Australian Government

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24 July 2008

Ms S Fox
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Dear Stephenie

Re: ED 34 *Social Benefits: Disclosure of Cash Transfers to Individuals or Households*
Consultation Paper: *Social Benefits: Issues in Recognition and Measurement*
Project Brief: *Long-Term Fiscal Sustainability Reporting*

Thank you for the opportunity to comment on:

- ED 34 *Social Benefits: Disclosure of Cash Transfers to Individuals or Households (ED34)*;
- Consultation Paper: *Social Benefits: Issues in Recognition and Measurement* (the Consultation Paper); and
- Project Brief: *Long-Term Fiscal Sustainability Reporting* (the Project Brief).

Issues considered significant by the AASB, as well as AASB comments on the specific questions posed in ED 34 and the Consultation Paper, are outlined in the attached submission, which is set out as follows:

Section 1: Significant Issues
Section 2: Specific Questions posed in ED 34
Section 3: Specific Questions posed in the Consultation Paper
Section 4: Other Issues

The AASB is supportive of the project to develop an International Public Sector Accounting Standard (IPSAS) for social benefits, given the significance of social benefits to public sector financial reporting in many jurisdictions, and given that these arrangements are not adequately dealt with by existing IPSASs or International Financial Reporting Standards (IFRSs). The AASB supports the approach taken by the International Public Sector Accounting Standards Board (the IPSASB) to consider ED 34, the Consultation Paper and the Project Brief together as an integrated package. The outcome of one element of the project will clearly have a direct impact on the other elements.

At a strategic level, the AASB considers that the IPSASB needs to take a more fundamental approach to the project. Applying existing asset and liability definitions to social benefit programs gives rise to significant conceptual issues. In developing a future exposure draft addressing the recognition and measurement of social benefits, the IPSASB's analysis should not be restricted to the existing asset and liability definitions, but should consider definitions in the context of the development of the conceptual framework as a whole. The AASB considers that the social benefits project should be developed in conjunction with the conceptual framework project, with the social benefits project effectively being a test case for the principles in the conceptual framework as they are being developed. Whilst it is recognised that constituents often argue that interrelated projects cannot be progressed until other projects are finalised (leading to stalemate at times), the AASB argues that the recognition principles in the social benefits project depend almost entirely on the definition of a liability for public sector financial reporting, and this is also a fundamental aspect of the conceptual framework project. If the IPSASB is to reach decisions that impact liability recognition requirements then it must also consider asset recognition requirements. A model which recognises as a liability any amount over and above the amounts due and payable at the reporting date, thereby arguably changing existing recognition requirements, without addressing the asset recognition requirements and the related issue of future taxation receipts, is not likely to be useful to users and is not likely to provide a fair representation of an entity's financial position.

The AASB does not believe that ED 34 is the most appropriate first step in signalling the importance of public sector entities providing users with relevant information about their social benefits programs. The AASB considers it premature to propose disclosure of amounts relating to cash transfers, other than disclosure of amounts due and payable at the reporting date. Public sector entities should not be asked to invest significant resources in developing estimates until the outcomes of the conceptual framework project and the social benefits project are clear. The AASB considers that the most appropriate first step for the social benefits project is to require all public sector entities (not only those using the accrual basis of accounting) to disclose the accounting policies adopted in recognising expenses and liabilities relating to all social benefit programs (not only cash transfer programs). In addition, public sector entities using the accrual basis of accounting should disclose amounts due and payable at the reporting date under all social benefit programs (not only cash transfer programs), by program.

The AASB agrees with the IPSASB that given the current conceptual framework, including the current definitions of assets and liabilities, that it is highly unlikely that the current reporting requirements would give rise to information that adequately meets users' needs. The IPSASB's work in developing a conceptual framework has identified a need for information that assists users with economic decision making and that also addresses accountability and stewardship. The AASB therefore supports the Project Brief and the need to progress a project to address long-term fiscal sustainability reporting. The AASB notes that a long-term fiscal sustainability report will only be meaningful at a whole of government level so that all expected future cash flows are reported together, providing the user with a complete picture of fiscal sustainability.

