

27 February 2012

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CANADA

Submitted to: [www.ifac.org](http://www.ifac.org)

Dear Stephenie

**Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances**

The New Zealand Accounting Standards Board (NZASB) is pleased to submit its comments regarding Exposure Draft 46 Proposed Recommended Practice Guideline *Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances* (ED 46). We have consulted on this document in New Zealand and expect that you will also receive comments directly from New Zealand constituents.

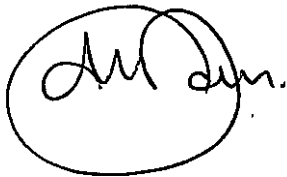
The NZASB strongly endorses the IPSASB's establishing principles for reporting on long-term sustainability. We consider that this approach will encourage high quality reporting without constraining the continuing development of reporting on long-term sustainability. This aspect is of particular interest to us given the ongoing developments in reporting on long-term sustainability in New Zealand.

We agree with the IPSASB's proposal to issue a Recommended Practice Guideline (RPG) as opposed to an IPSAS. We agree that, in some cases, there can be a role for guidance that is less authoritative than an IPSAS.

We note that central and local governments in New Zealand are already subject to statutory reporting requirements on fiscal sustainability. We also have a domestic financial reporting standard on the preparation and presentation of general purpose prospective financial statements. Any RPG issued by the IPSASB would therefore have immediate relevance for New Zealand entities.

We have responded to the specific questions posed in the Exposure Draft in the appendix to this letter. If you have any queries or require clarification of any matters in this submission, please contact Joanne Scott ([joanne.scott@xrb.govt.nz](mailto:joanne.scott@xrb.govt.nz)) or me.

Yours sincerely

A handwritten signature in black ink, enclosed within a hand-drawn oval. The signature appears to be 'A. Ryan'.

Angela Ryan

**Deputy Chairman – New Zealand Accounting Standards Board**

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## Appendix

### NZASB's comments and Responses to the Specific Matters for Comment on ED 46

#### 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.

We agree that the characteristics set out in paragraph 15, taken together, are useful indicators of the existence of users that are likely to be interested in information on long-term fiscal sustainability. However we do not consider that paragraph 15(c) (which refers to entities having wide decision making powers over service delivery levels) should be an indicator without the one of the other characteristics also being present.

We consider that paragraph BC13 clearly indicates the types of entities that the IPSASB considers should possibly provide information on fiscal sustainability. We therefore recommend that the comments in paragraph BC13 be included in the body of the RPG. For the avoidance of doubt we also suggest clarification that “reporting on the long-term fiscal sustainability of their finances is unlikely to be appropriate for individual government departments and sub-entities of local governments.” (See also our comments on the reporting boundary and application to sub-entities).

If characteristic (c) is retained, we consider that it should refer to both service delivery levels *and* types of services. We consider that there are more likely to be users for information on long-term fiscal sustainability in relation to entities that are responsible for providing a wide range of services rather than for a narrow range of services.

#### 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?

We support the dimensions of long-term fiscal sustainability in paragraphs 27–37, including the discussion of service capacity in paragraph 32. However, we consider that it would be useful for the document to acknowledge that some entities may be required, by legislation, to present information on projected flows based on continuing existing policies or current levels of services.

### **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?

We support the proposed disclosures. However, we recommend that the IPSASB make it easier for readers to identify the proposed disclosures. We have given some examples of how this could be done (see our “other comments”).

#### **Other comments**

##### *Reporting boundary and application to sub-entities*

Paragraph 10 expresses the view that entities and activities included in long-term fiscal sustainability projections should be the same as those for the financial statements. Paragraph 12 then goes on to describe one possible exception, being the disclosure of information based on the General Government Sector.

We would like the RPG to explicitly state that, other than this exception, the full requirements of the RPG should be applied at an entity level only. Our reason for making this suggestion is a concern about the interaction between legislation and regulations established for other purposes, and this RPG.

