International Federation of Accountants

Reporting on Long-Term Fiscal Sustainability
(Sustainability of the Public Finances)

10th Annual OECD Public Sector Accruals Symposium

Ian Carruthers: IPSASB Member and Chair of IPSASB Task Force
John Stanford: Deputy Technical Director: IPSASB

Paris: March 8th 2010
Background

• IPSASB project on social benefits (1)

  • Analysis of when present obligations & liabilities arise for social benefits distinguishing:
    • Collective goods and services (such as defense, policing)
    • Individual goods and services (such as education and health)
    • Cash transfers (such as entitlements for state pensions, unemployment benefit)

  • Analysis based on IPSAS 19, “Provisions, Contingent Liabilities and Contingent Assets” (equivalent of IAS 37)

  • Initial tentative view that present obligations and liabilities arise only for cash transfers on “due and payable” basis
Background

• **IPSASB project on social benefits (2)**
  - Alternative view that approach over-restrictive?
  - Distinction between cash transfers & individual goods and services artificial
  - ED 34, “Disclosure of Cash Transfers to Individuals and Households”: proposed disclosure of cash flows - not recognition and measurement of liabilities
  - ED 34 not supported at consultation
  - Consultation Paper: Social Benefits: Issues in Recognition and Measurement
  - Conclusion that traditional general purpose financial statements deficient for accountability purposes regardless of approach to present obligations and liabilities
  - Right to tax as an asset?
Background

• Conceptual Framework: First phase of this project considered:
  – Objectives
  – Scope
  – Reporting Entity
  – Qualitative Characteristics

• Preliminary Views that:
  • Prospective information necessary to meet users needs i.e. accountability and decision-making
  • Scope of reporting should extend beyond traditional financial statements

• Some reservations from respondents about broader scope
• Likelihood that pronouncements on broad scope issues will be in form of guidance
Composition of Task Force overseeing project

• Chaired by Ian Carruthers
• Includes Members from:
  – Eurostat
  – French Cour des Comptes
  – Swiss Federal Ministry of Finance
  – Swedish Audit Office
  – Australian Department of Finance and Deregulation
  – Canadian Public Sector Accounting Board
  – New Zealand Treasury
  – US Federal Accounting Standards Advisory Board
  – Organisation for Economic Co-operation and Development
  – International Monetary Fund
Background to current emphasis on long-term fiscal sustainability?

- Fiscal pressure points for governments
  - Demographics
  - Technological advances
  - Infrastructure
  - Environmental factors

- Inter-generational equity

- Extent of global financial crisis has added further pressures incl:
  - Guarantees
  - Purchase of, and/or insurance of, toxic assets
  - Quantitative easing
  - Credit lines
  - Equity holdings
What is long-term fiscal sustainability and how extensively is it reported?

• No globally accepted definition so working definition:

  –“The ability of government to meet its service delivery and financial commitments both now and in the future.”

• Recognizes ability to modify level of services and taxation levels (but constrained in global environment)

• Fiscal-sustainability reporting an increasing feature of public reporting over last 10-15 years

• Predominantly domain of economists, statisticians and policy makers—accountants generally peripheral

• How can this information be used in financial reports?
## Overview of Fiscal Future Reports at National and Supra-national Levels (1)

<table>
<thead>
<tr>
<th>Country</th>
<th>Legal Requirement</th>
<th>Title</th>
<th>Source</th>
<th>Start</th>
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</thead>
<tbody>
<tr>
<td>Australia</td>
<td>Charter of Budget Honesty Act</td>
<td>Intergenerational Report</td>
<td>Treasury</td>
<td>2002</td>
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<tr>
<td>Denmark</td>
<td></td>
<td>A Sustainable Future</td>
<td>Ministry of Finance</td>
<td>1997</td>
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<tr>
<td>Germany</td>
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<td>Report on Sustainability of Public Finance</td>
<td>Ministry of Finance</td>
<td>2005</td>
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<tr>
<td>Korea</td>
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<td>Vision 2030</td>
<td>Ministry of Planning and Budget</td>
<td>2006</td>
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<tr>
<td>Netherlands</td>
<td>EC Stability Program</td>
<td>Ageing and the Sustainability of Dutch Public Finances</td>
<td>Central Planning Bureau</td>
<td>2000</td>
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<tr>
<td>New Zealand</td>
<td>Public Finance Act</td>
<td>Long Term Fiscal Position</td>
<td>Treasury</td>
<td>1993</td>
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<tr>
<td>Norway</td>
<td></td>
<td>Long-term Perspective for Norwegian Economy</td>
<td>Ministry. of Finance</td>
<td>2004</td>
</tr>
<tr>
<td>Sweden</td>
<td></td>
<td>Sweden’s Economy (annex to budget)</td>
<td>Min. of Finance</td>
<td>1999</td>
</tr>
<tr>
<td>Switzerland</td>
<td></td>
<td>Long-term Sustainability of Public Finance in Switzerland</td>
<td>Federal Dept. of Finance</td>
<td>2008</td>
</tr>
</tbody>
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Source: OECD Fiscal Futures Project
# Overview of Fiscal Future Reports at National and Supra-national Levels (2)

