

## **Country Report for Japan**

Update of the previous report

July 2004

### **2. Financial Structure and Accounting System of the National Government**

#### **2.3 Prospects for the Accrual-based Accounting System**

According to the report on the accounting system of the National Government of Japan published by the Ministry of Finance (MOF) in June 2003, the accounting system should carry on with cash-based system. However, the MOF will continue to study the merits of the accrual-based accounting system.

Considering the latter, the ministries are required to prepare trial balance sheets for FY2002 by the middle of the year of 2004 using statistic data.

The MOF is now setting new standards for financial statements to be prepared by ministries, by examining the trial statements for FY 2002. The new standards will be published soon and the ministries will be required to prepare and present financial statements based on the new standards starting from FY 2003.

Besides, the MOF is planning to reconsider categories presented in Budget and Accounts. In doing so the ministers will be able to evaluate the performance of each ministry more efficiently. It will also make the budget more clear to understand.

**United States Country Report**  
**Prepared for the IFAC Public Sector Committee**  
**June 2004**

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

*Research Report.* In April 2004, the FASAB released a research report *Capital and Operating Leases* which describes existing standards issued by other standard-setters relating to lease accounting and identifies the various current leasing transactions used by federal agencies and whether these transactions create different or more urgent needs for FASAB guidance. The report will serve as a reference tool for future Board discussions on the varying lease transactions throughout the federal government.

*Inter-Entity Exposure Draft.* In April 2004, the FASAB issued a proposed standard, *Inter-Entity Cost Implementation: Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts*. SFFAS 4 requires that reporting entities report the full costs of outputs in general purpose financial reports. The full cost of an output should include the costs covered by other reporting entities. These costs are referred to as “inter-entity costs.” SFFAS 4 recognized the difficulties in attaining this goal and provided for gradual implementation of inter-entity costing. The proposal would require full implementation of the full cost standards in FY 2008 by amending Managerial Cost Accounting Standards to require inter-entity cost implementation.

*Significant Assumptions Disclosure Exposure Draft.* In March 2004, the FASAB issued a proposed standard, *Presentation of Significant Assumptions for the Statement of Social Insurance: Amending SFFAS 23*. The proposed standard would require disclosure of significant assumptions underlying the Statement of Social Insurance. That Statement reports the net present value of long-term cash flow forecasts of taxes and benefits relating to the Social Security, Medicare, Black Lung and Railroad Retirement Board programs. The proposal would reclassify significant assumptions as basic information rather than as required supplementary information. The proposed disclosures are intended to help financial statement users assess the uncertainty surrounding long-range projections. If adopted, the proposal would be effective for reporting periods ending after September 30, 2004.

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

*GASB Statement No. 44.* In June 2004, the GASB issued Statement No. 44 titled, *Economic Condition Reporting: The Statistical Section*. It enhances and updates the statistical section that accompanies a state or local government’s basic financial statements to reflect the significant changes that have taken place in government finance, including the more comprehensive government-wide financial information required by GASB Statement 34. It also replaces prior standards, which were oriented toward general purpose local governments, with clearer guidelines that can be implemented by any type of governmental entity. Statement 44 further improves the understandability and usefulness of statistical section information by requiring governments to augment their

schedules with notes regarding sources, methodologies, and assumptions, and narrative explanations of unfamiliar concepts, atypical trends, and anomalous data that users would not otherwise understand. Statement 44 is effective for periods beginning after June 15, 2005.

*GASB Statement No. 43.* In May 2004, the GASB issued Statement No. 43 titled, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. Statement 43 applies to OPEB plans that are included as trust funds in the financial reports of plan sponsors or employers, and to stand-alone financial reports of OPEB plans that are established as trusts, when issued by the public employee retirement systems, or other governmental entities that administer them. It also provides requirements for reporting of OPEB funds by administrators of multiple-employer OPEB plans, when the fund used is not a trust fund. Statement 43 provides a framework for transparent financial reporting by governmental entities that have fiduciary responsibility for OPEB plan assets regarding their stewardship of plan assets, the funded status and funding progress of the plan, and employer contributions to the plan. The approach taken generally is consistent with that adopted in the GASB's standards for pension plans, with modifications to reflect OPEB plan differences.

