International
Public Sector
Accounting
Standards Board

Consultation Paper

March 2008

Comments are requested by July 15, 2008

Social Benefits: Issues in Recognition and Measurement

International Federation
of Accountants

REQUEST FOR COMMENTS

The IPSASB welcomes comments on the proposals in this Consultation Paper. Please submit your comments, preferably by email, so that they will be received by **July 15, 2008**. All comments will be considered a matter of public record. Comments should be addressed to:

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International Federation of Accountants
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Email responses should be sent to: edcomments@ifac.org

Copies of this consultation paper may be downloaded free-of-charge from the IFAC website at http://www.ifac.org.

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SPECIFIC MATTERS FOR COMMENT

The IPSASB welcomes comments on all of the proposals in this Consultation Paper. Comments are most useful when they include the reasons for agreeing or disagreeing. If you disagree please provide alternative proposals. You are also asked to provide details of current policies for recognizing and measuring liabilities for programs that deliver social benefits in your jurisdictions

1. Do you agree that, within the constraints of the current implied conceptual framework for general purpose financial reporting, current financial statements such as the statement of financial position and the statement of financial performance cannot convey sufficient information by themselves to users about the financial condition of governmental programs providing social benefits? Please state your reasons.

2. Do you think that a present obligation to individuals or households arises at any time for:

   a) Collective goods and services; and/or

   b) Individual goods and services?

   If you think a present obligation does arise for either (a) or (b) or both (a) and (b) please indicate when and indicate your reasons.

3. Do you think that a present obligation to individuals or households in respect of cash transfers arises when all eligibility criteria have been satisfied for:

   a) Non-contributory programs; and/or

   b) Contributory programs?

   If you think that a present obligation arises at an earlier point for (a) or (b) or both (a) and (b), please indicate that point and give your reasons.

4. Where a cash transfer program requires individuals or households to revalidate their entitlement to benefits, do you think that revalidation is an attribute that should be taken into account in the measurement of the liability or a recognition criterion? Please state your reasons.

5. Do you think that in developing requirements for recognition and measurement of social benefits the IPSASB should further explore the executory contract accounting model briefly outlined in Key Issue 6. Please state your reasons.

Social Benefits: Issues in Recognition and Measurement

The IPSASB Strategy on Accounting for Social Benefits

1. The purpose of this Consultation Paper is to:
   - Explain the IPSASB's strategy for developing approaches to address the issues involved in accounting for social benefits, including the reason for initiating a project on long-term fiscal sustainability reporting;
   - Explore some key issues in recognizing and measuring liabilities and expenses related to social benefits; and
   - Spread knowledge, and stimulate discussion, of current approaches to recognizing and measuring liabilities and expenses for different types of programs delivering social benefits in particular jurisdictions.

Background

2. IPSAS 19, "Provisions, Contingent Liabilities and Contingent Assets" was issued in October 2002. Social benefits provided in non-exchange transactions were, however, excluded from the scope of IPSAS 19. An Invitation to Comment, "Accounting for Social Policy Obligations" was issued in January 2004. The ITC proposed that the principles in IPSASs should be applied to accounting for social benefits provided in non-exchange transactions. Comments from constituents generally supported this proposal, and the IPSASB decided to use the principles of IPSAS 19 to develop recognition and measurement requirements for social benefits provided in non-exchange transactions.
3. The IPSASB commenced a further stage of its project in April 2005, intending to develop an Exposure Draft of an IPSAS that proposed requirements for identifying present obligations related to all social benefits and recognizing and measuring liabilities.
4. In developing an exposure draft, the IPSASB considered:
   - The objectives of general purpose financial reports (GPFRs) in the public sector, in particular the GPFRs of governments responsible for providing social programs, and how best to meet the information needs of users;
   - Whether the financial position of governments would be faithfully represented by recognizing liabilities associated with expected future outflows for social programs, while at the same time not recognizing the future inflows of future tax revenue as an asset; and
   - The appropriateness of the current definitions in IPSASs, in particular those in IPSAS 19 associated with liabilities.
5. In considering these issues the IPSASB concluded that, within the constraints of its current implied conceptual framework for general purpose financial reporting, traditional approaches to liability recognition may not be suitable for conveying information to users about the future provision of social programs by governments. In doing so, the IPSASB acknowledged the limitations of the primary financial statements including the statement of financial position and notes thereto. These limitations exist because, although primary

financial statements use estimation techniques to measure liabilities by reference to settlement amounts in future reporting periods, they focus primarily on past events.