Finally, the AASB proposes an interim solution for public sector entities using the accrual basis of accounting whereby liabilities under social benefit programs are recognised when due and payable in the general purpose financial report (and disclosed by program in the notes to the financial statements) together with a separate long-term fiscal sustainability report. This would provide the IPSASB with more time to consider the conceptual issues. Whilst the AASB believes that the IPSASB needs to explore the conceptual issues first, it also sees merit in the interim solution being a pragmatic response to the conceptual issues posed by the social benefits project.

If you have any queries in relation to this submission please contact myself or Christina Habal (chabal@aasb.gov.au or +61 3 9617 7626).

Yours sincerely

David Boymal
Chairman

Submission to the IPSASB on the social benefits project comprising:

ED 34 *Social Benefits Disclosure of Cash Transfers to Individuals or Households* (the ED)

Consultation Paper *Social Benefits: Issues in Recognition and Measurement* (the Consultation Paper)

Project Brief *Long-Term Fiscal Sustainability Reporting* (the Project Brief)

Prepared by the
Australian Accounting Standards Board

July 2008

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AASB Submission to the IPSASB in relation to the social benefits project (July 2008)

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Section 1: Significant Issues

1.1 <u>The social benefits project should be developed in conjunction with the conceptual framework project</u>

The Consultation Paper bases its discussion of social benefits on a definition of a liability which is itself based on the IFRS definition of a liability. The AASB does not agree with this approach and considers that a more fundamental approach is needed. The AASB considers that the IPSASB needs to progress the social benefits project in conjunction with the project to develop a conceptual framework for public sector financial reporting, with the social benefits project effectively being a test case for the principles in the conceptual framework as they are being developed.

In paragraph 20 of the Consultation Paper various definitions are listed as a starting point to the discussion of the recognition and measurement of social benefits. These definitions are consistent with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. The AASB does not believe that this is the appropriate starting point for the social benefits project for the following reasons:

1. Social benefits liabilities are one of the most significant items in any consideration of a public sector entity's financial position, particularly at the whole of government level, and the principles guiding this project need to be consistent with those being developed in the conceptual framework project;
2. The IPSASB's conceptual framework project has identified important differences in users' needs and hence in the objectives for financial reporting in the public sector as compared to the for-profit sector. In the public sector there is an increased focus on accountability and stewardship; the needs of users are therefore wider. This indicates that different definitions of assets and liabilities may be appropriate;
3. The wider needs of users of public sector entity financial reports might also be met by expanding the scope of general purpose financial reports for public sector entities, for example, by including fiscal sustainability reporting within the scope of public sector general purpose financial reporting. Any expansion in the scope of public sector general purpose financial reporting could also impact on the definitions of assets and liabilities;
4. If the IPSASB is to reach decisions that impact liability recognition requirements then it must also consider asset recognition requirements. A model which recognises as a liability any amount over and above the amounts due and payable at the reporting date, thereby arguably changing existing recognition requirements, without addressing the asset recognition requirements and the related issue of future taxation receipts, is not likely to

be useful to users and is not likely to provide a fair representation of an entity's financial position; and

5. The existing definition of a liability is problematic when applied to social benefits. This is discussed further in section 1.2 of this submission.

An appropriate starting point for the social benefits project is the conceptual framework project that the IPSASB is undertaking. The AASB believes that these two projects need to be developed in tandem with the social benefits project effectively being used as a test case for the principles as they are being developed. This is supported by the role of the conceptual framework to aid in the efficient and effective development of consistent IPSASs underpinned by a consistent set of principles.

The first draft of the conceptual framework Consultation Paper dealing with the scope, objectives and qualitative characteristics of information in general purpose financial reports documents the following line of thinking – user needs determine the objectives of financial reporting, and the objectives of financial reporting influence the definition of the elements of financial statements. Where the needs of public sector users and for-profit sector users differ, therefore, the definitions of assets and liabilities may also need to differ.

