

In Brief

A plain and simple overview of PSAB’s Exposure Draft, “The Conceptual Framework for Financial Reporting in the Public Sector”

This is an overview of the key concepts proposed in PSAB’s Exposure Draft, “The Conceptual Framework for Financial Reporting in the Public Sector.”

Project objectives:	<p>PSAB is proposing changes to its Conceptual Framework and Reporting Model because:</p> <ul style="list-style-type: none"> • it is necessary for a standard setter to periodically review its conceptual framework to ensure it remains relevant; • the Board was asked to look at the existing conceptual framework to ensure it properly reflects and is grounded in the public sector environment; and • certain standards-level issues made some stakeholders question the foundations of public sector financial reporting, so reconfirming if they were appropriate was necessary.
The project stage:	The project is in the last consultation stage.
Next steps:	The feedback we receive will help finalize the revised Conceptual Framework and Reporting Model.
Comment deadline:	May 12, 2021
How to respond:	Submit your feedback by taking part in the Connect.FRASCanada.ca project or submitting a comment letter .

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

Plain and simple overviews of the revised Conceptual Framework proposals

Characteristics of public sector entities	3
What's new	4
Objective of financial reporting	5
What's new	6
Role of financial statements in financial reporting	7
Financial statement foundations	8
What's new	8
Financial statement objectives	9
What's new	10
Qualitative characteristics of financial statement information	11
Financial statements elements	12
What's new	12
Recognition	13
What's new	13
Exclusions from recognition	14
Measurement concepts	15
What's new	15
Presentation concepts	16
Impacts of the proposed Conceptual Framework on public sector entities	17
Impact on the PSA Handbook	18

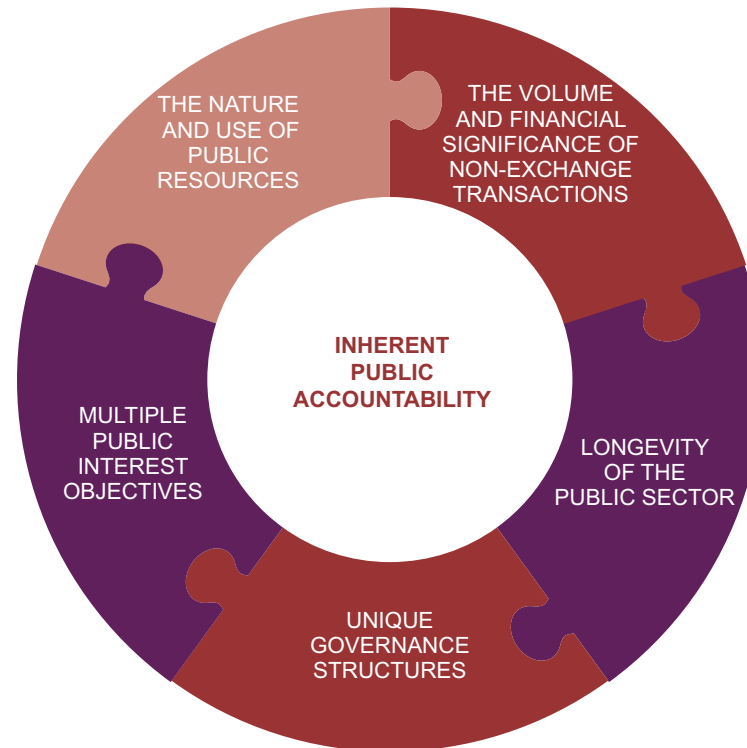
In Brief

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What are the characteristics of public sector entities?

Identifying the characteristics of public sector entities results in concepts and standards that are appropriate for the public sector.

Public sector entities exist to serve the public. The key characteristics of public sector entities are:



Inherent public accountability is the overriding characteristic of public sector entities because they are:

- entrusted with public resources; and
- responsible for how public resources are used, managed, and maintained.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"



What's new

Some respondents to the Statement of Concepts indicated that:

- not all characteristics apply to all public sector entities (specifically, not all the characteristics apply to government components and government organizations) and;
- the longevity of governments should be considered as an additional characteristic.

