AUDIT NEW ZEALAND
Mana Arotake Aotearoa

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John Stanford
Technical Director
International Public Sector Accounting Standards Board
277 Wellington Street West
Toronto
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Dear John

IPSASB Exposure Draft 63 *Social Benefits*

We appreciate the opportunity to comment on the IPSASB's Exposure Draft 63 *Social Benefits* (ED 63).

We are pleased the IPSASB has continued to progress the development of a standard for Social Benefits.

While we are broadly supportive of the proposals, we consider the IPSASB has further work to do to ensure there is sufficient clarity over both the scope of the standard and the criteria for application of the insurance approach to certain social benefit schemes.

Our responses to the Specific Matters for Comment are attached.

In preparing this submission, we have consulted with our colleagues at the Office of the Auditor-General.

If you would like to discuss any of our comments, please phone me on 021 222 6107 or email me at robert.cox@auditnz.govt.nz.

Yours sincerely

Robert Cox

Robert Cox
Head of Accounting

Our responses to the Specific Matters for Comment in Exposure Draft 63:

1. **Do you agree with the scope of this Exposure Draft, and specifically the exclusion of universally accessible services for the reasons given in paragraph BC21(c)? If not, what changes to the scope would you make?**

   We agree with the proposal to scope out universally accessible services from ED 63. However, it is important there is a clear boundary between social benefits and universally accessible services given the similar characteristics of these benefits. If that boundary is not clear, this could give rise to implementation issues in determining when the standard applies.

   We also note that the IPSASB's project for Non-Exchange Expenses is considering the accounting for universally accessible services. As that project is less advanced than the social benefits project, it is sensible in the meantime to exclude universally accessible services from ED 63. However, as the IPSASB develops its proposals further for universally accessible services, the IPSASB should revisit at a future date whether the accounting for universally accessible services should be addressed in a single standard that includes social benefits if the underlying accounting principles are similar.

   While we agree in the meantime with the scope exclusion for universally accessible services, we consider some of the reasons for this provided by BC21(c) are not convincing.

   BC21(c) suggests that social benefit expenses are not a type of non-exchange expense. We disagree and consider social benefit expenses are a sub-set of non-exchange expenses. We recommend the references to "non-exchange expenses" in BC21(c) be amended to "<u>other</u> non-exchange expenses". This amendment will help clarify that social benefit expenses are a type of non-exchange expense.

   Additionally, BC21(c) states that the liabilities and expenses associated with social benefits can be measured by reference to an individual's eligibility to receive the social benefit, which does not apply to non-exchange expenses. We disagree with this. Some non-exchange expenses (that are unlikely to be social benefits) are provided on the basis of an individual meeting eligibility criteria (which may be ongoing) that affects both recognition and measurement of the liability. For example, an entity may grant scholarships to students to help fund tuition costs for courses that span several years. The receipt of future funding under the scholarship however is dependent on the student passing their exams and remaining enrolled in the course.

2. **Do you agree with the definitions of social benefits, social risks and universally accessible services that are included in this Exposure Draft? If not, what changes to the definitions would you make?**

   We consider the definitions of social benefits, social risks and universally accessible services are not clear, particularly in relation to health services.

The definition of social risk refers to "health" as being an example of a social risk. This appears reasonable, but we note that the definition of universally accessible services requires eligibility criteria to be not related to social risk. Although a universal healthcare service is available to all, it is there to address the social risk of poor health and therefore we consider the eligibility to use the service is dependent on having a health issue (a social risk). Therefore, under the proposed definitions, our interpretation would be that a universal healthcare system is not a universally accessible service.

We consider that the definitions need to be reconsidered to clarify this and particularly whether the prohibition of eligibility being linked to social risk is needed in the definition of universally accessible services.

We note the statement in AG7 that:

> *Where benefits in kind are universally accessible, for example a universal healthcare service, these do not meet the definition of a social benefit for the purposes of this [draft] Standard.*

We do not consider that including this statement in AG7 resolves the problem with the definitions. If universal healthcare is not a social benefit and does not meet the definition of universally accessible services, then what is it?

We recommend greater clarity be provided on assessing when health benefits are a social benefit and when they are a universally accessible service.

A reasonable outcome would be definitions that allow the health services provided by a universal healthcare system to be accounted for as universally accessible services, but cash benefits paid to the sick and disabled to be accounted for as social benefits. We do not consider that the current definitions achieve this.

3. Do you agree that, with respect to the insurance approach:
- **(a) It should be optional;**
- **(b) The criteria for determining whether the insurance approach may be applied are appropriate;**
- **(c) Directing preparers to follow the relevant international or national accounting standard dealing with insurance contracts (IFRS 17, Insurance Contracts and national standards that have adopted substantially the same principles as IFRS 17) is appropriate; and**
- **(d) The additional disclosures required by paragraph 12 of this Exposure Draft are appropriate?**

If not, how do you think the insurance approach should be applied?

a) No, we consider that where an entity meets the insurance accounting criteria of paragraph 9, the entity should be required to apply a relevant insurance accounting standard and recognise liabilities as appropriate under that standard.

Removing the option for the general obligating event approach should help ensure greater international consistency, transparency and accountability for reporting on social benefit schemes intended to be fully funded, as the entity will be required to recognise liabilities incurred which are funded by the contributions received. We think it could be significantly misleading if an entity that meets the criteria of paragraph 9 were to present financial statements with significant assets for contributions invested but were to record minimal liabilities because the liability criteria of the obligating event approach were not met.

b) Generally, we consider that the criteria are appropriate. However, we believe that more guidance should be provided on the fully funded by contributions criterion. We discuss this further below.