The user of a public sector financial report is arguably just as interested in long-term fiscal sustainability, intergenerational equity and service delivery as in overall financial performance as currently reported in general purpose financial reports. As a result, there is an increased emphasis on stewardship and accountability as an objective of financial reporting for public sector entities when compared with for-profit entities. The social benefits project can tackle this in several ways:

1. conceptually, by considering definitions of a liability and/or an asset in a not-for-profit reporting context;
2. by expanding the scope of general purpose financial reports to include fiscal sustainability reporting;
3. by considering a different conceptual approach altogether, for example viewing the relationship between individuals/households and the government as a 'contract' and measuring all the expected cash flows under this contract; or
4. pragmatically, for example by considering a vested/unvested notion similar to that used in IPSAS 25 *Employee Benefits*. Under such a notion, recognition is triggered by the vesting event (a key event in meeting eligibility criteria) all further conditional events then being considered in the measurement of the liability; or
5. by considering a combination of the above.

Whatever the approach taken, given the scale of the social benefits project and its importance to public sector financial reporting, it can only be developed in conjunction with the development of the conceptual framework. The AASB recognises that a concern with such a strategy is that it could delay the project beyond a reasonable timeframe. The AASB therefore proposes an interim solution in section 1.4 of this submission.

1.2 Applying the existing definition of a liability to social benefits

Applying the existing definition of a liability to social benefits gives rise to significant conceptual issues.

The Consultation Paper explores the three categories of social benefits separately and considers:

1. whether or not social benefits create present obligations in the case of collective and individual goods and services; and
2. when an obligating event occurs for cash transfers.

Liabilities are present obligations arising from past events. 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." The existing definition, therefore, establishes that an obligation is something the entity has little discretion to avoid.

Some have argued that such a liability notion does not sit comfortably with social benefits, given the discretion that governments generally have over future legislation and given the high degree of likelihood that social benefits legislation will change in the future. It is very common for governments to make changes to social benefits legislation. Even fundamental aspects of social benefits legislation can change – for example, one can envisage the entitlement age for the aged pension in Australia being increased in the medium to long-term. However, the AASB does not support such a view and believes that liabilities should be based on legislation enacted, or substantively enacted, at the reporting date.

The Consultation Paper considers in some detail when an obligating event occurs for cash transfers but does not consider this as explicitly for other social benefits. The Consultation Paper also does not explicitly consider what the obligating event is.

The IPSASB will need to consider more explicitly what the obligating event is and when the obligating event occurs in the case of:

1. a legal obligation; and
2. a constructive obligation.

The answers could differ depending on the circumstances.

Legal obligations

A legal obligation is defined in the Consultation Paper as an obligation that arises from:

"(a) a contract;
(b) legislation; or
(c) other operation of law".

Social benefits programs are enacted in legislation and they will therefore give rise to legal obligations.

Obligating event for a legal obligation

It can be argued that, under the existing notion of a liability, encapsulated in IAS 37, other than the social benefits that are due and payable at the reporting date, any additional obligation, over and above the amount due and payable, is a possible obligation, or contingent liability, because its existence will be confirmed once all eligibility criteria have been satisfied in the future. The past event is enactment of social benefits legislation and the uncertain future event is the satisfaction of all eligibility criteria, including lodgement of a valid claim. The contingent liability would be disclosed unless the probability of an outflow of resources was remote; the uncertain future events are reflected in the measurement of the contingent liability. If this view were adopted there is the possibility of very significant contingent liabilities being disclosed in the balance sheet without disclosure of the future taxation receipts that would fund these liabilities as a contingent asset. Such a disclosure is not considered useful to users and is arguably meaningless.

Proposed amendments to IAS 37: legal obligations

The AASB notes that the IPSASB also needs to consider the IASB's proposed amendments to IAS 37. Under the proposed amendments to IAS 37, using unemployment benefit as an example, one interpretation is that the government, on enacting unemployment legislation, has an unconditional obligation to stand ready to settle claims for unemployment benefit, and a conditional obligation to pay unemployment benefit when a valid claim for unemployment benefit is lodged. The conditional obligation is recognised when the conditions are met, that is, when social benefits payments become due and payable. The unconditional liability is recognised immediately and would be measured by taking into account the probability of valid claims for unemployment benefit arising in the future. There would clearly be significant levels of judgement in measuring the unconditional obligation and the measurement is likely to become unreliable if projected too far into the future.

