

Reporting on the Long-Term Sustainability of Public Finances

Issues Paper: Proposal to Comment on the IPSASB's Consultation Paper

Purpose

1. This issues paper provides brief background to the IPSASB Consultation Paper *Reporting on the Long-Term Sustainability of Public Finances*, and discusses how the Boards may wish to respond to the IPSASB Paper (including the process for finalising their submission(s) if they confirm their intention to make a submission).

Background

2. For some years, the IPSASB has been working on how best to report on the financial consequences of social benefit programs of public sector entities, such as the amounts of liabilities and expenses. Examples of social benefits are social security pensions, unemployment benefits, health and education services, national defence, policing and judicial processes.
3. In March 2008, the IPSASB issued Exposure Draft ED 34 *Social Benefits: Disclosure of Cash Transfers to Individuals or Households*, Consultation Paper *Social Benefits: Issues in Recognition and Measurement* and a project brief on long-term fiscal sustainability reporting. After considering the comments received on those documents, the IPSASB decided to defer further deliberation on when liabilities arise in relation to social benefit programs until work progresses on the 'elements of financial statements' phase of its Conceptual Framework project.
4. During the development of its project on social benefits, the IPSASB concluded that amounts reported in financial statements cannot meet all of the information needs of those interested in assessing the viability of social benefit programs. This is regardless of the approach taken to identifying when obligations (liabilities) to provide social benefits arise and how such liabilities should be measured. The IPSASB therefore concluded that information reported about social benefit programs in financial statements needs to be complemented by information about the long-term fiscal sustainability of those programs.
5. The IPSASB considers that the importance of reporting information about long-term fiscal sustainability of governments and other public sector entities has been increased by the global financial crisis and the extent of governments' spending in response to that crisis – spending that has consequences for the ability of governments (and other public sector entities) to meet their service delivery and financial commitments in the long term.

6. The IPSASB also concluded that a single general purpose financial report (GPFR) might not encompass all of the information that users of those reports need. Those information needs may need to be met through different types of GPFRs. Accordingly, it would be unnecessary for each GPFR to include information about long-term fiscal sustainability or for long-term fiscal sustainability reports to be accompanied by general purpose financial statements.
7. Other general background information on the IPSASB Consultation Paper is contained in AASB ITC 22 (the AASB's Request for Comment on the IPSASB Paper), which is attached.
8. The Appendix to this paper sets out background information on New Zealand developments in reporting information on long-term fiscal sustainability. Due to the press of time, background information on Australian developments has not been prepared. A brief overview of Australian developments will be provided orally at the joint meeting.

Whether to Make a Submission

9. At the forthcoming meeting, each Board will be asked to confirm whether it wishes to make a submission on the IPSASB Paper.
10. AASB ITC 22 indicates that the AASB intends to provide comments to the IPSASB on the Paper. Whilst ITC 22 indicates that the AASB might not develop recommendations or requirements on this topic, it also says the AASB intends to participate in the international debate.
11. This is a priority 1 topic on the FRSB's workplan. At its December 2009 meeting the FRSB agreed to submit on the consultation paper, and expressed interest in preparing a joint submission with the AASB. At that meeting the FRSB acknowledged that, because of the difficulties associated with the recognition and measurement of social benefit obligations, it has previously encouraged the IPSASB to provide guidance on long-term fiscal sustainability reporting. Despite reaffirming its views on the importance of this issue, the FRSB noted that there is likely to be limited public interest in this paper in New Zealand. The issues discussed in the paper are likely to be of most interest to the Treasury, which prepares regular reports on long-term fiscal sustainability, and rating agencies as key users of those reports. In discussing this item the FRSB noted that there are links between long-term fiscal sustainability and long-term service sustainability. That is, long term fiscal sustainability reporting could be used to highlight any mismatch between resources and the services to be provided in future.
12. In its comments on the IPSASB's March 2008 Consultation Paper, the FRSB expressed a view that requiring long-term fiscal sustainability reporting is an essential part of public sector financial reporting. A key point for discussion at the joint Board meeting is whether

long-term fiscal sustainability reporting should be regarded as part of general purpose financial reporting.

13. Due to reservations some Board members (particularly AASB members) have previously expressed about whether this topic should fall within the scope of general purpose financial reporting and about their unfamiliarity with the topic, an issue to consider is whether the Boards should provide comments of 'some members' on the topic without indicating the Boards have made any formal decisions on the Paper's preliminary views.

Staff recommendation

14. The staff recommends that the Boards make a submission (either jointly or separately), while declining to express a view on some of the IPSASB's preliminary views. [See Agenda Paper B2.2 for the suggested extent of Board comments on those views.]

Joint Submission or Separate Submissions?

15. If the Boards confirm their intention to make a submission, and if they have similar comments on the IPSASB Paper, members are asked to decide whether the Boards wish to make a joint submission. The main arguments for making a joint submission in these circumstances are that it may be more effective to speak with a single strong voice and it should avoid duplication of effort. The main argument against making a joint submission is that the Boards may effectively be treated as a single respondent.

Staff recommendation

16. The staff recommends that the Boards make a joint submission.

Content of Submission(s)

17. The majority of the points that staff suggest be made in the submission(s) relate to the preliminary views in the IPSASB Paper (see Agenda Paper B2.2 for suggested comments).

