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Dear Stephenie

CONSULTATION PAPER ON REPORTING ON THE LONG-TERM SUSTAINABILITY OF PUBLIC FINANCES

The Public Sector Committee of The Institute of Chartered Accountants of Scotland (ICAS) welcomes the opportunity to comment on IPSASB's consultation paper "Reporting on the Long-term Sustainability of Public Finances". The Public Sector Committee is a broad based committee of ICAS members with representation across the public services.

The Institute's Charter requires its Committees to act primarily in the public interest, and our responses to consultations are therefore intended to place the general public interest first. Our Charter also requires us to represent our members' views and protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.

Overall comments

The ability of governments to report to the public on the long-term fiscal sustainability of public finances in a clear and consistent manner is a major challenge. The development of a suitable reporting framework would facilitate greater accountability and could encourage governments to consider more rigorously the impact of policies over a greater time horizon. However, developing a credible framework is a significant challenge for IPSASB and we have concerns as to whether the General Purpose Finance Report (GPFR) is the most appropriate medium for public sector reporting on fiscal sustainability. Therefore, we have significant concerns about the consultation paper's proposals for introducing long-term fiscal sustainability reporting into the GPFRs of public sector entities.

We believe that long-term fiscal sustainability reporting should be undertaken separately from financial reporting and that long-term fiscal sustainability reporting at whole of government level, only, is likely to be meaningful. Our key concern is the combining of an accounting framework which uses historic financial information with a statistical based framework which uses prospective financial information.

We believe that the stewardship aspect of accountability is the most important financial reporting objective for the public sector, which we see as being incompatible with a framework which uses prospective financial information. We also have concerns about the inclusion of material on long-term fiscal sustainability within the other information which is published with General Purpose Financial Statements (GPFs), on the grounds that management commentaries are becoming overburdened with too much information which detracts from the management's story about how an entity has performed over the financial year.

Central governments are responsible for setting fiscal policy and policies on how public services are funded. As public sector entities, including sub-national government entities, may have no or incomplete control over these matters, it is difficult to envisage how it will be possible for public sector entities to provide meaningful information on the long-term fiscal sustainability of the services they provide.

Any guidance on reporting on long-term fiscal sustainability will need to clearly distinguish between the material which is to be included within GPFs and that to be included within the other information published with GPFs; it does not do so at the moment. However, the consultation paper does discuss the extension of recognition and measurement criteria to include prospective financial information (exhibit 4) and discusses the inclusion of additional statements (preliminary view 2). These developments could impact on the Conceptual Framework, being developed by IPSASB, and on whether GPFs give "a true and fair view" or "present fairly...."

We disagree with IPSASB's statement in paragraph 7.5.4 that the "need for, level of and extent of assurance [on prospective financial information] is a matter for preparers to form a judgement on in conjunction with their auditors". Where developments impact on GPFs, the level of assurance needed will not be a matter for the preparers and the auditors as the prospective financial information would form part of the accounting framework.

It is also incumbent on standard setters to undertake a regulatory impact assessment of new standards and to draw conclusions as to whether the benefits of applying a new standard outweigh the costs. If a standard setter does not make this judgement and sets standards which are overly burdensome it could undermine the accounting framework they have established.

Please do not hesitate to contact me if you would like to discuss our response further.

Our comments on IPSASB's preliminary views are set out in the Appendix.

Yours sincerely



CHRISTINE SCOTT
Assistant Director, Charities and Public Sector

APPENDIX

Preliminary view 1

The presentation of information on long-term fiscal sustainability is necessary to meet the objectives of financial reporting (accountability and decision-making) as proposed in IPSASB's consultation paper, "Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities", issued in September 2008. (Section two)

Comments

We do not agree that the presentation of information on long-term fiscal sustainability is necessary to meet the financial reporting objectives of accountability and decision-making.

In our response to the consultation paper "Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities" (dated 31 March 2009), we stated that we believe that the following should be excluded from the scope of general purpose financial reporting:

- "prospective financial information and other information about the reporting entity's future service delivery activities and objectives and the resources necessary to support those activities."

This is on the basis that we do not agree that the scope of financial reporting should expand beyond historic financial information, other than information necessary to comply with IPSAS 14 "Events after the Reporting Date".

We also believe that the financial statements and other information contained in the GPFs of public sector entities should give accountability more weight than decision-usefulness and that this should be reflected in IPSASB's Conceptual Framework.

Section two of the consultation paper illustrates the information needs of users using set theory. The focus of this consultation is the GPF, of which GPFs are a sub-set. However, paragraph 2.3.1 of the consultation paper states that:

- "There is still considerable debate on (a) the type and format of information that should be referred to as GPFs and GPFs and (b) the demarcation lines between GPFs, GPFs and other information."

This is very much at the heart of this and related consultations and confirmation of IPSASB's views on changes to the scope of the GPFs and to the other information contained in the GPF is vital if commentators are to express their views clearly, with minimal risk of misinterpretation.

This distinction is essential for both the public sector entities and their auditors so that they understand and can comply with their respective responsibilities towards the GPFs and other information published with them.

We have concerns about exhibit four (following paragraph 2.5.1) which extends the recognition and measurement criteria of assets and liabilities to include the transfer of future economic resources. We believe that this approach distorts the statement of financial position and the statement of financial performance in a manner which would be counter to the stewardship objective.

