

# Technical Advisory Group

## Issue Paper

AGENDA ITEM: TAGED05-03

6 April 2022 – Online

### Section 2 – Concepts and Pervasive Principles - Exposure Draft

Summary	The paper sets out key issues associated with the first draft of the text for Section 2 of the INPAG and its Basis for Conclusions.
Purpose/Objective of the paper	This paper provides TAG members with the emerging technical issues associated with Section 2 – Concepts and Pervasive Principles of the INPAG that will form part of Exposure Draft 1 which is due to be published in late 2022. It highlights key areas where the INPAG Secretariat considers there may be outstanding technical considerations.
Other supporting items	N/A
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Actions for this meeting	<u>Advise</u> on the areas of the Section 2 – Concepts and Pervasive Principles and its Basis for Conclusions where there may be outstanding technical considerations.

# Technical Advisory Group

## Project Update – March 2022

### 1. Exposure Draft and paper format

- 1.1 Exposure Draft Tranche 1 is due to be published in late 2022. Included in Tranche 1 will be the Sections that relate to the framing of the INPAG. Following the format of the *IFRS for SMEs* Standard this will include Sections related to the Preface, Non-Profit Organisations, and the Concepts and Pervasive Principles.
- 1.2 The INPAG incorporates Sections from the *IFRS for SMEs* Standard directly where there is no NPO sector specific reason for any change to be made. Where NPO-specific financial reporting issues have not been comprehensively or appropriately dealt with in the existing *IFRS for SMEs* Standard, or where there is no related Section in the *IFRS for SMEs* Standard that provides financial reporting guidance, the INPAG may make a change to the *IFRS for SMEs* Standard.
- 1.3 The Sections that relate to the framing of the INPAG are some of those where the *IFRS for SMEs* Standard will be subject to the most extensive change. In order to assist TAG members in understanding where text from the *IFRS for SMEs* Standard has been incorporated directly or been subject to change, the following approach is being used:

Text colour	Explanation
Black	Original <i>IFRS for SMEs</i> Standard text
<del>Red strikethrough</del>	Deletion of text within original <i>IFRS for SMEs</i> Standard text
Green	Change of terminology only
Purple	Text originated from IFRS Standards
Blue	Original INPAG text
<u>Blue underlined</u>	Text originated from IPSAS Standards

- 1.4 In addition to the proposed Exposure Draft text relating to each Section and its associated Basis for Conclusions, a further document will be provided that maps the Section from the *IFRS for SMEs* Standard to the proposed Section of the INPAG.

## 2. Content and purpose of Section 2 – Concepts and Pervasive Principles

- 2.1 The purpose of Section 2 – Concepts and Pervasive Principles of the *IFRS for SMEs* Standard is to describe the objective of financial statements, the qualities that make the information in the financial statements useful, and to set out the concepts and basic principles underlying the financial statements.
- 2.2 Section 2 Concepts and Pervasive Principles of the INPAG has a similar purpose. It describes the objective of financial reporting by NPOs, who the users of NPO GPFs are, the qualitative characteristics of information in GPFs, defines the reporting NPO (to be considered separately at the May 2022 meeting), defines the elements of financial statements and associated recognition, measurement and presentation principles.
- 2.3 The Basis for Conclusions provides a summary of the considerations made during the development of Section 2 – Concepts and Pervasive Principles. Areas that have been included are:
- The use of the IFRS Conceptual Framework and the IPSASB's Public Sector Conceptual Framework;
  - Primary users of GPFs and their information needs;
  - Presentation in GPFs;
  - Qualitative Characteristics;
  - The Reporting NPO (to be considered separately at the May 2022 meeting);
  - Elements of financial statements
  - The Statement of Financial Position, Statement of Movement of Net Assets, and Income and Expenses Statement; and
  - Recognition and measurement of assets, liabilities, income and expenses in financial statements.

Question 1: Are there any areas that the TAG considers are missing from Section 2 – Concepts and Pervasive Principles or the Basis for Conclusions?

## 3. Specific areas for discussion

### Use of the IFRS and IPSAS conceptual frameworks

- 3.1 Section 2 – Concepts and Pervasive Principles of the INPAG makes use of the IASB's Conceptual Framework and the IPSASB's Conceptual Framework. These

conceptual frameworks have been used where they provide the concepts and principles needed to develop financial reporting guidance for NPOs on issues that are not comprehensively or appropriately dealt with in the existing *IFRS for SMEs* Standard.

- 3.2 In taking this approach, a hierarchy of standards has been used with the IFRS Conceptual Framework accessed first and then the IPSAS Conceptual Framework. This is consistent with the approach in the 'Rules of the Road.'
- 3.3 It is expected that significant parts of Section 2 of the *IFRS for SMEs* Standard will be updated to reflect the changes made to the IASB Conceptual Framework since the last review of the *IFRS for SMEs* Standard. Depending on the nature and extent of these changes, Section 2 of the INPAG is likely to be subject to further revision.

3.4

**Question 2: Do the TAG consider that the approach in using the IASB and the IPSASB Conceptual Frameworks are appropriate, noting that the *IFRS for SMEs* Standard is being updated to reflect changes made to the IASB Conceptual Framework?**

- 3.5 To ensure that the core guidance remains concise, only high-level concepts and principles are proposed to be included in Section 2 of the INPAG. Further detail supporting the concepts and principles is to be included in the authoritative application guidance. This means, for example, that the core guidance defines an asset, but that the detail behind the definition of aspects of this element such as 'a right', 'the capability to produce economic benefits or service potential', and 'control', are included in the application guidance.

