Accounting Standards Board

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The Technical Director
International Public Sector Accounting
Standards Board
International Federation of Accountants
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28 July 2008

Dear Sir

Consultation Papers on Social Benefits

The UK Accounting Standards Board (ASB) welcomes the opportunity to comment on the International Public Sector Accounting Standards Board's consultation on accounting issues relating to the provision of social benefits. This is a very significant issue for financial reporting by public sector entities.

This covering letter sets out the ASB's views on IPSASB's proposed strategic approach to this issue. More detailed comments are provided in Appendix A on the issues raised in Exposure Draft 34 'Disclosure of cash transfers to individuals or households' and in Appendix B on the Consultation Paper 'Social Benefits: Issues in Recognition and Measurement'. We have written separately expressing strong support for the proposed project on long-term fiscal sustainability reporting which we consider to be the a very innovative part of the proposed strategic approach.

The ASB fully acknowledges the very difficult issues involved in accounting for social benefits. These are issues that, assisted by its Committee on Accounting for Public Benefit Entities (CAPE), the ASB has previously considered as part of earlier IPSASB consultations and also, more recently, as we finalised our work on an Interpretation for Public Benefit Entities of the Statement of Principles for Financial Reporting (the Interpretation, published in June 2007). The Interpretation noted that further work is required in relation to governments and commitments to provide public benefits.

In view of the significance of these issues, the ASB is pleased to note that social benefits are also being considered as part of IPSASB's conceptual framework project. Importantly, this project will consider social benefits in the context of what is a government liability and whether the financial position of governments would be faithfully represented by recognising liabilities associated with expected future outflows of resources for social benefit programs.

The ASB also agrees with the overall direction of IPSASB's strategic approach and, despite having some reservations, acknowledges that publishing a disclosure-only standard should improve the information available to users on government commitments for social benefit programs. We therefore support publication of a disclosure-only standard, although we would emphasise it should not pre-empt the conclusions that might be reached on recognition and measurement issues later on.

We also have some concerns about the scope of the proposed disclosure standard, in particular the distinction that is made between "cash transfers to individuals and households" and "individual goods and services". We do not consider this to be a helpful distinction and, as explained in Appendix A, consider that treating cash transfers separately could result in different accounting treatments for similar policies. For this reason, we would suggest that social benefits are categorised as "individual goods and services" or "collective goods and services" and that cash transfers should form a sub-set of the former.

I hope you find the comments in this covering letter and the attached Appendix helpful. If you have any queries, or would like any further information, then please contact Alan O'Connor (+44 (0)20 7492 2421) or myself (+44 (0) 7492 2440).

Yours faithfully

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Appendix A

Exposure Draft 34: 'Social Benefits: Disclosure of cash transfers to individuals or households'

Specific matters for comment

Scope of the proposed Standard and definitions (questions 1 and 2) – *paragraphs 2 to 10 of ED*

We do not consider the scope of the proposed standard to be appropriate because we disagree with the distinction that is made in the exposure draft between "cash transfers to individuals or households" and "individual goods and services". In our view this distinction is not always helpful and that, in accounting terms, there could be very little difference between cash transfers and individual goods and services, especially as public sector entities may choose to provide substantively identical benefits either in cash or in kind. The Consultation Paper 'Social Benefits: Issues in Recognition and Measurement' also notes that the line between cash transfers and individual goods and services is sometimes blurred.

An example, as highlighted in paragraph 16 of the proposed standard, could be the provision of housing benefits where entities may either transfer cash to households or tenants for repairs and maintenance (hence the transfer would fall within the scope of the ED) or carry out this work directly (in which case the service would fall outside the scope of the ED). We believe there is a risk that the distinction may have the unintended consequence on providing an incentive towards giving non-cash benefits (on the grounds these would not need to be disclosed). We therefore suggest that IPSASB consider having only two categories of social benefits, these being individual and collective goods and services. Cash transfers would then be a sub-set of individual goods and services.

Determination of amounts expected to be transferred (question 3) –*paragraphs 30 to 44 of ED*

We note with interest the requirements in the proposed standard for determining the amounts expected to be transferred. These seem reasonable although, as mentioned in the covering letter, if a disclosure-only standard is issued, flexibility will need to be retained in terms of the conclusions that might be reached on measurement issues. We also note that the proposed requirement to disclose the present values of amounts to be transferred might seem to imply the amounts to be transferred are liabilities and should therefore be recognised as such in the balance sheet. We appreciate the need for present values but would suggest that disclosure of the periodic cost (or cash payments) in respect of social benefit programs might also be helpful.