*Tobacco Technical Bulletin.* In May 2004, the GASB issued Technical Bulletin (TB) 2004-1 titled, *Tobacco Settlement Recognition and Financial Reporting Entity Issues*. The TB clarifies asset and revenue recognition guidance for tobacco settlement transactions, including payments made to settling governments pursuant to the 1998 Master Agreement between major tobacco companies and state governments (settling governments). In addition, the TB clarifies accounting guidance on whether a tobacco settlement authority (TSA) that is created to obtain the rights to all or a portion of future tobacco settlement resources is a component unit of the government that created it.

*New GASB Chairman Named.* In February 2004, the Financial Accounting Foundation announced that Robert Attmore has been elected Chairman of the GASB, effective July 1, 2004. Mr. Attmore will succeed Tom Allen, who has served as GASB chairman since 1995. Previously, Mr. Attmore was the Deputy State Comptroller for the State of New York.

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

*Stock Options Exposure Draft.* In March 2004, the FASB issued an exposure draft titled, *Share-Based Payment*. The proposed change in accounting would replace existing requirements under FAS 123, *Accounting for Stock-Based Compensation*, and APB Opinion No 25, *Accounting for Stock Issued to Employees*. The exposure draft covers a wide range of equity-based compensation arrangements. Under the proposal, all forms of share-based payments to employees, including employee stock options, would be treated the same as other forms of compensation by recognizing the related cost in the income statement. The expense of the award would generally be measured at fair value at the grant date. Current accounting guidance requires that the expense relating to so-called

fixed plan employee stock options only be disclosed in the footnotes to the financial statements.

*FASB Staff Positions.* The following final staff positions were issued since February 2004 (all are available on the FASB Web site at [www.fasb.org](http://www.fasb.org)):

- FSP FAS 106-2, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (May 19, 2004)
- FSP FAS 141-1 and 142-1, Interaction of FASB Statements No. 141, *Business Combinations*, and No. 142, *Goodwill and Other Intangible Assets*, and EITF Issue No. 04-2, “Whether Mineral Rights Are Tangible or Intangible Assets” (April 30, 2004)
- FSP FIN 46 (R)-4, Technical Correction of FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, Relating to Its Effects on Question No. 12 of EITF Issue No. 96-21, “Implementation Issues in Accounting for Leasing Transactions involving Special-Purpose Entities” (April 30, 2004)
- FSP FAS 140-1, Accounting for accrued interest receivable related to securitized and sold receivables under Statement 140 (April 14, 2003)
- FSP FAS 129-2, Disclosure Requirements under FASB Statement No. 129, *Disclosure of Information about Capital Structure, Relating to Contingently Convertible Securities* (April 9, 2004)

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

*Statement of Social Insurance Exposure Draft.* In March 2004, the ASB issued an exposure draft of a proposed Statement of Position (SOP) titled, *Auditing the Statement of Social Insurance*. Among other things, the exposure draft describes the auditor’s responsibility when auditing the Statement of Social Insurance, including planning the audit, performing substantive procedures, and reporting on the statement of social insurance. The Statement of Social Insurance is a financial statement required by FASAB SFFAS No. 17, *Accounting for Social Insurance*, and SFFAS No. 25, *Reclassification of Stewardship Responsibilities and Eliminating the Current Services Assessment* which includes a long-term projection of the present value of the income to be received from or on behalf of existing and future participants of social insurance programs (for example, Social Security), the present value of the benefits to be paid to those same individuals, and the difference between the income and benefits.

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

The PCAOB has issued the following proposals and Final Rules since February 2004. Additional information on these items can be found on the PCAOB web site at [www.pcaobus.org](http://www.pcaobus.org).

- Release No. 2004-007: Rule Regarding Certain Terms Used in Auditing and Related Professional Practice Standards (Submitted to SEC for approval)

- Release No. 2004-006: Audit Documentation and Amendment to Interim Auditing Standards (Submitted to SEC for approval)
- Release No. 2004-005: Oversight of Non-U.S. Public Accounting Firms (Final Rule)
- Release No. 2004-003: Registration Deadline for Non-U.S. Accounting Firms (Final Rule)
- Release No. 2004-002: Conforming Amendments to PCAOB Interim Standards (Proposed)
- Release No. 2004-001: Auditing Standard No. 2. An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements (Final Rule)



DATE: 22 June 2004

MEMO TO: MEMBERS OF THE IFAC PUBLIC SECTOR COMMITTEE

FROM: Greg Schollum  
NEW ZEALAND REPRESENTATIVE

SUBJECT: UPDATE ON RECENT DEVELOPMENTS IN NEW ZEALAND

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## **Introduction**

This memorandum updates Members of the IFAC Public Sector Committee (PSC) on recent developments in New Zealand, specifically relating to:

- Generally Accepted Accounting Practice;
- Auditing and Professional Standards;
- Central Government;
- Local Government; and
- Other Developments.