Applicability of the characteristics to government components and organizations: Throughout Chapter 2 of the proposed Conceptual Framework, PSAB included material about how the characteristics apply to government organizations and government components. The material allows government components and organizations to see themselves in the characteristics. PSAB also recognizes that there are several characteristics that do not apply to all public sector entities (e.g., a monopolistic environment).

Longevity of the public sector: PSAB added this as a characteristic of public sector entities, which considers the longevity of governments.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What is the objective of financial reporting?

The objective of public sector financial reporting is accountability.

The financial reporting objective identifies a purpose. The qualitative characteristics of financial information and the concepts for recognition, measurement, and presentation follow logically from the objective.

The financial reporting objective leads to identifying those who a public sector entity is accountable to (the primary users) and for what (serving the public and the broad accountabilities in financial reporting).

Primary users

The public and its elected or appointed representatives are the primary users of public sector financial reports.

Complete, transparent information provided for accountability purposes supports the decision-making process of all users.

Serving the public

The purpose of a public sector entity is to serve the public. As such, identifying and measuring a public sector entity's capacity or ability to serve the public (or "service capacity") is important.

Broad accountabilities in financial reporting

The broad financial accountabilities expected to be reported in the financial reports of public sector entities are:

- the entity's financial condition (one aspect of service capacity);
- the entity's financial performance (one aspect of change in service capacity); and
- the extent to which the entity performed in accordance with its financial authorities and plan.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"



What's new

Broader notion of service capacity: Based on stakeholder feedback on the Statement of Concepts, PSAB decided to include the broader notion of service capacity in the discussion of the broad accountabilities in financial reporting. This is because service capacity underpins these accountabilities, specifically financial condition and financial performance as:

- reporting on financial condition provides insight into an entity's service capacity; and
- reporting on financial performance provides insight into how an entity's decisions, transactions and other events of the period have affected its service capacity.

The term "service capacity" would not replace any of the existing terminology in the financial statements.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What is the role of financial statements in financial reporting?

Financial statements are a fundamental component of the financial reporting of a public sector entity.

The information provided in financial statements can only show certain aspects of what an entity is accountable for.

Nevertheless, financial statements are a central feature of public sector financial reporting because they:

- serve as a means by which a public sector entity provides an accounting of its administration of public financial affairs and resources; and
- are an important anchor to an entity's other financial and accountability reporting, especially when they are audited.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What are the financial statement foundations?

The four financial statement foundations relate to the basic decisions standard setters make before establishing concepts and standards for financial statements.

1. **Identifying the Reporting Entity:** Financial statements should be prepared to report on the financial affairs, economic resources, and economic obligations of an identifiable reporting entity (including its components and organizations).
2. **Control:** Control is the basis used for associating economic resources and other entities with a reporting entity.
3. **Unit of Measure:** The Canadian dollar with no adjustment for changes in general purchasing power.
4. **Basis of Accounting:** Accrual.



What's new

Concept of Control: Although a majority of respondents to the Statement of Concepts agreed the concept of control should be included and described in the proposed Conceptual Framework, many of these same respondents were concerned with the way it was described. They felt that parts of the description contradicted text in Section PS 1300, Government Reporting Entity.

As a result, the Board amended the description of control to ensure that the proposed Conceptual Framework would support, build on and not contradict standards in the CPA Canada Public Sector Accounting (PSA) Handbook.

Service Capacity: Since financial statements can only measure and report part of an entity's service capacity, service capacity is no longer a foundation of financial statements. Discussion of service capacity was moved to Chapters 3 and 4 of the proposed Conceptual Framework.

In Brief

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What are the financial statement objectives?

Financial statement objectives establish the information to be included in financial statements to meet the overall accountability objective.