6. This view led the IPSASB to consider other ways of conveying relevant information about social benefit programs to users. The IPSASB saw merit in requiring disclosures within the GPFRs about amounts expected to be transferred to individuals or households presently eligible for benefits under social programs. It therefore developed an Exposure Draft (ED) 34, "Social Benefits: Disclosure of Cash Transfers to Individuals or Households." The IPSASB acknowledged that this is a preliminary step, of itself insufficient to satisfy user needs completely.

7. The IPSASB also began to explore the role that disclosures about long-term fiscal sustainability reporting could play in helping to convey relevant information to users about the future viability of a government's social programs. Although the IPSASB accepts that there is uncertainty associated with such information, it considers that such information is highly relevant.

Strategic Approach to Addressing Social Benefits Accounting Issues

8. Therefore the IPSASB has concluded that:

   - The proposed disclosure requirements in ED 34 represent an important first step in signaling the importance of governments providing users with relevant information about their social programs,
   - Further consultation should be carried out on certain key issues relating to the recognition and measurement of liabilities and expenses relating to social benefits, as a step in developing further guidance, and
   - A project should be initiated to assess whether disclosures about long-term fiscal sustainability might enhance the reporting of the impact of such programs by complementing the information reported in the GPFRs.

Conceptual Framework Projects

9. The IPSASB's Conceptual Framework project was initiated by the IPSASB in collaboration with a number of national standard setters in mid 2006. The project has already considered broadening (a) the objectives of financial reporting to include *accountability* and (b) the scope of financial reporting to include *general purpose financial reporting*, not just *general purpose financial statements*. The project has also recognized the long-term fiscal sustainability of social benefit programs as an aspect of financial reporting that could be significant to discharging accountability in the public sector. Also, the project has a component dealing with the elements of financial statements that will address the definitions of assets and liabilities. This is particularly significant, because many consider that applying the existing definitions of assets and liabilities in IPSASs would not lead to a faithful presentation of governmental responsibility for delivering social benefits in the future.

10. The IASB is revising its own Conceptual Framework and is also conducting a fundamental review of its Standard, IAS 37, "Provisions, Contingent Liabilities and Contingent Assets,"

on which IPSAS 19 was based. Developments in thinking as a result of both projects and the development of the IPSASB's Conceptual Framework are likely to influence the development of further approaches to recognizing and measuring liabilities related to all social benefits.

Long-term fiscal sustainability reporting

11. In its 2007-2009 Strategy and Operational Plan, the IPSASB stated its intention to initiate a project on long-term fiscal sustainability reporting and has issued a project brief on that subject. It welcomes comments on that brief.

12. At a very high level, fiscal sustainability involves an assessment of the extent to which governmental obligations under existing legal frameworks can be met in the future. The analysis of fiscal sustainability therefore takes account of both current and future eligible individuals or households, regardless of whether obligations to them exist at the reporting date. Fiscal sustainability is sometimes coupled with the concept of inter-generational equity, which evaluates the extent to which future generations of taxpayers will have to deal with the fiscal consequences of policies currently delivering social benefits in the form of goods and services.

13. Fiscal sustainability reporting may be a more versatile accountability tool than accrual-based financial statements, because such reporting involves the projection of inflows as well as outflows. Already a number of jurisdictions have made impressive progress in developing reports on long-term fiscal sustainability as key aspects of financial accountability, even though no universally-agreed framework exists for preparing such reports.

Conclusion

14. This Consultation Paper is one of three documents published together as an integrated package; the other two are ED 34, "Social Benefits: Disclosure of Cash Transfers to Individuals or Households" and a Project Brief on "Long-term Fiscal Sustainability Reporting."

15. The IPSASB looks forward to receiving comments from interested parties on ED 34, the long-term fiscal sustainability reporting project brief and the key issues relating to recognizing and measuring liabilities related to all social benefits identified in this Consultation Paper.

