Public Sector Accounting Discussion Group

Report on the Public Meeting

January 7, 2014

The Public Sector Accounting (PSA) Discussion Group is a discussion forum only. The Group's purpose is to support the Public Sector Accounting Board (PSAB) by enabling discussion in a public venue of issues arising from the application of the CPA Canada Public Sector Accounting Handbook (PSA Handbook). The Group comprises members with various backgrounds who participate as individuals in the discussion. Any views expressed in the public meeting do not necessarily represent the views of the organization to which a member belongs or the views of PSAB. The discussions of the Group do not constitute official pronouncements or authoritative guidance.

This document has been prepared by the staff of PSAB and is based on discussions during the Group's meeting.

Comments made in relation to the application of the PSA Handbook do not purport to be conclusions about acceptable or unacceptable application of the PSA Handbook. Only PSAB can make such a determination.

Items Presented and Discussed

ITEMS PRESENTED AND DISCUSSED

Section PS 1201: Presentation of Budget Information

Questions have been raised related to the presentation of budgeted results as required by *Financial Statement Presentation,* paragraphs PS 1201.130-.133. The most significant issue relates to the term "originally planned" and the applicability of the requirements to governmental units.[1]

Issue 1 – What does "originally planned" mean?

The standard does not define originally planned.

View 1

This view is based on paragraph PS 1201.131 being read literally that "originally planned" is the original budget that was approved by the appropriate level of authority in the entity. This may be the original budget as approved by council for levying property taxes or by the board of a governmental unit (i.e., those charged with governance.)

View 2

This view considers that there should be an ability to use the amended budget for governmental units. Governmental units often prepare amended budgets, sometimes required by the funding government, as further information becomes available. This could be a result of the notification of additional funded programs (such as Ministry funding to hospitals) and/or a change in the underlying source related to government funding (such as enrolment for school boards). The amended budget may be approved by the board of the governmental unit. In some cases, the funding government may prepare the amended budget on behalf of the governmental unit.

As the requirement to present a budget is to meet the objective of legislative control and financial accountability, the significance of the amounts "originally planned" may become less relevant and the amended budget may be more appropriate. However, numerous amendments to the budget make it difficult to assess accountability.

View 3

This view does not require the budget to be approved by the board.

This view may provide a more comparable budget to actual results as some organizations do not include the full breadth of their organization in their annual approved budget. Taken to an extreme, a budget may be approved by the board that relates solely to office administration and not include any of

[1] Governmental units are those government organizations that are not government business enterprises (GBEs). As the Introduction to the Public Sector Accounting directs GBEs to adhere to the standards applicable to publicly accountable enterprises in the CPA Canada Handbook – Accounting, this discussion does not apply to government organizations that are GBEs. Similarly this discussion does not apply to government not-for-profit organizations that have not yet adopted the standards in the PSA Handbook without Sections PS 4200 to PS 4270.

the programs that are administered by the governmental unit. Individual budgets may have been prepared by management for the funded programs, but the budget is likely to correspond with the timing of the program funding and may not correspond to the fiscal year end of the governmental unit.

Issue 2 – Are there any governmental units that should be outside the scope of this requirement under Section PS 1201?

View 1

The comparison of actual and budgeted financial results provides key accountability information and should be included for all publicly accountable organizations.

View 2

The PSA Handbook does not include an explicit requirement for governmental units to prepare a budget but requires organizations to include the budget within their financial statements. Therefore, some would view this as being only required when there is a formal process to prepare and approve a budget. Advocates of this view would also indicate that the key measure is not how funds were spent in accordance with budget but how the entity used the funds in various programs during the year.

Under International Public Sector Accounting Standard (IPSAS) 24, *Presentation of Budget Information in Financial Statements*, budget figures are presented by an entity that is required or elects to make their approved budgets publicly available. So advocates of this view would align with IPSAS 24 in that the PSA Handbook does not explicitly indicate that a budget is to be prepared and if there is no other legislative or other authority mandating it, disclosure of budget to actual would not be required under the PSA Handbook.

The Group's Discussion

Group members observed paragraph PS 1201.130 requires use of the budget originally approved by the legislature, council or body that governs an organization for the comparison of results. Accordingly discussion focused on application issues, cited in the alternative views for both issues.

