The Chartered Institute of Public Finance & Accountancy

EFRAG Discussion Paper

Non-Exchange Transfers - A Role for Societal Benefit?

Response from the Chartered Institute of Public Finance and Accountancy (CIPFA)

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the people in public finance

CIPFA, the Chartered Institute of Public Finance and Accountancy, is the professional body for people in public finance. CIPFA shows the way in public finance globally, standing up for sound public financial management and good governance around the world as the leading commentator on managing and accounting for public money.

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EFRAG Discussion Paper *Non-Exchange Transfers - A Role for Societal Benefit?*

This discussion paper has been reviewed by CIPFA's Accounting and Auditing Standards Panel.

<u>CIPFA's perspective</u>

CIPFA is a professional accountancy organisation whose principal focus is promoting high standards in public sector governance and public financial management. CIPFA generally responds to public sector focussed consultations, and those private sector consultations which have direct public sector ramifications, or where there are implications for accountancy generally that would impact on the public sector.

For this reason, CIPFA responds to the majority of consultations by the International Public Sector Accounting Standards Board (IPSASB), and many consultations by the International Accounting Standards Board (IASB), particularly where these deal with conceptual matters.

We would note that IPSASB's Conceptual Framework for *General Purpose Financial Reporting by Public Sector Entities (2014)* is substantially aligned with the IASB's *Conceptual Framework for General Purpose Financial Reporting (2018)*. CIPFA has strongly supported this alignment, and we would note that the two boards have maintained constructive dialogue on these issues for many years.

The discussion paper deals with transactions between public sector entities and private sector entities. While it considers the perspective of private sector entities, this is of interest to CIPFA because in general we would expect the treatment of these transactions to mirror the treatment of the same transactions from the perspective of public sector entities, except to the extent that there are asymmetries in access to information, assessment of risk, or specific differences in how the respective conceptual frameworks relate to these transactions.

CIPFA welcomes the introduction of 'societal benefit' into the discussion of private sector financial reporting for transfers to and from public sector entities. This resonates with the IPSASB discussion of 'service potential', which relates to the provision of services (and sometimes goods) to provide economic, social or other benefits to society as a whole, or to support individuals in line with views of government responsibility held by society in the jurisdiction of that government (typically determined through political process).

<u>The IPSAS context</u>

IPSASB has a well-developed understanding of how 'service potential' affects the economic position of public sector entities which are required to provide such services as part of their objectives, and this has consequences for public sector financial reporting in relation to, for example,

- The attribution of value to assets which do not generate income but can be used to provide services; and
- the recognition of liabilities in respect of services which an entity has an obligation to provide which do not arise from contracts with customers

We would note that the IPSASB is reviewing its standard on non-exchange revenue IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*. However, this is mainly to improve the standard and to make it more operationalisable while having regard to the approach taken by the IASB in its recent standard IFRS 15 *Revenue from Contracts with Customers*. The IPSASB is also taking the opportunity to review how its standards work for conventional exchange transactions, and how issues in respect of transactions with exchange and non-exchange aspects should be managed. There are no particular concerns that extant IPSAS 23 is inconsistent with either the IPSASB conceptual framework, or public sector interpretations of the IASB conceptual framework, or indeed, most IASB or IPSASB standards development since 2004 when the IASB began its project to review its conceptual framework.

Comments on the proposals and questions in the discussion paper

Against this background, CIPFA is very interested in any new discussion of matters relating to 'societal benefit' or 'service potential'. However, we would expect any treatment either to align closely with IPSAS 23, or to provide additional conceptual material which explains the basis for the different treatment. Given that the discussion paper is exploring possible changes that might be made to IFRS, we would also expect it to explain how its proposals fit into the IFRS conceptual context by providing financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity. Simply mentioning the words 'societal benefit' and relying on the reader of the paper to provide their own rationale does not provide an adequate conceptual support.

Unfortunately, the discussion paper does not address this key issue. It provides no overall indication of why societal benefit should affect the position of a private sector entity. Nor is it straightforward to determine why it should affect claims by or against the entity, except implicitly in the context of IPSAS 23 conditions, where the relevance of societal benefit to the objectives of the public sector counterparty, taken together with an enforcement mechanism makes the arrangement analogous to a contractual exchange.

CIPFA disagrees with the implications of point 4 in the Executive Summary, which states that

> *It is not generally possible to identify specific patterns in which entities receive or contribute to create societal benefits, such as those from the general activity of the Government, and it seems reasonable that many of these occur continuously.*

We strongly question whether this observation, and the suggestion that related transfers should be allocated smoothly, are relevant to financial reporting by the entity. Particularly where that entity is primarily engaged in profit making activities, and where reporting on those activities is naturally focussed on the entity's economic position. Even if the entity was in possession of complete information in relation to the effects on societal benefit, the discussion paper provides no explanation of why recognition in the main financial statements on this basis would be particularly useful to any readers of the financial statements.

Overall the discussion paper is interesting, and in some areas we considered it provided additional insight into the private sector perspective in areas where CIPFA has mainly considered the position of government entities.

However, in CIPFA's view the paper does not provide a conceptual basis for all of the steps in its proposed four step approach. Particularly in respect of steps 2 and 3. Inasmuch as we agree with the proposals, it is where they apply to arrangements which include IPSAS 23 conditions. CIPFA is therefore unable to support any of the proposals referred to in Question 3, and we disagree with key aspects of the positions in Chapters 2 and 3 which are explored in Questions 4 and 5.

Question 6 relates to Chapter 4, and we note that paragraphs 4.1-4.2 explain that the approach in previous chapters moves away from the control and obligation model. However, this departure from the Conceptual Framework 2018 is still not supported by any discussion of what it is that makes the provision of societal benefit relevant to financial reporting, let alone so relevant that it should determine the recognition of items in financial statements. Without such support, the provision of societal benefit is simply interesting information which can be provided in note disclosures.

On the specific matter of uncertainly, the discussion paper suggests that this should be a factor affecting recognition, rather than measurement. This is not the approach followed in the Conceptual Framework 2018, but again the paper has not explained why it has chosen a different approach to that determined by the IASB after extended discussion and debate.

We hope this is a helpful contribution to EFRAG's work.