The IASB's discussions on the existence of a present obligation, in their project to amend IAS 37, could provide a different interpretation of what the obligating event is and therefore when an obligating event occurs. The IASB's discussions, in a for-profit context, note that legislation, by itself, does not give rise to a present obligation; an action or event is also required. For example, consider legislation that provides for unemployment benefit to be paid to all unemployed people with assets less than $50,000, with a monthly requirement to demonstrate that they are actively looking for work. Unemployment benefit is due one month in arrears. Enactment of the legislation alone does not create a present obligation; an action or event is also required. Becoming unemployed in itself does not create a present obligation, the action or event, in this example, is that someone becomes unemployed and meets all of the eligibility criteria. At this point the legal obligation arises. The Consultation Paper notes that some argue that a liability cannot arise until the government is legally required to make a payment. Such a view is not consistent with the notion of a present obligation. A present obligation arises once an entity has little or no discretion to avoid settlement – it is irrelevant whether settlement is today or tomorrow. It is only the measurement of the liability that is impacted by the timing of the payment. If the present obligation is considered to arise only once all eligibility criteria have been satisfied, in the above example the liability expires the following month, because each month the recipient has to demonstrate that they are actively looking for work. All eligibility criteria have not been satisfied until this can be demonstrated.

It is clear from the discussions above that there are some important conceptual questions that need to be considered before a clear position is reached on the nature of the legal obligation under a social benefits program.

Constructive obligations

A constructive obligation is defined in the Consultation Paper as:

> "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."

Obligating event for a constructive obligation

Governments regularly make public announcements in relation to social benefits, for example in their political manifestos and in their periodic published budgets or plans, that may create constructive obligations. The definition of a constructive obligation refers to statements being 'specific' and this appears critical in the context of social benefits. The full range of public announcements should be interpreted in this context. Election manifestos, for example, are often accompanied by only limited detail and it could be difficult to argue that such promises are sufficiently specific to create valid expectations. Periodic published budgets and plans are perhaps the most specific announcement a government might make that could arguably create a valid expectation. However, the budget (or plan) by definition is short term in its scope and could arguably only create liabilities arising in the forthcoming budget (or plan) period, because that is generally the period covered by the promises.

Some might argue that some social benefits are such an established and integral aspect of everyday life that, by an established pattern of past practice, the government has created a valid expectation that it will accept certain responsibilities. An example might be the provision of public education to all children between the ages of 5 and 18 in Australia. However, governments could choose to provide education in a number of different ways. Successive governments in the same jurisdiction will often have very different approaches to the provision of education services. Is the provision of public education to all children between the ages of 5 and 18 in Australia sufficiently 'specific' to be considered a promise? If it is, given that a liability is only recognised if it can be reliably measured, can such a promise be reliably measured over anything but the short term given the many different ways in which it could be delivered under existing legislation?

One interpretation of the discussion above could be that social benefits programs will only give rise to constructive obligations over the short term. Clearly the position is ambiguous under existing definitions and the IPSASB needs to explore these issues in greater detail in developing the exposure draft and in the development of a conceptual framework for the public sector.

Proposed amendments to IAS 37: constructive obligations

The proposed amendments to IAS 37 are seen by many as narrowing the concept of a constructive obligation such that it is even less likely for a social benefits program to give rise to a constructive obligation. Under the proposed amendments to IAS 37 the definition of a constructive obligation is amended as follows (with significant changes shown in italics):

> "a *present* obligation that arises from an entity's past actions when:
> (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 *particular* responsibilities; and
> (b) as a result, the entity has created a valid expectation in those parties *that they can reasonably rely on it* to discharge those responsibilities."

The change from 'certain' responsibilities to 'particular' responsibilities creates a more specific obligation. The inclusion of an additional hurdle, that parties can also reasonably rely on the past actions, makes it more difficult to satisfy the definition.

