

**FIFTH DRAFT ED**

## Social Policy Obligations

### **REQUEST FOR COMMENTS**

The International Public Sector Accounting Standards Board, an independent standard-setting body within the International Federation of Accountants (IFAC), approved this Exposure Draft *Social Policy Obligations*, for publication in Month (xxxx) Year(xxxx). This proposed International Public Sector Accounting Standard may be modified in light of comments received before being issued in final form.

Please submit your comments, preferably by email, so that they will be received by xx xx xxxx. All comments will be considered a matter of public record. Comments should be addressed to:

The Technical Director  
International Public Sector Accounting Standards Board  
International Federation of Accountants  
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New York, New York 10017 USA

Email responses should be sent to: [publicsectorpubs@ifac.org](mailto:publicsectorpubs@ifac.org)

## **INTRODUCTION TO THE INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS**

The International Federation of Accountants' International Public Sector Accounting Standards Board (IPSASB) develops accounting standards for public sector entities referred to as International Public Sector Accounting Standards (IPSASs). The IPSASB recognizes the significant benefits of achieving consistent and comparable financial information across jurisdictions and it believes that the IPSASs will play a key role in enabling these benefits to be realized. The IPSASB strongly encourages governments and national standard-setters to engage in the development of its Standards by commenting on the proposals set out in Exposure Drafts.

The IPSASB issues IPSASs dealing with financial reporting under the cash basis of accounting and the accrual basis of accounting. The accrual basis IPSASs are based on the International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) where the requirements of those Standards are applicable to the public sector. They also deal with public sector specific financial reporting issues that are not dealt with in IFRSs.

The adoption of IPSASs by governments will improve both the quality and comparability of financial information reported by public sector entities around the world. The IPSASB recognizes the right of governments and national standard-setters to establish accounting standards and guidelines for financial reporting in their jurisdictions. The IPSASB encourages the adoption of IPSASs and the harmonization of national requirements with IPSASs. Financial statements should be described as complying with IPSASs only if they comply with all the requirements of each applicable IPSAS.

### **Due Process and Timetable**

An important part of the process of developing IPSASs is for the Committee to receive comments on the proposals set out in Exposure Drafts from governments, public sector entities, auditors, standard-setters and other parties with an interest in public sector financial reporting.

Accordingly, each proposed IPSAS is first released as an Exposure Draft, inviting interested parties to provide their comments. Exposure Drafts will usually have a comment period of four months, although longer periods may be used for certain Exposure Drafts. Upon the closure of the comment period, the IPSASB will consider the comments received on the Exposure Draft and may modify the proposed IPSAS in the light of the comments received before proceeding to issue a final Standard.

## **Background**

For many public sector entities a considerable proportion of their expenses relate to the provision of social benefits in non-exchange transactions. Key issues related to accounting for social benefits include the point at which liabilities should be recognized in relation to different programs and activities and the amount of such liabilities. These issues have not been addressed by International Public Sector Accounting Standards, and other international guidance does not address these issues from a public sector perspective.

This Exposure Draft has been developed following consideration of responses to an Invitation to Comment (ITC) that was developed by a Steering Committee appointed by the former Public Sector Committee (PSC). (At its November 2004 meeting, the IFAC Council approved a change in name of the Public Sector Committee to the International Public Sector Accounting Standards Board (IPSASB.)). The ITC was published by the PSC in January 2004 with a request for comments to be received by June 30, 2004.

## **Purpose of the Exposure Draft**

This Exposure Draft proposes requirements for the accounting treatment of a range of social policies of governments and public sector entities including those related to social security pensions.

## **Request for Comments**

Comments are invited on any proposals in this Exposure Draft by xx xx xx 2007. The IPSASB would prefer that respondents express a clear

overall opinion on whether the Exposure Draft in general is supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the issues in the Exposure Draft. Respondents are also invited to provide detailed comments on any other aspect of the Exposure Draft (including Implementation Guidance and the Basis for Conclusions) indicating the specific paragraph number or groups of paragraphs to which they relate. It would be helpful to the IPSASB if these comments clearly explained the issue and suggested alternative wording, with supporting reasoning, where this is appropriate.

## **Specific Matters for Comment**

The IPSASB would particularly value comment on whether you agree that:

1. Only obligations from social benefits provided by an entity in non-exchange transactions should be within the scope of the Standard rather than obligations arising from all non-exchange transactions (paragraph 2)? Please give your reasons.
2. Social security pensions and other social benefits giving rise to non-exchange transactions for which retirement age is an eligibility criterion should be included within the scope of this Standard (paragraph 4). If you think that social security pensions and other social benefits for which retirement age is an eligibility criterion should be dealt with in a separate Standard please give your reasons.
3. Contributory and non-contributory programs giving rise to non-exchange transactions should be within the scope of this Standard (paragraph 6). If you think that contributory and non-contributory programs giving rise to non-exchange transactions should be dealt with in a separate Standards please give your reasons.
4. The definition of social benefits at paragraph 11 is sufficiently clear and comprehensive? If you disagree can you explain how this definition should be modified.

5. The definitions of collective goods and services, individual goods and services and cash transfers at paragraph 11 are necessary and appropriate. If they are not necessary or appropriate can you explain how they should be modified?
6. A present obligation in respect of cash transfers arises when all eligibility criteria have been satisfied (paragraph.36) If you disagree please indicate at what point a present obligation in relation to cash transfers arises.
7. A present obligation to beneficiaries in respect of collective and individual goods and services does not arise (paragraph 40). If you disagree please indicate at what point does such a present obligation arise and to whom.
8. The amount of the liability in respect of present obligations for cash transfers is the amount that the entity has no reasonable alternative but to settle (paragraphs 47-48). This will normally be the amount of the next payment accrued to the reporting date unless governing legislation or regulations specify otherwise. If governing legislation or regulations specify otherwise the liability may be:
  - The full amount of the next payment following satisfaction of the eligibility criteria; or
  - A series of payments covering the current reporting period and one or more subsequent reporting periods.

If you do not think that this should be the requirement relating to the amount of the liability for cash transfers following the satisfaction of eligibility criteria what is the amount of the liability that you think should be recognized and please indicate your reasons?

9. The ED should not require the disclosure of the projected future cost of major cash transfer programs. If you think that the disclosure of the projected future cost of major cash transfer programs provides useful information please indicate the basis on which such a disclosure should be made

and whether such a disclosure should be encouraged or required?

10. There is no need for transitional provisions. If you think that there is a need for transitional provisions please indicate to which part of the Standard transitional provisions should apply and their duration.

# International Public Sector Accounting Standard ED XX

## Social Policy Obligations

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A. Amendments to other International Public Sector Accounting  
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International Public Sector Accounting Standard XX, “Accounting for the Social Policies of Government” (IPSAS XX) is set out in paragraphs 1-56. All the paragraphs have equal authority. IPSAS XX should be read in the context of its objective, the Basis for Conclusions and the “Preface to the International Public Sector Accounting Standards”. IPSAS 3, “Accounting Policies, Changes in Accounting Estimates and Errors” provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

## **Introduction**

IN1. The Standard prescribes the accounting and disclosure by public sector entities for social policy obligations giving rise to non-exchange transactions. For many public sector entities expenses and liabilities related to the provision of social benefits in non-exchange transactions have a very significant impact on financial performance and financial position.

