



Mr David Moyal
Chairman
Australian Accounting Standards Board
P O Box 204
Collins St West
MELBOURNE VIC 8007

Dear Mr Moyal

ABS COMMENTS: ED 142 (Financial Reporting of General Government Sectors by Governments)

I attach our comments on Exposure Draft 142 (Financial Reporting of General Government Sectors by Governments) and thank you for the opportunity to comment.

The AASB has shown considerable leadership in developing an exposure draft in which both GFS and generally accepted accounting principles co-exist within the same presentation. This is a world-first and we thank the Board for placing Australia at the forefront of financial reporting in the public sector.

I would also like to thank the AASB for adhering to GFS principles where the information has been presented on a GFS basis in the Exposure Draft. We clearly view this as an important aspect of the Exposure Draft so as to avoid confusion with the GFS that the ABS will continue to publish. In this context, 'look-alike' versions of GFS are therefore not something that we would encourage.

Throughout the development of the Exposure Draft, there has been extensive and on-going liaison with the technical staff of the AASB. I would like to convey my appreciation for the cooperation so readily extended to us in this process.



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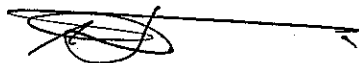
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Any questions or queries relating to these comments may be addressed to Tulsi Ram,
Assistant Director, Public Finance Section, ph 02 6252 6117 or via email t.ram@abs.gov.au in
the first instance.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Peter Harper', with a long horizontal line extending to the right.

Peter Harper
Deputy Australian Statistician
Economic Statistics Group

27 October 2005

Australian Bureau of Statistics: Comments on ED 1421

General comments

The AASB has shown considerable leadership in developing an exposure draft in which both GFS and generally accepted accounting principles co-exist within the same framework. This is a world-first and we already know that it has received considerable attention from the international statistical community. We thank the Board for providing such strong leadership in this field.

We also note that the aspects of ED that relate to GFS are in fact on a bona-fide GFS basis², thus ensuring that the GFS-related information published in financial statements will be essentially consistent with the GFS that will continue to be published by the ABS.³ We believe that it is essential for the standard to adhere to GFS principles where it purports to be on a GFS basis. While, as an independent agency, the ABS cannot be bound by the standard, ensuring that the standard is based on GFS principles will minimise and possibly eliminate any differences between the GFS aspects of the standard and the GFS published by the ABS.

In this regard, we are of the strong view that the standard be based on the ABS's interpretation of GFS, as promulgated in our publication *Government Finance Statistics: Concepts, Sources and Methods* (ABS GFS CSM), rather than the IMF's 2001 *Government Finance Statistics Manual* (GFSM 2001).⁴ We believe that, over time, this approach will result in a greater degree of harmonisation between GFS and GAAP-based results in the standard. We elaborate our reasons for this position in our response to Matter for Comment (p).

If the proposals relating to GFS in the ED are accepted into an accounting standard, the ABS expects to have a role in the interpretation of GFS issues within the context of the particular standard. In this context, the ABS would be willing, if invited, to attend the Urgent Issues Group (UIG) process as a technical adviser. As stated above, if the ED is accepted into a standard then the ABS will continue to publish GFS as it currently does, and we believe that it is important that differences between the standard and ABS GFS remain minimal.

Specific Matters for Comment

The AASB would particularly value comments on:

- (a) the proposal in paragraph 5 that the GGS (as defined in GFSM 2001) of a government is a reporting entity;

ABS comments:

We encourage the Board to focus on the considerable utility of a set of financial statements relating to the GGS as a reporting entity, especially as the definition of the reporting entity is not being compromised in any substantial way in our view.

There is extensive user-interest in the GGS. This user-interest is due in our view to the fact that the mainly non-market characteristic of the GGS is economically different to the market-oriented public corporations controlled by the particular government. The market and non-market proportions in each of the nine jurisdictions affected by this ED are individually significant; hence, we see a need for their separate identification and reporting.

Even if the (whole of) a government was the reporting entity we would argue (as we did during the development stages of the current AAS31 back in the eighties) that the separate identification and reporting of the GGS would be highly desirable in view of their fundamentally different characteristics.