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<th>Source</th>
<th>Start</th>
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<tbody>
<tr>
<td>US: Congressional Budget Office</td>
<td></td>
<td>Long -Term Budget Outlook</td>
<td>Congressional Budget Office</td>
<td>1991</td>
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<tr>
<td>(CBO)</td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>US: General Accountability</td>
<td></td>
<td>Long -Term Fiscal Outlook</td>
<td>General Accountability Office</td>
<td>1992</td>
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<td>Office (GAO)</td>
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<td></td>
<td></td>
<td></td>
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<tr>
<td>Budget (OMB)</td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>Government</td>
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<td>Surveillance</td>
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<tr>
<td>International Monetary Fund</td>
<td></td>
<td>Financial Transparency Reviews</td>
<td>Fiscal Affairs Department</td>
<td>2001</td>
</tr>
</tbody>
</table>

Source: OECD Fiscal Futures Project
Information needs of users & spectrum of reporting

Information useful as Input to Assessments of Accountability and for Resource Allocation and other Decisions

All Financial Reporting

General Purpose Financial Reports (includes annual financial reports and other reports)

Additional Information – may include non-financial, prospective financial, compliance and additional explanatory material

Special Purpose (and other) Financial Reports outside scope of IPSASB

For example, donor and other special purpose and compliance reports, and finance statistics and other financial reports and forecasts outside GPFRs

Economic, statistical, demographic and other data

Other Information
Information provided in an accrual-based statement of financial position

- **Past cash flows**
  - Assets obtained and realized to date
  - Liabilities incurred and settled to date

- **Future cash flows**
  - Present economic benefits realized in the future (Assets)
  - Expected resources to be realized in the future
  - Expected obligations to be settled in the future
  - Present economic sacrifices settled in the future (Liabilities)
How information on fiscal sustainability can enhance the statement of financial position

<table>
<thead>
<tr>
<th>Inflows</th>
<th>Future cash flows</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets obtained and realized to date</td>
<td>Present economic benefits realized in the future (Assets)</td>
</tr>
<tr>
<td>Liabilities incurred and settled to date</td>
<td>Expected resources to be realized in the future</td>
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<tr>
<th>Outflows</th>
<th>Future cash flows</th>
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<tr>
<td>Present economic sacrifices settled in future (Liabilities)</td>
<td>Expected obligations to be settled in the future</td>
</tr>
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</table>
Reporting boundary

• Boundary for long-term fiscal sustainability reporting unlikely to be same as for financial statements:
  – Based on statistical accounting- esp. Europe (SNA 95) and GFSM 2001
  – Budget based

• Consolidated reports or individual entities?

• Relevance at sub-national levels but different focus and approach:
  – Ability to generate revenue
  – Fiscal dependence on other tiers of government
Models for reporting long-term fiscal sustainability reporting in GPFRs

- **Model One:** Additional statements providing details of projections:
  - US Statements of Social Insurance
  - Federal Accounting Standards Advisory Board: SFFAS 36, “Reporting Comprehensive Long-Term Fiscal Projections for the U.S. Government”.

- **Model Two:** Summarizing projections in narrative reporting
  - US Citizens Guide

- **Model Three:** Cross-references in GPFRs to other reports addressing long-term fiscal sustainability
  - IPSASB Preliminary View that Models 1 & 2 appropriate
Additional Statement: Long-term fiscal projections for the US Federal Government

<table>
<thead>
<tr>
<th>Long-Term Fiscal Projections for the U.S. Government</th>
<th>As of January 1, 20XX (Current Year)</th>
<th>As of January 1, 20XX (Prior Year)</th>
<th>Change from Prior Year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>PV Dollars in trillions</td>
<td>% GDP*</td>
<td>PV Dollars in trillions</td>
</tr>
<tr>
<td>Receipts</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medicare</td>
<td>$ 10.7</td>
<td>1.5%</td>
<td>$ XX.X</td>
</tr>
<tr>
<td>Social Security</td>
<td>36.3</td>
<td>5.1%</td>
<td>XX.X</td>
</tr>
<tr>
<td>All Other Receipts</td>
<td>91.0</td>
<td>12.6%</td>
<td>XX.X</td>
</tr>
<tr>
<td>Total Receipts</td>
<td>$ 137.9</td>
<td>19.4%</td>
<td>$ XX.X</td>
</tr>
<tr>
<td>Spending</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medicare</td>
<td>$ 44.8</td>
<td>6.3%</td>
<td>$ XX.X</td>
</tr>
<tr>
<td>Medicaid</td>
<td>15.6</td>
<td>2.2%</td>
<td>XX.X</td>
</tr>
<tr>
<td>Social Security</td>
<td>40.5</td>
<td>5.7%</td>
<td>XX.X</td>
</tr>
<tr>
<td>Rest of Federal Government**</td>
<td>73.9</td>
<td>10.4%</td>
<td>XX.X</td>
</tr>
<tr>
<td>Total Spending</td>
<td>$ 174.9</td>
<td>24.6%</td>
<td>$ XX.X</td>
</tr>
<tr>
<td>Spending in excess of receipts</td>
<td>$ 37.0</td>
<td>5.2%</td>
<td>$ XX.X</td>
</tr>
</tbody>
</table>
Possible reporting indicators