IN2. The Standard deals with three categories of social benefits:

- (a) Collective goods and services
- (b) Individual goods and services
- (c) Cash transfers

IN3. The Standard does not deal with cash transfers that are provided as consideration in exchange for service rendered by employees, including where such cash transfers are provided through composite social security programs. The Standard also does not deal with:

- Goods and services provided in exchange transactions, including individual goods and services provided to individuals and households in exchange for consideration of approximately equal value; and
- Contracts with employees and third parties for the delivery of social benefits to individuals and households.

IN4. No present obligation arises in respect of the beneficiaries of collective goods and services and individual goods and services.

IN5. For cash transfers present obligations arise when all eligibility criteria have been satisfied, regardless of whether an entity has a legal obligation to transfer resources.

IN6. Where present obligations for cash transfers meet recognition criteria they are recognized as liabilities. The amount of the liability will normally be the amount of the next payment following satisfaction of eligibility criteria, accrued to the reporting date, unless governing legislation or regulations specify otherwise. In these cases, depending upon the specification in governing legislation or regulations, the liability

that the entity determines that it has no realistic alternative but to settle may be:

- The full amount of the next payment following satisfaction of the eligibility criteria; or
- A series of payments covering the current reporting period and one or more subsequent reporting periods.

IN7. Unless the possibility of any outflow in settlement is remote, an entity is required to disclose for cash transfers at the reporting date a brief description of the nature of contingent liabilities and, where practicable, an estimate of financial effect, indications of uncertainty and, where relevant, details of possible reimbursements. Contingent liabilities in respect of collective and individual goods and services do not arise.

IN8. The Standard becomes effective for annual financial statements beginning on or after XX XX 20xx.

# **INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARD IPSAS XX**

## **Accounting for Social Policy Obligations**

### **Objective**

1. Governments and public sector entities provide constituents with social benefits in the form of goods, services and cash transfers in the pursuit of social policy objectives. The objective of this Standard is to identify the circumstances in which such social policies provided in non-exchange transactions give rise to a liability.

### **Scope**

2. **An entity which prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in accounting for social benefits provided in non-exchange transactions.**
3. Social benefits are provided to members of the community in non-exchange transactions, often without any consideration. They include health and educational services and cash transfers such as unemployment benefit.
4. This Standard applies to social security pension benefits provided in non-exchange transactions, as well as to other cash transfers and goods and services provided by governments in non-exchange transactions to individuals where attainment of retirement age is an eligibility criterion. In some jurisdictions cash transfers to individuals who have reached retirement age and satisfied other eligibility criteria are made through composite social security programs. Composite social security programs may also operate as post-employment benefit plans. Cash transfers that are provided as consideration in exchange

for service rendered by employees are not within the scope of this Standard (see paragraph 7).

5. In some jurisdictions governments or public sector entities may provide individual goods and services such as health, housing and transport in exchange for consideration of approximately equal value - for example, when a hospital has a wing for patients who pay the full cost of medical services. Such transactions are exchange transactions and are outside the scope of this Standard.
6. It is also quite common for governments or public sector entities to provide individual goods and services in exchange for consideration that is not approximately equal in value to the benefits transferred by the government or public sector entity- for example, an individual may be required to contribute a nominal amount to the cost of an educational course or pay part of the cost of a consultation with a doctor. Such arrangements are within the scope of this Standard. Certain cash transfer programs may also require contributions on or behalf of individuals. Such programs are within the scope of this Standard provided that the amount of the contributions is not approximately equal to the economic benefits transferred by the government or public sector entity.
7. This Standard does not apply to employee benefits, including post-employment benefits provided to government employees and other employees in exchange for their services, Requirements in respect of employee benefits should be accounted for in accordance with the separate Standard dealing with employee benefits. This Standard does also not apply to exchange transactions for the provision of goods and services by third parties.

### **Government Business Enterprises**

8. This Standard applies to all public sector entities other than Government Business Enterprises (GBEs).
9. The Preface to International Public Sector Accounting Standards issued by the International Public Sector Accounting Standards Board (IPSASB) explains that GBEs apply International Financial Reporting

Standards, which are issued by the International Accounting Standards Board (IASB).

## Definitions

10. The following terms are used in this Standard with the meanings specified. These terms have been defined in other IPSASs:

A **constructive obligation** is an obligation that derives from an entity's actions where:

- (a) By an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and
- (b) As a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

A **contingent liability** is:

- (a) A possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
- (b) A present obligation that arises from past events but is not recognized because:
  - (i) It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or
  - (ii) The amount of the obligation cannot be measured with sufficient reliability.

An **exchange transaction** is a transaction in which one entity receives assets or services, or has liabilities extinguished, and

**directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.**

**Expenses paid through the tax system are amounts available for beneficiaries regardless of whether or not they pay taxes.**

**A legal obligation is an obligation that derives from:**

- a) A contract through its explicit or implicit terms;**
- b) Legislation; or**
- c) Other operation of law.**

**Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.**

**Non-exchange transactions are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange or gives value to another entity without directly receiving approximately equal value in exchange.**

**An obligating event is an event that creates a legal or constructive obligation that results in an entity having no realistic alternative to settling that obligation.**

- 11. The following terms are used in this Standard with the meaning specified:**

**A cash transfer is a non-exchange transaction, which is either settled in cash, or is an expense paid through the tax system, to protect individuals against certain social risks where use of the cash payment is at the discretion of the individual.**



**Collective goods and services** are goods and services provided for consumption by the entire population or by a particular segment of the population in any jurisdiction in order to protect the population or segment of the population against certain social risks.

An **eligibility criterion** is a requirement that must be met for entitlement to individual goods and services and cash transfers.

**Individual goods and services** are goods and services provided for individual consumption to protect an individual or individual household against certain social risks.

**Retirement age** is an age at which an individual will become eligible for social security pensions, subject to the satisfaction of other eligibility criteria.

**Social benefits** are cash transfers and individual and collective goods and services provided in a non exchange transaction to protect the entire population, or individuals or individual households against certain social risks.

A **social security pension** is a cash transfer payable only to that segment of the population that has reached retirement age

A **social risk** is an event or circumstance that may adversely affect the welfare of households either by imposing additional demands on their resources or by reducing their incomes.

Terms defined in other International Public Sector Accounting Standards are used in this Standard with the same meaning as in those other Standards and are reproduced in the Glossary of Defined Terms published separately.

## **Goods and Services Encompassed by Social Benefits**

12. Government social policies are developed to address and respond to certain social risks. In pursuit of these social policies,

governments and public sector entities provide goods and services to their citizens without receiving approximately equal consideration in exchange. Such transactions are non-exchange transactions. Goods and services may be provided for collective consumption or for consumption by individuals or individual households. Government and public sector entities also provide social benefits in the form of cash transfers. These goods and services and cash transfers are generally termed social benefits.

### **Collective Good and Services**

13. Collective goods and services are made accessible simultaneously to all members of the community or to all members of a particular section of the community, such as all households living in a particular region. Such goods and services differ from individual goods and services and cash transfers in that they are automatically available and consumed by all members of the community, or group of households in the community or section of the community. By their nature, collective services cannot normally be sold to individuals in the market place. Goods and services provided for collective consumption vary in different jurisdictions. Examples include:

- (a) National defense;
- (b) The conduct of international relations;
- (c) Public order and safety (including police services, fire protection services, law courts and prisons);
- (d) The efficient operation of the social and economic system of a country; and
- (e) The formulation and administration of government policy, setting and enforcement of standards, regulation and licensing of personnel and institutions, and applied research and experimental development.