It is our view that a complete set of financial statements, identifying all flows of income and capital (between the GGS of a government and other entities) is highly desirable for the GGS – in this context, whether the GGS is seen as a reporting entity in its own right, a segment or some other designation in a whole-of-government context, is rather less of an issue in our view.

We appreciate the significance of the reporting entity concept in the accounting standards; however, we would encourage the Board to adopt an interpretation that identifies the GGS as a reporting entity.

(b) the proposal, implicit in paragraph 5, that a GGS financial report prepared on a partial consolidation basis is a GPFR together with the proposal in paragraph 18 that the GGS should be prohibited from consolidating controlled entities in the PNFC sector and the PFC sector;

ABS comments:

We understand the significance some users may attach to the 'GPFR' versus 'SPFR' distinction; however, this is not such a critical issue from the ABS perspective. It is our view that the GGS should be separately identified, reported and audited upon, based faithfully on GFS standards where aspects of the reporting purport to be on that basis.

Expressions such as 'partial consolidation' and 'be prohibited from consolidating' seem to carry the connotation that a GGS's finances are somehow being misrepresented. It should be noted that in GFS the net worth of the GGS component includes the value of the GGS's equity interests in non-GGS entities. As there is no misrepresentation of the net worth, it is our view that the GGS is, in effect, consolidating the controlled entities, albeit in a single line rather than the traditional line-by-line basis. We therefore encourage the Board to take the view that this method of consolidation is a difference in form rather than in substance.

If the paucity of information associated with a single line is of concern here, we suggest a note disclosure detailing the GGS's equity interest in each of its controlled entities (or at least the significant ones). Such a note disclosure could identify the entities by name, together with their opening and closing levels of the assets and liabilities. This approach may also help allay the concerns of those critics concerned with the possible narrow focus of the GGS.

The single-line method has the strong advantage of preserving certain details that relate exclusively to the GGS, and so satisfying users interested in the sector. The total controlled assets and liabilities, on a line-by-line basis, would continue to be available in the whole-of-government financial statements.

It is not meaningful in our view to acknowledge the stand alone existence of the GGS on the one hand but to undertake a line-by-line consolidation on the other. This would in effect achieve a whole-of-government type presentation results, thereby defeating the very purpose of separately identifying the GGS.

(c) the proposal in paragraphs 8 to 12 that, with limited significant exceptions, the GGS financial report should comply with other Australian Accounting Standards and, where it does not conflict with Australian Accounting Standards, GFSM 2001. The Board is particularly interested in comments on the proposal that where Australian Accounting Standards allow for optional treatments, only those treatments aligned with GFSM 2001 should be applied for the purposes of GGS financial reporting;

ABS comments:

We support the proposal adopted in the ED that, with limited exceptions, the GGS financial report should comply with other Australian Accounting Standards and, where it does not conflict with Australian Accounting Standards, ABS GFS CSM (rather than GFSM 2001). In cases of conflicts, disclosures through mandatory notes would be desirable in our view.

(d) the proposal in paragraphs 13 to 17 to require or allow disclosure of information in the GGS financial report that is determined in accordance with GFSM 2001 and, where it is determined in a different manner from corresponding information prepared in accordance with Australian Accounting Standards, provide a reconciliation to the GFS-related information;

ABS comments:

Where corresponding information prepared under the Australian Accounting Standards and GFS differ, reconciliation to the GFS-related information should be a requirement, rather than an optional disclosure. It is our view that anything purporting to be on a GFS basis should in fact be on a bona-fide GFS basis, as users should rightfully be given the opportunity to have confidence in both 'views' of the underlying information. Mandating a requirement would be helpful in this regard.

(e) the proposals in paragraphs 19 to 23 that:

- (i) the GGS's equity investment in non-consolidated controlled entities should be measured at fair value where fair value is reliably measurable and at the government's proportional interest in the net assets of the controlled entities where fair value is not reliably measurable;

ABS comments:

GFS uses market valuation as a basis for valuing GGS's equity investments in corporations if the shares or other equities are traded in the market and as the proportional interest in the net assets if valuation via such a market mechanism is not available. We accept that the GFS market value concept is operationally equivalent to fair value; hence we support the proposal strongly.