What is the obligating event in the case of a constructive obligation? The Consultation Paper puts forward an argument that an obligating event could arguably arise before all eligibility criteria have been met. The example given relates to the existence of a constructive obligation to pay a pension to those over age 65. A policy statement by the government that it intends to continue to provide the aged pension to those over the age of 65 could, some might argue, create a constructive obligation; the obligating event, if one adopted such a view, would be the publication of the policy statement. In the case of a constructive obligation, therefore, the obligation arises from past practice and published policies. A constructive obligation could, therefore, arise before all eligibility criteria have been reached. This is clearly at odds with the discussion of legal obligations above. A future exposure draft needs to consider these differences.

1.3 ED 34 proposals

The AASB does not agree with the disclosures proposed in ED 34.

The AASB proposes that public sector entities adopting the accrual basis of accounting disclose amounts due and payable under social benefits programs, by program, and that all public sector entities disclose their accounting policy for recognising expenses and liabilities related to their social benefits programs.

In ED 34 the IPSASB has tentatively concluded that disclosure of certain cash transfers (and information about social benefits programs) represent an important first step in signalling the importance of governments providing users with relevant information on their social benefits programs. The AASB is not convinced that the ED 34 proposals are the appropriate first step.

ED 34 proposes disclosing the best estimate of the present value of amounts expected to be transferred under cash transfer programs. The best estimate is determined on the basis of continuous entitlement, that is, assumptions are made about the proportion of those eligible for benefits at the reporting date who will continue to be eligible into the future, and the corresponding amounts are included in the best estimate liability. ED 34 does not suggest that the amount determined is a 'liability', it is simply an amount to be disclosed. There is, however, a risk that users will consider this amount to be a liability, and that the disclosure could therefore be misleading.

As discussed in section 1.2 of this submission, it is not clear to the AASB, because it requires further research, whether an entity has a present obligation to pay unemployment benefit to someone in two months time, if, before that time, the person is required to demonstrate that they are making themselves available for work. The AASB is not in favour of requiring public sector entities to disclose amounts that may ultimately not be regarded as liabilities, once the conceptual framework project and social benefits project are finalised. The AASB believes that entities should not be asked to invest significant resources to produce information that may not ultimately be required in a future recognition and measurement standard.

AASB proposals

The AASB considers that the IPSASB could better achieve the same objective of signalling the importance of public sector entities providing users with relevant information on their social programs by requiring:

1. disclosure of amounts due and payable under social benefits programs, by program, by public sector entities using the accrual basis of accounting; and
2. disclosure by all public sector entities of the accounting policy for recognising expenses and liabilities related to their social benefits programs.

This is seen as a minimum level of disclosure and is an interim step, while the IPSASB considers the conceptual issues discussed in section 1.1 and 1.2 of this submission. The AASB considers that public sector entities using the cash basis of accounting should be within the scope of a future standard, but should only be required to provide disclosure of accounting policies. The AASB considers that this would better achieve the IPSASB's objective in issuing ED 34 of signalling the importance of public sector entities providing users with relevant information about their social programs.

1.4 An interim solution

The AASB proposes an interim solution in which public sector entities using the accrual basis of accounting recognise amounts due and payable under social benefits programs in their general purpose financial report (and disclose by program) and, in a separate report, at a whole of government level, report on their long-term fiscal sustainability.

As discussed in section 1.1 of this submission, the AASB believes that the social benefits project needs to be considered in conjunction with the conceptual framework project. This will establish an appropriate definition of an asset and liability in general purpose financial reporting for the public sector and whether or not a long-term fiscal sustainability report belongs within the scope of the general purpose financial report.

Such a conceptual project will take time. The AASB therefore propose an interim solution in which public sector entities using the accrual basis of accounting recognise amounts due and payable under social benefits programs in their general purpose financial report (and disclose by program) and, in a separate report, at a whole of government level, report on their long-term fiscal sustainability. Such a solution is relatively uncontroversial and could be implemented within a shorter timeframe to allow time for a full consideration of the conceptual issues.

Whilst the AASB believes that the IPSASB needs to explore the conceptual issues first, it also sees merit in this interim solution being a pragmatic response to the conceptual issues posed by this project for two key reasons.

