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John Stanford
Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street, 4th Floor
Toronto, ONTARIO
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Dear Mr. Stanford:

SUBJECT: Consultation Paper: Public Sector Specific Financial Instruments

Thank you for the opportunity to comment on the Consultation Paper: *Public Sector Specific Financial Instruments* issued in July 2016.

The Government of Canada bases its accounting policies on the accounting standards issued by the Public Sector Accounting Board (PSAB) of Chartered Professional Accountants of Canada (CPA Canada). Although the Government of Canada is not required to follow the International Public Sector Accounting Standards (IPSAS), IPSAS are regarded as an important secondary source of generally accepted accounting principles.

Our comments with respect to the preliminary views and specific matters for comment in the Consultation Paper (CP) are included in the attached appendix. We have incorporated comments from our Department of Finance in the response.

We thank you again for providing the opportunity to comment on this Consultation Paper. If you require further information, please do not hesitate to contact diane.peressini@tbs-sct.gc.ca (613-369-3107) or christopher.meyers@canada.ca.

Canada

Yours sincerely,

Diane Peressini
Executive Director,
Government Accounting Policy and
Reporting

c.c.: Bill Matthews, Comptroller General of Canada

Christopher Meyers, Executive Director & Deputy CFO, Department of Finance

APPENDIX

Responses to Preliminary Views and Specific Matters for Comment

Preliminary View – Chapter 2 (following paragraph 2.9)
Definitions are as follows:
(a) Monetary authority is the entity or entities, including the central bank or a department(s) of the central (national) government, which carry out operations usually attributed to the central bank.
(b) Reserve assets are those external assets held by monetary authorities that are readily available for balance of payments financing needs, intervention in the currency markets to affect exchange rates and maintaining confidence in the currency and the economy.
Do you agree with the IPSASB's Preliminary View – Chapter 2?

We agree.

Preliminary View – Chapter 3-1 (following paragraph 3.10)
Definition is as follows:
Currency in Circulation is physical notes and coins with fixed and determinable values that are legal tender issued by, or on behalf of the monetary authority, that is, either that of an individual economy or, in a currency union to which the economy belongs.
Do you agree with the IPSASB's Preliminary View – Chapter 3-1?

We agree (although the sentence structure of this definition needs improvement).

Preliminary View – Chapter 3-2 (following paragraph 3.30)
Notes and coins (currency) derive value because they are legal tender and accepted as a medium of exchange and therefore serve the same purpose and function in the economy. As the purpose and function of notes and coins is the same, the IPSASB's view is the accounting treatment should be consistent for both (as noted in paragraph 3.12), with the recognition of a liability when issued.
Do you agree with the IPSASB's Preliminary View – Chapter 3-2?

We do not agree with this preliminary view, as it is not the purpose and function of the types of currency that establishes an obligation. Whether a jurisdiction has a liability depends on its obligations related to notes and coins respectively, and whether these are binding legal or non-legal obligations.

In Canada, while there is legislation related to notes that creates a legal obligation, there is no legal obligation for the exchange or redemption of coins. We do not agree with paragraph 3.29 which states that a past practice of redeeming coins necessarily creates a present non-legally binding obligation. For example, in 2012 the Government of Canada (through the Royal Canadian Mint) announced its intention to eliminate the penny, and decided to reimburse financial institutions for redeeming these coins. Consequently, a liability was recognized equal to the estimated value of the pennies in circulation. However, this past history does not create a present obligation for the government with respect to other coin denominations in circulation. In our view, the past event that creates a liability for the future elimination of another coin denomination would arise only on the government's announcement to accept responsibility.

Consequently, we believe that it is not appropriate to require that the accounting treatment for notes and coins must be the same – the related obligations should be assessed for each type of currency and, in certain circumstances, for each denomination of coins or notes, to determine if/when the definition of a liability is met.

Specific Matters for Comment – Chapter 3-1 (following paragraph 3.43)
When the monetary authority assesses that a present obligation does not exist as a result of the issuance of currency, because of the absence of a legal or non-legally binding obligation (approach 1), it results in the recognition of revenue (approach 2), please explain your view and your thoughts on what is the appropriate financial statement in which to recognize revenue:
(i) Statement of financial performance; or
(ii) Statement of net assets/equity?