### **Individual Goods and Services**

14. Governments and public sector entities provide a range of goods and services for individual consumption. Such goods and services are provided to an individual or individual household and are used to satisfy the needs and wants of that individual or members of that household. Unlike collective goods and services, individual goods and services can be bought and sold in the market place. However, in many cases, there is no requirement for the beneficiaries of these goods and services to pay an amount equivalent to the fair value of the services provided. Goods and services provided for individual consumption vary in different jurisdictions. Examples include:

- (a) Health services,
- (b) Educational services,
- (c) Housing services,
- (d) Transport services; and
- (e) Social services to the community.

15. The provision of individual goods and services is often intended to contribute to the collective welfare by, for example, creating a workforce that is better educated or technically competent in certain areas, or a population that is in better health. However, individual goods and services are provided in the first instance for consumption by individuals or individual households. Unlike collective goods and services, individual goods and services are subject to the satisfaction of eligibility criteria. Such eligibility criteria can differ widely between types of benefits in their number and complexity.

16. Some eligibility criteria may need to be revalidated at regular intervals -for example, where the provision of medical services is only available to those with incomes below a specified level. Individual goods and services can be provided in a number of ways. For example methods

to provide free or subsidized health and educational goods and services to individuals include:

- a) The direct provision of the goods and services. Governments and public sector entities may deliver services directly, for example, in government controlled schools or hospitals with government employed teachers and medical staff.
- b) Paying another organization to deliver goods and services to individuals. For example, a government may pay a private hospital a set fee per service, such as for performing an operation on an individual. Normally such arrangements will require the hospital to meet certain criteria specified by the government. Governments may also pay private sector providers of educational services a subsidy for each student. Frequently upper limits are set on the amount that the government will pay under such arrangements.
- c) The reimbursement of households and individuals for certain types of expenditure. Rather than providing free or subsidized goods or services at the point of purchase or consumption, a government may require individuals to purchase the goods and services and then apply for reimbursement. For example, individuals attending a doctor's surgery may be required to pay a standard fee, which a government will reimburse in full for certain individuals or a government may reimburse individuals with disabilities for the cost of certain home services when proof of receipt of those services is provided; and
- d) Providing individuals with vouchers that can be redeemed for goods and services. For example, some jurisdictions provide individuals with vouchers that entitle them to free education at one of a selected number of schools. The school then redeems the voucher with the government.

17. There may be certain instances where a service may be provided on both a collective and an individual basis. For example policing and criminal justice services may be both collective and individual goods and services. Members of the community are subject to the protection of the police as a component of the broader criminal

justice system and normally do not have to satisfy eligibility criteria in order to consume such services. However, there are occasions when an individual does have to satisfy eligibility criteria in order to benefit from policing and criminal justice services. For example, an individual in a witness protection scheme may have to meet eligibility criteria.

18. Individual goods and services can be distinguished from cash transfers because the resources transferred are intended to be used for the service potential embodied in the goods and services specified by the transferor. They therefore differ from cash transfers to individuals where the individual has a wider discretion over the purposes for which the economic benefits may be used (see below paragraphs 19-21). It may, of course, be possible for a recipient of goods to sell the goods rather than use them for the purposes intended by the transferor. Such a course of action, however, requires a positive further action by the recipient beyond receipt of the economic benefits transferred. Where the resources embodied in individual goods and services involve the transfer of cash as at paragraph 16(c) this is a specific reimbursement.

### **Cash Transfers**

19. In many instances governments and public sector entities will provide social benefits in the form of cash transfers to address social risks facing individuals and/or their households. Such benefits include:

- a) Social security pensions
- b) Child benefits;
- c) Invalidity and sickness benefits;
- d) Unemployment benefits;
- e) Income supplements; and
- f) Housing benefits (where paid to the applicant rather than directly to the landlord).

20. As noted at paragraph 18 the characteristic distinguishing cash transfers from individual goods and services is that the purposes for which the cash transferred may be used are completely at the discretion of the recipient. If a recipient has to validate that the cash has been used for a purpose specified by the transferor the transaction is a reimbursement rather than a cash transfer and is within the definition of an individual good or service.

21. On occasions cash transfers will be made to beneficiaries as reductions in the amount of income tax that they have to pay rather than as a direct cash payment. In such cases, for administrative efficiency, the taxation system is used to process a transfer, which would otherwise be made directly in cash. Such reductions in taxation are expenses paid through the tax system and are within the definition of cash transfers in this Standard. ED 29, “Revenue from Non-Exchange Transactions (Including Taxes and Transfers)” provides additional commentary on tax expenses and tax expenditures. Tax expenditures are preferential provisions of the tax law that provide certain concessions to tax payers that are not available to others.

22. There may be instances where a particular program or arrangement providing social benefits includes both cash transfers and individual goods and services. An example is a housing support program where rental allowances for the tenants of private landlords are paid to recipients in cash, whereas rental allowances to recipients who are tenants of public housing authorities are paid directly to the social housing authority. In such cases resource outflows under the program may be differentiated between cash transfers and individual goods and services.

### **Social Security Pensions and other Social Benefits where Retirement Age is an Eligibility Criterion**

23. Social security pensions operate to provide cash transfers to individuals who have attained a retirement age laid down in governing legislation or regulations, as well as satisfying other eligibility criteria. The retirement age is normally the age at which an individual is no longer expected to be active in the full-time work-force and becomes eligible for the social security pension. As well as an eligibility criterion for the social security pension the retirement age may also be the age at

which an individual ceases to be eligible for certain other state benefits—for example unemployment benefit. The age varies between jurisdictions and may vary within jurisdictions. For example, in some jurisdictions an individual may work beyond retirement age and not be entitled to the retirement pension. Programs for social security pensions vary across jurisdictions and often contain highly detailed and complex provisions. There are two types of social security pensions within the definition of social security pensions in this Standard:

- Basic/welfare pensions; and
- General/contributory pensions

24. Basic/welfare pensions do not require contributions from, or on behalf of, beneficiaries. In some cases basic/welfare pensions operate as “safety nets” for individuals, who have not met the eligibility criteria for the general/contributory pension or whose contribution record is insufficient to provide more than a low level of benefits under the general/contributory pension.

25. General/contributory pensions require contributions by, or on behalf, of an individual during their working lives or other periods specified in governing legislation or regulations. Benefits may be:

- Related to the amount of those contributions but not approximately equal to the value of those contributions: and/or
- Linked to a minimum period over which contributions must be made in order for an individual to be eligible.

26. General/contributory pensions may be administered as stand-alone programs or together with basic/welfare pensions. In some cases general/contributory pensions and basic/welfare pensions may be administered in composite social security programs that also operate as multi-employer plans for delivering post-employment benefits. In such cases, it will be necessary to distinguish benefits provided as consideration for employment services rendered and benefits which are not consideration for employment services rendered. In accordance with paragraphs 5 and 7 only the latter are addressed in this Standard.

27. Many jurisdictions also provide citizens with other cash transfers and individual goods and services once they have reached retirement age. The requirements in this Standard apply to all social benefits for which attainment of retirement age is an eligibility criterion.

### **Obligating Events and Present Obligations**

28. The existence of a present obligation as a result of a past event is the threshold condition for recognition of a liability. For an event to be an obligating event, it is necessary that the entity has no realistic alternative other than to settle the obligation created by the event. An obligating event may give rise to a legal or constructive obligation.

