

October 1<sup>st</sup>. 2003.

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Asunto: ***Mexico's Country Report***

From June to September, 2003, the exposure term on projects issued in the prior months, continued. No new projects have been issued in this quarter.

Regards,

<b>To</b>	Members of IFAC Public Sector Committee (PSC)
<b>Date</b>	October 2003
<b>Subject</b>	<b>Country Briefing Report for Germany</b>

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## 1. General Information on the Wirtschaftsprüfer Profession in Germany

We are honoured that the PSC has accepted the invitation of the Institut der Wirtschaftsprüfer in Deutschland (IDW) and the Wirtschaftsprüferkammer (WPK) to meet in Berlin, Germany. Therefore we would like to give you some background on the Wirtschaftsprüfer profession in Germany. The IDW, a private organization, and the WPK, a professional self-regulatory body under public law, represent the German audit profession.

### 1.1. Wirtschaftsprüferkammer

*WPK* is the self-regulatory organisation of all *Wirtschaftsprüfer (WP)*<sup>1</sup>, *vereidigte Buchprüfer (vBP)*<sup>2</sup> and firms of *WP* and *vBP* in Germany. In this capacity *WPK*

- represents the professional interests of its members and
- is the profession's partner, advisor and service provider.

The main responsibilities assigned to *WPK* by the 1961 legislation are

- overseeing members' compliance with their professional duties and imposing disciplinary measures for minor violations and
- co-ordination and assistance of the external quality assurance system.

For further information on the main responsibilities see below a) and b).

Its mission is to enable members to provide valuable services in the highest professional manner as expected by the public.

Public accountants provide credibility to the information subject to audit, which can be relied upon by investors, employees, creditors, government regulators, and other interested parties to make various economic decisions. In order to

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<sup>1</sup> Professional designation granted to officially certified professionals in public practice entitled to conduct all kinds of statutory audits in Germany. In addition, *WP* may provide accounting services, assurance services, tax services, business consulting services as well as trusteeship. (Public Auditor/Accountant).

<sup>2</sup> Professional designation granted to officially certified professionals in public practice entitled to conduct statutory audits of medium-sized limited liability companies and medium-sized partnerships only. In addition, *vBP* may provide accounting services, assurance services, tax services, business consulting services as well as trusteeship. (Sworn Auditor/Accountant).

maintain public confidence members must adhere to the fundamental principles of professional conduct in the performance of professional services. Fundamental ethical principles governing the profession as laid down in the Law Regulating the Profession of WP (*Wirtschaftsprüferordnung/WPO*) and in the by-laws (*Berufssatzung WP/vBP*) are independence, integrity, professional competence & due care, professional responsibility and confidentiality. Furthermore, a member shall not commit an act discreditable to the profession.

Reviewing and assuring compliance with these fundamental ethical principles would normally be a matter of state control. However, with the enactment of the Law Regulating the Profession of WP (*WPO*) in 1961, the legislator opted for the more modern alternative and delegated its duties to the self-regulatory corporation established under public law. To accomplish its task with flexibility and without any bureaucratic barriers, the corporation is organised in the same manner as a private entity.

In order to exercise those privileges accorded by law duly, all public accountants in Germany are required to be members of *WPK*. *WP* and *vBP* are thereby represented by professional colleagues working as volunteers in *WPK* committees. To ensure that the requirements and expectations of the public and the state are met by the profession, *WPK* operates under the oversight of the Federal Ministry of Economics and Labour.

*WPK*'s responsibility is nation-wide. The regional offices, which are not legally independent, assist the head office in Berlin in advising members of the profession and safeguarding the interests of the profession.

*WPK* has been a member of the International Federation of Accountants (IFAC) since 1984. IFAC is the global association of national professional accountancy organisations, the harmonisation of the accountancy profession being its objective. This includes the issuance of the International Standards on Auditing (ISA), which are now increasingly accepted as the uniform auditing standards world-wide.

#### a) Disciplinary Oversight

The chief public prosecutor's office and *WPK* are responsible for the disciplinary oversight of the profession.

For minor violations of professional conduct, *WPK* may take remedial action, such as reprimand. More serious violations are investigated by the chief public prosecutor's office and – in case of sufficient evidence – are subject of disciplinary jurisdiction by court. The nature of sanctions varies with the seriousness of misconduct and other mitigating or aggravated factors. Sanctions may include revocation of professional license to practice.

If a criminal lawsuit has already been filed against members, investigation and prosecution of allegations of professional misconduct will be postponed.

The professional duties are specified in the Law Regulating the Profession of *WP* (*WPO*) and the by-laws (*Berufssatzung WP/vBP*).

#### b) Quality Assurance System

As from January 1, 2001 all *WP/vBP* who are engaged in an audit of financial statements must subject their practice to an external quality assurance system. The quality review involves a study and evaluation of a *WP*-firm's quality control policies and procedures by another *WP*, who is especially qualified for this purpose. However, this does not represent a second audit of financial statements.