Scope: Financial statements should account for the full nature and extent of an entity's financial affairs. They should also account for the economic resources that an entity controls and the economic obligations it must settle, including those of its components and controlled organizations.

Reporting Financial Position: Such information describes the entity's economic resources and economic obligations at the end of the accounting period.

Reporting Changes in Financial Position: This information describes: the sources, allocation, and consumption of the entity's economic resources; how the entity financed its activities; and how it met its cash requirements in the accounting period.

Comparing Actual Performance to that Budgeted: The actual-to-budget comparison is meaningful when the budget is prepared on the same basis of accounting, follows the same accounting principles, is for the same scope of activities, and uses the same classifications as the financial statements. Accountability is best achieved when financial statement users understand the information provided to them.

Disclosing Non-compliance with Financial Authorities: Financial statements should provide information useful in demonstrating whether the following were administered in accordance with the appropriate financial authorities:

- financial affairs;
- economic resources; and
- economic obligations.

Financial statements should provide information to allow users to assess the significance and financial implications of non-compliance.

Disclosing Risks and Uncertainties: Financial statements should provide information to describe the risks and uncertainties that could affect the entity's financial position or changes in financial position. This is useful for evaluating risks and uncertainties – and the entity's management of them.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"



What's new

Objective 2 – Reporting Financial Position: In response to the feedback received on the Statement of Concepts, the description of the objective is refined to be clear that reporting on financial position incorporates many aspects, such as reporting on:

- the entity's financial and non-financial assets;
- the entity's financial and non-financial liabilities;
- the entity's net financial assets or net financial liabilities indicator (currently known as net debt — we are proposing to rename "net debt" in the [Exposure Draft, "Financial Statement Presentation, Proposed Section PS 1202"](#));
- the entity's net assets or net liabilities which measures net financial position; and
- the various sources (or components) of net assets or net liabilities.

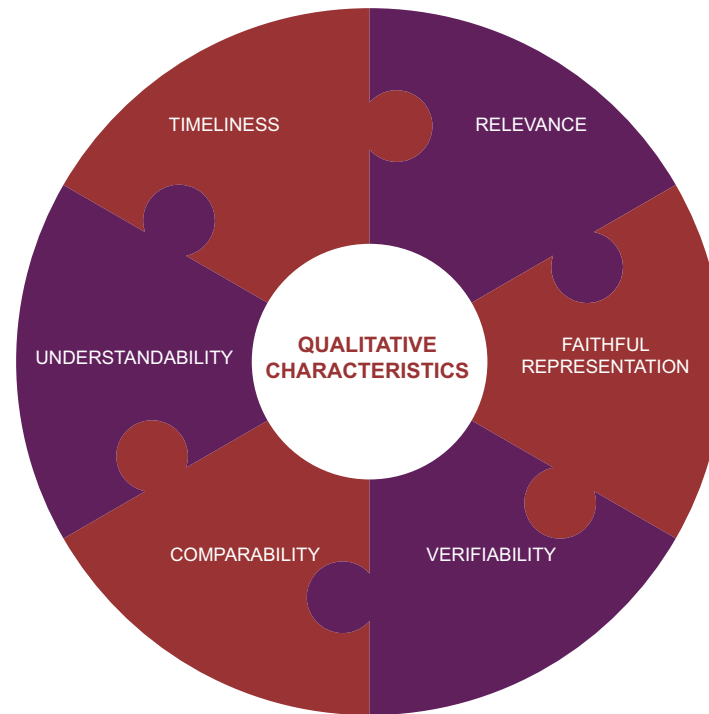
In Brief

A plain and simple overview of PSAB’s Exposure Draft, “The Conceptual Framework for Financial Reporting in the Public Sector”

What are the qualitative characteristics of financial statement information?

Qualitative characteristics are the attributes that make financial statement information useful to users for accountability purposes.

The qualitative characteristics of the information reported in financial statements are:



PSAB believes that financial statements should aim to achieve an appropriate balance among the qualitative characteristics.