Group members discussed an example whereby a funding government, subsequent to the adoption of the original estimates, requires school boards controlled by it to amend their budgets. The amendments could arise either from updated enrollment information or a new program initiative.

Several Group members expressed the view that the results for the accounting period presented in the school boards' financial statements should be compared to the original budget. Management has the opportunity to report the reasons behind the variances. The original and amended budgets could be included in a management discussion and analysis or, in the case of those entities who do not prepare an annual report, in a note to the financial statements.

Group members noted that the school boards' original budgets formed the basis of the funding for government's own process of setting its revenue requirements. If the school boards were to compare their results to budget figures that were amended, this would create inconsistencies in the base line information used for accountability.

An application issue occurs in the event of an election resulting in the adoption of a new budget by the legislature. In such a case, if the new government also required entities controlled by it to adopt a new budget, some Group members explained both the new government and the organizations controlled by it would present amended figures instead of budget figures adopted by the preceding administration. The rationale for this view is that following an election there is, in effect, a new government that would now be accountable for its budget as opposed to what was previously tabled. Other Group members did not support this interpretation of the standard.

View 3 in Issue 1 describes circumstances where the scope of budget does not align with the scope of the operations reported on in the consolidated financial statements. Group members noted that situation is addressed in paragraph PS 1201.131: "Planned amounts should be presented for the same scope of activities and on a basis consistent with that used for actual amounts."

It was apparent from the discussion that both governments and governmental units can encounter situations where a budget does not cover the same scope of activities as reported on in the consolidated financial statements. Group members observed that a note disclosure could be used to inform readers of limitations that may exist in the budget figures. Paragraph PS 1201.132 addresses this situation:

"On the statement of operations or the statement of change in net debt, when the scope of financial activity reported in the fiscal plan is not the same as that reported in the financial statements, it may be necessary to restrict the comparison of actual and budgeted results to the scope of financial activity reported in the budget or main estimates of expenditures. This comparison would be presented in a note or supporting schedule. To ensure that this disclosure is reconcilable to the information reported in the financial statements, a government would highlight the differences between the reporting entity used for the financial statements and that used for the fiscal plan."

One Group member explained another situation that can give rise to an application issue. The situation was described as follows: a provincial government funds a new program initiative to be managed by municipalities. A municipality receives funds but as the program announcement occurred after its budget by-law was passed, the budget for the new program is approved in a separate by-law.

In discussing this situation, the Chair asked Group members to consider what is in the best interests of the users of financial statements. Some group members expressed the view that updating the budget figures would make the budget-to-actual comparison easier to understand. As a new program, the "first plan" for the new program can be considered as being "originally approved" budget. Other Group members did not support this approach, saying new program announcements are commonplace and only amounts approved in the initial budget by-law can be considered "originally approved". In their view, the users' best interests were served by enhancing disclosures to explain the variances that would inevitably arise when the new program is not contemplated in the original budget.

A variation on this situation is described in Issue 2 View 2. Group members observed that when a budget is not prepared, or it is not reviewed and approved by those charged with governance, this should be highlighted in a note disclosure. The discussion also touched on the situation where the budget is not prepared on a basis consistent with that used to report the actual results. As paragraph

PS 1201.133 indicates, it would be necessary to provide a reconciliation of the restated information with that originally presented in the fiscal plan.

Other Group members commented that the circumstances of governmental units were sufficiently different from those of governments to consider alternatives to the approach set out in paragraphs PS 1201.130-.133. In justifying these comments, these Group members observed that the mandates of governmental units vary from those of government and circumstances attributable to the control exercised by governments necessitate some flexibility in the budget figures a governmental unit uses for its comparison.

The Chair indicated that in addition to making PSAB aware of the application issues identified during the discussion, he will suggest efforts be made to communicate the value of using the original budget as a basis for a comparison with results.

Section PS 1201: Reporting on Financial Position by a Governmental Unit

Is the net debt model (including the net debt presentation in the statement of financial position and statement of change in net debt) a required presentation for governmental units?[2]

Issue

The Introduction to Public Sector Accounting Standards states: “The standards in the CPA Canada PSA Handbook generally meet the needs of users of general purpose financial statements of other government organizations.”

