HM TREASURY

Director, Financial Management & Reporting
Tel: 020 7270 5960
Fax: 020 7451 7603
lindsey.fussell@hmtreasury.gsi.gov.uk
www.hm-treasury.gov.uk
1 Horse Guards Road
London
SW1A 2HQ

15 March 2012

Stephenie Fox
Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street West
Toronto, Ontario M5V 3H2
Canada

Dear Stephenie

**IPSASB Exposure Draft 46 – Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances**

1. HM Treasury welcomes the opportunity to respond to the exposure draft (ED) on proposed recommended practice guidelines for reporting on the long-term sustainability of a public sector entity's finances. The ED is released at a time when the importance of the long-term sustainability of public sector finances has been forcefully highlighted by the sovereign debt crisis. We commend the IPSASB for engaging with this issue over the past decade and in reaching the stage where this ED has now been released.

2. In recent years the UK central government has sought to strengthen public finance management and the quality of our financial reporting. We recognise that this is a process of continuous improvement, but have made significant progress through policies such as the introduction of accrual accounting and the reform of the Parliamentary supply and budgetary system.

3. A major achievement in the UK in the last year has been the publication of audited Whole of Government Accounts (WGA). This is a consolidated set of IFRS based financial statements for the UK public sector encompassing central government departments, arms' length bodies, local authorities, devolved administrations, the health service, and public corporations. WGA provides resource providers, service recipients, their representatives, and the government with an understanding of the financial position and performance of the whole of the UK public sector. WGA is not only leading to improvements in how all public sector entities manage their finances but, in time, will undoubtedly assist in meeting the information needs of users for accountability and decision making purposes. (see http://www.hm-treasury.gov.uk/psr_government_accounts.htm for further information)

4. 2011 also saw the publication of the Office for Budget Responsibility's (OBR) *Fiscal Sustainability Report*. The OBR was created by HM Treasury in 2010 to provide independent and authoritative analysis of the UK's public finances. One of its main roles is to assess the long-term sustainability of the public finances through an annual fiscal sustainability report. This report sets out long-term projections for different categories of spending and revenue, analyses the public sector's balance sheet (on both a statistical "national" accounting and IFRS WGA basis) and reports different indicators of long-term sustainability. (see http://budgetresponsibility.independent.gov.uk/ for further information)

5. HM Treasury, therefore, supports the IPSASB's goal of promoting the publication of information on the long-term sustainability of public finances and we hope that our thoughts and comments will assist the IPSASB in determining appropriate guidelines for public sector entities. Our responses to the specific matters for comments noted in the Exposure Draft are in Annex.

6. I hope these comments will be of benefit to the IPSASB when finalising the Recommended Practice Guidelines. If you would like any further information, or to discuss the contents of this letter, please contact Chris Wobschall in the first instance (chris.wobschall@hmtreasury.gsi.gov.uk, +44 (0)20 7270 4508), whom of course you know as the Technical Adviser to the UK IPSASB member.

Yours sincerely

Lindsey Fussell

Lindsey Fussell

Director, Financial Management and Reporting

**Annex: Specific Matters for Comment**

**Specific Matter for Comment 1**
***Do you agree that the characteristics of an entity that indicate whether users exist for information on long-term fiscal sustainability are those set out in paragraph 15? If you consider that there are more appropriate indicators please provide them.***

The characteristics of an entity noted in the ED which indicate whether users exist for information on long-term sustainability are:

(a) Significant tax and/or revenue raising powers;
(b) powers to incur debt; or
(c) wide decision-making powers over service delivery levels.

We agree that the broad characteristics noted in the ED are useful in indicating whether users exist for information on long-term sustainability and in limiting the scope of this reporting to relevant entities. Our view is that the information needs of users related to long-term sustainability reporting will be rightly focussed on major macro political, societal, and economic issues such as the affordability of state pension entitlements or the ability to finance major infrastructure projects that will last over multiple generations. As such we would stress the importance of the words "significant" and "wide" in the above characteristics and would question whether it is not also necessary to include a similar scope limiting description in connection with powers to incur debt. Characteristic (b) could be rephrased to note "powers to incur significant debt."

We do recognise that compared to many jurisdictions, the United Kingdom has a relatively centralist public finance structure. Most resources utilised by public sector entities are provided to them from the central government finance ministry (either directly to or by way of other central government bodies) once budgets have been approved by Parliament. Where bodies do have the power to borrow, such borrowing is controlled by statutory codes. As such tax and revenue raising powers, powers to incur debt and wide decision-making powers over service delivery levels are significantly constrained. If it were deemed appropriate to introduce long-term sustainability reporting into GPFR in the United Kingdom, therefore, it would most likely be at the whole of government level. Its suitability at a local government level given the current constraints on these bodies would need to be further considered.