Social Benefits: Issues in Recognition and Measurement

Definitions

16. The IPSASB defines *social benefits* as;

    (a) Cash transfers; and

    (b) Collective and individual goods and services

    that are provided by an entity to individuals or households in non-exchange transactions to protect the entire population, or a particular segment of the population, against certain social risks."

17. The IPSASB has distinguished three types of social benefits:

Collective goods and services are social benefits in the form of goods and services provided to the entire population or to a particular segment of the population in any jurisdiction, to protect the population or one of its segments against certain social risks. Collective goods and services include national defense and most aspects of the criminal justice system.

Individual goods and services are social benefits in the form of goods and services provided to protect an individual or household against certain social risks. Individual goods and services include healthcare and educational services provided directly to the recipient.

A cash transfer to an individual or household is a social benefit, which is either provided directly in cash, or is an expense paid through the tax system, to protect individuals or households against certain social risks where use of the resources transferred is at the discretion of the individual or household**.** Cash transfers include social security pensions, child benefits and unemployment benefits.

18. These terms were used in the ITC, although they have been modified slightly during the course of the project. They are similar to, although not synonymous with, the definitions used in statistical accounting. Access to cash transfers and individual goods and services requires the satisfaction of eligibility criteria by individuals or households. Eligibility criteria are requirements that must be satisfied for entitlement to individual goods and services or cash transfers. Conversely, collective goods and services are automatically consumed by all or part of the population and, therefore, are not normally subject to the satisfaction of eligibility criteria.

19. There is one main distinction between individual goods and services and cash transfers. For individual goods and services the transferor can stipulate the purposes to which the resources must be applied, whereas for cash transfers the recipient has full discretion how to use those transferred resources. The IPSASB acknowledged that, in cases in which the transfer of economic benefits is in the form of goods, it may be possible for the recipient to sell those goods rather than use them for the purposes specified by the transferor. However, this requires a positive further action on the part of the recipient and is likely to be at a distressed value.

20. The IPSASB holds the view that the principles in IPSASs can be applied to the recognition and measurement of social benefits provided in non-exchange transactions. It has therefore considered how definitions and requirements in IPSAS 19, "Provisions, Contingent Liabilities and Contingent Assets" can be used, in a non-exchange environment, to develop accounting requirements for different types of social benefits. The core of the project has been to determine when obligating events occur for different types of social benefits. It is therefore important to provide a number of definitions included in IPSASB's current suite of Standards that are central to this discussion:

Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.

A *present obligation* only arises from a past event and may be a legal obligation or a constructive obligation. In most cases it is clear whether a past event has given rise to a present obligation. In cases where this is unclear an entity determines whether a present obligation exists at the reporting date.

An *obligating event* is an event that creates a legal or constructive obligation that results in an entity having no realistic alternative to settling that obligation.

A *legal obligation* is an obligation that derives from:

(a) A contract (through its explicit or implicit terms);

(b) Legislation; or

(c) Other operation of law.

A *constructive obligation* is an obligation that derives from an entity's actions where:

(a) By an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and

(b) As a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

Assets are resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.

Structure of the Consultation Paper

21. The majority of this Consultation Paper considers whether and, if so, when (a) obligating events occur and therefore (b) subject to the satisfaction of recognition criteria, liabilities should be recognized for:

- Collective goods and services;
- Individual goods and services;
- Cash transfers for non-contributory programs; and
- Cash transfers for contributory programs.

22. This Paper also considers whether requirements to revalidate eligibility criteria are recognition criteria or measurement attributes. This distinction is important because of the effect on the amount of liabilities recognized. This Paper concludes with a brief section asking whether models should be explored that are not based on IPSAS 19 principles.

23. This Paper only considers non-exchange transactions. Exchange transactions, such as the supply of goods and services under contractual arrangements (for example, a private sector entity providing home care services to aged persons under a contractual agreement with a government agency) are outside its scope,. Throughout this Paper the term "government" is used. The term encompasses all public sector entities.

Key Issue 1: Do present obligations to beneficiaries for collective goods and services occur?