29. An obligation always involves another party to whom the obligation is owed. In many commercial contracts both parties will know to whom the obligation is owed. However, specific identification of the other party is not necessary for the establishment of an obligation. The obligation arising from a governmental social policy may be to a large number of citizens.

### **Legal Obligations and Constructive Obligations**

30. A legal obligation exists when a party has a legal or otherwise enforceable right to obtain judgment through a court of competent jurisdiction to enforce payment, performance or compensation. A determination of whether a particular transaction or event would give rise to a legal obligation must ultimately be made by a court or other quasi-judicial mechanism. A legal obligation exists when it is clear from legislation or previous examples of legal action that, if the issue were taken to court, the issue would be decided in the applicant's favor. This may be the case for a number of cash transfers where the particular circumstances of an applicant's eligibility may not have been tested in court, but the experience of similar previous cases may suggest that an obligating event has occurred.

31. Legal obligations often arise as a result of contractual obligations. A contract is an agreement with specific terms between two or more persons or entities in which one agrees to provide goods or services or to take certain actions in return for valuable consideration, including where the consideration provided by one party is not of



approximately equal value to the value of the benefits conferred by the other party to the contract. In some cases, the consideration may be nominal in relation to the benefits conferred (for example, a small monetary consideration may be provided merely to give the transaction the form of a contract).

32. In some jurisdictions, a government's perceived commitment to deliver social benefits to constituents may be referred to as a "social contract". The use of the term "social contract" does not establish a legally enforceable agreement with specific terms as in paragraph 30.

33. Future obligations can be distinguished from present obligations. A government's implicit or explicit agreement to provide social benefits in future periods does not constitute a legal contract and does not give rise to a present obligation.

34. Present obligations may also arise when legal obligations do not exist. Such obligations are constructive obligations. Constructive obligations are broader than legal obligations. Constructive obligations encompass obligations that a government has a duty to honor because it has led individuals or entities to believe that it will settle such obligations and has no realistic alternative but to do so. In the context of this Standard a constructive obligation arises where an individual has satisfied all eligibility criteria for a cash transfer, even though the date at which the transfer must be made under legislation or regulations governing the program has not yet occurred (see paragraphs 36-39).

35. An obligation always involves a commitment to another party. Therefore it follows that a decision by a government or public sector entity's management, governing body or controlling entity does not give rise to a constructive obligation at the reporting date unless the decision has been communicated before the reporting date to those affected by it in a manner sufficiently specific to raise a valid expectation in them that the entity will discharge its responsibilities and the entity has no realistic alternative but to do so. General political commitments or statements of policy intention do not give rise to present obligations, because these statements are not sufficiently specific to give rise to constructive obligations.

## **Present Obligations**

### **Cash Transfers**

**36. A present obligation for social benefits which are cash transfers arises when all eligibility criteria have been satisfied.**

37. Under the requirements of this Standard a present obligation for a cash transfer arises when all eligibility criteria have been satisfied, even though the date at which the payment must be legally made may be after the satisfaction of those eligibility criteria. Some programs may require the satisfaction of a large number of criteria and those criteria may not all have to be satisfied at the same time. An example is a child benefit program, where the child must have reached a specified age but further eligibility criteria related to the child's parents income and/or asset holdings must be satisfied before a payment of benefit is triggered. In such cases a present obligation does not arise until all eligibility criteria have been satisfied.

38. Some programs may include termination benefits. These are one-off payments for which a present obligation arises when an individual who has previously satisfied eligibility criteria ceases to satisfy those eligibility criteria. For example a child benefit program providing economic benefits for the parents of children under the age of 16 years may have a provision whereby the parents of a child receive a final lump sum on the child's sixteenth birthday. Under such circumstances the present obligation arises when the eligibility criteria cease to be satisfied and the individual(s) becomes eligible for the lump sum.

39. This Standard reflects the view that an entity has no realistic alternative but to settle its obligations arising from the satisfaction of eligibility criteria. Whilst governments and other public sector entities can modify eligibility criteria, it is unlikely that such changes will be retrospective. The assessment of when a present obligation arises is made in the context of the current legal framework governing a program or activity. Paragraphs 47-48 of this Standard provide requirements and commentary on the liability that arises from this present obligation.

## **Collective and Individual Goods and Services**

40. Under the requirements of this Standard a present obligation for collective and individual goods and services does not arise to beneficiaries of those goods and services. An entity may have contracts with third parties for the supply of goods and services needed to provide collective and individual goods and services on an ongoing basis, including into future reporting periods. Collective goods and services may also be provided directly by public sector entities using their own employees. The fact that the reporting entity has entered into contracts with third parties for the supply of goods and services or employment contracts with employees involved in the provision of collective and individual goods and services for future periods does not create a present obligation in relation to beneficiaries of those goods and services.

41. Where an individual purchases goods and services and seeks reimbursement from a public sector entity a present obligation may arise at the point at which the goods and services are provided to the individual. This is the case if it can be demonstrated that the individual had a prior authorization to purchase the goods and services and had met all eligibility criteria and the entity providing the reimbursement has sufficient information to measure the amount outstanding reliably. In such circumstances the individual is, in substance, acting as an agent of the public sector entity and is incurring expenditure on behalf of that entity.

## **Initial Recognition**

**42. Where a present obligation has arisen for social benefits which are cash transfers a liability shall be recognized when:**

- **It is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; and**
- **A reliable estimate can be made of the amount of the obligation.**

*Probable Outflow of Resources Embodying Economic Benefits or Service Potential*

43. For a liability arising from a present obligation to be recognized an outflow of resources embodying economic benefits or service potential must be probable. There may be rare instances where a present obligation arises from a constructive or legal obligation, but it is deemed that an outflow of economic benefits and service potential is not probable. In such cases an entity discloses a contingent liability, unless the possibility of an outflow of resources embodying economic benefits or service potential is remote.

*Reliable Estimates*

44. There may be cases where, although a liability exists, no reliable estimate can be made of the amount. In the context of the requirements of this Standard in relation to social benefits such instances are likely to be extremely rare. Where no reliable estimate can be made a liability exists that cannot be recognized. That liability is disclosed as a contingent liability (see paragraphs 50-52).

## **Contingent Liabilities**

45. **An entity shall not recognize a contingent liability in respect of social benefits.**

46. Contingent liabilities are not recognized because they do not satisfy either the definition of, or recognition criteria for, a liability. IPSAS 19, “Provisions, Contingent Liabilities and Contingent Assets” provides further guidance on contingent liabilities and their relationship to provisions.

## **Measurement –Cash Transfers**

47. **The amount recognized as a liability for cash transfers shall be the amount of the next payment following satisfaction of eligibility criteria, accrued to the reporting date, unless governing legislation or regulations specify otherwise.**

48. Under the requirements of this Standard liabilities arise for cash transfer programs when all eligibility criteria have been satisfied by beneficiaries. The amount that the entity has no realistic alternative but to settle is normally the accrued amount of the next payment which relates to the reporting period, following satisfaction of the eligibility criteria. However, there may be circumstances where governing legislation or regulations explicitly specify otherwise. In these cases, depending upon the specification in governing legislation or regulations, the liability that the entity determines that it has no realistic alternative but to settle may be:

- The full amount of the next payment following satisfaction of the eligibility criteria; or
- A series of payments covering the current reporting period and one or more subsequent reporting periods.