***Are the proposed disclosure requirements appropriate and verifiable? (questions 4 and 5) –** paragraph 45 of ED*

We consider the proposed disclosure requirements are appropriate and should convey useful and relevant information to users of the financial statements. The disclosures will however need to be understandable and complement the information on expenses and liabilities for social benefit programs that may already be being reported in the primary statements.

In terms of the detailed disclosures we would suggest:

- In addition to information on the present value of the amounts expected to be transferred (paragraph 45 (b) of the ED), IPSASB also consider requiring information to be disclosed on the periodic cost (or cash payments) in respect of social benefit programs for future periods. This might be analysed by expected date, for example less than one year, 2 to 5 years, 6 to 15 years, 16 to 30 years and over 40 years.

- A requirement for sensitivity analysis might be introduced. This would complement the disclosures required in paragraph 45(f) on changes to the principal assumptions since the last reporting date;

The proposed requirements allow considerable scope for entities to report the information which they consider appropriate in terms of meeting the requirements of the proposed standard. Whilst this approach appears reasonable, it is likely to raise issues for auditors.

***Implementation arrangements (question 6) –**paragraphs 50 to 53 of ED*

We agree with the proposal not to require comparative information in the first year of implementation. We also consider that it is reasonable to require implementation two years after issuance, but would encourage early adoption particularly as the proposed standard represents an interim measure.

Appendix B

Consultation Paper: 'Social Benefits: Issues in Recognition and Measurement'

The Consultation Paper raises a number of very important issues that, in advance of work on the conceptual framework project (and the definition of a liability in the context of providing social benefits) it is perhaps too early to answer. These are also very difficult technical issues; hence our support for the proposed work on long-term fiscal sustainability which we believe can be progressed at a rate that will allow IPSASB more time to consider recognition and measurement issues.

Key issue 1: Do present obligations to beneficiaries for collective goods and services occur? *(paragraphs 24 to 26 on page 9 of Consultation Paper)*

We do not consider a present obligation arises to beneficiaries for collective goods and services on the grounds that a liability to provide services cannot be enforced by individuals and governments can withdraw services. This view is consistent with the following text that is included in the ASB's Interpretation for Public Benefit Entities of the Statement of Principles for Financial Reporting (the Interpretation):

> *General Commitments*
>
> 4.29 A general or policy statement that the entity intends to provide goods and services to certain classes of potential beneficiaries in accordance with its objectives will not necessarily give rise to a liability. Such statements do not of themselves create an obligation such that the entity cannot withdraw or amend the terms on which the goods and services will be provided. Potential beneficiaries of the goods and services may envisage they will receive them, but they do not have the ability to insist on their receipt.
>
> 4.30 Examples of general commitments are political commitments made by governments, for example the announcement of a forthcoming new initiative to provide cash benefits to members of the public. Governments make, and amend, such promises and policies as part of their ongoing political processes to manage the economy and redistribute wealth within or between periods and generations. As such they do not give rise to constructive obligations. Equally a charity would not have a liability as a result of a general policy of providing grants and/or other services to certain classes of people or entities.

Key issue 2: Do present obligations to beneficiaries for individual goods and services occur? *(paragraphs 27 to 31 on pages 9 to 11 of Consultation Paper)*

We consider that in some circumstances present obligations arise to individuals for goods and services but that a liability should only be recognised where there is a valid expectation that leaves the entity with little, if any, discretion to avoid the transfer of economic benefits. It would seem that these circumstances are likely to be rare and that the amounts are unlikely to be significant, although further research will be necessary to determine whether this is the case.

Key issue 3: When do obligating events occur for cash transfers for non-contributory programs? *(paragraphs 32 to 43 on pages11 to 13 of Consultation Paper)*

In our comments on ED 34, we expressed concern about the distinction between cash transfers to individuals and households and individual goods and services. We would therefore argue that key issue 3 should also be considered in the context of individual goods and services.

We think that more research is needed on when an obligating event occurs. In taking forward this work, we would encourage IPSASB to consider further the extent to which a liability may arise before all eligibility criteria have been met, for example for a person that has worked for a number of years and therefore has a valid expectation that they will receive a state pension once they reach retirement age.