Arguments of those who do not consider that present obligations occur

24. As highlighted above collective goods and services are consumed automatically by all or part of the population and are not normally subject to the satisfaction of eligibility criteria. While the future existence of governments depends on providing collective goods and services (such as defense and criminal justice) at some minimum level in the future, many argue that governments do not have a present obligation to individuals or households for the delivery of collective goods and services. They acknowledge that governments publicly announce future policy intentions, but do not think that such pronouncements are sufficiently specific to give rise to constructive obligations. They also accept that current legal frameworks will require a certain level of provision in the future, but consider that it is important to distinguish present obligations and future obligations or commitments. The general purpose financial statements are only concerned with present obligations.

25. Furthermore the existence of present obligations would lead to recognizing expenses and liabilities where delivery of the goods or services to settle the obligation occurs in subsequent reporting periods. Such an approach would be analogous to a manufacturer recognizing the production costs that will be incurred in future reporting periods on the grounds that it needs to incur such costs in order to remain a going concern.

Arguments of those who consider that present obligations occur

26. Others argue that it is possible for governments to have present obligations for collective goods and services. They consider that, through past practice and public announcements (such as budget reports, policy statements and electoral manifestos), (a) governments have indicated they will continue to provide collective goods and services, (b) citizens have valid expectations that such goods and services will be provided and (c) it is unrealistic for governments to avoid providing such items in the future. The extent of the obligation will depend on the specificity of the past policy announcement.

Key Issue 2: Do present obligations to beneficiaries for individual goods and services occur?

Arguments of those who do not consider that present obligations occur

27. This section of the Paper explores whether present obligations occur for individual goods and services. Those holding the view that governments do not have a present obligation to provide goods and services for individual or household consumption rely on the argument outlined above for collective goods and services–that is, one, or more, of the conditions necessary for the existence of a present obligation has not been satisfied.

Arguments of those who consider that present obligations occur

28. Those who challenge this view put forward similar arguments to those made in asserting that governments have a present obligation to provide collective goods and services. They emphasize that, like cash transfer programs, access to individual goods and services depends on the satisfaction of eligibility criteria. Satisfaction of eligibility criteria increases

expectations that an individual or household will receive goods and services, and makes it more difficult for governments to avoid providing them. They may also question whether the method by which resources are transferred should dictate accounting treatments for programs that are otherwise similar; they consider it inconsistent for governments to recognize liabilities for individuals or households that have met eligibility criteria under programs delivering benefits in cash, but not to recognize liabilities where those benefits are delivered in the form of goods and services. An example of the latter type of program is one that provides medical benefits where (a) the individual is treated by a third party medical provider under a contractual arrangement with a government agency and (b) the agency pays the medical provider directly.

29. Furthermore, they highlight that the line between cash transfers and individual goods and services is sometimes blurred. For example, individuals may be authorized to purchase specified goods or services and be reimbursed for the expenditure incurred. Some programs may provide both cash transfers and individual goods and services. For example, a housing support program may have a cash transfer component and another component in which third party landlords provide accommodation to beneficiaries under contractual arrangements with a government agency. If it is deemed that a present obligation does not occur to beneficiaries for individual goods and services, an entity might recognize the cash transfer component as a liability to eligible individuals or households, but not the component in which the government agency pays the third party landlord directly.

Extent of present obligations

30. Accepting the view that a present obligation exists for individual goods and services raises the issue of the extent of that obligation. The obligation might be narrow or very broad, dependent on (a) the legal framework governing a program and (b) whether a particular stipulation is deemed to operate as an eligibility criterion or merely as an administrative requirement. For instance, in jurisdictions where free or subsidized education or health care is universally available, that availability raises the issue whether the present obligation is for education or healthcare services throughout an individual's life or, more narrowly, whether it depends on an individual meeting the eligibility criteria of specific entities. Such entities include school boards and hospitals, which may establish criteria for admittance to a school roll or acceptance onto a hospital waiting list. Resolution of this issue may depend on whether the focus is on the individual entity, or on an economic entity such as the whole-of-government.

Impact of arrangements for the provision of goods and services by third parties

31. As previously indicated, this Paper does not discuss present obligations and liabilities arising from contracts with employees and third parties for the delivery of goods and services to individuals or households. The accounting treatment of such contracts is likely to be the same as for any other executory contract. There is a view that the existence of contracts for the supply of goods and services for periods beyond the reporting date implies a commitment to provide benefits beyond the reporting date and therefore potentially a present obligation to individuals or households. Others reject such a link, and consider that the accounting treatment of such executory contracts is remote from, and has no relevance

to, the analysis of whether and when present obligations to individuals or households occur in a non-exchange context.