The first reason is that social benefits are usually funded by general taxation revenue. Social benefits paid today are usually funded by taxation receipts received today or held in reserve. As a result, any social benefits 'liability' beyond that which is due and payable today, could be funded by future taxation receipts and, hence, any reporting which does not recognise future taxation receipts does not provide a complete picture of fiscal sustainability. Recognising as a 'liability' any amount beyond that which is due and payable today and recognising as an 'asset' future taxation receipts would require amendments to existing liability and asset recognition requirements.

Long-term fiscal sustainability reporting does not consider assets and liabilities; it considers expected future cash flows. Under long-term fiscal sustainability reporting, therefore, both expected social benefits cash outflows and expected future taxation cash inflows would be considered, it would not be necessary for existing liability and asset recognition requirements to be amended.

A second reason is that this could arguably produce the most understandable information for users. Consider the following example in relation to unemployment benefit.

As at the reporting date:

- $5m of unemployment benefit is due and payable;
- $12m is the amount that is expected to be paid to those unemployed at the reporting date and those who remain unemployed beyond the reporting date up to the point at which they need to reapply for unemployment benefit (e.g. prove that they are actively looking for work);
- $20m is the amount that is expected to be paid to those unemployed at the reporting date and those who remain unemployed beyond the reporting date;
- $50m is the amount that is expected to be paid to those unemployed at the reporting date and those who remain unemployed, or will again become unemployed after a period of being in the workforce;
- $200m is the amount that is expected to be paid in unemployment benefit, to those adults at the reporting date, capable of being in paid employment, over the next 10 years;
- $300m is the a amount that is expected to be paid in unemployment benefit over the next 10 years; and
- $700m is the amount that is expected to be paid in unemployment benefit over the next 20 years.

The list of possible 'liabilities' is seemingly endless. There is an argument for adopting the extremes so that users understand exactly what is meant by the amount reported, that is, the balance sheet reports amounts due and payable of $5m and the fiscal sustainability report picks up all expected cash outflows (for consistency and comparability defined as all expected cash flows within a set timeframe).

1.5 Implications of the IASB's insurance contracts project

The social benefits project should consider the implications of the IASB's insurance contracts project to ensure that arrangements that could fall within the scope of both projects are appropriately treated.

IFRS 4 *Insurance Contracts* defines an insurance contract as:

> "a contract under which one party (the insurer) accepts significant risk from another party (the policyholder) by agreeing to compensate the policyholder if a specific uncertain future event (the insured event) adversely affects the policyholder".

There is a potential overlap between the insurance contracts project and the social benefits project because it is possible to conceive of arrangements that would satisfy both the definition of an insurance contract and of a social benefit. In Australia, where all entities are required to adopt IFRSs, amended where appropriate in respect of not-for-profit entities, this would mean that an arrangement that met both definitions would be treated under IFRS 4, unless the AASB made a specific exemption in this case.

Social benefits are non-exchange transactions where there is a payment, in cash or in kind, to protect the entire population, or specific segments of it, against certain social risks. A 'social risk' is an event or circumstance that may adversely affect the welfare of households either by imposing additional demands on their resources or by reducing their incomes. There is clearly an overlap between 'social risk' and 'insurance risk', for example, you can buy an insurance policy to protect yourself against costs associated with loss of employment. It is possible, therefore, that in some jurisdictions there might be arrangements between governments and individuals that could be considered social benefits but that could also meet the definition of an insurance contract. Similarly, the government could have in place insurance contracts, where the government acts as insurer of last resort, that meet the definition of a non-exchange transaction, because they are effectively subsidised by the government, and could, therefore, be considered social benefits.

If social benefits arrangements were treated as insurance contracts this could have significant implications. Under the IASB's current proposals for insurance contracts[1], insurance contracts are to be measured at current exit value; this includes recognising future premiums under existing contracts (together with the corresponding liability) that the policyholder must pay to retain guaranteed insurability. Guaranteed insurability is a right that permits continued coverage without reconfirmation of the policyholder's risk profile, at a price that is contractually constrained. These insurance proposals could potentially result in a very different accounting treatment for social benefits arrangements from that ultimately required in a social benefits standard.