We also believe that if long-term sustainability reporting is to meet the information needs of users then it must be robust, comprehensive and if possible updated on an annual basis. Users must also be sure of its objectivity, which could require a measure of formal assurance. Our view is that this level of robustness is more likely to be achieved at a "national" level, as it will require a significant resource investment that is likely to be beyond the means of smaller and individual entities.

**Specific Matter for Comment 2**
***Do you agree that the "dimensions" of long-term fiscal sustainability in paragraphs 27–37 provide a viable framework for narrative reporting on the long-term sustainability of an entity's finances that complements and interprets the projections? If not, how would you modify this approach?***

The dimensions of fiscal sustainability noted in the ED are:

- fiscal capacity;
- service capacity; and,
- vulnerability

We believe that these dimensions provide a useful framework for the presentation of information to assist in ensuring faithful representation.

With respect to vulnerability, however, this is one of the reasons why we believe it is most appropriate for long-term sustainability reporting to be focussed at a "national" or whole of government level. Where an entity is highly vulnerable and has limited control over the sustainability of its finances, we do not believe that providing projections of fiscal and service capacity actually provides users with any useful information. While the entity will be a going concern for accounting purposes, the lack of control it has over future income will mean that the degree of uncertainty over any long-term sustainability projections will make them less useful and in many cases meaningless.

**Specific Matter for Comment 3**
***Do you agree with the guidelines in this ED on disclosure of principles and methodologies, including risks and uncertainties? If not, how would you modify these guidelines?***

While we believe that the inclusion of long-term sustainability information within GPFR does have the possibility of supplementing and enhancing the information already presented in the General Purpose Financial Statements (GPFS). This is only the case if:

- the principles and methodologies on which the projections are based are robust;
- the projections are updated normally on an annual basis and the information presented on long-term sustainability is explained with reference to the accounting figures in the financial statements; and
- the information presented is subject to a sufficient degree of assurance so that users can be sure of its objectivity.

The information presented will necessarily be based on economic analysis and we would expect that entities would look to guidance provided by organisations such as the OECD to ensure that they are following best practice.

We are generally content with the approach noted in the ED, but believe there are two areas where the guidelines could be more prescriptive.

The first relates to the updating of projections and ensuring that the information presented is explained with reference to the accounting figures in the financial statements. The ED notes that “regular updates are desirable”, whereas there is a case for saying that annual updates are essential. The GPFR and the GPFS cover an annual period, showing the financial results of the entity for that year and the financial position of the entity at year end. Long-term sustainability information, the GPFS and other information in the GPFR should be explained with reference to each other. For the long-term sustainability information to be of use to users for accountability and decision making purposes, it would make sense then for it, like all other information in the GPFR, to normally be updated on an annual basis.

The sovereign debt crisis has highlighted how rapidly perceptions of sustainability can alter. The inclusion of outdated information would devalue the GPFR to such an extent that the ability of users to utilise them for accountability and decision making purposes would be substantially diminished. Given this, we believe that the burden on individual entities of updating information would be excessive and so believe this would further support a limitation of such reporting to the “national” level, or at least at a level where the transactions are likely to be significant and influenced.

The second area where we feel more prescriptive guidance may be necessary is with relation to the objectivity of figures presented and of the need for some measure of formal assurance being provided over them so that users can be sure that they are a faithful representation.

There are a number of possible ways to ensure objectivity and to gain some measure of assurance over the long-term sustainability figures and narrative included in the GPFR. At the most basic level this may be through the existence of an independent body, such as the United Kingdom’s OBR, that produces its own long-term sustainability report. Provided this has a similar reporting boundary and is based on suitably close principles and methodologies then users will be able to compare the GPFR to the independent report to ensure objectivity has been achieved. Alternatively, the sustainability report included within the GPFR could actually be produced by the independent body. While this would ensure objectivity it could, however, raise accountability issues as the responsible individual for the GPFR may not have been able to assure themselves that the figures have been produced using robust principles and methodologies. Finally, the reporting entity could put in a place a more formal assurance framework, with either its external auditor or another suitably qualified individual undertaking a set of agreed upon procedures or an engagement in accordance with the requirements of ISAE 3000 *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information*.