Aside from the benefit-versus-cost consideration included in the existing conceptual framework, we propose including **materiality** and **prudence** as additional considerations to achieve an appropriate balance among the qualitative characteristics.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What are the elements of financial statements?

Elements are the basic building blocks from which financial statements are constructed.

The elements of financial statements are:

- assets
- liabilities
- revenues and
- expenses.

Existing asset and liability definitions were modified to be singular and constructed in a parallel fashion.

The revenue definition now requires that changes in assets and liabilities result in an increase in net assets or decrease in net liabilities. Similarly, the expense definition requires that changes in assets and liabilities result in a decrease in net assets or an increase in net liabilities.

In PSAB's existing conceptual framework, this effect is only recognized in the guidance accompanying the revenue and expense definitions.

Importance of all elements

Revenue and expense are defined in terms of changes in assets and liabilities. But for accountability purposes, revenues, and expenses are just as important as assets and liabilities.

No deferred inflows or deferred outflows as elements

The elements of financial statements are defined in terms of economic resources, economic obligations, and changes in them. Deferred inflows and outflows that do not meet the definition of assets or liabilities would not be recognized in the financial statements.



What's new

Defining "Economic Resources" and "Economic Obligations": In response to feedback received on the Statement of Concepts, and given the significant number of references to "economic resources" and "economic obligations" in the proposed Conceptual Framework, PSAB added the definitions of "economic resources" and "economic obligations" in the proposed Conceptual Framework. The definitions are consistent with the guidance in Section PS 3200, Liabilities, and Section PS 3210, Assets.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What is recognition?

Recognition is the inclusion of an item, transaction or other event within one or more financial statements.

Recognition does not mean disclosure in the notes to the financial statements.

Recognition

An item, transaction, or other event is recognized in the financial statements when:

- the item, transaction, or other event meets the definition of an element;
- it is expected that the related future economic benefits related to the item will be obtained or sacrificed; and
- the item, transaction, or other event can be measured.

Derecognition

Derecognition is the removal of all or part of a previously recognized item from the financial statements. This normally happens when:

- all or part of an item no longer meets the definition of an asset or liability;
- it is no longer expected that the future economic benefits related to the item will be obtained or sacrificed; or
- the item can no longer be measured.



What's new

Derecognition Criteria: In response to the feedback received on the Statement of Concept, PSAB decided to enhance the derecognition criteria so that they would be the inverse of the general recognition criteria.

The enhancements to the derecognition criteria would allow them to stand alone without referring to the general recognition criteria.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What is PSAB proposing to do with the exclusions from recognition?

The Board proposes that the exclusions from recognition in financial statements be moved to the revised Financial Statement Presentation Standard (Proposed Section PS 1202) until it considers the topics.

These exclusions are standards-level decisions – not concepts underlying financial statements.

The PSA Handbook sets out exclusions from recognition in financial statements in the Conceptual Framework. These exclusions relate to:

- inherited natural resources;
- inherited crown lands;
- all art and historical treasures; and
- inherited and developed intangibles.

These items were excluded from recognition on the basis that their costs, benefits, and economic value could not be reasonably and verifiably quantified using existing methods.

PSAB concluded that these pragmatic exclusions are not conceptually based and should be removed from the Conceptual Framework. However, the Board also thought that the exclusions should continue to be retained for now. The Board proposes moving the exclusions to the revised financial statement standard, Proposed Section PS 1202. This will allow the Board to consider these topics when setting its future technical agenda.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What are the measurement concepts?

Measurement is the result or process of determining the monetary amounts at which individual items, transactions, or other events are to be recognized in the financial statements.

Measurement attribute

A measurement attribute is the feature of the asset or liability that is quantified, such as its historical cost or its fair value.

There are a number of measurement attributes that can be used for initial or subsequent measurement in financial statements.