This practise is expected to significantly strengthen the position of German professionals in the international competition.

The external quality assurance system is enforced by *WPK*. A Commission on Quality Assurance with its thirteen members, being elected by *WPK*'s Advisory Board, is responsible for:

- the registration of reviewers for quality assurance;
- receiving reviewer's reports;
- granting certificates of participation;
- corrective measures imposed on firms that refuse to co-operate in the conduct of the review or fail in the quality assurance process.

To meet the public interest requirement, the external quality assurance system is subject to review by the Public Oversight Board on Quality Assurance. The Board is composed of five members who are not members of *WPK*. Instead they are appointed from the field of accounting, financial reporting, academic, and judicature. They are independent and not subject to any direction.

### 1.2. Institut der Wirtschaftsprüfer in Deutschland e.V.

The origins of the Wirtschaftsprüfer profession in Germany go back to 1932. At that time Wirtschaftsprüfer and Wirtschaftsprüfungsgesellschaften (firms of Wirtschaftsprüfer) organised themselves in the Institut der Wirtschaftsprüfer (IDW) on a voluntary basis. Presently the IDW comprises approx. 10,170 Wirtschaftsprüfer and 960 professional firms and thus represents approximately 87% of the Wirtschaftsprüfer profession.

The Institute's headquarter is in Düsseldorf. Furthermore there are 6 regional offices in Munich, Hamburg, Frankfurt, Stuttgart, Leipzig and Berlin. Associated with the IDW are the IDW-Verlag (Publishing House) and the Wirtschaftsprüfer Academy (Education).

Those Wirtschaftsprüfer and firms of Wirtschaftsprüfer who are members of the IDW commit themselves to keep to strict professional rules which in parts are more strin-

gent than the minimum requirements provided for under the law. The IDW offers its members a number of professional services.

The IDW considers it one of its major responsibilities to ensure that the professional performance of its members is at a high level of quality. In furtherance of this objective it provides its members with a large number of technical services.

#### a) Standard Setting for Auditing Standards for the Private Sector

Responsibility for drafting standards lies within the IDW with the main Technical Committee and specialised Technical Committees for particular industry sectors, eg, banking, insurance, IT, etc. Committee members are predominantly Wirtschaftsprüfer; others with specialist knowledge may be invited to the Committee, if appropriate.

The IDW is regarded as the standard setter for auditing standards in Germany and a member of IAASB since its inception. So the IDW is just about completing the transformation of the ISAs in auditing standards. Taking account of the national context a literal translation of the ISA was not possible to be used as audit standard in Germany. The overall objectives of the audit and the rights and powers of the auditor are specified in law.

Draft standards are published for comment in technical journals as well as on the IDW homepage so that members and other interested parties may comment. This reflects a due process that was decided upon by the responsible organs of the IDW. The revised drafts are considered by the Institute's Technical Committees and thereafter issued as IDW Auditing Standards. The IDW publishes these "IDW Prüfungsstandards". One of the first auditing standard published by the IDW includes an authority statement.

#### b) Preparation of statements in the field of Accounting

Even after the foundation of a German Accounting Standard Setter the Institute is still engaged in the development of accounting principles and offers recommendations for solution of open accounting issues. For this reason the IDW is maintaining a close contact to the GASC (German Accounting Standards Committee).

From the very beginning the IDW has been member of the former IASC and FEE and has actively contributed to their technical and professional work.

#### c) Rules for the Exercise of the Profession

Another significant part of the IDW's technical activities is taken up by the development of rules for the professional work. Here the IDW is both commenting the regulations set forth by law and by the Wirtschaftsprüferkammer and setting up rules for the professional conduct of its member.

d) Information of Members

The IDW regularly informs its members on the latest developments as regards legislation and jurisdiction both at national and international level. This is achieved by means of the monthly news bulletin "IDW-Fachnachrichten", our homepage and by a wide range of publications issued by the IDW-owned publishing house.

To the extent required the IDW also provides assistance to the individual member faced with a specific technical problem.

e) Pre-qualification Education and Continuing Professional Education

In order to meet the increasing requirements in the fields of pre- and post- qualification education, the IDW offers to its members and their employees a wide range of pre-qualification and continuing professional education measures. Each year these courses attract approx. 15,000 participants – a fact which reveals the importance Wirtschaftsprüfer being members of the IDW attach to their continuing professional education. In addition, there are educational programmes specially designed for professional trainees as well as an extensive courses programme offered by the Wirtschaftsprüfer Academy (established by the IDW).

f) International Cooperation

Within IFAC and FEE and on a bilateral level with other accounting institutes the IDW works together with professionals from all over the world and especially Europe.

## **2. Accounting of the Public Sector in Germany**

### **2.1. Geographical and Political Background**

We would like to give you a short geographical and political background, before we provide an update on the development of the conversion from the cash basis of accounting to the accrual basis of accounting in Germany.