**Question 3: Do the TAG agree with the approach of including only high level concepts and principles in the core guidance, with additional detail included in the authoritative application guidance?**

## Primary users of GPFRs

- 3.6 The inclusion of groups such as internal users and donors as users of GPFRs has been discussed with the PAG and TAG. Following these discussions, Section 2

proposes that GPFRs are not developed specifically to respond to any individual information needs. This is because NPOs may have users of their GPFRs that can be primary users in some circumstances but may have rights to tailored information in other situations.

**Question 4: Do the TAG have any further comment on how the users of NPO GPFRs are articulated, including the position of groups such as donors?**

### Fundamental and enhancing qualitative characteristics

- 3.7 In the IASB Conceptual Framework there is a distinction between fundamental and enhancing qualitative characteristics of information in GPFRs. Such a distinction between fundamental and enhancing characteristics is not present in either the existing *IFRS for SMEs* Standard or the IPSASB Conceptual Framework.
- 3.8 The use of these qualitative characteristics is significantly different to the qualitative characteristics of information in financial statements currently in the *IFRS for SMEs* Standard. Given the tentative decisions taken by the IASB, the expectation is that Section 2 will be revised to align more closely with the IASB Conceptual Framework. The drafting of Section 2 may need to be updated once the exposure draft for the revised *IFRS for SMEs* Standard has been published.

**Question 5: Do the TAG agree with the inclusion of the distinction between fundamental and enhancing qualitative characteristics?**

### Elements of financial statements

- 3.9 The IASB Conceptual Framework includes 'elements' which provide definitions of the key components of financial statements. The current *IFRS for SMEs* Standard is not built exactly on this conceptual basis and has standalone definitions of key components of the financial statements. In anticipation of the alignment activities with the IASB conceptual framework, it is proposed that INPAG is based around the use of elements.

- 3.10 The most significant change to the elements from the IASB Conceptual Framework is a proposed new element called 'net assets' that includes equity. This is to reflect the NPO context, where an element is needed to incorporate restricted funds, unrestricted funds, reserves and equity. This recognises that many NPOs will manage their assets and liabilities within separate funds, some of which may be subject to an externally mandated restriction. It also leaves open the possibility that there may be holders of equity claims.

**Question 6: Do the TAG agree with the adoption of elements from the IASB Conceptual Framework?**

**Question 7: Do the TAG agree with the incorporation of equity within the broader element of net assets that also includes restricted funds, unrestricted funds and reserves?**

- 3.11 In addition to the proposed new element of net assets, changes are also proposed to income and expenses to reflect a user focus on surplus and deficit rather than comprehensive income.
- 3.12 It is currently proposed that financial performance is shown in a statement to be called the statement of income and expenses. This statement will show the surplus or deficit generated by an NPO that includes its revenue and expenses that include realised gains and those unrealised gains prescribed in the Guidance.
- 3.13 Adopting this approach means that some unrealised gains and losses will not be recognised in the statement of income and expenses but instead will be recognised in the statement of movement in net assets, which will show movements in funds, reserves and equity. This will ensure that these unrealised gains and losses do not impact on the surplus or deficit recognised for the reporting period.
- 3.14 Further discussion on the naming of financial statements will be included in the analysis of the feedback from the consultation paper on the financial statement topic to be presented at the May TAG meeting.



Question 8: Do the TAG agree that with the distinction between realised and unrealised gains and losses and how they are to be recognised in the financial statements?

## Recognition and measurement principles

- 3.15 Service potential is proposed to be included as a measurement approach to elements for the INPAG as it is relevant for those assets that are held by NPOs for the services they provide and not to generate cash flows. As part of measurement, Section 2 therefore proposes to include value in use as a potential measurement basis, as this incorporates the concept of service potential. This may be updated pending IPSASB discussions on measurement.

Question 9: Do the TAG consider the inclusion of a value in use measurement basis appropriate given the inclusion of service potential within the definition of the elements?

## Undue cost exemption

- 3.16 The *IFRS for SMEs* Standard provides for exemptions based on undue cost and effort. It is proposed to retain this exemption in addition to a general recognition that cost is a pervasive constraint on useful financial reporting. However, we are aware that in practice it has been difficult to apply this exemption. It is understood that a decision has not yet been made by the IASB on whether this exemption will be retained as part of the review of the *IFRS for SMEs* Standard.

Question 10: Do the TAG agree with the inclusion of the undue cost or effort exemption?

## Presentation of GPFRs

- 3.17 IPSAS provides guidance in its conceptual framework about the presentation of GPFRs. Its guidance includes considerations around the selection location and



organisation of information in considering the needs of users. This guidance goes to meeting the aim to provide information that contributes towards the objectives of financial reporting and achieving the qualitative characteristics of information.

- 3.18 This type of guidance will be of significant benefit to preparers of financial statements. With INPAG going wider than just financial statements, it is proposed to include key principles around the presentation of GPRS in Section 2 as it is a pervasive principle for GPFs. This will be supported by application and implementation guidance.

**Question 11: Do the TAG agree that the presentation of GPFs should be included in Section 2 as a concept or pervasive principle?**

#### 4. Content drafting

- 4.1 As set out in paragraph 1.4, Annex A contains the current drafts of the guidance, basis for conclusions and a table that sets out the differences between the draft INPAG guidance and the *IFRS for SMEs* Standard. As noted above this does not currently include draft text relating to the reporting entity as this will be considered at the May meeting. The TAG are invited to provide detailed comments on the draft in correspondence.

**Question 12: Do the TAG have any key points of principle arising from the current drafting outside of the key issues described in section 2 and 3?**

March 2022