There are some entities in New Zealand, such as local authorities, that are required to prepare long-term financial forecasts to which this RPG would apply. Often, the legislation or regulations requiring the forecasts also stipulates that the finances, performance measures etc must be reported at an activity or group of activity level, (that is, at a sub-entity level). We would be concerned if the RPG were interpreted as having to be at the sub-entity level. In some instances it might be appropriate to do so, but in many instances it would not.

Although it could be argued the tests proposed in paragraph 15 (a) and (b) would be met only an entity level, it could also be argued that the presentation requirements in paragraph 17 should be applied to a sub entity. Proponents of this argument could look to paragraph 10 in support – paragraph 10 refers to "entities and activities".

In our view implementing the proposals in the RPG at a sub-entity level would require arbitrary allocations, and would create work that would add little, if any, value to the reader. We consider that because local authorities are able to prioritise between their activities, it is appropriate to test and report sustainability at an entity level only.

See our suggested amendment to paragraph BC13 (in our response to SMC 1) as one way of addressing this issue.

##### *Location of material*

We consider that some of the discussion in the body of the proposed RPG would be better located in the Basis for Conclusions. The ED reflects the tensions involved in developing a less restrictive style of guidance. Nevertheless, we encourage the IPSASB to consider the purpose of specific sentences. For example, individual sentences may (i) establish the recommended practice, (ii) support/explain the recommended practice or (iii) explain why the IPSASB has taken the position it has in the recommended practice. We consider that the third category belongs in the Basis for Conclusions. Paragraph 3 is an example where there is a mixture of recommended

practice and the Board’s rationale in the same paragraph (refer to the first item in the table of editorial suggestions below).

*Editorial suggestions*

We have also identified some editorial suggestions as follows.

Proposed change	Comment
<p>3. <del>The flows relating to programs providing social benefits, including entitlement programs that require contributions from participants, can be a highly significant component of reporting on long-term fiscal sustainability for many entities. However,</del> The scope of this RPG includes all an entity’s projected flows <del>and</del>. <u>It</u> is not limited to those related to programs providing social benefits.</p>	<p>We consider that the first sentence in this paragraph should be located in a Basis for Conclusions.</p> <p>Alternatively if it is kept in the body of the RPG, we recommend that it be accompanied by an explanation that although the scope of the RPG includes all projected flows, entities may wish to provide more detailed information or subsets of information on significant components such as flows relating to social benefits.</p>
<p>10. <del>This RPG reflects the view that</del> Entities and activities included in long-term fiscal sustainability projections should be the same as those for the financial statements. This enhances the understandability of projections and increases their usefulness to the users of general purpose financial reports.</p>	<p>We consider that the document should clearly state what the IPSASB considers to be best practice.</p>
<p>11. <del>If in the event that entities within the reporting entity boundary for the long-term fiscal sustainability projections differs from the reporting entity for the financial statements are different to those for the long-term fiscal sustainability projections, the differences those entities</del> should be identified, and, where possible, the estimated impact on the projections disclosed.</p>	<p>We propose the changes for ease of reading.</p>