Staff recommendations

18. In addition to commenting on the preliminary views, the staff recommends that the Boards:
 - (a) encourage the IPSASB not to make this topic a high priority, in view of:
 - the importance of the Conceptual Framework project and public sector standards projects; and
 - it not having been determined whether information on long-term fiscal sustainability belongs within the scope of GPFs; and

(b) request the IPSASB to clarify its intended due process on this topic, in view of that not having been indicated in the Consultation Paper.

19. In view of the uncertainty about whether information on long-term fiscal sustainability falls within the scope of GPFRs, the staff suggests that the Boards encourage exploration of, and experimentation with, reporting this information, either within or outside GPFRs.

APPENDIX

New Zealand developments in reporting information on long-term fiscal sustainability

New Zealand Government

1. The New Zealand Treasury is required under the Public Finance Act 1989 (as amended 2004) to publish a statement on New Zealand's long-term fiscal position at least every four years. Each statement must have a projection-horizon of at least 40 years. The New Zealand Government uses the same boundary for these reports as for the consolidated financial statements.
2. The most recent statement, *Challenges and Choices: New Zealand's Long-term Fiscal Statement*, was published on 29 October 2009.¹ This document is set out in three sections.
 - Part A discusses the broad issues facing New Zealand.
 - Part B looks at broad choices in relation to tax and spending.
 - Part C considers three possible scenarios and their impact on the projected fiscal position.
3. At present the financial statements of the New Zealand Government do not include a summary of the information in the long-term fiscal statement. This possibility has been considered but given the way the long-term fiscal statement is structured it would be difficult to decide which aspect to include in the financial statements.
4. The long-term fiscal statement is used by international rating agencies and others with an interest in the Government's long-term fiscal position.

New Zealand Local Authorities

5. Local authorities are required, under sections 84 and 93 of the Local Government Act 2002, to publish Long-Term Council Community Plans (LTCCPs) which include projected financial statements with a 10-year time horizon. Local authorities prepare these financial statements in accordance with the New Zealand domestic standard, FRS-42 *Prospective Financial Statements*.
6. The main purpose of prospective financial statements in the LTCCP is to provide users with information about the core services that the Council intends to provide ratepayers, the expected cost of those services and, as a consequence, how much the Council requires by way of rates to fund the intended levels of service.
7. In addition to the ten year horizon explicitly required by the Local Government Act, the Act has other requirements which effectively require local authorities to prepare long-term asset

¹ URL on Treasury website at October 2009: <http://www.treasury.govt.nz/government/finances/longterm/fiscalposition/2009>
Persistent URL: <http://www.purl.org/nzt/o-1243>

management plans. The 10th Schedule of the Act requires that the LTCCP contain information on how the council will identify future asset requirements to manage services and to maintenance requirements. The only effective way that a local authority can verify that it has done so is to have an asset management plan, and due to the nature of infrastructure assets, this plan must often extend for 40 or 50 years. Asset management plan may be published as part of an LTCCP or in a separate document. Because LTCCPs are audited, the auditor also reviews the asset management plans. The audit opinion covers underlying information of which the asset management plans are a key component.

8. Users of the financial information in LTCCPs include ratepayer associations, Statistics New Zealand, universities and lenders.
9. An extract from the Local Government Act 2002 is set out below:

Local Government Act 2002
Schedule 10
Part 1 Information to be included in long-term council community plans

Council plans and reports
2 Group of activities

(1) A long-term council community plan must, in relation to each group of activities of the local authority,—

- (a) identify the activities within the group of activities;
- (b) identify the rationale for delivery of the group of activities (including the community outcomes to which the group of activities primarily contributes);
- (c) outline any significant negative effects that any activity within the group of activities may have on the social, economic, environmental, or cultural well-being of the local community;
- (d) identify the assets or groups of assets required by the group of activities and identify, in relation to those assets or groups of assets,—
 - (i) how the local authority will assess and manage the asset management implications of changes to—
 - (A) demand for, or consumption of, relevant services; and
 - (B) service provision levels and standards;
 - (ii) what additional asset capacity is estimated to be required in respect of changes to each of the matters described in subparagraph (i);
 - (iii) how the provision of additional asset capacity will be undertaken;
 - (iv) the estimated costs of the provision of additional asset capacity identified under subparagraph (ii), and the division of those costs between each of the matters in respect of which additional capacity is required;
 - (v) how the costs of the provision of additional asset capacity will be met;
 - (vi) how the maintenance, renewal, and replacement of assets will be undertaken;
 - (vii) how the costs of the maintenance, renewal, and replacement of assets will be met;
- (e) include the information specified in subclause (2)—
 - (i) in detail in relation to each of the first 3 financial years covered by the plan; and
 - (ii) in outline in relation to each of the subsequent financial years covered by the plan.

(2) The information referred to in subclause (1)(e) is—

- (a) a statement of the intended levels of service provision for the group of activities, including the performance targets and other measures by which actual levels of service provision may meaningfully be assessed;
- (b) the estimated expenses of achieving and maintaining the identified levels of service provision, including the estimated expenses associated with maintaining the service capacity and integrity of assets;
- (c) a statement of how the expenses are to be met;
- (d) a statement of the estimated revenue levels, the other sources of funds, and the rationale for their selection in terms of section 101(3).