- (ii) where net assets is used as the basis of measurement, it is determined in a manner consistent with the net assets that are consolidated into the whole of government GPFR;

ABS comments:

We accept and support the need for overall consistency between the GGS and whole-of-government reports.

- (iii) changes in the carrying amount of the GGS's equity investment in non-consolidated controlled entities during a reporting period are treated in a manner consistent with the treatment of a change in fair value under AASB 139 even if the carrying amount is not fair value; and

ABS comments:

Supported.

- (iv) specify the treatment of jointly controlled entities and associates;

ABS comments:

If the treatment of jointly controlled entities and associates is specified in the notes users would not be left with any uncertainty. We therefore support the proposal.

- (f) the proposals in paragraphs 26 to 31 relating to the format and content of the balance sheet and the treatment of convergence differences;

ABS comments:

Strongly supported.

- (g) the proposals in paragraphs 32 to 40 relating to the format and content of the operating statement and the treatment of convergence differences, including the proposal:

ABS comments:

The proposed format of the operating statement is supported, as it provides both GFS and the GAAP views. The convergence difference column would have minimal entries for most jurisdictions and are expected to decline over time. We would not be concerned though, if convergence differences were treated as line item entries (as appropriate) rather than shown in a separate column, as long as the key GFS aggregates remained on the face of the statement.⁵

- (i) to mandate the classification of income and expenses by nature on the face of the operating statement, with the classification aligned with the GFSM 2001 classification scheme to the extent appropriate;

ABS comments:

We strongly support mandating the classification of income and expenses by nature on the face of the operating statement aligned with ABS GFS CSM (rather than GFSM 2001) because the operations of each of the nine jurisdictions impacted by the proposed ED are very similar. A mandated format would also not be such an issue in our view as these jurisdictions have been reporting on a mandated basis as part of the UPF arrangement, without any significant issues we understand. A mandated format also provides for easier comparison across jurisdictions.

- (ii) to mandate a comprehensive income approach whereby all non-owner movements in equity are recognised in a single operating statement; and

ABS comments:

Strongly supported, for reasons similar to g(i) above.

- (iii) that the option in AASB 119 Employee Benefits (December 2004) of partially deferring actuarial gains and losses on defined benefit superannuation plans using a "corridor approach" should be prohibited, and that the remaining options of recognising them in operating result or in the other non-owner movements in equity section of the operating statement should be allowed. The Board is particularly interested in comments on whether the Standard should remove options entirely, and in so doing, prohibit recognition directly in other non-owner movements in equity;

ABS comments:

The ABS supports the prohibition of the "corridor approach", as it is not consistent with GFS principles. The GFS treatment of the other options referred to in AASB 119 (Employee Benefits) would be determined by their economic type (as either GFS 'transactions' or 'other economic flows'). Since both 'transactions' and 'other economic flows' are separately identified in the operating statement, the treatment of these options is not a particular issue from a GFS perspective.

(h) the proposals in paragraphs 41 to 43 relating to the format and content of the cash flow statement. The Board is particularly interested in comments on whether the Standard should also require a distinction between cash flows relating to investing in financial assets for “policy” and “liquidity management” purposes on the face of the cash flow statement and whether such a distinction would be useful and could be made with sufficient rigour for GPFR purposes;

ABS comments:

The format and content of the cash flow statement are supported. In our view, a requirement for a distinction between cash flows relating to investing in financial assets for “policy” and “liquidity management” purposes on the face of the cash flow statement would be difficult to justify as no balances are currently derived in the ED based on this distinction. However, a note disclosure could be strongly encouraged as a distinction would be useful and could be made with sufficient rigour. The ABS will continue to show the distinction in its GFS presentation because of the analytical usefulness of the information.

(i) the proposals in paragraphs 44 and 45 relating to additional information to be provided in the note containing the summary of significant accounting policies, illustrated in Appendix C. In particular, the Board is interested in comments on whether the proposed disclosures provide sufficient information to minimise the risk that users might perceive the GGS financial report as being a substitute for the whole of government GPFR;

ABS comments:

We do not see any problems in providing additional information in a note containing the summary of significant accounting policies. However, we encourage the Board to adopt a more neutral expression by avoiding words such ‘minimise the risk that users might perceive ...’