Proposed change	Comment
<p><b>Determining Whether to Report on Long-Term Fiscal Sustainability</b></p> <p>14. In evaluating whether to report on the long-term sustainability of its finances an entity needs initially to assess whether potential users exist for prospective financial information.</p> <p><del>15. The relevance of reporting on an entity's long-term fiscal sustainability should be considered in the context of that entity's funding and capacity to determine service delivery levels. There are likely to be users for long-term fiscal sustainability information for entities with one or more of the following characteristics:</del></p> <p style="padding-left: 20px;"><del>(a) Significant tax and/or other revenue raising powers;</del></p> <p style="padding-left: 20px;"><del>(b) Powers to incur debt; or</del></p> <p style="padding-left: 20px;"><del>(c) Wide decision-making powers over service delivery levels.</del></p> <p><u>15 The relevance of reporting on an entity's long-term fiscal sustainability should be considered in the context of that entity's funding and capacity to determine service delivery levels.</u></p>	<p>We consider that paragraphs 14 and 15 would flow better as shown. Our comments on SMC 1 are also relevant.</p>
<p>39. The date at which a full set of projections was made and the basis and timing of subsequent updating should be disclosed.</p> <p><u>39A. While regular updates are desirable, this RPG acknowledges that annual updating may not be realistic for all entities, particularly those at sub-national levels, which may be making and reporting on projections for the first time. However, there is an inverse relationship between the robustness of assumptions on which projections are made and the elapse of time since they were made. During periods of global financial volatility the risk that projections made some time before the reporting date are outdated increases, with a consequent reduction of the ability of such information to meet the objectives of accountability and decision-making.</u></p>	<p>We recommend separating the recommended best practice from the accompanying explanation.</p>
<p><u>39.A An entity should disclose:</u></p> <p style="padding-left: 20px;">(a) <u>the assumptions regarding the continuation of current policy through the projection period</u></p> <p style="padding-left: 20px;">(b) <u>relevant legal limitations on future flows and how these have been addressed in making the projections; and</u></p> <p style="padding-left: 20px;">(c) <u>relevant sunset provisions and how these have been addressed in making the projections.</u></p> <p>40. <del>This RPG adopts the view that,</del> Where flows for particular programs and activities are individually modeled, information is most useful if it is assumed that current policy is held constant through the entire</p>	<p>We propose that the RPG highlight the recommended disclosures. We then suggest that you acknowledge the difficulties that might arise and note that the disclosures may not be required for flows that are not individually projected.</p>

Proposed change	Comment
<p>projection period. There can be tensions if (a) there is a conflict in legal obligations or (b) if current programs have “sunset provisions.” For example a social security program may be governed by legal provisions that it is unlawful to make payments once an earmarked fund is exhausted, although entitlements of beneficiaries will continue after the exhaustion of that fund. Assuming that the fund will not meet obligations once it is exhausted might reflect a strict legal position, but an entity may need to assess whether the presentation of projections on such a basis underestimates the extent of the fiscal challenge facing the social security program.</p> <p>41. Some programs have sunset provisions whereby they terminate after a specific period. In many cases there may be a strong probability that such programs will be replaced by similar programs, so adopting a strict legal termination principle may lead to an underestimate of outflows, which impairs the usefulness of information. <del>The approach to any legal conflicts and sunset provisions should therefore be disclosed.</del></p> <p>42. For flows that are not individually projected, the distinction between current and future policy is unlikely to be critical to the projections and it may be sufficient to disclose general assumptions.</p>	
<p><u>42A An entity should disclose:</u></p> <p><u>(a) The main sources of taxation and other revenue flows;</u></p> <p><u>(b) the approach taken in projecting taxation and other revenue flows.</u></p> <p>43. The main sources of taxation and other revenue flows, such as inter-governmental transfers, should be identified, together with their significance to an entity’s revenue sources. Taxation flows may be projected to grow in line with nominal gross domestic product or an inflation index or may be individually modeled using a more sophisticated approach. Users need to be informed of the approach and of any relevant considerations relating to tax banding, allowances and thresholds.</p>	<p>We propose that the RPG highlight the recommended disclosures.</p>

Proposed change	Comment
<p>48. Entities should <u>disclose</u>:</p> <ul style="list-style-type: none"> <li><u>(a) the approach to inflation;</u></li> <li><u>(b) the discount rates applied;</u></li> <li><u>(c) the reasons for their selecting these rates;</u></li> <li><u>(d) any changes in these rates since the last reporting date; and</u></li> <li><u>(e) the reason for such changes.</u></li> </ul> <p>48A. There are two approaches to inflation: (i) it may have <del>indicate how they deal with inflation, in particular whether inflation has</del> been taken into account in making projections or (ii) <del>whether</del> projections <u>may have been</u> <del>are</del> made at current prices (prices prevailing at the reporting date). If the projections include inflation, then the discount rate should also include inflation. If the projections are at current prices, the discount rate should exclude inflation. <del>Entities are advised to disclose: (a) the approach to inflation (b) the discount rates applied, (c) the reasons for their selecting these rates, (d) any changes in these rates since the last reporting date, and (e) the reason for such changes.</del></p>	<p>We propose that the RPG highlight the recommended disclosures.</p>