The Federal Republic of Germany (short Germany) has a political system with a pronounced federal structure which has three levels of government: federal (Bund), state (Länder) and local communities (Gemeinden). Germany is divided into 16 states. We refer to the following page for a map of Germany with its 16 states. There are assigned about 14,000 local communities to the states.



The German Constitutional Law (Grundgesetz) defines the responsibilities of the different levels of government. The local communities are responsible in particular for local utilities and services such as water supply, sewage and waste disposal, the construction and maintenance of local roads, etc. They are also responsible for the provision of supplementary welfare benefits, especially social assistance benefits. The Constitutional Law guarantees the local communities the right to manage their own affairs independently. In practice this independence is rather restricted because the local communities heavily rely on grant financing from the states and the vast majority of expenditures are mandatory expenditures. In addition, the states have to approve all borrowing of local communities and deficit financing can be denied and is frequently denied by the states if it is suspected that the local communities will not be able to meet the expected future financial obligations associated with the borrowing.

The states are responsible for cultural affairs, in particular for schools and education, the administration of justice, police and health services. In addition, the states and the federal government cooperate on the planning and financing of joint activities, such as regional economic policy, coastline preservation, agricultural policy as well as public-funded research inside and outside of universities.

The distribution of tax revenues among the levels of government is characterized by two aspects of fiscal federalism in Germany:

- A pronounced fiscal equalization system that is driven by the request of the Constitutional Law to achieve uniformity of living conditions across the regions and
- the almost complete lack of regional differentiation in taxation.

## **2.2. Existing Accounting Frameworks**

Traditionally, financial accounting and reporting of the private and the public sector in Germany is, to a large extent, ruled by federal respectively state legislation. In general the statements of the public sector in Germany are still prepared under the cash basis of accounting.

## **2.3. Responsibilities of Courts of Audit and Accountants**

The accrual based financial statements of private sector entities and government business enterprises are audited by Wirtschaftsprüfer.

The federal and state courts of audit are supreme state authorities. As independent bodies of government auditing they are subject only to the law. The courts of audit's primary task is auditing. The audit courts audit the budget account on the revenue and expenditure rendered by the Ministers of Finance for the previous financial year as well as the efficiency and regularity of the entire financial management including special assets and commercial undertakings. In contrast to other countries the auditors of the courts of audit are not part of the accountants profession.

## **2.4. Current Developments**

Item 7.1 *Country Briefing Report from Germany*

PSC Berlin November 2003

The reform of Public Sector Accounting is, currently, an emerging issue in Germany. The German states have a few exclusive areas of legislative competence, e.g. in respect of budgeting and accounting of the local communities. Therefore as mentioned in our previous country briefing reports, a number of states initiated programs establishing full accrual accounting for the local communities based on the German Commercial Code (Handelsgesetzbuch – short HGB) which is an historical cost full accrual accounting framework.

Two states, North Rhine-Westphalia (NRW) and Lower Saxony, announced the following dates for the legislation and transition process of their assigned local communities from cash basis of accounting to the accrual basis:

	<u>NRW</u>	<u>Lower Saxony</u>
Legislation process	in 2004	2004/2005
Effective date of the law	1. Jan. 2005	1. Jan. 2006
Transitional period	3 years	5 years
End of the transitional period	1. Jan. 2008	1. Jan. 2011

The state Hesse decided to implement the accrual basis of accounting not only for the local communities but also for the state itself. The state Baden-Württemberg leaves the decision in respect of a transition of the accounting method to the local communities. Both states did not announce any dates for a transition yet. Due to the legislative autonomy in respect of setting accounting standards for the local communities the different states developed different transition concepts at the moment. As mentioned above these concepts adopt in a big extent the Commercial Code, i.e. the German accounting standards for the private sector. The concepts differ especially in respect of the valuation in the opening balance. None of the states issued yet any exposure draft of their accounting standards. But they set up a steering committee to harmonize their concepts.

Due to the experience with the audit of government business enterprises and accrual basis of accounting, the IDW issued a discussion paper on accounting for the public sector in December 2001. The proposed accounting principles base upon the requirements of the German Commercial Code. Members of the IDW public sector committee had several meetings with representatives of different states to discuss the paper and to stress the importance of a harmonized set of accounting standards.

The newest developments will be presented in the joint seminar of PSC and IDW. Prof. Dr. Dr. Lüder will give an overview on the reform of government accounting in Europe. Prof. Dr. Harms will speak on the developments and demands in Germany and Dr. Vogelpoth will compare the IPSAS and the German Public Sector Accounting Approaches.

## **IFAC COUNTRY REPORT: UNITED KINGDOM**

### ACCOUNTING STANDARDS BOARD (ASB) DEVELOPMENTS

#### **Statement of Principles for Public Benefit Sector**

The Accounting Standards Board (ASB) and the Board's Public Sector and Not-for-profit Committee (PSNC) are currently considering the responses to the Discussion Paper, *Statement of Principles, Proposed Interpretation for Public Benefit Entities*. The majority of respondents has been supportive of the ASB's initiative and has agreed that the current private sector oriented Statement of Principles can be adopted with appropriate interpretation for the public benefit sector.