This implies that the entire PSA Handbook is applicable to other government organizations.[3]

Section PS 1201, *Financial Statement Presentation*, provides the general financial reporting principles and presentation and disclosure requirements for government financial statements. Financial statements are intended to serve as a means by which a government demonstrates its accountability for its resources, obligations and financial affairs.

Throughout the standard, the net debt figure (the difference between liabilities and financial assets) is described as an important indicator of financial position and the statement of change in net debt as a statement that provides an important understanding of the changes in financial assets and liabilities of a government. The standard conveys that the net debt figure is important because it reflects a

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3 “Other government organizations” is the term that applies to government organizations that are neither GBEs nor government not-for-profit organizations.

government's future revenue requirements, and its ability to finance its activities and meet its liabilities and commitments. Paragraph PS 1201.006 requires net debt to be clearly identified.

View 1

Paragraph PS 1201.031 clearly states that financial statements should include a statement of change in net debt, while paragraphs PS 1201.037 and PS 1201.040 state that net debt must be presented on the statement of financial position. As a result, all entities reporting in accordance with the PSA Handbook must follow the net debt model. PSAB clarified this view in an article in the PSAB Matters August 2012 newsletter titled: "Indicator 1: Net debt or net financial assets."

> "Net debt or net financial assets, representing the difference between liabilities and financial assets, indicates whether an entity can afford additional spending. A public sector entity reports a net debt when liabilities exceed financial assets at the end of an accounting period. It indicates the extent debt and other liabilities were taken on by the entity and its net future revenue requirements to pay for them. A public sector entity reports net financial assets when financial assets exceed liabilities at the end of an accounting period. It indicates the extent of net financial resources that are available to finance future operations and spending."

View 2

The presentation of net debt and the statement of change in net debt are not required for governmental units for the following reasons:

- Section PS 1201 only refers to governments and the government reporting entity that leaves it open to interpretation as to whether governmental units can determine what is important (for example, present a standard balance sheet only or present a standard balance sheet and disclose the net debt figure).
- The net debt indicator is not a key indicator for a governmental unit. Net debt is a measure of future revenue requirements, which is very important and meaningful to governments. However, for other governmental units, their ability to continue as a going concern is completely dependent on the government controlling them. Therefore, the measure of net debt is not a true indicator of their future revenue requirements or of their ability to sustain their operations as an organization.
- For many governmental units, their operations may actually be financed by debt at the government level. Thus, the net debt figure, while showing the ability of the government to provide future services, would not convey a governmental unit's ability to fulfil its not-for-profit mandate or provide social services. Thus, in some cases, an entity may show net financial assets while the controlling government, in fact, has net debt.

View 3

Are there some fact patterns where net debt is a key indicator to governmental units and some where it isn't?

The Group's Discussion

The majority of Group members supported View 1. Applying Section PS 1201 and reporting the net debt measure contributes to an understanding by governmental units of the overall financial reporting accountabilities of their controlling government.

It was acknowledged that the net debt model is not intuitive for those who are new to it. Most financial professionals are trained and are comfortable with the presentation framework applied by profit-oriented entities. The Group members who supported the relevance of the net debt model felt its use supported better conversations between public sector entities and those ministries of the government to which they are accountable. The focus of the net debt model is to make it clear as to what funds would ultimately have to be raised from future taxes.

Some Group members expressed the view that PSAB should assess the value of applying the Section PS 1201 reporting model to governmental units. It was observed that inconsistencies arising from Section PS 3410, *Government Transfers*, can work to diminish the usefulness of the measure of net debt when the financial statements report large deferred capital contributions.

Another Group member supported the need for PSAB to review presentation of financial information by governmental units. This Group member asserted governmental units manage their financial position by assessing the key components of their net assets (restricted, unrestricted, capital assets and amounts subject to internal restrictions).

The Chair indicated he would ask PSAB to consider the need for additional outreach or, whether a more fundamental assessment of the information needs of the users of the financial reports issued by governmental units is warranted.

