied as the Board intended. Additional commentary has been included to clarify the terms "reporting entity", "group reporting entity" and "economic entity".

BC25. The Board identified three scenarios in which a reporting entity or group reporting entity will arise. Firstly, the reporting entity is an entity (or group of entities) that is required to prepare GPFRs based on a legislative or similar requirement. Secondly, the reporting entity is an entity identified in the first scenario but that elects to prepare GPFRs for a portion, programme or identifiable area of activity within that entity. The Board considered that the third scenario exists where legislation or similar requirements do not identify reporting entities. In the last two scenarios, the Board concluded that the entity should consider the characteristics of a reporting entity and if the preparation of GPFRs satisfies the objectives of financial reporting.

BC26. Some respondents observed that in the second scenario, an entity may elect to prepare

GPFRs for a portion, programme or identifiable area of activity within an entity (for example ring-fenced bank accounts) that has the effect of not reflecting that portion of an entity, programme or activity in the financial statements prepared in accordance with legislation or similar means. The Board is of the view that the principles in the Conceptual Framework do not override the specific requirements in the Standards of GRAP that require an entity to prepare financial statements and/or consolidated financial statements, whether in terms of a legislative requirement or the election in this Conceptual Framework. As such, entities required to prepare financial statements in accordance with the Standards of GRAP, are required to include in their financial statements, the revenue, expenses, assets and liabilities of a portion of that entity, programme or activity in terms of the applicable Standards of GRAP.

BC27. The Board also noted the importance of distinguishing between the group reporting entity and the economic entity. For example, GPFRs prepared by a group reporting entity are not only based on a control relationship between entities, as is the case for GPFSs of an economic entity.

Chapter 5 – Elements in financial statements

BC28. The IPSASB provided extensive guidance on key features of the elements. The Board concurred with this guidance as it clarifies the aspects of definitions that may have been problematic to apply, particularly the concept of service potential and the past events that give rise to assets and liabilities. The Board, however, did not believe that it should include the discussion on other economic phenomena that may not meet the definition of the six elements. The IPSASB indicated in Chapter 5 that the recognition of such items would be limited to circumstances determinable by the IPSASB at a Standards' level. The Board understood the IPSASB's reasons for including this discussion in its Conceptual Framework, but was concerned that, in the absence of guidance from the IPSASB and/or the Board, concepts relating to the recognition of "other resources" and "other obligations" may be misapplied locally. As such the Board agreed not to include these concepts on the basis that they will be addressed, indirectly, when the Board considers how the IPSASB uses them at a Standards' level.

BC29. Some respondents considered it necessary for the Board to include the discussion as a means to provide clarity. The Board disagreed with this view as it is of the view that the concept, if included in the Conceptual Framework, will be of no relevance to preparers as its use will be limited to the Board.

BC30. Some respondents raised concerns over the use of the terms "political necessity" and "economic coercion" in the Conceptual Framework. The relevance of the terms in the local environment was questioned with some respondents suggesting that the terms should be removed. The Board considered the suggestion but concluded that it has no persuasive arguments to depart from the IPSASB's Conceptual Framework in this regard. The Board is concerned that when guidance is developed that warrants the use of the terms at a Standards' level, there will be no conceptual basis for their use in the Conceptual Framework.

BC31. Other respondents questioned the use of the term "non-legally binding obligations". It was noted that the term is too long and has been used repeatedly in the section dealing with liabilities. It was recommended that the Board considers replacing the term with "other obligations". The Board considered the recommendation but concluded that the use of "other obligations" is associated with other economic phenomena i.e. "other resources" and "other obligations" which do not meet the definition of the six elements discussed in this Chapter. The Board agreed to retain the term "non-legally binding obligations" to avoid the unintended consequence of the Board using different terminology once new IPSASs are developed.

Chapter 6 – Recognition in financial statements

BC32. The Board considered whether the guidance on the unit of account should be introduced to the Conceptual Framework. The unit of account refers to the group of assets and/or liabilities to which the recognition and measurement requirements apply. The Board agreed to add a section that deals with the unit of account based on some of the guidance included in the IASB's Exposure Draft of the *Conceptual Framework for Financial Reporting* (ED/2015/3). Respondents to the Exposure supported the inclusion of the guidance in the Conceptual Framework.

Chapter 7 – Measurement of assets and liabilities in financial statements

BC33. The Board did not make any significant modifications to Chapter 7 of the IPSASB's Conceptual Framework.

Chapter 8 – Presentation in General Purpose Financial Reports

BC34. The Board considered the IASB's approach to presentation objectives in ED/2015/3. The IASB regards presentation and disclosure as communication tools, and explains that in achieving efficient and effective communication, one of the key considerations is the use of "presentation and disclosure objectives and principles instead of rules that could lead to purely mechanistic compliance". It is for this reason that the Board concluded that it should modify Chapter 8 such that entities understand more clearly the objectives of disclosures.