Preliminary view 2

IPSASB guidance should recommend that long-term fiscal sustainability information in GPFRs be presented either through:

- *Additional statements providing details of projections; or*
- *Summarised projections in narrative reporting. (Section 3)*

Comments

We do not believe that additional statements providing details of projections should be included within the GPFSs of public sector entities or within other information contained in GPFRs.

Public sector entities are expected to apply the going concern concept to the preparation of GPFSs and GPFRs, prepared in accordance with generally accepted accounting practice, are required to give “a true and fair view” or “present fairly” the financial position and financial performance, etc of the entity. Providing additional statements which include prospective financial information would require consideration of how these two cornerstones of financial reporting are affected.

Central governments are responsible for setting fiscal policy and policies on how public services are funded. As public sector entities, including sub-national government entities, may have no or incomplete control over these matters, it is difficult to envisage how it will be possible for public sector entities to provide meaningful information on the long-term fiscal sustainability of the services they provide even if it is assumed that policies on service delivery remain unchanged for the purposes of sustainability reporting.

Preliminary view 3

IPSASB guidance should be based in the concept of the reporting entity and should provide recommended practice for consolidated reports presented by all levels of government. (Section 4)

Comments

In our comments on preliminary view 2, we set out the reasons why we do not believe it is possible for individual public sector entities to report on fiscal sustainability and our comments apply equally to the concept of the reporting entities generally.

However, we would welcome the preparation of whole of government accounts by national governments and believe that it would be desirable for GPFRs prepared at whole of government level to be accompanied by narrative which explains what the figures say about the state of the public finances and how successful the government has been in working towards or achieving its policy commitments.

ICAS has developed a policy on how we believe the UK Government could improve its accountability through the preparation of whole of government accounts with accompanying narrative commentary. This includes recommendations on developing both short and long term outcome objectives against which progress can be reported on an annual basis. Our policy would appear relevant in other jurisdictions.

The policy position is set out in our pre-UK general election briefing 'Beyond the Numbers' and the key points we raise in relation to accountability are as follows:

- We believe that the Government should produce narrative commentary to accompany UK whole of government accounts in the style of a Business Review, as is required from large UK companies. The Business Review should clearly explain what the figures say about the state of the public finances and how existing commitments are to be met. This approach would provide an opportunity for Government to report on both its achievements and shortcomings against short and long term outcome objectives.
- The current reporting framework is weak in relation to longer term issues where timescales extend beyond Government terms of office. Developing both short and long term outcome objectives for reporting in the Business Review provides an opportunity to improve accountability by setting out intentions in advance and by making a commitment to report back on actual performance. Performance reporting should focus on achievement against short term objectives and on progress against longer term objectives.

The full version of 'Beyond the Numbers' is available on the ICAS website at:

www.icas.org.uk/beyondthenumbers

Preliminary view 4

IPSASB guidance should recommend that long-term fiscal sustainability indicators be selected based on a) their relevance to the entity, b) the extent to which the indicators meet the qualitative characteristics of financial reporting, and c) their ability to describe the scale of the fiscal challenge facing the entity. It should also recommend that comparative information is provided and that the reasons for ceasing to report indicators, if this occurs, are disclosed. (Section 5)

Comments

We do not believe that fiscal sustainability reporting is feasible below whole of government level and we set out our views on whole of government accounts and accompanying narrative information in our response to preliminary view 3.

We are not against the publication of information on long-term fiscal sustainability separate from whole of government accounts. However, prospective financial information of this nature does not fit well with information prepared to comply with accounting frameworks and we consider that such information should be made available in a separate document.

Preliminary view 5

IPSASB guidance on long-term fiscal sustainability reporting in GPFs should recommend that the entity disclose:

- *Any deviations from the principle that long-term fiscal sustainability projections are based on current policy;*
- *The basis on which projections of inflows from taxation and other material revenue sources are made;*
- *Any other key assumptions underpinning long-term fiscal sustainability projections; and*
- *Details of key aspects of the governing legislation and regulation, and the underlying macro-economic policy and fiscal framework. (Section 6)*

Comments

We agree that guidance on long-term fiscal sustainability should include the information mentioned, although we do not believe it would be appropriate for such information to be based on anything other than current policy. Also, we do not agree that information on long-term fiscal sustainability as set out in the consultation paper should be included in GPFRs.

Preliminary view 6

IPSASB guidance in long-term fiscal sustainability reporting in GPFRs should recommend that the entity disclose:

- *Time horizons for fiscal sustainability projections presented or discussed in the GPFRs as well as the reason for modifying time horizons and any published plans to modify those horizons;*
- *Discount rates, together with the reason of their selection;*
- *Results of key sensitivity analyses; and*
- *Steps taken to ensure that projections are reliable.*

Comments

We agree that entities should report key underlying assumptions when presenting information on long-term fiscal sustainability. However, we believe that information on long-term fiscal sustainability as set out in the consultation paper should not be included in GPFRs.

Preliminary view 7

IPSASB guidance on the long-term fiscal sustainability reporting in GPFRs should recommend that a) the underlying projections should have been prepared or updated within five years of the reporting date, and b) the date of preparation or update should be disclosed.

Comments

We believe that it would make sense for reports in long-term fiscal sustainability to be updated annually and for the reporting date to be the final date of the financial year just past. (Section 7)