Section PS 2120: Adjustments Made in a Period Subsequent to Identification of an Accounting Error

The treatment of errors identified in a period by an auditor, but not corrected by a government until a subsequent period is addressed in *Accounting Changes*, paragraph PS 2120.31. Other accounting frameworks being applied in Canada approach the reporting of an error in a different manner. As well, the requirement that a correction made in a subsequent period is not considered an error may be interpreted inconsistently, which has reporting implications.

Issue

Paragraph PS 2120.31 states:

> "An issue raised with a government by its auditor in one period but not corrected by the government until a subsequent period is not an error, for purposes of this Section; the issue would be accounted for in the period in which the correction was made."

The guidance in paragraph PS 2120.31 differs from other accounting frameworks generally accepted for use in Canada. Under these other frameworks, the treatment of an error corrected in a subsequent period is not affected by a past discussion of the matter. Correction of an error in a subsequent period results in:

- restatement of the comparative figures for the prior periods presented in which the error occurred; or
- if the error occurred before the earliest prior period presented, restating the opening balances of assets, liabilities and equity for the earliest prior period presented.

As a result of the provision in paragraph PS 2120.31, entities applying the PSA Handbook do not restate prior year's figures (including opening surplus or deficit) for the effects of an error that was the subject of a discussion between the entity and its auditor in an earlier reporting period.

We understand through discussions with PSAB staff that the guidance is to support the goal of accountability in the preparation of financial statements. Should a government not choose to correct an error in the period presented, the requirement to reflect the correction in the period it is corrected ensures that the item is recorded in the current period revenues and expenses and is compared to the budget originally presented by the governmental unit.

There are concerns that:

- awareness needs to be raised about this difference between the frameworks; and
- the words "is not an error" in paragraph PS 2120.31 may be interpreted to mean that reflecting the amount in the current period's financial statements is viewed to be fair presentation in accordance with the PSA Handbook and not a misstatement of the results of the period.

There are implications for the communications of auditors who must identify and evaluate misstatements. Canadian Auditing Standards in the CPA Canada Handbook – Assurance require an auditor to communicate misstatements to management and those charged with governance, and to consider if a modification to the auditor's report is necessary. Is there a misstatement in the current or a prior period if management has presented the matter in accordance with paragraph PS 2120.31?

Fact Pattern 1

In 20X1, there is a single cut-off error related to expenses. Expenses and accounts payable are understated in 20X1 by a material amount. The matter is identified by the government's auditor. The government chooses not to correct the error in 20X1. In 20X2, the government records and pays the expense.

In 20X1, the auditor communicates the misstatement to management and those charged with governance and, the auditor issues a qualified audit opinion.

In 20X2, the financial statements include the expense that was not reported in 20X1. There are two views on the reporting implications.

View A

While expenses are presented in accordance with the requirements of paragraph PS 2120.31, the auditor still needs to consider whether the 20X2 financial statements are fairly presented. Expenses for

20X2 are overstated by a material amount. Accordingly, the misstatement is communicated to management and those charged with governance. The auditor issues a qualified opinion on the 20X2 financial statements.

View B

There is no misstatement as expenses for 20X2 are presented in the financial statements as paragraph PS 2120.31 requires. There is no communication of the overstatement of expenses by the auditor, nor is there a qualification on the financial statements as they are presented in accordance with requirements in the PSA Handbook.

Fact Pattern 2

Fact Pattern 1 applies but the error discovered and reported to management and those charged with governance is not material. Therefore, the focus of this illustration is not on whether the opinion is qualified, but rather on reporting the error to management and those charged with governance in 20X2. There are two views on the reporting implications.

View A

While expenses are presented in accordance with the requirements of paragraph PS 2120.31, the auditor still needs to consider whether the 20X2 financial statements include an error. Accordingly, the misstatement is communicated to management and those charged with governance.

View B

There is no misstatement as expenses for 20X2 are presented in the financial statements as paragraph PS 2120.31 requires. There is no communication of the overstatement of expenses by the auditor as they are presented in accordance with requirements in the PSA Handbook.