(j) the proposals in paragraphs 46 to 48 relating to additional disclosures. The Board is particularly interested in comments on whether the proposal in paragraph 46(d) to require disclosure of explanations of key technical terms used in the financial report is useful;

ABS comments:

The proposal to require disclosure of explanations of key technical terms used is strongly supported.

(k) the proposals in paragraphs 49 to 52 relating to disclosures that provide disaggregated information about GAAP and GFS amounts on a functional basis, whereby functions are determined in accordance with GFSM 2001;

ABS comments:

We strongly support the disaggregation of information on a functional basis as set out in ABS GFS CSM for expense and acquisition of non-financial assets items. We do not support the proposal to provide a disaggregation of all elements of the GGS financial statements using the functional basis. The functional basis is only intended to be applied to expenses and the acquisition of non-financial assets. The proposed extended application to tax revenues, assets, liabilities, etc may cause some interpretation issues, despite the attempt to pre-empt this through the use of cautionary words such as “to the extent it can be reliably done”.

We recommend that the functional splits applied to expenses and the acquisition of non-financial assets be at a more detailed level than currently proposed in the ED. Based on our experience, we believe that users will find the more detailed economic by functional cross-classification of expenses and acquisition of non-financial assets, as per the ABS GFS

CSM, more useful than the proposed less-detailed split being applied to all items. Moreover, as the detailed cross-classified information is currently provided to the ABS by each of the jurisdictions, the underlying information already exists.

In making the above comments, we are mindful of the Board's use of the functional classification as a basis for segmentation of the GGS. If full segmentation of the GGS is required then the use of a somewhat related but alternative classification Australia and New Zealand Standard Industry Classification (ANZSIC) could be investigated further. The ABS would be pleased to provide assistance to the Board on investigating this.

(l) the proposals in paragraphs 53 to 56 to specify principles for the presentation of performance indicators;

ABS comments:

No comments.

(m) the proposals in paragraphs 57 to 62 to require disclosure of:

- (i) the original budget, restated if necessary so that it is presented on a basis that aligns with the basis on which the financial statements and notes have been prepared (in accordance with the Standard); and

ABS comments:

We strongly support the requirement for the disclosure of the original budget, restated if necessary so that it is presented on a comparable basis.

- (ii) an explanation of major variances between the original GGS budget and actual amounts;

ABS comments:

This is supported as the explanation of major variances will provide the basis for a better understanding of the information.

(n) the proposals in paragraphs 63 to 67 relating to transitional requirements. In particular, the Board is interested in assessments of the costs and benefits of the approach proposed, compared with alternative approaches, including remaining silent in the Standard about transitional requirements, and thereby effectively requiring AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors to operate in its own right;

ABS comments:

No comments.

(o) the illustrated acceptable format for the financial statements and notes related to convergence differences in Appendix B. The Board is particularly interested in comments on:

- (i) the columnar approach illustrated for the balance sheet and operating statement. In addition to any criticisms of the columnar approach, respondents are invited to provide an alternative that is consistent with the Exposure Draft's proposals for the Board's consideration; and

ABS comments:

The columnar approach, as an illustration, is strongly supported. It has the major advantage of being visually concise, as all the key elements of both GAAP and GFS are in close proximity and the information relating to a particular year is less likely to be spread over multiple pages. As mentioned previously, we would not be concerned though, if convergence differences were treated as line item entries (as appropriate) rather than shown in a separate column, as long as the key GFS aggregates remained on the face of the statement.

We are hopeful that a format similar to the illustrative format will in fact be adopted by all preparers; however, it would not be such an issue were this not to occur. We note that the illustrated statements do not preclude preparers from adopting alternatives.