Key Issue 3: When do obligating events occur for cash transfers for non-contributory programs?

32. This section explores when an obligating event to individuals or households occurs for cash transfers for non-contributory programs–programs largely funded from general taxation that do not require contributions by or on behalf of individuals or households to entitle them to resources. There are a number of views regarding when constructive and legal obligations might arise.

Those who take the view that an obligating event does not occur before all eligibility criteria have been satisfied

33. One view is that an obligating event occurs when, and only when, all eligibility criteria have been satisfied, regardless of whether a legal obligation exists at this point. Those holding this view may accept that some individuals or households have expectations that benefits will be paid in the future. They may also accept that past practice indicates that the government accepts a responsibility to provide benefits. However, they consider that until all eligibility criteria have been satisfied, a government does have a realistic alternative to providing benefits by, for example, modifying governing legislation. The consequence of this view is that any liability recognized in the financial statements is limited to amounts that are due to be paid to individuals or households that have satisfied all eligibility criteria at the reporting date. Globally this has become known as the "due and payable" approach.

34. In most cases a legal obligation will likely occur when all eligibility criteria have been satisfied. However, there may be cases when a legal obligation does not occur until a later time. For example, eligibility criteria may have to be satisfied on 1 March, but payment is not legally required until 1 April. Some take the view that a present obligation can only arise as a result of a legal obligation. Under this view a liability does not arise until the date on which a government is legally required to make a payment even though all eligibility criteria have previously been satisfied. In the above example the liability would arise on 1 April not 1 March. Until an individual or household has a legal entitlement the entity can avoid transferring resources.

35. Some would go further than the above argument and contend that such a present obligation does not extend beyond the reporting date. This is because, although legislation for a program is in place, funding of benefits under that program depends on periodic (normally annual) appropriations. Until appropriations been made it is not legal to make the cash transfer, and therefore the government is unable to pay benefits even if all eligibility criteria have been satisfied.

Those who take the view that an obligating event occurs before all eligibility criteria have been satisfied

36. Another view is that an obligating event creating a constructive obligation might occur at a number of points before satisfaction of all eligibility criteria by individuals or households.

These points have been referred to as “key participatory events.” There are a range of potential “key participatory events” and not all these events are relevant to every program.

37. To explain the term “key participatory events,” consider the simplified example of a social security pension program paying benefits to individuals who are 65 or more years of age. There are no other eligibility criteria. Potential “key participatory events” for such a program include, but are not limited to:

- Birth;
- Attaining school age;
- Attaining the minimum age for entry into the workforce; and
- A point between the minimum age for entry into the workforce and 65 years of age.

38. The rationale for maintaining that an obligating event occurs, for example, on entry into the workforce, is that the government has:

- Indicated through a pattern of past practice, published policies or a sufficiently specific current statement, that it will accept the responsibility of paying benefits to individuals when they reach retirement age;
- Created a valid expectation for individuals that it will discharge those responsibilities and that expectation crystallizes when an individual attains the minimum age for entry into the workforce; and
- No realistic alternative to paying benefits after an individual attains the minimum age for entry into the workforce even though the age at which benefits will be paid is many years in the future.

39. This would mean that, if recognition criteria are met, the government would recognize a liability and an expense in respect of the social security pension for individuals when they reach the minimum age for entry into the workforce. The liability and expense would be determined using actuarial principles and would be reassessed at each reporting date.

Practical issues in identifying when an obligating event occurs

40. Some accept that, in principle, an obligating event may occur before satisfaction of all eligibility criteria, but they highlight practical difficulties in identifying that event. Key participatory events may vary between jurisdictions and even between programs within jurisdictions. They may also vary between reporting periods of the same entity for a program as citizen expectations change. For example, in a number of jurisdictions survey evidence shows that younger age groups have lower expectations of a viable social security pension on retirement than older age groups and that those expectations are diminishing. Some consider that this variability would make consistent financial reporting difficult and undermine comparisons between governments. They would therefore prefer to identify the same point at which an obligating event occurs and a liability is recognized for all programs and in all jurisdictions.