The Group's Discussion

Group Members initially discussed Fact Pattern 1. Group members acknowledged an apparent conundrum as application of paragraph PS 2120.31 presents a figure for expenses in 20X2 that is arguably overstated. Group members asked PSAB staff to provide some historical perspective on the origins of this requirement. Applying the fact patterns cited, paragraph PS 2120.31 works to ensure an expense knowingly excluded from the statement of operations in 20X1 will flow thorough expenses in 20X2. Paragraph PS 2120.31 ensures all expenses are at some point reported in the statement of operations. If the expense was presented as a charge to the opening deficit, the expense would never affect the annual measure of surplus or deficit. The annual surplus or deficit of a government is widely reported and a common accountability measure. Limited attention is given to restatements of the figures of a prior year.

Group Members noted an apparent conflict between the mandate in Canadian Auditing Standards for an auditor to communicate significant audit findings to those charged with governance and the treatment of errors under paragraph PS 2120.31. It is not apparent how reporting this overstatement of expenses is relevant when the public sector entity complies with paragraph PS 2120.31.

Group members acknowledged the circumstances in Fact Pattern 2. Despite the fact that the amount involved is not material, the matter might still require communication to those charged with governance.

The Chair indicated he would report to PSAB on the concerns identified during this discussion and of the need to raise awareness in the case of this difference between the PSA Handbook and other accounting frameworks.

Sections PS 2510 and PS 3230: Presenting Debt Obligations of a Government Business Enterprise

The PSA Handbook is silent on how to report debt when, in a period subsequent to a debt issue, a governmental unit[4] is reclassified as a government business enterprise (GBE) and the conditions in *Long-term Debt*, paragraph PS 3230.12(c), are satisfied.

Fact Pattern

A governmental unit is reclassified to a GBE and, at the time of its reclassification, there are outstanding debt obligations issued by the government specifically on its behalf.

In some jurisdictions, the government issues virtually all of the debt for its government organizations including debt required by GBEs. The classification of a government organization does not impact how this debt is issued by the government. As a result, borrowings specifically on behalf of the governmental unit are issued by the government in exactly the same manner as borrowings specifically on behalf of a GBE.

Section PS 3230 provides guidance on how to account for debt issued on behalf of GBEs. This guidance is clear on how to account for debt issued specifically on behalf of GBEs in a period in which an organization is classified as a GBE. The PSA Handbook also provides specific guidance in paragraph PS 3230.13 on how to account for debt in a period subsequent to its issue, where an organization no longer satisfies paragraph PS 3230.12, or essentially no longer meets the definition of a GBE. The PSA Handbook fails to provide specific guidance is how to report debt in a period subsequent to its issue, when a government specifically borrowed on behalf of a governmental unit and that governmental unit has been reclassified to a GBE. To summarize, the guidance in Section PS 3230 is not clear whether an organization needs to be a GBE at the time debt is issued in order to satisfy paragraph PS 3230.12. It would seem reasonable to look to paragraph PS 3230.13 and apply the opposite in this situation; however in the absence of specific guidance, there are conflicting opinions on how to account for such debt.

Section PS 2510, *Additional Areas of Consolidation*, provides guidance on how to account for a change in classification of a governmental unit to a GBE. Specifically, paragraphs PS 2510.42 and PS 2510.44 recommend that the governmental unit be accounted for using the modified equity method from the date its status changes, and that the financial position and results of prior periods not be adjusted to

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4 Governmental units are those government organizations that are not government business enterprises (GBEs).

reflect the change in status of the organization. This guidance is clear and, as such, the accounting treatment in the period prior to its reclassification was not restated. Section PS 2510 does not clarify how to apply paragraphs PS 3230.10 and PS 3230.12 and, therefore, is not relevant to the issue.

Alternative Views

When a government organization is reclassified from a governmental unit to a GBE subsequent to the period in which debt was issued specifically on its behalf, two alternative views have been identified.

View 1

Continue to report the debt in accordance with paragraph PS 3230.06, presented as a liability with the related receivable from the GBE as a financial asset in the consolidated statement of financial position. This assumes that in order for paragraph PS 3230.12 to be satisfied, a debt issue must be made specifically on behalf of an organization during a period in which an organization is classified as a GBE.

View 2

Begin reporting the debt in accordance with paragraph PS 3230.10, with the debt and the related receivable from the GBE presented on a net basis in the consolidated statement of financial position. This assumes that paragraph PS 3230.12 can be satisfied subsequent to the date of a debt issue upon a government organization being classified as a GBE.