The main areas highlighted in responses, which require further consideration, are:

- **the defining class of user:** some commentators questioned whether the proposal that the defining class of user be "funders and financial supporters" is too narrow and others suggested that it is unhelpful.
- **whether the definitions of the elements of financial statements should be changed:** a few commentators considered that new definitions are required, or that the expanded interpretations of the definitions, such as assets, have effectively changed the definitions themselves.
- **liabilities:** in relation to the making of grants by public benefit entities some respondents did not agree with the suggestion that a liability for a grant-making charity to pay a grant will normally only arise when the applicant has met all the relevant criteria. They felt that this would result in liabilities being recognised later than appropriate and that this treatment is not in accordance with FRS 12, *Provisions, Contingent Liabilities and Contingent Assets*
- **contributions from controlling parties:** there is a view that in practice it may not be straightforward to distinguish contributions made in the capacity of a controlling party from other inflows. Certain transactions may have hybrid characteristics. Some respondents have suggested that it should be up to the controlling party to designate whether an inflow should be treated as a contribution or a gain, which mirrors the approach in the draft Non-Exchange Revenue ITC.
- **capital grants:** a number of respondents expressed particular unease with the proposal that where a capital grant is repayable on disposal of the asset, which it has been used to finance, that grant should be recognised as a liability and not reflected as a gain.
- **notional transactions:** some respondents, principally from the voluntary sector, expressed reservations that the paper's proposed presumption that notional transactions should not be recognised might preclude the recognition of gifts in kind

or services provided on a voluntary basis. This proposal primarily related to capital charges and was not meant to extend to such items, so the raising of this issue reflects some confusion in terminology over what is and is not 'notional'. Clarification may therefore be necessary.

- **business combinations:** some respondents, whilst accepting the rationale for the developing approach to business combinations in the private sector, expressed the view that combinations of public benefit entities are often genuine mergers and are concerned that combinations of public benefit entities would have to be treated as acquisitions.

A fuller analysis will be provided in the UK Country Report for the next meeting of the PSC, together with an indication of the way forward for the project envisaged by the ASB.

### **Heritage Assets**

A project on heritage assets is being co-ordinated by the National Audit Office's (NAO) representative on the PSNC and carried out under the aegis of the PSNC. One of the main catalysts for this project has been reservations expressed by the Financial Reporting Advisory Board to the Treasury over the current "mixed measurement" approach in the central government sector. This approach involves the capitalisation of additions to collections, but the existing collection remaining off-balance sheet.

As well as the NAO the project group comprises representatives from central government, non-departmental public bodies and the charitable sector. The evolving approach is underpinned by the distinction between operational and non-operational heritage assets, which is fundamental to the requirements in the central government Resource Accounting Manual (RAM) For non-operational assets, such as art collections, there is a focus on narrative disclosure with readers being provided with an overall impression of the size and value of collections through an indication of the curator's valuation of the most significant items. It is expected that feedback will be provided to the PSNC later this year or early in 2004.

### **Disposal of Non-Current Assets and Presentation of Discontinued Operations**

In accordance with its support for the IASB's convergence programme, the ASB issued Financial Reporting Exposure Draft (FRED 32), *Disposal of Non-Current Assets and Presentation of Discontinued Operations* in July 2003. FRED 32 is congruent with the proposed new International Financial Reporting Standard on the same topics and reflects the ASB's intention to issue a UK standard on these subjects. Such a standard will replace parts of FRS 3, *Reporting Financial Performance*.

Amongst the requirements proposed in FRED 32 is the introduction of a classification, "held for sale", applying to both non-current assets individually and groups of assets to be disposed of in a single transaction (disposal groups). One of the most significant and, from a UK perspective, controversial aspects of the proposals is that assets designated as held for disposal should not be depreciated, regardless of whether they are still in operational use. This is a major change from the current requirements in FRS 15, *Tangible Fixed Assets*. The ASB itself indicates that it does not favour the suspension of depreciation of assets that are being used because they have been designated for sale within a year. The consultation period ended on 24 October 2003

## Other Consultations/Pronouncements

Since the last UK Country Report the ASB has also issued:

- A draft Urgent Issues Task Force Abstract on the Purchase and Sale of an Entity's Own Shares
- An exposure draft of a Supplement to FRED 30, *Financial Instruments: Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk*
- An exposure draft of an amendment to Urgent Issues Task Force Abstract 17, *Employee Share Schemes*

There are few, if any, public sector implications of these exposure drafts. The ASB has also issued the IFRIC proposals on *Accounting for Changes in Decommissioning, Restoration and Similar Liabilities*.