41. However, others are less concerned with the fact that the point at which an obligating event occurs may vary between programs and between different entities. They argue that this is

consistent with the principle that different transactions should not be accounted for in the same way. They consider that the term "key participatory event" should be defined as the point, before satisfaction of all eligibility criteria, at which an obligating event occurs. Preparers can then determine when that event occurs, program-by-program. They accept that this event may occur at a different point for similar programs in different jurisdictions, and that this point may fluctuate over time. Even within jurisdictions there may not be a consistent approach to identifying a "key participatory event" in different programs.

42. Those with reservations about recognizing expenses and liabilities before the satisfaction of all eligibility criteria may also question whether such an approach faithfully represents an entity's financial performance and financial position. They believe that recognizing very large expenses and liabilities related to social benefits on the face of the statement of financial performance and the statement of financial position is inappropriate for what they consider are commitments, but not present obligations. Recognition would present a misleading view of financial condition by showing a Government in an unsound financial light when that may not be the case. In this context, most standard setters that have considered the issue currently take the view that a government's right to tax does not give rise to an intangible asset that would counter-balance the amount reported as a liability for these events.

43. Those who do not accept the above argument consider that, transactions and other events that meet currently accepted recognition and measurement criteria should be recognized. According to this view it is not acceptable to exclude items because of their magnitude, and because recognition might not show a government in a sound financial light.

Key Issue 4: Do present obligations for cash transfers financed by contributions occur at an earlier point than for non-contributory programs?

Arguments of those who consider that an obligating event occurs at an earlier point

44. Some consider that whether a program is contributory affects the point at which an obligating event occurs. Contributory programs are sometimes known as "social insurance programs." According to this view, although the conceptual approach taken for Key Issue 3 can be applied, contributory programs should be considered separately from non-contributory programs. This is because it is suggested that an obligating event occurs at an earlier point for contributory programs. Under this view an obligating event occurs earlier because the payment of a specified number, or amount, of contributions creates a valid expectation (or reinforces an existing one) that an individual or household will receive benefits on the basis of a formula under the existing legal provisions governing the program. Such expectations are stronger than for non-contributory programs that are primarily funded from general taxation. Allied to such expectations is the argument that it is unrealistic for the government to avoid paying benefits, even though the point at which payment is required may be many years in the future. This expectation of receiving benefits may be strengthened by other factors such as:

- Individuals receiving or accessing personal details of estimated future benefits on a periodic or real-time basis; or

- The program operating on a trust fund basis, so that fund assets can only be used for the legally specified purposes of the program and cannot be diverted for other governmental objectives.

45. Some argue that an obligating event occurs for a contributory program when an individual has recorded sufficient contributions to become eligible for benefits at a specified future date without taking further action. For example, for the US Social Security program this point is after an individual has been in 40 quarters of "covered" employment i.e., employment for which contributions are paid by or on behalf of an individual. A variant of this view is to acknowledge that an obligating event occurs before all eligibility criteria have been satisfied, but that, until all are satisfied, the amount of any entitlement cannot exceed the amount of an individual's contributions, rather than being determined by an actuarially-based estimate.

46. A different argument, but one that also shares the view that an obligating event occurs before all eligibility criteria have been satisfied, is that contributory programs give rise to quasi-exchange transactions. In this view, obligations under such programs should be recognized and measured in a similar manner to post-employment benefit obligations under IPSAS 25, "Employee Benefits", which is based on IAS 19, "Employee Benefits." According to this view, an obligating event occurs when a contribution is first made by or on behalf of a beneficiary. The fact that a proportion of those making contributions (or for whom contributions are being made), will not build a contribution record sufficient to achieve any entitlement to future benefits is (a) a variable to be taken into account in measuring the liability, but (b) is not a reason for not recognizing a liability.

Arguments of those who do not consider that an obligating event occurs at an earlier point

47. Those who argue that a present obligation does not arise until all eligibility criteria have been satisfied challenge the view that there is an earlier point at which a government has no viable alternative but to pay benefits. They emphasize that governments have the ability to amend or repeal legislation, an attribute that distinguishes them from private sector entities. They may acknowledge that individuals receive personal information on the benefits that they are likely to receive, but note that such communications are often accompanied by caveats or other qualifications, for example, that the payment of projected benefits depends on the future viability of the fund from which those benefits are paid. Therefore they argue that the validity of those expectations is doubtful.