The Group's Discussion

Group members supported View 2. When the conditions outlined in paragraphs PS 3230.11-.12 are met, under View 2 the government presents the related debt obligations in accordance with paragraph PS 3230.10. In the circumstances described in the fact pattern, the amount owed to the government by the GBE would be offset against the related debt obligation in the issuing government's consolidated financial statements.

View 2 was favoured over View 1 as it reflects the current status of the organization as a GBE. The status of the organization, a governmental unit when the debt was issued, is not considered to taint the debt as that of a governmental unit. However, Group members observed there is no restatement of the financial position and results of prior periods, which is not permitted under *Additional Areas of Consolidation*, paragraph PS 2510.44. Any changes in presentation arising from the reclassification of the governmental unit as a GBE apply from the date of the change in the government organization's status.

Group members did not recommend adding guidance to the PSA Handbook on this matter.

Additional Discussion

Following consideration of the submission, there was a discussion about the use of the modified equity method when governments report on their GBEs. Unlike other controlled entities, the debt obligations of GBEs are excluded from the total debt liabilities of the controlling entity as the investment balance that is reported is net of any debt obligations the GBE has. This discussion touched on the origins of the requirement and whether the public interest is well served by the current approach. The Chair indicated that he would include this discussion in his meeting summary to PSAB.

Section PS 3260: Determining When Assets Are "No Longer in Productive Use"

Questions have been raised on the scope of application for Section PS 3260, *Liability for Contaminated Sites*. These questions relate to whether contamination of a site that is currently in productive use is within the scope of the standard and what is meant by "productive use" as it is not a defined term.

Defining the scope of the standard is critical as entities begin to prepare to apply this standard for fiscal periods beginning on or after April 1, 2014. From a work effort standpoint, entities only want to consider sites that are within the scope.

Issue 1 - Are sites that are currently in productive use within the scope of Section PS 3260?

View 1 – They are not within the scope of Section PS 3260

Subparagraphs PS 3260.05(a), (b), and (c) provide examples of items that would normally result in a liability and all three examples refer to the sites no longer in productive use. In addition, paragraph PS 3260.06(b) states that the asset retirement obligation for an asset currently in productive use would not be within the scope of the standard. Proponents of this view believe that the examples in paragraphs PS 3260.05-.06 make it very clear that sites currently in productive use are scoped out of the standard.

It should be noted that proponents of this view agree a liability within the scope of Section PS 3260 could arise on a site in productive use as a result of an unexpected event as described in paragraph PS 3260.05(d). It is contamination that is a result of the current or a previous use of the site that they believe would not be within the scope of this standard.

It is also important to note that proponents of this view do not believe the scope of Section PS 3260 would prevent the recognition of a liability meeting the definition in Section PS 3200, *Liabilities*. For example, if remediation of the site was currently demanded, a liability would be required regardless of whether the site was in productive use or not.

View 2 – They are within the scope of Section PS 3260

This view is based on the presumption that subparagraphs PS 3260.05(a), (b) and (c) are only examples and paragraph PS 3260.06(b) was meant to only exclude asset retirement obligations. Proponents of this view would point to paragraph PS 3260.04, which defines a contaminated site as a site at which substances occur in concentrations that exceed the maximum acceptable amounts under an environmental standard and, therefore, this standard applies to all sites that meet this definition.

View 2A – Sites that are in productive use are within the scope, however, the liability would exclude amounts related to asset retirement

This view is similar to View 2. The costs of retiring an asset from productive use would include remediation of contamination, but exclude costs not related to contamination such as the removal of equipment and buildings. Proponents of this view believe it is these non-contaminated related costs that are be excluded from the scope by paragraph PS 3260.06(b).

The Group's Discussion

Group members observed inquiries are increasing as entities prepare to implement the standard. Entities are seeking to focus their efforts, including the engagement of experts, on sites within the scope of the requirements. Group members noted the recognition criteria in Section PS 3260 may lead an entity to conclude many sites evidencing pre-existing contamination, exhibit the characteristics associated with contamination liabilities. It was suggested that View 2 captures this desire to address a broad range of liabilities associated with contamination, as the scope of View 2 is broader than the scope of View 1. Several Group members explained that they have observed governments that put in place accounting policies to address site contamination prior to this standard being issued, do not generally distinguish between liabilities associated with assets in productive use and those that are not in productive use.