The IPSASB should explore the potential overlaps between these two projects in developing the exposure draft.

1 The IASB issued Discussion Paper *Preliminary Views on Insurance Contracts* in May 2007

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Section 2: Specific Questions posed in ED 34

2.1 Question 1

Do you agree that the scope of this Exposure Draft is appropriate (paragraphs 2-8)? If you do not think the scope is appropriate, please detail how you would modify the scope? Please state your reasons.

AASB response

For the reasons noted in section 1.3 of this submission, the AASB does not agree with the disclosures proposed by ED 34 and would propose only a minimum level of disclosure.

However, if the IPSASB is to continue with its proposals to require more detailed quantitative and qualitative disclosures, the AASB would propose more comprehensive disclosure along the following lines: that all public sector entities (not just those using the accrual basis of accounting) disclose the following information:

1. a general description of all the social benefits programs in place during the reporting period, including the principal legislation and regulations governing the programs (ED 34 only requires information in relation to cash transfer programs);
2. a general description of programs that have been amended or discontinued since the reporting date (this is similar to the proposed disclosure in ED 34 paragraph 45(h); and
3. the entity's accounting policy for recognising expenses and liabilities related to all social benefits programs (ED 34 only requires information in relation to cash transfer programs).

Where such information is available in other reports, public sector entities should be able to cross reference to these other reports in their financial statements.

In addition, public sector entities using the accrual basis of accounting should disclose information about the amounts due and payable under social benefits programs as at the reporting date, by program.

The AASB also notes that if the IPSASB is to continue with its proposals to require more detailed quantitative and qualitative disclosures it might want to consider disclosure of expected future cash flows over set timeframes – for example it could consider expected cash flows within the next 12 months, expected cash flows between 12 months and 2 years and expected cash flows beyond 2 years.

2.2 Question 2

Do you agree that the new definitions in this Exposure Draft at paragraph 10 are sufficiently clear and comprehensive? If you disagree, please indicate how these definitions should be modified and any new definitions that should be introduced. Please state your reasons.

AASB response

As noted in section 1.5 of this submission, the AASB considers that there are potential overlaps between the definition of 'social risk' under ED 34 and 'insurance risk' under IFRS 4. The AASB considers that the IPSASB needs to conduct further research in this area.

The AASB also notes that the definitions of 'social benefits' and 'individual goods and services' are not logical as both refer to the other.

The AASB also notes that the differences in the three categories of social benefits are not necessarily clear and may require further clarification. The AASB also questions the need to differentiate between the three categories of benefit, other than to provide examples of the type of benefits addressed by the accounting standard, given that the principles underlying the accounting treatment should be the same for each.

2.3 Question 3

Do you agree that the requirements for the determination of amounts expected to be transferred to eligible individuals and households are appropriate (paragraphs 30-44)? If you do not think they are appropriate, please indicate what those requirements should be. Please state your reasons.

AASB response

For the reasons noted in section 1.3 of this submission, the AASB does not agree with the proposal to require disclosure of amounts expected to be transferred to eligible individuals and households under cash transfer programs.

2.4 Question 4

Do you agree that the disclosure requirements in paragraph 45 are appropriate? If you think they are unduly onerous, which disclosures should not be required? Conversely, if you think the disclosures are inadequate, which further disclosures would you include? Please state your reasons.

AASB response

See AASB response to question 1 in section 2.1 of this submission.

2.5 Question 5

Do you agree that the disclosure requirements in paragraph 45 would provide information that is verifiable? If you think the disclosure requirements would not provide information that is verifiable, please identify the specific disclosures and state what those implications are.

AASB response

The AASB notes that the IPSASB is currently considering the place of verifiability in its conceptual framework. The IASB considers verifiability a quality of information that may assure users that information faithfully represents the economic phenomena that it purports to represent. Verifiability implies that different knowledgeable and independent observers could reach general consensus, although not complete agreement, that either: the information represents the economic phenomena that it purports to represent, or an appropriate recognition or measurement method has been adopted, without material error or bias.