When a liability is recognized an expense is also recognized for the amount of that liability. The liability is extinguished when the cash transfer is made. If the liability has not been extinguished at the reporting date it is reflected in the statement of financial position.

**Example Illustrating Application of Paragraph 48. (This example is not authoritative)**

An entity has a reporting date of December 31 20x6. A beneficiary for a cash transfer program satisfies all eligibility criteria at December 1 2006. The subsequent payment is 600 currency units (CU) covering the period December 1 20x6- May 31 20x7. In most cases the entity recognizes an expense for 100CUs and, if the payment was not made before the reporting date, a liability for 100CUs. If the payment of 600CUs was made before the reporting date the entity recognizes an expense of 100 CUs and a prepayment of 500CUs.

Only where governing legislation or regulations specify, the entity may determine that the amount that it has no realistic alternative but to settle is more than 100 CUs. If, in accordance with governing legislation or regulations, the entity determines that, following the satisfaction of all eligibility criteria, it cannot realistically avoid settling the full amount of the next payment it recognizes an expense of 600 CUs and an equivalent liability. The liability is extinguished when the cash payment is made.

There may be rare circumstances where an entity concludes that, in accordance with governing legislation and regulations, following the satisfaction of all eligibility criteria, it cannot realistically avoid settling the amount of a series of payments covering one or more reporting periods. In such a case it will recognize a liability of 600CUs x the number of payments that it determines that it cannot realistically avoid settling.

## Presentation and Disclosures

### Line Items

49. This Standard does not require a separate line item for liabilities for social benefits as cash transfers and does not require separate line items for expenses related to social benefits. However, IPSAS 1, “Presentation of Financial Statements” requires additional line items to be presented on the face of the statement of financial position and the statement of financial performance or in notes to the financial statements when such presentation is necessary to present fairly the entity’s financial position and financial performance.

### Contingent Liabilities

50. **Unless the possibility of any outflow in settlement is remote, an entity should disclose for social benefits at the reporting date a brief description of the nature of the contingent liabilities and, where practicable:**

- (a) An estimate of the aggregate financial effect of those contingent liabilities, measured under paragraphs 47-48;**
- (b) An indication of the major uncertainties relating to the amount or timing of any outflow; and**
- (c) The possibility of any reimbursement.**

51. This Standard requires entities to disclose a brief description of how those contingent liabilities relating to social benefits have arisen, an estimate of the aggregate financial effect and details of the timing of any outflow and the likelihood of any reimbursement.

52. For cash transfers a contingent liability will be disclosed where a large number of individuals have applied for a program, such as income support, but, due to ambiguity over interpretation of the rules governing the program, there is uncertainty over whether one or more of the eligibility criteria have been met. If the eligibility criterion/criteria in

question had/have been met the individuals would have been entitled to receive a payment.

53. This may have led to a legal action that should result in a clarification of the nature and extent of any liability. If the results of this legal action will not be known until after the reporting date then a contingent liability will be disclosed unless the possibility of a judgment inimical to the entity is remote. Such a disclosure includes, where feasible, an estimate of the financial implications in the event of the court deciding that the key eligibility criterion/criteria has/have been satisfied

54. Present obligations to beneficiaries in respect of collective and individual goods and services do not arise before the goods and services are delivered. Therefore an entity does not disclose the existence of a contingent liability in respect of obligations to beneficiaries for collective and individual goods and services provided in non-exchange transactions.

## Effective Date

**55. This International Public Sector Accounting Standard becomes effective for annual financial statements covering periods beginning on or after XX XX 200X. Earlier application is encouraged.**

56. When an entity adopts the accrual basis of accounting as defined by International Public Sector Accounting Standards for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.



## Appendix A

### Amendments to Other IPSASs

In IPSAS 1, “Presentation of Financial Statements” (version approved by the IPSASB in 2006) the following wording is deleted from paragraph 88(k).

88(k) payables under exchange transactions

In IPSAS 19, “Provisions, Contingent Liabilities and Contingent Assets” the following paragraph is deleted:

99. Where an entity elects to recognize in its financial statements provisions for social benefits for which it does not receive consideration that is approximately equal to the value of the goods and services provided, directly in return from the recipients of those benefits, it should make the disclosures required in paragraphs 97 and 98 in respect of those provisions.

## Implementation Guidance

### **Accounting for Social Policies of Government — Examples**

*This guidance accompanies, but is not part of, proposed IPSAS XX. In all the examples there is a reporting date of 31 December.*

### **Example 1: Collective Goods and Services: General Commitments**

- IG1 A government operates a national police service. The government has publicly stated its intention to increase uniformed police officers from current levels over the next two years in a series of policy pronouncements.

#### *Analysis*

#### **Present obligation as a result of a past obligating event —**

- IG2 There is no present obligation to provide policing services to the community in future periods, regardless of whether statements have been made of intentions to increase police numbers, reduce them or maintain them at current levels.
- IG3. Notwithstanding the fact that, under the requirements of this Standard present obligations to the beneficiaries of collective goods and services do not arise, general policy statements of intent still leave the government with a realistic alternative to settling any obligation created by the announcement. Therefore such general statements of intent are not obligating events.

### **Example 2: Individual Goods and Services: Free Health Care-Universal to Residents**

- IG4. Under legislation, a government is required to provide free health care services to all citizens who satisfy residential eligibility criteria. Health care is provided by a combination of government operated hospitals and clinics and healthcare institutions operated by both for-profit and not-for-profit entities.

### *Analysis*

- IG5. **Present obligation as a result of a past obligating event —**  
There is no present obligation to provide healthcare services in future periods to beneficiaries.

### **Example 3: Individual Goods and Services: Free Health Care to Low Income Individuals**

- IG6. Under healthcare legislation a government provides specified healthcare services free to both adults and children under 18 years of age of families where the individual income is less than 300 currency units. Individuals wishing to obtain free healthcare services have to apply to the government's Department of Health providing evidence that their monthly income is less than 300 currency units. When their applications have been validated they are eligible for free healthcare services for a 6 month period, after which time their eligibility has to be revalidated. The government arranges for the healthcare services to be provided through clinics and hospitals operated by non-for-profit foundations.

### *Analysis*

- IG7. **Present obligation as a result of a past obligating event—**  
There is no present obligation for the delivery of the healthcare, even where programs have detailed eligibility criteria and individuals may have confirmed their eligibility into future reporting periods.

### **Example 4: Individual Goods and Services: Legal Aid**

- IG8. A government provides legal aid to individuals whose income in the previous financial year was below a specified annual amount. Legal aid is provided by law firms with which the government has long-term contracts rather than the government's own employees. The government's legal aid program is highly detailed and well-documented and legal aid has been consistently provided in conformity with it for over 20 years. All individuals charged with an indictable criminal

offence are advised of their right to request legal aid. At the reporting date 1,500 individuals had had applications for legal aid approved. Estimates of the cost of legal representation are based on a standard costing model that stratifies offences according to the nature of the offence and likely duration of the trial. Past experience has suggested that the estimates provided by this model are robust. The estimated cost of providing legal services for the 1,500 cases is 5 million currency units.

### *Analysis*

- IG9. **Present obligation as a result of a past obligating event** —A present obligation does not arise to the beneficiaries of legal aid. The existence of contracts with external parties (in this case law firms) conveying rights and obligations into future reporting periods does not give rise to a present obligation to the beneficiaries of legal services.