Please provide the reasons for your support of your preferred option, including the conceptual merits and weaknesses; the extent it addresses the objectives of financial reporting and how it provides useful information to users.

We agree that, in the absence of a legally or non-legally binding obligation arising as a result of the issuance of notes or coins, revenue should be recognized. In our opinion, approach (i), recognition in the Statement of Financial Performance is the most appropriate presentation, as the issuance of currency is related to a transaction of the current period and results in an increase in the net financial position of the entity.

We do not agree that the cost of fulfillment is the appropriate measurement basis for a liability arising from a non-legally binding obligation for currency, as currency transactions always take place at the face value of the currency.

Preliminary View – Chapter 4 (following paragraph 4.14)
Definitions are as follows:
(a) Monetary gold is tangible gold held by monetary authorities as reserve assets.
(b) Tangible gold is physical gold that has a minimum purity of 995 parts per 1000.
Do you agree with the IPSASB's Preliminary View – Chapter 4?

We agree.

Specific Matters for Comment – Chapter 4-1 (following paragraph 4.50)
Should entities have the option to designate a measurement basis, based on their intentions in holding monetary gold assets (as noted in paragraphs 4.5-4.6)? Please provide the reasons for your support for or against allowing an option to designate a measurement basis based on intentions.

The measurement basis for financial statement items should represent the operational, service or financial capacity of the entity. In our opinion, monetary gold held for trading or held as a reserve asset to promote financial stability and long-term wealth preservation, is in both cases primarily held for its financial capacity. Consequently, an option to designate a measurement basis based on intention would still lead to market value as the most appropriate basis.

However, the revaluation of gold at market value when it is held for trading or as a reserve asset may warrant a different presentation of the changes in its value – through surplus/deficit or through net assets/equity. We believe that the fluctuations in the market value of gold held as a reserve asset is more appropriately reflected directly in net assets/equity, or in a dedicated revaluation surplus account similar to that used by the revaluation model for property, plant and equipment. This is because inter-period volatility in the price of gold is not relevant to the operations of the current period when the government's intent is to hold it for an indeterminate period.

Specific Matters for Comment – Chapter 4-2 (following paragraph 4.50)
Please describe under what circumstances it would be appropriate to measure monetary gold assets at either:
i. Market value; or
ii. Historical cost?
Please provide reasons for your views, including the conceptual merits and weaknesses of each measurement basis; the extent to which each addresses the objectives of financial reporting; and how each provides useful information.

If you support measurement based on intentions as discussed in SMC 4-1, please indicate your views about an appropriate measurement basis for each intention for which monetary authorities may hold monetary gold, as discussed in paragraph 4.5 (i.e., intended to be held for its contribution to financial capacity *because of its ability to be sold in the global liquid gold trading markets, or intended to be held for an indeterminate period of time).*

Please see discussion above for SMC 4-1.

Preliminary View – Chapter 5-1 (following paragraph 5.12)
Definitions are as follows:
(a) The IMF Quota Subscription is the amount equal to the assigned quota, payable by the member on joining the IMF, and as adjusted subsequently.
(b) SDR Holdings are International reserve assets created by the IMF and allocated to members to supplement reserves.
(c) SDR Allocations are obligations which arise through IMF member's participation in the SDR Department and that are related to the allocation of SDR holdings.
Do you agree with the IPSASB's Preliminary View – Chapter 5-1?

We agree with the definitions proposed.

The IPSASB should consider whether the IMF'S holdings of member currency (IMF Notes Payable, promissory notes, from the member perspective) merit explicit definition. The value of IMF Notes payable will fluctuate based on prevailing exchange rates through the Maintenance of Value calculation as well as drawings by the IMF. Accordingly, it is distinct from the IMF Quota Subscription itself.

The Maintenance of Value calculation on the promissory notes is, in our view, a unique transaction to the public-sector in that actual settlements (or encashment) of notes will occur based on prevailing exchange rates. There is no Maintenance of Value calculation performed on the Quota Subscription.

In addition to the balances identified above, it is worth noting that the IMF engages in a number of bi-lateral and multi-lateral lending arrangements with member countries (i.e. the New Arrangements to Borrow).