Key issue 4: Do present obligations for cash transfers financed by contributions occur at an earlier point than for non-contributory programs? *(paragraphs 44 to 50 on pages 13 to 15 of Consultation Paper)*

We agree there is a need to consider contributory programs separately, particularly in terms of the individuals who are making contributions having a greater expectation that they will receive the expected benefits, for example when they retire. We accept there might be a specific set of circumstances that might create an earlier obligating event.

The state pension highlights the difficult issues involved, particularly where an individual is making the necessary contributions in terms of taxation and could therefore be said to have already "earned" at least a part of the eventual pension entitlement. We therefore acknowledge the argument that individuals can earn the right to benefits such as the old age pension before reaching retirement age – and that this could be said to represent an obligation on the part of government that should be recognised in the financial statements. We also acknowledge in the Interpretation that a constructive obligation may be created by communicating information to individuals and the Consultation Paper does include in paragraph 44 the example of an individual's expectation of receiving a state pension being strengthened by receiving details of estimated future benefits.

At this stage however, and without having a sound conceptual basis for saying so, we would argue that any pension "earned" should not be reported as a liability in the government's financial statements. We do, however, consider that this is important information that should be covered in financial reporting or, more likely, in long term fiscal sustainability reporting.

We would also argue that, were a liability to be recognised before an individual reached the state retirement age, the present obligation should only arise for the benefits that have been earned, for example the number of years of contribution, and should not include expected future years of contribution.

Key issue 5: Is the revalidation of Eligibility Criteria a Recognition Criteria or a Measurement Attribute? *(paragraphs 51 to 55 on pages 15 to 17 of Consultation Paper)*

This can depend on the particular social benefit that is being considered and the eligibility criteria that are being revalidated. In principle, revalidation of eligibility criteria should be an important recognition criteria, particularly for social benefits such as unemployment benefit, which an individual might only expect to receive for a short period of time before returning to the workplace. For such short-term benefits, we agree with the view that the government's obligation should not exceed the maximum amount that an individual is entitled to receive from one revalidation point to another

A different view may however be reached for social benefits that are more long-term in nature, for example the state old age pension and incapacity benefit. The main eligibility criteria for these benefits are unlikely to change and, whilst annual declarations of existence or incapacity may be an important feature of administering these programs, the extent of the government's obligation should not be limited to the next revalidation point. For these longer-term benefits, the government's obligation should be based on other information, such as actuarial assumptions regards life expectancy.

Key issue 6: An alternative model: executory contract accounting with the recognition of liabilities arising only from legal obligations (*paragraphs 24 to 26 on page 9 of Consultation Paper)*

Having proposed a similar approach in the Exposure Draft of the Interpretation, we have reservations about the executory contract model, particularly in terms of identifying exactly what it is that is being received in exchange for social benefits provided. This exchange, which is clearly more than the receipt of taxes, is very difficult to rationalise in terms of individuals not being poor (eg, through the provision of unemployment benefit) or being alive (eg through the provision of healthcare).

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We note the arguments put forward in the consultation paper in support of the executory contract model, in particular the argument that recognising liabilities at the point a legal entitlement arises is less ambiguous than identifying the point at which a constructive obligation arises. We would, however, advise caution in taking forward work on an executory contract approach, both because of the difficulties involved in identifying the exchange and the fact accounting is moving in a direction that focuses more on the substance of providing services rather than the legal form of contracts.

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28 July 2008

Dear Sir

Project Brief on Long-term Fiscal Sustainability Reporting

The UK Accounting Standards Board (ASB) welcomes the decision by IPSASB to make the Project Brief on Long-Term Fiscal Sustainability Reporting publicly available. The ASB strongly supports the proposed project and believes that sustainability reporting has a very important role to play in reporting on the long-term fiscal sustainability of governmental programs and finances. We shall follow the progress of this project with interest.

Since 2002 the UK Government has published a long-term public finance report to provide comprehensive analysis of long term demographic developments and their likely impact on the public finances. The information provided in this report, which analyses trend and forecast data over several decades, assists the Government in managing the public finances in the long term interests of the UK. This suggests that information on long-term fiscal sustainability can be helpful and relevant to users, in particular Ministers and Parliament.

The ASB notes the link between sustainability reporting and the separate consultation that IPSASB is carrying out on accounting for social benefits. We consider sustainability reporting to be a very innovative part of the proposed strategic approach on accounting for social benefits. We also consider the scope of the sustainability project should cover all governmental programs.

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