48. Contributory programs vary widely in nature and may also depend partially on general taxation for their funding. Some therefore challenge whether citizens' expectations of receiving benefits in the future for contributory programs are more valid than for non-contributory programs, such as those providing education and housing. Even when a program is non-contributory, individuals may have strong expectations of receiving benefits on the grounds that they are contributing indirectly through general taxation. Dependent upon local circumstances, these expectations may be as strong as if the individuals had made separate contributions, and governments may find it equally unrealistic to avoid providing benefits. Those who emphasize the above factors conclude that accounting for contributory programs should not differ from that for non-contributory

programs and that obligating events occur at the same point, which might be when all eligibility criteria have been satisfied.

49. In some instances fiscal projections suggest that existing benefit levels are unsustainable, and that, assuming that corporate and personal taxation levels and debt levels are viable in a global environment, the government will have little choice but to take action such as raising participants' contributions, reducing benefit levels or deferring the age at which benefits are first received. When programs are administered on a fund basis, benefits may be legally limited to the amount of the accumulated fund balance, so that, under current legislation, at a future point the fund will be exhausted and payments of benefits will not be legally possible unless benefit entitlements or contributions are modified. Therefore, some argue that recognizing liabilities under programs that are unaffordable and unsustainable is misleading, and could not faithfully represent the financial position of a government.

Reservations about relying on the ability of governments to make legislative changes to programs in evaluating present obligations

50. Some disagree with the views identified above. Although they accept that governments have the ability to make legislative changes to existing programs, and that on rare occasions governments have enacted retrospective legislation that repudiates existing liabilities, they are distrustful of a reliance on a government's ability to change legislation when determining the existence and extent of present obligations. They contend that identification of a present obligation should be in the context of the current legislation affecting social benefit programs. They consider that reliance on a government's ability to enact legislative change might be used to disregard a number of obligations, including those that have arisen through exchange transactions. They argue that if a government does modify the legislation affecting social benefit programs, the impact of that change should be reflected in the financial statements for the period in which the change is enacted, and not before. That is, preparers should not prejudge possible changes in legislation. Furthermore, although they acknowledge the tension between legislation specifying the social benefits to be provided and legislation specifying limits on government expenditures or debt, they do not consider that the limited future fiscal sustainability of a program is an adequate reason for not recognizing obligations under current legislation.

Key Issue 5: Is the Revalidation of Eligibility Criteria a Recognition Criterion or a Measurement Attribute?

The Issue

51. This section of the Paper deals with the accounting treatment of the revalidation of eligibility criteria. Many programs delivering social benefits require eligible individuals or households (those who have satisfied threshold eligibility criteria) to revalidate their eligibility at a future date in order to maintain their entitlement to benefits. Requirements for revalidation are normally laid down in the legislation or regulations governing the program. The key issue is whether revalidation is a recognition criterion or a measurement attribute. This decision is significant because it dictates the extent of the present obligation and, if recognition criteria are met, the measurement of the resultant liability.

Arguments of those who argue that revalidation is a recognition criterion

52. Those who believe that revalidation is a recognition criterion consider that the extent of a present obligation cannot exceed the maximum amount that an individual is entitled to receive from one revalidation point to the next. This view is based on the assumption that an entity can avoid further payments beyond the next revalidation date. Some who perceive revalidation as a recognition criterion go further, arguing that "continuing existence" of a beneficiary is an implicit eligibility criterion for all cash transfer programs. "Continuing existence" operates to limit the obligation to that which relates to the reporting date, even where an individual has satisfied all eligibility criteria explicitly laid down in governing legislation or regulations. From an assets and liabilities perspective, such an approach may be based on a presumption that an entity will not have to make further payments beyond the reporting date if an individual were to die. There might be programs under which (a) "continuing existence" is an explicit eligibility criterion and (b) governing legislation or regulations make it clear that the government can recover any resources paid I relation to the period beyond the time of death. Such an approach also results in the cost of providing benefits in what some would consider to be inappropriate reporting periods (also see below paragraph 58 for a discussion of inter-period equity).

