PSAB
Public Sector
Accounting Board

PSAB's Proposed New Reporting Model: Two Exposure Draft Proposals

Extract, PSA Discussion Group Report on the Public Meeting – April 8, 2021

PSAB issued four exposure drafts in January 2021:

- One proposes a new conceptual framework.
- Another proposes a new reporting model for all public sector entities.
- Two others set out consequential amendments related to the conceptual framework and reporting model proposals.

In the reporting model Exposure Draft, PSAB proposes to split liabilities into two categories: financial and non-financial. The Group was asked whether the distinction between them is clear and can be applied.

PSAB also proposes new guidance on the going concern assumption. The Group was asked if the proposed guidance is sufficient and appropriate for the public sector. Due to time constraints, the Group could not discuss this second issue at the meeting.

Issue 1

PSAB proposes to split liabilities into two categories: financial and non-financial liabilities.

- A **financial liability** is a liability that is expected to be settled using financial assets. Financial liabilities include but are not limited to financial performance obligations. (Paragraph.005(c) of the Exposure Draft)
- A **non-financial liability** is a liability that cannot be settled through the use of financial assets but only through the use of non-financial assets or economic resources excluded from recognition in paragraph PS 1202.071. A non-financial liability does not represent a future financial resource requirement. Non-financial liabilities include but are not limited to non-financial performance obligations. (Paragraph.005(d) of the Exposure Draft)

PSAB's primary reasons for doing so are:

- to ensure the net debt indicator reflects future financial resource requirements, its original meaning. What the indicator purports to show has been muddied by including liabilities that will not be settled through the use of financial assets; and
- to refine the net debt calculation to ensure only liabilities that represent future financial resource requirements are included in measuring the indicator.

The Group was asked:

- Do you agree with splitting liabilities into financial and non-financial?

- Is the distinction between financial and non-financial liabilities clear? Consider some examples from your own experience. Can you determine if the liability should be classified as financial or non-financial?
- If the distinction is not clear, how can the definitions and guidance be clearer?

One Group member asked for clarification on the extent of non-financial liabilities and the types of organizations in which they might exist. The submitters explained that the main examples of non-financial liabilities are:

(a) liabilities settled through the use of a tangible capital asset acquired through a transfer;

(b) non-financial performance obligation liabilities arising from the user-pay model of public private partnership arrangements; and

(c) non-financial performance obligation liabilities that will be settled by providing an individual or another entity with a degree of access (simple, exclusive, unrestricted, restricted or shared) to certain rights or resources over the term of the arrangement.

For some senior governments and for many government-not-for-profit organizations (GNFPOs), example (a) is sometimes called “deferred capital contributions” or “spent deferred capital contributions”. These can be material.

Two Group members questioned whether capital transfer-related non-financial liabilities may exist for local governments, as the illustrative financial statements in the reporting model Exposure Draft show deferred capital contributions for senior governments but not local governments. The submitters noted that input received from local governments during the project to develop GOVERNMENT TRANSFERS, Section PS 3410, was that the liability related to a capital transfer is to buy or build the asset. Any expectation by the transferor that the asset will be used to provide services over its useful life is likely a valid one. However, it would not create the type of obligation that meets the definition of a liability and can be recognized in financial statements. Local governments also told PSAB that they are capital intensive. Requiring deferral and amortization of capital transfers received over the useful life of the related assets would impose an administrative burden and add little accountability value to their financial statements. Nevertheless, Section PS 3410 would determine the nature and extent of a liability and its revenue-recognition pattern based on the terms of the transfer arrangement and any related constructive obligation the transfer recipient creates. The definition of a liability would have to be met, but it is possible for any public sector entity to have a liability related to a capital transfer received that would be recognized in revenue over the useful life of the related asset or another term specified in the transfer arrangement.

The Group supported the financial/non-financial liability split and the look of the restructured statement of financial position. Having more precision in the net debt indicator was cited as one reason for the support, as was consistency with the existing financial/non-financial asset split. One Group member commented that presenting liabilities in the two categories would be appropriate only if the items removed from net debt are material.

After discussing the intent behind the proposals and if they would change existing standards, the submitters clarified that the financial/non-financial split is merely a presentation requirement. The split would not override any existing standard, except in relation to presentation of liabilities on the statement of financial position. Once an entity has applied all other Public Sector Accounting Standards (PSAS) and has determined it has liabilities, then, for presentation purposes, it would consider whether to present each liability as financial or non-financial; and so inside net debt or outside of net debt. Regarding examples of performance obligations in REVENUE, Section PS 3400, the financial/non-financial liability proposal would not require an entity to further split performance obligations beyond that already required by Section PS 3400 for transactions with multiple performance obligations.

The Group asked PSAB:

- to reconsider if the definition of a non-financial liability should refer to expectation, as the definition of a financial liability does. Is this difference appropriate?
- if the simple distinction between financial and non-financial assets could also be made for the financial/non-financial liabilities definitions.
- to consider whether the following examples would be appropriately classified, given the proposed definitions:
  - performance-type liabilities, originally intended to be settled without the use of financial resources, would be settled using financial assets if the expected terms and conditions of the (non-financial) liability were breached;
  - borrowings for capital;
  - unamortized debt premiums;
  - deferred rental income;
  - lease inducements; and
  - prepaid leases; and
- to explain why a statement of net debt was more appropriate than presenting this information in the notes and schedules.