- (ii) whether the illustration provides guidance that is helpful in implementing the proposals in the Exposure Draft, particularly those that adopt the requirements in AASB 101 as effectively amended by the proposals;

ABS comments:

We believe the ED is helpful in providing guidance in implementing the proposals, especially those relating to GFS. In this context, we note that each of the nine jurisdictions affected by the ED have compiled and published similar information as part of the Uniform Presentation Framework for several years. They have also provided similar information to the ABS. We do not foresee any particular difficulties with the GFS aspects of the proposals as far as preparers are concerned; however, the situation with most auditor generals is less clear.

(p) whether it is appropriate for the Standard to cross-reference to GFSM 2001, given that GFSM 2001 is not prepared by the AASB and that there is a need for the AASB to consider whether amendments to the Standard are necessary each time GFSM 2001 is amended. The Board is also interested in comments on whether instead of GFSM 2001 the Standard should cross-reference to the GFS Manual published by the Australian Bureau of Statistics (ABS);

ABS comments:

We are of the strong view that the standard be based on the ABS interpretation of GFS, as promulgated in our publication *Government Finance Statistics: Concepts, Sources and Methods* (ABS GFS CSM), rather than IMF's 2001 *Government Finance Statistics Manual* (GFSM 2001).

It is important that GFS in Australia are prepared with regard to the Australian context to maximise their usefulness, and while ABS GFS CSM closely follows GFSM 2001, the ABS reserves the right to depart from international standards where it is appropriate for the local context.⁶ It is expected that departures would only ever be few in number and will only occur where

1. it can be clearly demonstrated that the GFSM 2001 treatment is not appropriate for Australia, because of circumstances particular to Australia
2. the application of rules-based treatments in GFSM 2001 to Australian circumstance leads to results that are not inconsistent with the underlying concepts and principles of GFSM 2001 or those of the broader System of National Accounts⁷
3. harmonisation with GAAP can be improved
4. the departures could be carried through, as appropriate, into other ABS macro-economic statistics such as the national accounts, in order to retain consistency with these statistics and the GFS
5. the departures could be implemented in such a way as to enable a straightforward reconciliation with GFSM 2001.

As an independent agency responsible for Australia's GFS, the ABS is the sole decision maker regarding departures, but in making decisions we will consult widely, including with the IMF, Australian governments, auditors, accounting standards setters and users of GFS statistics. Departures, including the reasons for them, will be well-publicised in, for example, the ABS GFS CSM.

Furthermore, on matters of interpretation, it will be more straightforward for financial reporters, standards setters and auditors to consult with the ABS than the IMF.

(q) whether there are any aspects of GFSM 2001 that you consider should be prohibited from forming part of the basis upon which the GGS's financial report is prepared; and

ABS comments:

There are no aspects of the ABS GFS CSM that should not be reflected in the GFS-based aspects of the GGS's financial reporting.

(r) whether, overall, the proposals result in financial reports that are useful to users.

ABS comments:

Overall, we believe that the use of the GFS basis of distinguishing 'transactions' and 'other economic flows', as per the illustrated format of the operating statement, will result in financial reports that are useful to users. Moreover, as the key GFS balances are readily available – on a bona-fide GFS basis, we believe that there will be substantially less confusion for users of GGS financial reports and ABS GFS.

- 1 The ABS comments are provided as 'boxed' text, following the order in the exposure draft.
- 2 A minor issue concerning the extended application of the functional classification, as noted elsewhere in this document, is a possible exception.
- 3 The ABS, as Australia's independent statistical agency, will continue to publish its own set of GFS, even if the ED is accepted into a standard. These statistics are important in their own right as measures of the economic activities of government, as well as being a key input into the broader national accounts. Furthermore, the ABS has an obligation to report GFS to the IMF.
- 4 It should be noted that, for the moment at least, there are minimal differences between GFSM 2001 and ABS GFS CSM, with most of the differences relating to matters of detail and presentation.
- 5 With these key GFS aggregates continuing to be presented on a bona-fide GFS basis.
- 6 GFSM 2001 is a standard that is broadly applicable to all countries in the world, regardless of their state of economic development or the state of government financial reporting. As such, in developing the standard compromises between what is suitable for one country and what may be suitable for another are made.
- 7 In international statistical standards, GFSM 2001 is subordinate to the System of National Accounts (SNA), which provides a standard for the comprehensive measurement of e