PSAB is confirming historical cost as the primary measurement attribute. However, the Board recognizes that other measurement attributes might be required at the standards level (when necessary) to meet the accountability objective.

Any PSAB requirement of a measurement attribute other than historical cost would be determined at the standards level. Its use would be justified and explained in terms of how it contributes to better information for accountability purposes.



What's new

Going concern: Based on the feedback received on the Statement of Concepts, improvements were made to the going concern discussion to reflect the Canadian public sector environment, such as considering the longevity of governments.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What is presentation and why are presentation concepts needed?

PSAB believes that general presentation concepts and guidance are required to increase the understandability and cohesiveness of the information presented – increasing the accountability value.

Presentation includes:

- the recognition and reporting of items, transactions, or other events on the face of the financial statements, either individually or within totals; and
- disclosure in the notes and schedules to the financial statements.

The objective of presentation is to present information in a manner that maximizes the accountability value of the financial statements to the users. It should also portray a cohesive financial picture of an entity's economic activities in a way that:

- meets the objective of financial reporting;
- meets the specific financial statement objectives;
- considers the qualitative characteristics of financial statement information and the related considerations; and
- achieves fair presentation.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What are the impacts of the proposed Conceptual Framework on public sector entities?

PSAB will start using the revised Conceptual Framework once it is issued. The revised concepts will guide the Board as it develops or amends standards.

The changes to the existing conceptual framework would not have an immediate effect on the financial statements of most reporting entities.

Entities would be required to use the revised Conceptual Framework when no standard specifically applies to a particular economic resource, economic obligation, transaction, or other event. In such circumstances, the revised Conceptual Framework would be applied prospectively.

Applying the new presentation concepts in Chapter 10 of the revised Conceptual Framework may lead entities to review the nature, extent, and structure of their financial statement disclosures.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

What is the impact of the proposed Conceptual Framework on the PSA Handbook?

A series of consequential amendments are being proposed to various Sections of the PSA Handbook to make them consistent with the proposed Conceptual Framework. The proposed consequential amendments are editorial in nature.

PSAB expects to issue the final amendments after it finalizes the proposed Conceptual Framework. Like the Conceptual Framework, the amendments will be effective immediately when issued.

The proposed consequential amendments would include the withdrawal of the existing conceptual framework and a revision to the definition of "materiality", as well as amendments to:

- references to the existing conceptual framework in the PSA Handbook;
- the general application standards, LIABILITIES, Section PS 3200, and ASSETS, Section PS 3210;
- REVENUE, Section PS 3400
- the "Introduction to Public Sector Accounting Standards" to recognize the conceptual framework;
- DISCLOSURE OF ACCOUNTING POLICIES, Section PS 2100 to consider emerging technology in displaying information in the notes;
- references to "measurement uncertainty" in particular renaming Section PS 2130, Measurement Uncertainty, to "Section PS 2130, Estimation Uncertainty", as the standard speaks solely to "estimation uncertainty";
- references to "service capacity" as service capacity in the proposed Conceptual Framework is being defined to be much broader than it is currently defined in the PSA Handbook; and
- references to "reliability" as this qualitative characteristic is being replaced by "representational faithfulness" in the proposed Conceptual Framework.

Refer to the [Exposure Draft, "Consequential Amendments Arising from the Proposed Conceptual Framework"](#) for further information on these consequential amendments.

In Brief

A plain and simple overview of PSAB's Exposure Draft, "The Conceptual Framework for Financial Reporting in the Public Sector"

Next steps

The deadline for comments is
May 12, 2021.

Comment on the proposals

This is a once-in-a-generation chance to weigh in on the concepts that will affect public sector standard setting for years to come. Read the [Exposure Draft, "The Conceptual Framework for Financial Reporting in the Canadian Public Sector"](#) and our various supporting materials.

Submit your feedback by taking part in the [Connect.FRASCanada.ca project](#) or submitting a [comment letter](#).

We value your input and look forward to your feedback.

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