### **Example 5a: Cash Transfer: Child Benefits (amount accrued to the reporting date)**

- IG10. Government A has legislation that specifies the eligibility criteria for child benefits. The parents of each eligible child receive 400 currency units every two months from Government A. The eligibility criteria are:
- The child is a resident of the country; and
  - The child is aged 16 years or under.
- IG11. Entitlement commences when an application has been received and approved. No payments are made for periods prior to the date on which eligibility has been confirmed. Payments are made at the beginning of each month.
- IG12. At year-end (31 December), 6,000 children have satisfied eligibility criteria, as a result of which their parents are in receipt of benefits. The payment due on 1 December has not yet been made. A further 4,000 babies have met the eligibility criteria and had applications approved but have not yet received the first

instalment of benefit. The average amount owed is one month's entitlement, in addition to the payment due on 1 December.

- IG13. Therefore, at the reporting date, 10,000 children in total (including the 4,000 babies newly eligible) have validated their eligibility for entitlement to child benefits for the next 12 month period. It is expected that 1,000 babies will be born in the year following the reporting date.

### *Analysis*

- IG14. **Present obligation as a result of a past obligating event** — A present obligation arises when children have satisfied all eligibility criteria. There is no present obligation in respect of the babies not yet born.
- IG15. **An outflow of resources embodying economic benefits or service potential in settlement** — Probable in respect of the 10,000 children whose eligibility has been confirmed.
- IG16. **Recognition**—A liability is recognized in respect of the present obligations for the amounts outstanding for 4,000 babies who have recently satisfied eligibility criteria and the amount of the next payment for all 10,000 children, accrued to the reporting date.
- IG17. **Measurement**—At year-end, the government recognizes a liability of 800,000 currency units for the amounts outstanding for the 4,000 babies who had applications approved but have outstanding payments under the program (4,000 x 200) and 2,000,000 currency units for the amount of the 1 December payment in respect of all 10,000 eligible children (10,000 x 200), which relates to the reporting period and had not yet been made at the reporting date..

### **Example 5b: Cash Transfer: Child Benefits (full amount of next payment)**

- IG18. Government B operates under legislation that specifies the eligibility criteria for child benefits. The parents of each eligible child receives 200 currency units every three months from the

government if their children meet eligibility criteria at a specified date—in this case 31 December. There is no backdating of entitlement (ie a child born between dates at which eligibility criteria have to be satisfied is not eligible until the next date for satisfaction of eligibility criteria) Governing legislation and regulations state explicitly that the parents are entitled to the full amount of the next payment, regardless of whether the child continues to satisfy eligibility criteria until the next validation date. The eligibility criteria are that:

- The child is a resident of the country; and
- The child is aged 16 years or under.

- IG19. At year end, 15,000 children had satisfied the eligibility criteria. Payment is due on 15 January of the next reporting period. Of these 1,000 had not received the payment due on 15 October as a result of satisfying eligibility criteria on 30 September. A further 1,100 babies are expected to be born in the financial year following the reporting period.
- IG20. **Present obligation as a result of a past obligating event** — A present obligation arises when children have satisfied all the eligibility criteria. Therefore, at reporting date, there is a present obligation for the 15,000 children who have confirmed their eligibility. There is no present obligation in respect of the 1,100 babies expected to be born in the year following the reporting date.
- IG21. **An outflow of resources embodying economic benefits or service potential in settlement** — Probable in respect of the 15,000 children who have confirmed eligibility.
- IG22. **Recognition**— A liability is recognized in respect of all 15,000 children who have satisfied eligibility at the reporting date.
- IG23. **Measurement**—. At year end, the government recognizes an expense and liability of 3,000,000 currency units for the next instalment of benefit in respect of all 15,000 children who had satisfied eligibility. (15,000 x 200). An expense and liability is

also recognized for a further 200,000 currency units in respect of the 1,000 children who had not received the payment due on 15 October as a result of satisfying eligibility criteria on 30 September (1,000 x 200).

**Example 5c: Cash Transfer: Child Benefits (Termination Benefit when Beneficiary Ceases to Satisfy Eligibility Criteria)**

- IG24. Government C operates under legislation that specifies the eligibility criteria for child benefits. Entitlement ceases when a child has reached 17 years of age. On reaching 17 years of age there is an entitlement to a termination benefit of 500 CUs. At the reporting date 100 children had reached the age of 17 years but had not yet received the termination payment. A further 200 children currently entitled to child benefit will reach the age of 17 years in the first quarter of the next reporting period.
- IG25. **Present obligation as a result of a past obligating event** — A present obligation arises when children have satisfied the eligibility criterion for the termination benefit. Therefore, at reporting date, there is a present obligation for the 100 children who have reached the age of 17 years and for whom payment is outstanding. There is no present obligation in respect of the 200 children currently entitled to child benefit who will reach the age of 17 years in the first quarter of the next reporting period.
- IG26. **An outflow of resources embodying economic benefits or service potential in settlement** — Probable in respect of the 100 children who have reached the age of 17 years at the reporting date.
- IG27. **Recognition**—A liability is recognized in respect of the 100 children who have satisfied eligibility at the reporting date.
- IG28. **Measurement**—At year end, the government recognizes an expense and liability of 50,000 currency units (500 x 100)

### **Example 6: Cash Transfer: Unemployment Benefits**

IG29. A government agency provides support through unemployment benefits to people who are unable to find paid employment. To receive an unemployment benefit, a claimant has to demonstrate that he or she meets the entitlement criteria when making a claim.

IG30. Unemployment benefit will be paid if the claimant is:

- aged over 18, but under retirement age for a basic/welfare social security pension;
- available for work; and
- actively seeking work — the government agency has the discretion to terminate the benefit if an individual rejects more than 3 offers of work. This discretion has been rarely exercised in the past.

IG31. Unemployment benefit is paid to eligible claimants at a two-weekly interval. Individuals have to re-satisfy eligibility for the benefit at the beginning of each month by registering at one of the agency's offices. Payment is then made on the 15<sup>th</sup> of the month and the last day of the month.

IG32. The benefit is 400 currency units per four weeks. The final payment in the reporting period occurs on 31 December. The benefit is payable from date of approval of an application. As at reporting date, there are 100 individuals whose applications have been approved but whose payments have been delayed because they were not entered into the payment system in time for the December 31 payment. These individuals are owed, on average, one week's benefit.

#### *Analysis*

IG33. **Present obligation as a result of a past obligating event** — A present obligation exists only to those individuals who have satisfied all eligibility criteria required to qualify for an unemployment benefit.



- IG34. **An outflow of resources embodying economic benefits or service potential in settlement** — Probable.
- IG35. **Recognition** — 400 currency units are expensed every four weeks for each claimant satisfying eligibility criteria at the beginning of the month and a further amount for those satisfying eligibility criteria for the first time during the month. The government records a liability at year-end for any payments for which individuals have confirmed eligibility but which are outstanding at the reporting date and relate to the period up until the reporting date. There is no liability for those who satisfied eligibility criteria at the beginning of the month because the payment subsequent to satisfaction of the eligibility criteria has been made in the reporting period and the next satisfaction of eligibility criteria is in the next reporting period. There is a liability for those who satisfied the eligibility criteria for the first time during the month and whose payments are outstanding.
- IG36. **Measurement** — At year-end, the government recognizes a liability of 10,000 currency units for those individuals who satisfied eligibility criteria during the month and whose payments had not been processed at December 31 (100 × 100 currency units).