## **Generally Accepted Accounting Practice**

### *Adoption of International Standards in New Zealand*

The Financial Reporting Standards Board (FRSB) continues working to adopt New Zealand equivalents to IFRS/IAS. A list of all exposure drafts issued for comment is included on the ICANZ website ([www.icanz.co.nz](http://www.icanz.co.nz)). The following table summarises FRSB progress to date.

<b>Status of Issue of NZ EDs/NZ IFRSs as at 11 June 2004</b>	
EDs of IASs issued – comment period closed	29
EDs of IASs issued – comment period open	4
EDs of IASs yet to be issued	-
Total IASs to adopt	33
EDs of NZ IFRS/NZ IFRICs issued	15
Other NZ specific EDs/ITC issued	4
NZ IFRSs or IASs agreed as Pending Standards	12

Once standards have been tentatively approved by the Accounting Standards Review Board (ASRB) they are issued as Pending Standards on the Institute and the ASRB web sites. This provides constituents with one final opportunity to raise any concerns with the standards. It also provides time for the FRSB to conduct a final review of the standards to remove any

inconsistencies and to work with the AASB to remove unnecessary differences between NZ and Australian standards.

The FRSB has established a number of working groups (as listed below) to assist it in adopting IFRS/IAS in the New Zealand environment – details of each were outlined in the previous country report:

- Conversion Working Group
- Insurance Contracts Working Group
- Business Combinations Working Group
- Financial Instruments Working Group
- Tax Working Group.

#### *Prospective Financial Information*

New Zealand currently has on issue FRS-29 covering Prospective Financial Information. The FRSB recently established a Prospective Financial Information Working Group to review FRS-29. Prospective financial information is of particular importance in the local government sector as the Local Government Act 2002 requires local authorities to prepare a long term council community plan every three years covering a period of not less than 10 consecutive financial years. Forecast information included in that plan is required to be prepared in accordance with generally accepted accounting practice. In addition, from 2006, such plans are required to contain a report from the local authority's auditor on—

- (a) the extent to which the local authority has complied with the requirements of the Local Government Act 2002 in respect of the plan; and
- (b) the quality of the information and assumptions underlying the forecast information provided in the plan; and
- (c) the extent to which the forecast information and performance measures provide an appropriate framework for the meaningful assessment of the actual levels of service provision.

#### *IASB Projects - Management Commentary*

The New Zealand Institute of Chartered Accountants is leading the IASB project on Management Commentary in the research phase, working alongside representatives from fellow Partner Standard Setters Canada, Germany and the UK. The IASB has also allocated staff along with the Board members responsible for liaising with the relevant standard setters.

The first task for the IASB Working Group is to produce a discussion paper for the IASB outlining how an international financial reporting standard for Management Commentary could be developed. This paper outlines some of the issues the working group is considering, and early thoughts on the subject, including:

- existing requirements in various countries around the world;
- current drivers of non-financial disclosure;
- whether a Standard is needed;
- the objective of Management Commentary;
- characteristics of Management Commentary;
- whether information should be in the financial statements or the Management Commentary; and
- what should be disclosed in Management Commentary?

### *Accounting Standards Review Board Release 8*

The ASRB has issued Release 8. Release 8 outlines the ASRB's functions, the nature of approved financial reporting standards, the ASRB's expectations as to the content of financial reporting standards, and the criteria the ASRB employs in evaluating proposed financial reporting standards, and amendments to approved financial reporting standards, which are submitted to it for approval in accordance with the Financial Reporting Act 1993. Specifically the ASRB has decided that the following guidelines should be observed in adapting an IFRS for issue as a New Zealand equivalent to IFRS:

- a. The IFRS disclosure requirements cannot be reduced for profit-oriented entities;
- b. Additional disclosure requirements can be added for all entities;
- c. Recognition and measurement requirements in an IFRS cannot be amended for profit-oriented entities;
- d. Recognition and measurement requirements can be amended for public benefit entities, with a rebuttable presumption that amendments are based on existing IPSAS<sup>5</sup> or existing FRS, as applicable;
- e. Guidance materials may be added based on the same principles as applying to addition of recognition and measurement requirements as outlined in 'd' above; and
- f. Where an IFRS contains alternative permissible treatments the Board may determine that only one option can be applied to be able to comply with New Zealand GAAP. Where an IFRS permits options that are not allowed in existing FRS, a strong argument will need to be made for the Board to agree to such options in the New Zealand equivalents to IFRS. In reaching a view on this issue the Board will be mindful of the approach adopted by the AASB.