• Gross debt.
• Net debt
• Net Worth.
• Net Financial Worth
• Fiscal gap
• Inter-temporal budget gap
• Fiscal dependency
Principles for selecting indicators: Allen Schick’s Framework

- **Solvency**: the capacity of governments to finance existing and probable future liabilities/obligations;

- **Growth**: the capacity of government to sustain economic growth over an extended period;

- **Fairness**: the capacity of government to provide net financial benefits to future to future generations that are not less than the net benefits provided to current generations; and

- **Stable taxes**: the capacity of governments to finance future obligations without increasing the tax burden.
Basic principles for Disclosure

• Current versus future policy
• Revenue inflows
• Demographic and economic assumptions
• Approach to age-related and non-age-related programs
• Impact of legal requirements and policy frameworks

Disclosure of approach and underpinnings
Specific methodology issues

• Time horizons for projections and their rationale (including changes or planned changes)

• Discount rates & rationale

• Frequency of reporting: tension with annual basis of GPFSs

• Sensitivity analysis

• Reliability of projections
  - Long-term fiscal sustainability reports not generally subject to assurance
  - In USA the SOSI is subject to opinion from GAO
  - View in Consultation Paper is that assurance matter for preparers but that good practice to disclose approach to ensuring reasonableness of assumptions
<table>
<thead>
<tr>
<th>Country</th>
<th>Title</th>
<th>Time Horizon</th>
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<td>Australia</td>
<td>Intergenerational Report</td>
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<tr>
<td>Germany</td>
<td>Rpt on Sustainability of Public Finance</td>
<td>45</td>
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<tr>
<td>Korea</td>
<td>Vision 2030</td>
<td>25</td>
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<tr>
<td>Netherlands</td>
<td>Aging and Sustainability of Dutch Public Finances</td>
<td>Until 2100 (with separate discussion to 2040)</td>
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<tr>
<td>New Zealand</td>
<td>LT Fiscal Position</td>
<td>40</td>
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<tr>
<td>Norway</td>
<td>2006 White Paper</td>
<td>55</td>
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<td>Sweden</td>
<td>Sweden’s Economy (annex to budget)</td>
<td>45</td>
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<tr>
<td>United Kingdom</td>
<td>LT Public Finance Report</td>
<td>30</td>
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<tr>
<td>USA: CBQ</td>
<td>LT Budget Outlook</td>
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<td>USA: GAO</td>
<td>LT Fiscal Outlook</td>
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<td>US: OMB</td>
<td>LT Budget Outlook in Analytical Perspectives</td>
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<td>European Union Countries</td>
<td>Public Finances – EMU</td>
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<tr>
<td>Switzerland</td>
<td>Long-term sustainability of public finance in Switzerland</td>
<td>40</td>
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Current Position & Next Steps

- Consultation period until April 30th, 2010

- Analysis of responses by IPSASB: Late June, 2010

- Dependent upon response analysis possibility of a non-binding framework-principles rather than rules-based c.f. IASB approach to narrative reporting

- Exposure Draft on Conceptual Framework: late 2011

- All IPSASB pronouncements and exposure drafts available at www.ifac.org
Consultation Paper: Preliminary Views (1)

1. Presentation of information on long-term fiscal sustainability necessary to meet objectives of financial reporting

2. Presentation of information on long-term fiscal sustainability through additional statements or narrative reporting

3. Guidance based on concept of reporting entity & recommended practice for consolidated reports at all levels of government
4. Selection of long-term fiscal sustainability indicators based on (a) relevance to entity, (b) extent to which indicators meet qualitative characteristics, and (c) ability to describe scale of fiscal challenge. Provision of comparative information and disclosure of reasons for ceasing to report previously reported indicators.

5. Disclosure of:
   • Deviations from principle of projections based on current policy
   • Basis on which projections of inflows from taxation and other material revenue sources have been made
   • Other key assumptions underpinning projections
   • Details of key aspects of governing legislation & regulation and underlying macro-economic policy and fiscal framework
6. Disclosure of:
   • Time horizons for projections presented or discussed in GPFRs, as well as reasons for modifying time horizons and any published plans to modify
   • Discount rates and reason for selection
   • Results of key sensitivity analyses
   • Steps taken to ensure that projections are reliable.

7. Guidance should recommend that (a) underlying projections should have been prepared or updated within 5 years of reporting date, and (b) the date of preparation or update should be disclosed