### **Example 7: Cash Transfer: Social Security Pensions**

- IG37. Government F provides benefits under a basic/welfare type social security program to individuals who have reached retirement age of 65 years and also meet eligibility criteria that:
- Individuals have been residents for a continuous period of three years before reaching retirement age; and
  - Individuals have annual incomes no greater than 10,000 currency units per annum.
- IG38. Eligibility criteria have to be satisfied every three months and the last date for satisfaction of eligibility criteria is on 31 December. The next payment is made on 15 January and is for 1,000 currency units. Governing legislation states that the full amount of the next payment will

be made regardless of whether eligibility criteria cease to be satisfied at any point up to the next satisfaction of eligibility criteria. At 31 December 90,000 individuals have satisfied the eligibility criteria.

### *Analysis*

- IG39. **Present obligation as a result of a past obligating event** — A present obligation exists in respect of the 90,000 individuals who satisfied eligibility criteria on 31 December.
- IG40. **An outflow of resources embodying economic benefits or service potential in settlement** — Probable.
- IG41. **Recognition** — An expense and liability are recognized in respect of all 90,000 individuals who have been met eligibility criteria.
- IG42. **Measurement** — At year-end, the Government H recognizes an expense and liability of 90,000,000 currency units (90,000 × 1,000 currency units).

### **Example 8: Cash Transfer (Payment to Family of Individual Called Up for Military Service)**

IG43. The legislature of Country H has enacted legislation that allows Government H to conscript able bodied men and women between the ages of 18 and 45 years into the armed forces. At the same time a program was enacted providing cash payments of 5,000 currency units to the families of individuals conscripted for military service. The payment is made over a two year period in ten instalments of 500 currency units. Governing legislation states that the full amount of the payment of 5,000 currency units will be made regardless of the length of an individual's service with the armed forces. At 31 December 10,000 individuals had been conscripted, but payments had not been made to their families.

### *Analysis*

- IG44. **Present obligation as a result of a past obligating event** — A present obligation exists to the families of the 10,000 individuals who have been conscripted.
- IG45. **An outflow of resources embodying economic benefits or service potential in settlement** — Probable.
- IG46. **Recognition** — An expense and liability are recognized in respect of all 10,000 individuals who have been conscripted.
- IG47. **Measurement** — At year-end, Government H recognizes an expense and liability of 50,000,000 currency units (10,000 × 5,000 currency units).

### **Example 9: Disaster Relief – Provision of Collective and Individual Goods and Services**

- IG48. On December 10 200X, a massive earthquake struck Country A. On December 14, 200X the national government of Country X made a public commitment to participate in a multi-national relief initiative and pledged to provide policing services, by sending 100 officers for a 2 month period, and to also provide specified medical supplies. This commitment was communicated to a major supra-national organization and a number of national governments, which have also agreed to assist in the relief effort. Government X made a similar commitment following a disaster in Country B, a neighbour of Country A, two years earlier and honored that commitment. A separate contingency fund exists for such purposes and no further budgetary authorisation is required to allow the government to access these funds. The total cost of the policing component of the commitment, including transportation, is estimated to be 10 million currency units and the cost of the medical supplies is estimated to be 5 million currency units. At the reporting date of 31 December only 3 million currency units had been spent.

### *Analysis*

- IG49. **Present obligation as a result of a past obligating event** — Regardless of the public commitment, and its communication to very significant multi-national partner organizations and the previous honouring of similar commitments there is no obligating event giving rise to a present obligation to either the international partners or to the citizens of Country A. The government is likely to have a present obligation to external suppliers if it has taken delivery of medical supplies but not yet transferred them to Country A. This Standard does not deal with such transactions.

## **Basis for Conclusions**

*This Basis for Conclusions accompanies, but is not part of, the proposed IPSAS XX."*

### **Introduction**

BC1. This Basis for Conclusions summarizes the International Public Sector Accounting Standards Board's (IPSASB) considerations in reaching the conclusions in ED XX, "Accounting for Social Policy Obligations". Individual members of the IPSASB gave greater weight to some factors than to others. In forming their views the IPSASB members considered in depth the views expressed by the Steering Committee on Social Policy Obligations in the Invitation to Comment (ITC), "Accounting for the Social Policies of Governments", issued in January 2004 and to the views of constituents who responded to the consultation on that ITC.

BC2. The social benefits addressed in this proposed Standard, which include social security pensions, can have a major influence on the financial position and financial performance of governments and public sector entities. For entities in jurisdictions currently reporting on the full accrual basis the most common practice in respect of accounting for the social benefits provided by government is for resources used in the provision of those benefits to be expensed as goods and services are delivered. Most jurisdictions currently recognize as liabilities only those social benefits that are provided by cash transfer and that are legally due for payment. A minority of jurisdictions may also recognize the portion of periodic cash transfers that has accrued since the previous payment. The IPSASB therefore considers that it is essential to develop well understood, generally agreed methods of accounting for social policy obligations, supported by sound conceptual arguments.

BC3. The IASB's ED, "Proposed Amendments to IAS 37, Provisions Contingent Liabilities and Contingent Assets" and other IASB projects may deal with matters that are relevant for this proposed Standard. However, the IPSASB does not consider it appropriate to pre-empt the outcome of the IASB's due process, and, given the significance of accounting for the social policy obligations of governments and public

sector entities, does not consider that it would be appropriate to defer issuance of this proposed Standard.

### **Conceptual Underpinnings**

BC4. Social benefits were scoped out of IPSAS 19 to allow further consideration to be given to the topic. Subsequently the PSC established a Steering Committee comprising both PSC members and individuals from outside the Committee. The IPSASB accepted the Steering Committee recommendation that the conceptual approach and definitions in IPSAS 19 could be applied in determining when obligations arise from social policies in a non-exchange context. The IPSASB also noted that this approach had received strong support from respondents to the ITC.

### **Scope**

BC5. The Steering Committee and the majority of respondents to the ITC were of the view that a proposed Standard should be developed to deal with all social benefits including social security pensions and other benefits to citizens who have reached a specified retirement age. The IPSASB considered this issue at length. It recognized the views of those who argue that social security pensions are so significant to the financial position of governments and public sector entities that they should be addressed in a separate Standard.

BC6. The IPSASB concluded that, in the light of its views that present obligations for social security pensions arise at the same point as for other programs providing cash transfers to beneficiaries, social security pensions should be dealt with in the same Standard as other cash transfer programs where attainment of retirement age is not an eligibility criterion. The IPSASB saw little merit in developing a separate Standard, which would largely mirror the requirements and guidance for social benefits where attainment of retirement age is not an eligibility criterion.

BC7. The IPSASB also debated whether the scope of the proposed Standard should include all goods and services provided in non-exchange transactions. It is unlikely that the accounting for goods and services or cash transfers in a non-exchange transaction will be different dependent on whether they are provided as social benefits or not. However, it was decided to limit the scope of this Standard to social benefits in order to ensure compatibility with IPSAS 19. In paragraph 1(a) of IPSAS 19 the

scope exclusion for non-exchange transactions is limited to those arising from social benefits.