Arguments of those who argue that revalidation is a measurement attribute

53. Those with reservations about treating revalidation as a recognition criterion highlight practical problems. First, they argue that treating validation points as key parameters in the determination of obligations and liabilities is not conducive to financial reporting that enhances comparisons between different governments. It leads to recognizing different liabilities, depending completely on the timing and frequency of eligibility revalidation requirements. Thus, two programs with identical benefits and nearly identical eligibility requirements can have different liabilities, because of different revalidation dates.

54. This can be illustrated by considering two social security pension programs. One program does not require the revalidation of eligibility criteria; the other requires those receiving benefits to complete and return a form confirming the beneficiary's address and that he/she is still alive—this is not just an administrative procedure, because benefits are discontinued if the form is not returned by a specified date. If the entity adopts a policy of recognizing a liability when all eligibility criteria have been satisfied, the obligation for the second program would only extend to the date of revalidation, which may be a matter of a few days or weeks after the reporting date. On the other hand, the obligation recognized under the first program would extend to the end of a beneficiary's life. Some argue that a difference in the timing of revalidation requirements should not give rise to a large difference in the amount of the recognized liability.

55. Second, they argue that restricting the extent of the present obligation to the maximum amount between revalidation points can give incentives to "gaming". Liabilities and expenses can be artificially limited by instituting revalidation points shortly after the reporting date. In their view, these arguments lean towards treating revalidation as a measurement attribute. Under that treatment, the expected cash flows included in the

measurement of a liability for social benefits would take into account the probability that existing beneficiaries will satisfy revalidation criteria at future revalidation points.

Key Issue 6: An Alternative Model: Executory Contract Accounting with the Recognition of Liabilities Arising Only from Legal Obligations

56. The previous sections of this paper have highlighted some of the challenges and differences of opinion that have arisen in developing an approach to recognizing and measuring liabilities and expenses related to social programs based on the principles in IPSAS 19. These difficulties lead to the question whether applying another model would provide more useful information about social benefit programs.

57. One alternative model is to view obligations to provide social benefits by governments as quasi-contractual in nature, and adopt executory contract accounting. Executory contracts are contracts in which neither party has performed any of its obligations, or where both parties have partially performed their obligations to an equal extent. Under this model, (a) governmental obligations to provide goods, services and cash transfers to individuals or households and (b) the rights of individuals or households to receive those benefits, are acknowledged as commitments. However, those governmental obligations are effectively offset by the ongoing duty of individuals or households to contribute taxes and other sources of finance. Under this model, liabilities would not arise until legal entitlements have been established. The advantage of recognizing only legal obligations is that the point at which they arise is more objectively identifiable, and therefore subject to less ambiguity than the point at which constructive obligations arise. Long-term fiscal sustainability reporting would complement executory contract accounting by providing a fuller picture of a program's future viability.

58. For some, one advantage of such an approach is that it is consistent with the concept of "inter-period equity." The concept of inter-period equity has been developed by the US Governmental Accounting Standards Board and is a key element of its reporting model. Inter-period equity measures whether revenues in a particular reporting period are sufficient to pay for the goods and services provided in that period. The concept, which is strongly linked to accountability, is based on a view that governments generally have little earned revenue and no profit motive and are very different from profit-oriented entities. Inter-period equity also facilitates the analysis of outputs, outcomes and other performance measures and promotes inter-governmental comparability. Inter-period equity might not be supported by those who favor the strict "assets and liabilities" approach that is reflected in many IPSASs. Under the "assets and liabilities" approach the recognition of revenue and expenses is related to increases and decreases in assets and liabilities.

59. Some may find aspects of this model problematic and it would need to be explored much further before it could be applied. The model is a method of using an exchange transaction approach with modifications for the public sector environment for accounting for social benefits and taxation, which are the main examples of public sector specific non-exchange arrangements. It might also be difficult to argue that constructive obligations do not arise for social benefits, but do arise in areas such as accounting for post-employment benefit

obligations. The model can also be seen as a device that avoids dealing with the conceptual issue of the government's right to tax.

Conclusion

60. Accounting for social benefits is a developing area. The IPSASB acknowledges that the publication of ED 34 and this Consultation Paper are early steps in a journey to developing consistent and globally accepted accounting policies for social benefits. The IPSASB hopes that this Consultation Paper will stimulate debate on the major issues in accounting for social benefits and looks forward to receiving comments from interested parties.

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