## AUDITING PRACTICES BOARD

The Auditing Practices Board (APB) has issued a consultation exposure draft of a Practice Note, (PN 25), *Attendance at Stocktaking*. This is intended to replace a guidance note that was issued in 1983. The primary focus of the PN is on audit evidence on the existence of stocks. The PN provides guidance on how the requirements of the relevant and current auditing standards should be applied. These include Statement of Auditing Standards (SAS) 300, *Accounting and Internal Control Systems and Audit Risk Assessments*, SAS 400, *Audit Evidence* and SAS 520, *Using the Work of an Expert*. This publication can be downloaded from the APB's website ([www.apb.org.uk](http://www.apb.org.uk)).

The APB has also issued a research study, *Communication between Auditors and Audit Committees*, which summarises the results of research into the practical application of SAS 610, *Communication of Audit Matters to those Charged with Governance*. The study is based on interviews with a number of finance directors, chairs of audit committees and the external auditors of listed companies.

## FINANCIAL REPORTING COUNCIL

The UK Financial Reporting Council has issued a new Combined Code. The Code supersedes the existing Code and applies to reporting periods beginning on or after 1 November 2003. The Code incorporates the recommendations of the Higgs Report on non-executive directors and the Smith Report on audit committees, which were produced earlier this year.

The Code is directed at listed companies and given effect through the listing rules of the Financial Services Authority. Notwithstanding its primary focus, the revised Combined Code will have an impact on the public benefit sector. Many parts of the UK public sector have already stated to examine their governance processes in the light of the Smith and Higgs Reports.

## RESOURCE ACCOUNTING AND BUDGETING/WHOLE OF GOVERNMENT ACCOUNTS

## Whole of Government Accounts

The Treasury has recently initiated a project to bring together on a single platform the financial information functions currently performed by three systems:

- Government On-Line Data (GOLD) – the consolidation system collecting and reporting audited data for government bodies;
- General Expenditure Monitoring System (GEMS) – spreadsheets that collect high level outturn and forecast figures for the current financial year;
- Public Expenditure Statistics (PES) – a bespoke system that holds more detailed expenditure plan and outturn data covering three forward years, the current year and five prior years.

Departments have highlighted problems using three separate systems which do not interface and which all use different coding structures. Within the Treasury, there are also significant overheads in running three separate systems on different platforms, each with their own specialist staffing, maintenance and upgrade requirements. The outline plan for the SDS project envisages an overall timescale of 2 to 3 years for implementation of the new system, depending on the solution adopted.

The project will help ensure that the better quality data collected through the Whole of Government (WGA) programme is integrated into the data sets used for decision-making within the Treasury and is used for National Accounts purposes wherever possible. Treasury is, of course, also participating in the international ‘Convergence Group’ that is considering the future actions to take in respect of the convergence of GAAP, Government Financial Statistics (GFS) and National Accounts frameworks.

In June 2003 Treasury issued guidance to Consolidation Managers on identifying transaction streams and balances between bodies and the seven main public sector pension schemes within the central government boundary. This guidance (DCO 5/03) is available on the WGA website ([www.wga.gov.uk](http://www.wga.gov.uk)).

## LOCAL GOVERNMENT

The CIPFA/LASAAC Joint Committee, which is responsible for developing and maintaining *the Code of Practice on Local Authority Accounting in the United Kingdom* (the Local Government Statement of Recommended Practice or SORP) under the auspices of the ASB has developed the consultation exposure draft of the 2004 edition of the SORP. Subject to the approval of the ASB it will be issued on a three-month consultation in early November 2003.

The main change proposed in the consultation is a very significant modification of the current requirements relating to group accounts. Currently UK local authorities are only required to produce group accounts as supplementary statements if interests in subsidiaries, associates and joint ventures are material in aggregate. In practice only a small minority of authorities has produced such supplementary statements and recent research suggests that, amongst this minority, there has been considerable diversity of practice over format. The consultation proposes that local authorities should produce full consolidated statements and emphasises

the qualitative aspects of materiality, so that the strong presumption is that all interests should be consolidated.

The proposals are based on definitions in UK Generally Accepted Accounting Practice (GAAP) with some re-expression to reflect local authority circumstances. In producing a flow chart to guide accounts-preparers in assessing the nature of interests the flow chart in IPSAS 6, *Consolidated Financial Statements and Accounting for Controlled Entities* has been a model..

A particularly difficult issue has been the treatment of “statutory bodies”, such as fire authorities, joint boards and , in Scotland, police authorities, to which local authorities have rights to nominate members and an exposure to financial risk. The proposal is that such bodies should be treated consistently with other entities. However, in due course, if local authorities and statutory bodies are designated for incorporation into Whole of Government Accounts, there will be a rebuttable presumption, in accordance with FRS 2, *Subsidiary Undertakings* that an individual local authority cannot be the “parent” of such a body. Such a rebuttable presumption will only be available once the decision regarding entities to be consolidated into WGA has been made and communicated by central government.