The ASRB has also established a "super-user review group" to review the Pending standards before they are formally approved.

### *Guidance for Public Benefit Entities*

The adoption of IFRS in New Zealand has created issues on how to implement a sector neutral approach to standard setting in New Zealand. To date, all additional guidance applicable to public benefit entities has been included in the body of the proposed New Zealand equivalents to IFRS. In some cases, this has meant the inclusion of many additional guidance paragraphs that may be seen to "clutter" a standard. In other cases, certain guidance that might be considered useful to public benefit entities has been excluded from the standard because it creates a perceived imbalance in the standards, which generally do not contain profit-oriented examples or guidance within their body.

To address these concerns the Institute has announced new initiatives to ensure New Zealand retains high quality and workable financial reporting standards for the public and not-for-profit sectors that are based on international financial reporting standards.



Additional resources are to be devoted to produce application guidance and presentation standards for the public and not-for-profit sectors. The Institute has also established a Not-for-Profit Taskforce to help develop guidance specific to that sector.

#### *Trans-Tasman Accounting Standards Advisory Group*

An Advisory Group has been established with the purpose of advising the Australian and New Zealand accounting standard and oversight bodies on strategies to:

- Establish a single set of trans-Tasman accounting standards within the broader context of both jurisdictions' objective of adopting international accounting standards;
- Maximise the influence of Australia and New Zealand in the development of international accounting standards and the international accounting standard setting process.

The Advisory Group will also help formulate advice to the two governments on these issues.

In undertaking this role, the Advisory Group will be guided by the fundamental principle contained in the Australia/New Zealand Memorandum of Understanding on Business Law Co-ordination that entities should only have to comply with one set of rules and have certainty as to the application of those rules in the other jurisdiction. It will also be guided by the principles attached to these terms of reference.

The Advisory Group will provide advice under three broad headings:

- Standards setting – this will be advice primarily to the Australian Financial Reporting Council (FRC) and the Accounting Standards Review Board (ASRB).
- Policy co-ordination – this will be advice primarily to the Australian and New Zealand governments.
- Joint institutions – this will be advice primarily to the Australian and New Zealand governments.

The Advisory Group comprises three nominees of the FRC, one nominee of the Australian Accounting Standards Board, two nominees of the ASRB, and one representative of each of the Australian Treasury and the New Zealand Ministry of Economic Development.

## **Auditing and Professional Standards**

### *Auditing Standards*

The Professional Practices Board (PPB) is continuing its work on moving to adopt International Standards on Auditing.

## **Central Government**

### *The Public Finance (State Sector Management) Bill.*

An amendment to the Public Finance Act was presented to Parliament in September 2003. The main aims of the amendment are to provide additional flexibility to the public service and to establish clearer governance arrangements for government entities. Provisions in the Act regarding accrual accounting remain essentially unchanged.

This Bill is now being examined by a select committee. It is expected to be reported back to the House of Representatives in October 2004.

#### *Adoption of IFRS*

The Government has announced that it will produce forecast and actual Crown financial statements in accordance with NZ IAS/NZ IFRS from 2007 (first audited set 30 June 2008). Until that date, the Government will continue to comply with NZ GAAP represented by the sector-neutral standards produced.

#### **Local Government**

Local authorities in New Zealand are beginning to gear up for the adoption of NZ equivalents to IFRS/IAS and it appears likely that all Long-term Council Community Plans (containing 10 year forecasts) adopted on or around 30 June 2006, will need to be prepared on the basis of the new standards.

#### **Other Developments**

##### *Charities Bill*

In March 2004 the Government released the Charities Bill. Under the Bill, charities would be required to register with a Charities Commission. Registration will enable charities to retain their tax-free status but will require charities to file an annual return. The content of the annual return has not been finalised but is likely to include financial data.

If you have any questions about any of these matters please feel free to raise them with me.

Greg Schollum  
**NEW ZEALAND REPRESENTATIVE**