Preliminary View – Chapter 5-2 (following paragraph 5.33)
The IPSASBs view is that:
- *(a) The IMF Quota Subscription satisfies the Conceptual Framework definition of an asset and should be recognized, with initial measurement at historical cost. Subsequent measurement may be at historical cost when the translated value of the quota subscription equals the cumulative resources contributed to the IMF, when it does not it should be measured at net selling price.*
- *(b) SDR holdings satisfy the Conceptual Framework definition of an asset and should be recognized, with measurement at market value.*
- *(c) SDR allocations satisfy the Conceptual Framework definition of a liability and should be recognized, with measurement at market value.*

Do you agree with the IPSASB's Preliminary View – Chapter 5-2?

We do not agree with part (a) of this preliminary view with respect to subsequent measurement, but do agree with parts (b) and (c).

For part (a), we agree that the IMF Quota Subscription is an asset that should be initially measured at historical cost. However, we do not agree that the revaluation of the subscription in future periods due to foreign exchange rate fluctuations implies that the item should be valued at net selling price. As the IMF quota subscription cannot be sold, we question the relevance of applying this basis. As well, when a monetary item is measured at historical cost, the guidance in IPSAS 4 *The Effects of Changes in Foreign Exchange Rates,* is intended to translate the historical cost of the item into the functional currency of the entity – it does not change the measurement basis from historical to current.

SDR holdings and allocations are essentially currency, and therefore we agree that market value is the best measure of their financial capacity.

We also believe that the IPSASB should consider the presentation of the IMF balances. In particular, the Reserve Tranche Position, which is the net of the IMF Quota Subscription less any notes payable pertaining to the Quota Subscription, is a balance that represents the member country's external reserves. The IMF describes this Reserve Tranche position as a member's liquid claim on the IMF, much like a demand deposit in a commercial bank. We believe that the IPSASB should specifically permit the offsetting of the Quota Subscription and the related notes payable in order to promote the most relevant presentation of the entity's foreign reserves on the statement of financial position

Other matters for consideration

Multi-lateral development institutions

In our review of the proposed accounting treatment for the IMF Quota Subscription, we noted many similarities with issues arising in accounting for capital subscriptions to multilateral development banks, e.g. the World Bank group. The objectives of multilateral development banks are to reduce global poverty and improve people's living conditions and standards, to support sustainable economic, social and institutional development; and to promote regional cooperation and integration. This is achieved through the provision of low cost/low interest financing to the poorest countries and non-concessional lending to middle income countries.

Similar to the IMF, a member government's investment in these institutions provides an assigned proportionate shareholding that determines voting power and influence (control) on the organization, and demonstrates service potential through defined exit provisions that protect the return of capital and proportionate shares of accumulated earnings. Members may receive future benefits through their ability to leverage the paid-in capital for development lending, to optimize their policy development on the global stage, to advance their economic and political interests internationally, as well as increasing economic opportunities for member's national firms in international markets. Certain multi-lateral development banks operate non-concessional lending windows designed to generate market or near-market returns

These organizations typically do not pay dividends to shareholders. These investments cannot be sold and the only way to recover the investment is to withdraw from these organizations; in such situations, the member is entitled to the net asset value, i.e. the paid-in capital plus retained earnings or minus accumulated deficit. In practice, it is rare that members withdraw from these organizations.

As these investments are held exclusively by sovereign shareholders and have very specific development mandates, they are also clearly public-sector specific financial instruments. We believe that an expansion of the concepts put forth in the CP to investments in international financial institutions more generally would be advisable.

Foreign-reserve holdings

The CP correctly defines Reserve Assets and identifies IMF balances as a component of Reserve Assets.

We feel that the IPSASB should explore further the scope of guidance being provided for Reserve Assets. Although IMF balances are typically a significant component of Reserve Asset holdings, the extent of holdings is much more far ranging than just the IMF. The CP duly points this out.

Although it could be said that the specific types of Reserve Assets (i.e. debt securities and other financial instruments) are well served by existing standards, Reserve Asset portfolios are held in ways and for purposes that are unique to public-sector entities. The same could be said for the manner in which these Reserve Assets are financed.

Consequently, it is possible that the application of private-sector based financial instruments standards is not adequate in terms of representing the ultimate policy objectives of Reserve Asset portfolios held in the public sector at the sovereign and/or Central Bank level.