The exposure draft also proposes a change to the discount rate for liabilities relating to the main local government defined benefit pension scheme. When the SORP introduced the full implementation of FRS 17, *Retirement Benefits* in 2003 the view was taken that, as local authorities do not have the same ability to curtail or close the scheme as most private sector entities with defined benefit schemes, it was appropriate to use a long-term risk free rate to discount scheme liabilities rather than the AA Corporate Bond rate specified in FRS 17. However, the ASB has raised concerns that the rate currently used in the SORP, which is set by the Government Actuary’s Department, at 3.5% “real” is higher than current AA Corporate Bond rates. The ASB referred to this issue in its negative assurance statement on the 2003 SORP. Therefore for 2004 it is proposed that the rate adopted be the AA Corporate Bond rate. Subject to further research there is a possibility of reverting to a public sector specific rate in the future.

Other changes proposed include:

- ensuring that the SORP’s provisions in relation to the definition and measurement of finance leases accord with SSAP 21, *Accounting for Leases and Hire Purchase Contracts* and that the full disclosure requirements of SSAP 21 are incorporated in the SORP
- that the minority of local authorities which have financial instruments listed or publicly traded on a stock exchange should provide the disclosures required by FRS 13, *Derivatives and Other Financial Instruments*

## PUBLIC AUDIT FORUM

The Public Audit Forum, which brings together the United Kingdom’s four national audit agencies, has published a second edition of its Discussion Paper on the *Audit Implications of Electronic Service Delivery*, which was first issued in April 2001. The Discussion Paper, which is directed at both auditors and management, emphasises that electronic service should not erode accountability. It is therefore important that management is able to convince third parties of the reliability of records. It explains that the adequacy and appropriateness of

controls is dependent on the quality of risk analysis that underpins the selection of controls for particular types of electronic record. In addition to its effect on the work that they carry out to form their audit opinions, the Discussion Paper highlights other implications for auditors such as the need for awareness of information security risks, controls and standards and the maintenance of relevant skills in the electronic area. It also argues that external auditors have an important role to play in promoting management's client awareness of best practice in building and maintaining secure and effective systems, including information system standards. The full text of the paper is available on the Public Audit Forum's website at [www.publi-audit-forum.gov.uk](http://www.publi-audit-forum.gov.uk).

The April UK Country Report highlighted the Public Audit Forum's report, *The Whole Truth or Why Accruals Accounting Means Better Management*. The Audit Liaison Group, which brings together the National Audit Office, Treasury and central government departments, will be considering the barriers to enjoying the full benefits of accruals accounting identified in the paper at a meeting later this year.

*John Stanford, UK Technical Adviser*

## United States Country Report Prepared September 2003

The following summarizes the standards, proposed standards, and other documents that have been issued by various U.S. standard-setting bodies since the last reporting date of June 2003.

### **Recent Activity of the Federal Accounting Standards Advisory Board (FASAB)**

*SFFAS 25.* In July 2003, the FASAB issued Statement of Federal Financial Accounting Standards (SFFAS) No. 25, *Reclassification of Stewardship Responsibilities and Eliminating the Current Services Assessment*. Information about stewardship responsibilities is currently designated Required Supplementary Stewardship Information (RSSI), a category unique to federal financial reporting. Pursuant to this SFFAS, information about Risk Assumed will become required supplementary information (RSI). The Statement of Social Insurance will become a basic financial statement, while the remaining information about Social Insurance required by SFFAS 17, *Accounting for Social Insurance*, will be reported as RSI. The requirement to report the Current Services Assessment will be eliminated effective for reporting periods beginning after September 30, 2002. Information about Risk Assumed shall be presented as RSI for reporting periods beginning after September 30, 2002. The information required by paragraphs 27(3) and 32(3) of SFFAS 17 shall be presented as a basic financial statement rather than as RSSI for periods beginning after September 30, 2004, with earlier implementation encouraged. Other information required by SFFAS 17 shall be presented as RSI rather than as RSSI, except to the extent that the preparer elects to include some or all of that information in notes that are presented as an integral part of the basic financial statements, for periods beginning after September 30, 2004.

*Exposure Draft: Heritage Assets.* In August 2003, the FASAB issued an Exposure Draft of a proposed SFFAS titled, *Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Stewardship Information*. Heritage assets and stewardship land information is currently classified as RSSI. The Board is proposing that heritage assets and stewardship land information be classified as basic information, except for condition information. The Board proposes that condition information be classified as RSI. The Board is also proposing to require additional reporting disclosures about entity stewardship policies and an explanation of how heritage assets and stewardship land are pertinent to the entity's mission.

*AAPC Exposure Drafts: Direct Loan and Loan Guarantees.* The Accounting and Auditing Policy Committee (AAPC) of the FASAB is requesting comments on two Exposure Drafts of proposed Federal Financial Accounting and Auditing Technical Releases related to direct loan and loan guarantee accounting and auditing. The first Exposure Draft (proposed Technical Release 6), *Preparing Estimates for Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act (Amendments to Technical Release 3: Preparing and Auditing Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act)*, would replace the earlier preparation guidance found in Technical Release 3 with more current guidance. The second Exposure Draft, *Auditing Estimates for Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act (Amendments to Technical Release 3: Preparing and Auditing*

*Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act*), would preserve, with minor technical changes, the existing audit guidance in Technical Release 3.