One Group member noted Section PS 3260 results in recognizing the full liability for estimated cost of remediation at the financial statement date. Contrast this with standards that apply to asset retirement obligations, where recognition of the estimated cost of remediation occurs over the useful life of the asset. This explains why paragraph PS 3260.06(b) scopes out "liabilities associated with the retirement of a long-lived tangible capital asset in productive use …" PSAB staff confirmed that while it is the eventual aim to address the financial reporting issues associated with assets that are in productive use and those that are not, PSAB initially focused on assets that are not in productive use. A follow-on project is addressing the reporting issues associated with assets in productive use (asset retirement obligations). A statement of principles on asset retirement obligations is expected to be issued in the summer of 2014.

The discussion also clarified the purpose of the reference in paragraph PS 3260.05(d) to "an unexpected event resulting in contamination …" When it is "expected" that activities associated with the use of an asset will result in contamination, the anticipated costs should form part of the estimated liability associated with an asset retirement obligation. The phrase "unexpected event" aims to result in the recognition of any liabilities that were not anticipated and warrant immediate recognition.

Issue 2 – What is the definition of productive use?

View 1 – Productive use is linked to the use before contamination

The standard does not define productive use. The only reference to "use" is in paragraph PS 3260.42 related to measurement, which states: Estimated costs would be those required to bring a site up to the current minimum standard for its use prior to contamination.

If we were to link this paragraph to the definition of productive use, any site not being used in the same manner for which it was being used prior to contamination, would be considered to be not in productive use.

View 2 – Any use of the site would be considered productive use

To explain this view it is best to use an illustration:

A site that was previously a gas station has been paved over and is currently being used as a municipal parking lot. The site is contaminated and contamination exceeds the environmental standard for use of the site other than as a parking lot. If this site was to be used as a gas station again, the contamination currently exceeds the minimum standard for use as a gas station and therefore costs would have to be incurred to bring the site up to this minimum standard. The site currently meets the minimum standard for use as a parking lot and, as a result, would not meet the definition of a contaminated site as defined in paragraph PS 3260.04.

Proponents of this view would argue that any use of a site would require the site to meet the minimum standard for that use and, therefore, as long as the site continues to be used in that manner, it is not considered a contaminated site. As a result, View 2 is consistent with View 1 in Issue 1.

View 3 – Productive use is a "good use" of the site

Proponents of this view generally do not agree with View 1; however, they feel View 2 could lead to abuse. For example, under View 2, a site could be excluded if only a small portion of the site is being used or if it is being used in manner that provides minimal value or service potential to the entity.

This view would require the use of significant professional judgment to determine if the current use is a good use of the site. An extreme interpretation of this view would be to apply the "highest and best use" concept in International Financial Reporting Standard (IFRS) 13, *Fair Value Measurement*.

The Group's Discussion

Group members discussed measurement of the liability and implications associated with the statement in paragraph PS 3260.42 that the "estimated costs would be those required to bring a site up to the current minimum standard for its use prior to contamination." The measurement approach described in View 2 was supported by several Group members as long as the estimate is representative of the legal obligation associated with remediation. A Group member observed that when remediation contains the contamination, the entity may have satisfied its legal obligations.

One member supported View 1. Several members supported View 2 but, in doing so, expressed the concern that applying paragraph PS 3240.42 in the strictest sense could result in the need to accrue costs over and above those needed to comply with legal obligations to remediate the site. A view was that it would be desirable to clarify this provision in the standard. Other members supported View 3.

In concluding discussion of the item, the Chair expressed the view that Group members reached a consensus on the need to establish a liability for contaminated sites. When the contamination is associated with a long-lived tangible capital asset in productive use, an accounting policy for its recognition and measurement would consider standards that apply to the reporting of asset retirement obligations. In other cases, Section PS 3260 would apply.

The Chair indicated that he will apprise PSAB that there is a need to be cognizant of the potential for boundary issues in developing the statement of principles on asset retirement obligations.