Our consideration of the insurance approach is in the context of New Zealand's accident compensation scheme, which is administered by the Accident Compensation Corporation (ACC). ACC presently applies insurance accounting using a Standard based on IFRS 4 *Insurance Contracts.*

ACC's obligations are funded by levy payers (e.g. individuals, businesses, motorists) and also government appropriation. ACC is required to operate five separate "accounts" where it tracks the levy and appropriation funding received and the obligations for each of those accounts. The government provides a significant amount of appropriation funding to ACC each year, which primarily funds ACC's obligations for the "non-earners" account, such as for accident costs arising from children, beneficiaries and retirees. For the 30 June 2017 financial year, ACC received government appropriations of $1.2bn and gross levy revenue of $2.9bn. The non-earners account has the second largest outstanding claims liability at $8b and is therefore significant for ACC. The ACC scheme funds both health services (treatment and rehabilitation) as well as compensation for loss of earnings.

In the context of ACC, we raise the following matter:

Paragraph 9(a) requires that the social benefit scheme is intended to be fully funded from contributions. Some guidance on this is provided in AG12 which requires the scheme to be funded by "contributions or levies paid by or on behalf of….". We find this unclear, particularly how to interpret government appropriation funding paid into a scheme on behalf of those not able to contribute themselves (e.g. beneficiaries and children).

From the Whole of Government reporting perspective, arguably the ACC scheme is not fully funded as the appropriation funding for the non-earners account comes from general taxation.

From the perspective of ACC as a separate legal and reporting entity, it appears the criterion is met as the non-earners part of the scheme is in effect funded by contributions by the government on behalf of the potential beneficiaries. This would potentially mean that the criteria are met for a reporting entity within the Government but not for the Whole of Government financial reporting.

We consider the Standard could be clarified further in relation to Government funding into a social benefit scheme on behalf of beneficiaries who are not in a position to contribute themselves.

c) As IFRS 17 is reasonably new and implementation is several years away in the commercial sector, we have no practical experience of applying the standard and our knowledge is limited. Overall, we would be supportive of an approach of applying IFRS 17 based standards under the insurance approach. However, we are concerned that some aspects of IFRS 17 may not be appropriate for the public sector (particularly in relation to discount rates and risk adjustments). We note the discussion of these matters in the basis for conclusions in the ED, but do not agree with IPSASB decision to not address and resolve the concerns about discount rates and risk adjustments.

d) We are comfortable with the disclosure requirements for the insurance approach in the ED.

4. Do you agree that, under the obligating event approach, the past event that gives rise to a liability for a social benefit scheme is the satisfaction by the beneficiary of all eligibility criteria for the next benefit, which includes being alive (whether this is explicitly stated or implicit in the scheme provisions)?

If not, what past event should give rise to a liability for a social benefit?

We acknowledge that determining the point at which a liability arises for a social benefit is complex and difficult, and the consequences of different recognition points could be substantially different.

We consider the conceptual basis for the IPSASB's purposed recognition point, including being alive, is weak, and we see merit in the alternative views expressed in the ED. However, we consider it important that a standard in this important area is concluded. The proposal in the ED is relatively straight forward to implement and from a pragmatic perspective, we can support the proposed recognition approach as a reasonable outcome given the difficulties in this area.

5. Regarding the disclosure requirements for the obligating event approach, do you agree that:

(a) The disclosures about the characteristics of an entity's social benefit schemes (paragraph 31) are appropriate;

Yes, we believe that the disclosures about the characteristics of an entity's social benefit schemes are appropriate.

(b) The disclosures of the amounts in the financial statements (paragraphs 32–33) are appropriate; and

Yes, we believe that the disclosures about the amounts in the financial statements are appropriate.

(c) For the future cash flows related to from an entity's social benefit schemes (see paragraph 34):

(i) It is appropriate to disclose the projected future cash flows; and

(ii) Five years is the appropriate period over which to disclose those future cash flows.

If not, what disclosure requirements should be included?

We consider that longer-term financial information (beyond five years) on the forecast future cash outflows for social benefit schemes together with information on how those outflows will be funded provides important information relevant to the readers of a Government's (or public sector agency's) financial statements. A longer-term view to the disclosure of social benefit information may help readers understand the longer-term cost and sustainability of current social benefit scheme policy settings.

We encourage the IPSASB to consider how it could improve the reporting in this area, particularly when governments do not publish long-term fiscal sustainability information.

Notwithstanding our comments above, we believe that the future cash flow disclosures proposed in the ED are a reasonable minimum level of disclosure where an entity does not disclose fuller future cash flow information elsewhere.

If an entity discloses future cash flow information for periods for more than 5 years elsewhere, such as in a long-term fiscal strategy document, we consider the entity should disclose where that information can be located. In this case, we don't think it should be mandatory for the entity to disclose the 5 year forecast information when it is able to cross-reference to much more informative information.

6. Do you think the IPSASB should undertake further work on reporting on long-term fiscal sustainability, and if so, how?

If you think the IPSASB should undertake further work on reporting on long-term fiscal sustainability, what additional new developments or perspectives, if any, have emerged in your environment which you believe would be relevant to the IPSASB's assessment of what work is required?

We have no comments to make on this question.

7. Other comments

We have no further comments to make on ED 63.