*Rule 203 Activity.* The AICPA recently appointed a panel to review the FASAB's continuing authority to set generally accepted accounting principles for the federal government under Rule 203 of the AICPA Code of Conduct. The panel will assist the AICPA Board of Directors and Council by providing its recommendations on the continued recognition of the FASAB in accordance with an October 1999 Council resolution on the initial recognition of FASAB under Rule 203. The Council resolution called for the Board of Directors to, by no later than October 2004, review the mission and operations of the FASAB, evaluate whether the FASAB continues to meet Council-approved criteria used to assess standards-setting bodies designated under Rule 203, and recommend to Council whether the Council shall continue to designate the FASAB under Rule 203.

### **Recent Activity of the Governmental Accounting Standards Board (GASB)**

*TB 2003-1.* In June 2003, the GASB issued Technical Bulletin (TB) 2003-1 titled, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets*, which supersedes TB 94-1, *Disclosures about Derivatives and Similar Debt and Investment Transactions*. TB 2003-1 clarifies and adds guidance on derivatives disclosures pending results of the GASB's project on reporting and measurement of derivatives and hedging activities. The disclosures are intended to provide information to financial statement users that would enhance their understanding of the significance of derivatives to a government's net assets and would assist them in assessing the amounts, timing and uncertainty of future cash flows. The TB also discusses what methods are acceptable for determining a derivative's fair value. The TB is effective for reporting periods ending after June 15, 2003.

*Exposure Draft: Economic Condition.* In September 2003, the GASB issued this Exposure Draft titled, *Economic Condition Reporting: The Statistical Section*. The statistical section that accompanies a state or local government's basic financial statements comprises schedules presenting trend information about revenues and expenses, outstanding debt, economics and demographics, and other subjects. These schedules are intended to provide financial statement users with contextual information to better assess a government's financial health. The proposal would revise the statistical section to include more comprehensive government-wide financial information. Further, it would update the statistical section to reflect the significant changes that have taken place in government finance. The proposal also would replace the current standards, which are oriented toward general-purpose local governments, with clearer guidelines that can be implemented by any type of governmental entity. Although the statistical section is a required part of a comprehensive annual financial report (CAFR), state and local governments are not required to prepare a statistical section if they present their basic financial statements in a report other than a CAFR. These circumstances would not be changed by the proposed standard. The proposal would, however, govern any statistical section accompanying a government's basic financial statements, whether presented in a CAFR or not.

*Special Report on Performance Information.* In August 2003, the GASB issued a Special Report titled, *Reporting Performance Information: Suggested Criteria for Effective Communication*.

The report describes a set of 16 suggested criteria that state and local governments can use to produce effective reports on service efforts and accomplishments (also referred to as performance information). The report is the result of the fourth of six phases in a GASB research project on service efforts and accomplishments. The report also discusses the process used to develop the criteria, the history of performance reporting, the “managing for results” concept, accountability and citizen engagement, and good practices.

*Annual GASB Implementation Guide.* This new annual volume in question-and-answer format is comprised of all the existing implementation guides—updated and supplemented to incorporate provisions of subsequently issued Statements through Statement 39. The 2003 edition covers Statements 3, 9, 10, 14, 25-27, 31, and 34.

### **Recent Activity of the Financial Accounting Standards Board (FASB)**

*Exposure Draft: Pension Benefits and OPEB Disclosures.* In September 2003, the FASB issued an Exposure Draft titled, *Employers’ Disclosures about Pensions and Other Postretirement Benefits*, that would revise the financial statement disclosures for defined benefit plans. The FASB proposes to require that companies provide more details about their plan assets, benefit obligations, cash flows, benefit costs and other relevant information. For the first time, companies would be required to provide financial statement users with a breakdown of plan assets by category, such as equity, debt and real estate. The expected rates of return and target allocation percentages, or target ranges, for these asset categories also would be required in financial statements. Cash flows would include projections of future benefit payments and an estimate of contributions to be made in the next year to fund the pension and other postretirement benefit plans. In addition to expanded annual disclosures, the FASB seeks to improve the information available to investors in interim financial statements. Companies would be required to report the various elements of pension and other benefit costs on a quarterly basis.

*FASB Staff Positions.* The following final and proposed staff positions were issued since June 2003:

- Determining Whether a One-Time Termination Benefit Offered in Connection with an Exit or Disposal Activity Is, in Substance, an Enhancement to an Ongoing Benefit Arrangement (final)
- Determination of Cost Basis for Foreclosed Assets under FASB Statement No. 15, *Accounting by Debtors and Creditors for Troubled Debt Restructurings*, and the Measurement of Cumulative Losses Previously Recognized under Paragraph 37 of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (proposed)
- Issuer's Accounting for Freestanding Financial Instruments Composed of More Than One Option or Forward Contract Embodying Obligations under FASB Statement No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity* (proposed)
- Accounting for Mandatorily Redeemable Shares Requiring Redemption by Payment of an Amount that Differs from the Book Value of Those Shares, under FASB Statement No.