The AASB has received mixed feedback from its constituents in relation to whether information required to be disclosed under ED 34 would or would not be verifiable. Given the definition of verifiability noted above, any model which introduces prospective accounting is likely to have initial problems with verifiability until preparers, users and auditors become more familiar with the models in place. However, whilst there might be differences in judgment, and whilst it might be challenging to reach a general consensus, it has not been suggested to the AASB that the measurement process could not be agreed upon and audited.

2.6 Question 6

Do you agree that the implementation arrangements are appropriate (paragraphs 50-53)? If you think the implementation arrangements are inappropriate, please specify how you would change them and state your reasons.

AASB response

See section 4.1 of this submission. The AASB considers that, if the IPSASB were to continue with the proposals outlined in ED 34, consideration would need to be given to public sector entities using the cash basis of accounting, and in particular their future implementation of the Standard.

Section 3: Specific Questions Posed in the Consultation Paper

3.1 Question 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 (and notes thereto) cannot convey sufficient information by themselves to users about the financial condition of governmental programs providing social benefits? Please state your reasons.

AASB response

The AASB considers that public sector general purpose financial reporting needs to address accountability and stewardship of governments including service delivery and the interrelated issues of fiscal sustainability and intergenerational equity.

Given the current conceptual framework, including the current definitions of assets and liabilities adopted by the IPSASB, the AASB agrees that it is highly unlikely that the current reporting requirements would adequately meet users' needs. The most significant reason for this is that under the current regime future taxation receipts do not qualify for recognition as assets.

The question is expressed as follows: "…. cannot convey sufficient information by themselves ….". This implies that, if it is accepted that current financial statements are not adequate to meets users' needs, the way in which this would be addressed is with additional reporting (most likely, long-term fiscal sustainability reporting). The AASB notes that another way of addressing this problem could be to expand the definition of a liability for public sector financial reporting. The AASB has not proposed such an approach in this submission.

3.2 Question 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 (a) and/or (b), please indicate when and indicate your reasons.

AASB response

In section 1 of this submission the AASB argues that such a question can only be considered in the context of the development of the conceptual framework for public sector financial reporting as a whole.

3.3 Question 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.

AASB response

See response to question 2 in section 3.2 of this submission.

3.4 Question 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.

AASB response

See response to question 2 in section 3.2 of this submission.

3.5 Question 5

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

AASB Response

It is not clear to the AASB how an executory contract accounting model as discussed in paragraphs 56 to 59 of the Consultation Paper would work in practice.

It appears that what is proposed is a restricted interpretation of liabilities, to those due and payable, enhanced by fiscal sustainability reporting. This is similar to the interim solution discussed in section 1.4 of this report. The AASB does not believe an executory contract accounting model is necessary to achieve such a result.

3.6 Current Australian accounting policies and reporting

The Consultation Paper asks respondents to provide details of current policies for recognising and measuring social benefits liabilities. In Australia liabilities under social benefits programs are recognised when due and payable. Please refer to www.finance.gov.au/Publications for the latest Commonwealth Consolidated Financial Statements.

The AASB also notes that the Australian Government produces an Intergenerational Report every five years which addresses fiscal sustainability and intergenerational equity. Refer to www.treasury.gov.au/igr/IGR2007.asp for the latest Intergenerational Report.

Section 4: Other Issues

4.1 Implications for entities using the cash basis of accounting

The IPSASB should consider the implications of the social benefits project on entities contemplating a transition from the cash basis of accounting to the accrual basis of accounting.

ED 34, as currently drafted, only applies to those entities using the accrual basis of accounting. ED 34 will create significant additional requirements for the public sector entities that are required to adopt them. It will, therefore, create an even greater hurdle for those jurisdictions contemplating moving from the cash basis of accounting to the accrual basis of accounting.

The AASB notes it is a key objective of the IPSASB to encourage all entities to move to the accrual basis of accounting and considers that the social benefits project should not frustrate this. Accordingly, if the IPSASB is to continue with the current ED 34 proposals, the AASB recommends that the adoption of the social benefits requirements is made voluntary for those entities that have been applying the accrual basis of accounting for less than a defined period of time.