150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity* (proposed)

### **Recent Activity of the AICPA Auditing Standards Board (ASB)**

*SOP: Greenhouse Gas Emissions.* In September 2003, the ASB issued Statement of Position (SOP) 03-2, *Attest Engagements on Greenhouse Gas Emissions Information*. The SOP provides performance and reporting guidance to practitioners on examinations of information about (a) greenhouse gas (GHG) emissions (known as a GHG *inventory*) for a compliance period, such as a year or (b) a GHG emission reduction. Such examination engagements should be performed pursuant to Chapter 1, “Attest Engagements,” of Statement on Standards for Attestation Engagements (SSAE) No. 10, *Attestation Standards: Revision and Recodification*, as amended. Clients may request such services in connection with (a) registering their GHG inventory information with a GHG registry or (b) trading emission reduction credits.

*Attestation Interpretation, XBRL.* In September 2003, the Audit Issues Task Force of the ASB issued a new interpretation of chapter 1 of SSAE No. 10. The Interpretation is titled *Attest Engagements on Financial Information Included in XBRL Instance Documents*. *XBRL*, the business reporting aspect of the Extensible Markup Language (XML), makes it possible to store or transfer data, along with complex process, data processing hierarchies and description that enable analysis and distribution. An *XBRL Instance Document* provides financial information in a machine-readable format. The new attest interpretation defines the terms *XBRL* and *XBRL Instance Document* and describes the practitioner’s considerations when he or she has been engaged to examine and report on whether an XBRL Instance Document accurately reflects certain client financial information. It also provides example examination reports.

### **Recent Activity of the AICPA Accounting Standards Executive Committee (AcSEC)**

*SOP: Non-Traditional Long-Duration Insurance Contracts.* In July 2003, AcSEC issued SOP 03-1, *Accounting and Reporting by Insurance Enterprises for Certain Non-Traditional Long-Duration Contracts and for Separate Accounts*. The SOP provides guidance on accounting and reporting by insurance enterprises for certain nontraditional long-duration contracts and for separate accounts. The SOP is effective for financial statements for fiscal years beginning after December 15, 2003, with earlier adoption encouraged. The SOP may not be applied retroactively to prior years’ financial statements, and initial application should be as of the beginning of an entity’s fiscal year.

*Exposure Drafts: Investment Industry.* In July 2003, AcSEC issued an Exposure Draft of a proposed SOP titled, *Reporting Financial Highlights and Schedule of Investments by Nonregistered Investment Partnerships: An Amendment to the Audit and Accounting Guide Audits of Investment Companies and AICPA Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships*. The Exposure Draft provides guidance on the application of certain provisions of AICPA Audit and Accounting Guide, *Audits of Investment Companies*, to nonregistered investment partnerships. Also, in July 2003, AcSEC issued an Exposure Draft of a proposed SOP titled, *Financial Highlights of Separate Accounts: An Amendment to the Audit and*  
**Item 7.1 Country Briefing Report from USA**  
 PSC Berlin November 2003

*Accounting Guide Audits of Investment Companies.* The exposure draft provides guidance on reporting financial highlights by separate accounts of insurance enterprises.

### **Recent Activity of the U.S. General Accounting Office (GAO)**

*Yellow Book Revision.* Certain laws, regulations, and contracts require auditors to follow *Government Auditing Standards* (also known as the Yellow Book) promulgated by the Comptroller General of the United States. The GAO issued a comprehensive revision to *Government Auditing Standards* on June 25, 2003. This is the fourth revision of the overall standards since they were first issued in 1972. This revision of the standards supersedes the 1994 revision, including amendments 1 through 3. The revision affects all chapters of the Yellow Book, including those relating to both financial and performance audits. Among other things, the proposed changes are intended to clarify the types of audits and services that are performed under the Yellow Book, strengthen and streamline certain provisions of it, and improve understandability of the standards. The revisions are effective for financial audits and attestation engagements of periods ending on or after January 1, 2004, and for performance audits beginning on or after January 1, 2004. Early application is permissible. An electronic version of the standards and a summary of the major changes from the 1994 revision can be accessed on the GAO web site at [www.gao.gov/govaud/ybk01.htm](http://www.gao.gov/govaud/ybk01.htm).

### **Recent Activity of the Public Company Accounting Oversight Board (PCAOB)**

The PCAOB has issued the following Proposed Releases and Final Rules since June. Additional information on these items can be found on the PCAOB web site at [www.pcaobus.org](http://www.pcaobus.org).

2003-012	Proposed Rules on Investigations and Adjudications
2003-013	Proposed Rules on Inspections of Registered Public Accounting Firms
2003-014	Proposed Rules on Withdrawal from Registration
2003-009	Final Rule on Compliance with Auditing and Related Professional Practice Standards – Advisory Groups
2003-008	Final Rule on Ethics Code for Board Members, Staff, and Designated Contractors and Consultants