## **Definitions**

BC8. The IPSASB considered whether the term “social benefits” should be defined. It noted the view of the Steering Committee that what constitutes social benefits varies from jurisdiction to jurisdiction and that this makes the adoption of an exhaustive definition problematic. The IPSASB also acknowledged the view of the Steering Committee that if items were not considered as a “social benefit” they would be dealt with under another International Public Sector Accounting Standard and that this reduces the consequences and risks of not defining the term. At consultation on the ITC, responses were almost evenly split as to whether a definition is necessary.

BC9. There is an attraction of relying on a broad notion of social benefits. However, on balance, it was decided that the term should be defined. In reaching this conclusion the IPSASB felt that a convincing analysis of whether and when a present obligation to beneficiaries in relation to different types of social benefit arises would be difficult unless the term is defined and sub-categorized. As a starting point, the IPSASB took the definition used in the scope-out in IPSAS 19. The IPSASB agreed that any definition should be generic rather than a detailed list of which benefits fall in which category.

BC10. The IPSASB also noted the definition used in the scope-out to IPSAS 19 and the current definition of social benefits in statistical reporting bases including the Government Finance Statistics Manual 2001 (GFSM 2001), which itself is consistent with the System of National Accounts (SNA 1993). The IPSASB agreed with the view of the Steering Committee that, whilst this proposed Standard should use terminology consistent with statistical reporting bases wherever possible, the definition of social benefits should be broader than that used in GFSM 2001. In this context, the IPSASB noted that GFSM 2001 explains that “there is no universally accepted definition of the scope of social benefits and the social risks covered are liable to vary from scheme to scheme and from government to government.”

BC11. The IPSASB adopted a three-part definition of social benefits as:

- Goods and services provided for collective consumption;
- Goods and services provided for individual consumption;  
and
- Cash transfers

BC12. In the proposed Standard the short hand terms “collective goods and services” and “individual goods and services” are used. Although the accounting requirements for collective and individual goods and services are the same, the distinction between collective goods and services and individual goods and services is so entrenched in statistical accounting circles that the IPSASB concluded that it should be retained. It is also useful for analytical purposes as many programs and arrangements for individual goods and services have eligibility criteria, unlike collective goods and services. This characteristic is shared with cash transfers.

BC13. Whilst the distinction between collective and individual goods and services is valid, there may be circumstances where activities can operate as both collective and individual goods and services. This may occur, for example, in the area of criminal justice. Whilst the protection which the criminal justice system is meant to provide is available to all citizens in a jurisdiction there may be cases where eligibility criteria operate. This is acknowledged in paragraph 17 of the Standard, which uses the example of eligibility for a witness protection scheme.

BC14. The IPSASB examined the nature of individual goods and services and cash transfers and considered whether the differences between them are sufficient to merit consideration of separate accounting requirements. The IPSASB concluded that there is one important distinction. Whereas for individual goods and services the transferor can stipulate the purposes to which the resources sacrificed must be applied, for cash transfers the recipient has full discretion how to use those transferred resources. The IPSASB acknowledged that in cases where the transfer of economic benefits is in the form of goods it may be possible for the recipient to sell those goods rather than use them for the purposes specified by the transferor. However, this requires a positive further action on the part of the recipient.



BC15. There may be cases where beneficiaries are provided with cash for the purchase of goods and services. The IPSASB is of the view that such transfers are reimbursements and therefore goods and services. In common with other methods of providing individual goods and services the recipient does not have full discretion as to how the resources are to be used. The expenditure relating to such reimbursements will often require prior authorization and normally reimbursements will only be made after documented proof that the expenditure for which reimbursement is sought has been for purposes specified by the transferor. Such transactions are therefore in substance different from cash transfers.

BC16. In some cases cash transfers will be made to beneficiaries as reductions in the amount of income tax for which they are liable. If such transactions are available to individuals regardless of whether they pay taxes they are expenses paid through the tax system and are within the definition of a cash transfer in this Standard. Such expenses are recognized as if the payment had been made directly in cash to the recipient. In such cases the tax system is used for administrative purposes. However, if allowances are only available to individuals who incur tax liabilities they are tax expenditures- preferential provisions of the tax law that provide taxpayers with concessions that are not available to others- and are not social benefits. Consistent with the approach adopted in ED 29, “Non-exchange Revenue (including Taxes and Transfers)” tax expenditures are foregone revenue; consequently they are not expenses incurred by the entity. They are therefore outside the scope of this Standard. This treatment is also consistent with the requirements on offsetting in paragraphs 48 and 49 of IPSAS1, “Presentation of Financial Statements”

## **Present Obligations for Social Benefits**

### *General*

BC17. The definition of an obligating event requires that a government or other public sector entity has no realistic alternative but to settle the obligation. For social benefits, governments, because of their sovereign powers, have a number of realistic alternatives to providing goods and services in future periods and have considerable discretion to reduce the level of services, introduce alternative programs with a resultant impact on demand or even to cease to provide the service altogether. However,

financial reporting reflects the position at the reporting date based on known conditions; analysis of when a present obligation arises is made within this context. For this reason it is inappropriate to rely on the sovereign powers of government to justify a widespread non-recognition of liabilities for legal obligations. The establishment of such a principle would have far-reaching consequences and bring into question the recognition of liabilities by public sector entities relating to exchange transactions arising from commercial contracts. The IPSASB also considers that there are general and inappropriate risks if accounts-preparers adopt a widespread practice of pre-empting legislative changes.

*Collective and individual goods and services*

BC18. The IPSASB therefore debated at length when a present obligation for financial reporting purposes arises in respect of each of the three types of social benefits. For collective and individual goods and services the Board considered whether a present obligation to beneficiaries might arise. The Board acknowledged that many citizens have a very strong expectation that their government will continue to provide collective and individual goods and services into the future. Indeed a failure to maintain a basic defense capability, a minimum law enforcement capability and a core administrative apparatus might imperil the continued existence of government and state. However, whilst these are important considerations they do not of themselves give rise to a present obligation for a number of reasons.

BC19. First, the provision of collective and individual goods and services is an ongoing activity of government. It is important to note that the Standard addresses obligations of governments from a financial reporting perspective and not the more general obligations of governments from a broader perspective. Consistent with IPSAS 19 an entity would not recognize estimates of future outflows of economic benefits and service potential projected to be necessary for it to remain as a going concern in the future. A present obligation arises as a consequence of a past event; the need to incur costs in the future does not qualify as a past event. For a government to do so would be akin to a manufacturing entity recognizing estimates of employee costs and the costs of raw materials for future accounting periods. Such outflows represent the cost of future obligations rather than present obligations.

BC20. Second, there is not a present obligation for financial reporting purposes, whether legal or constructive, to provide such services in the future. Notwithstanding the view of the IPSASB in paragraph BC.17 that an assessment of the existence of a present obligation is made in the context of the current legal framework, a current legal obligation should not be taken to convey a future legal obligation. Similarly while constructive obligations may occur less frequently in the context of social benefits, a current constructive obligation should not be taken to convey a future constructive obligation. Whilst there will be assumptions that a government will continue to provide collective and individual goods and services, and citizens may have a valid expectation that such provision will occur, there is not a past event, which creates an obligation that an entity has no realistic alternative but to settle.

BC21. Third, particularly in relation to individual goods and services, whilst certain points in an individual's life such as birth, entry to primary education, entry to the workforce and marriage are valuable for forecasting future demand levels for certain social benefits they do not constitute obligating events. Consequently, they do not give rise to present obligations.

BC22. The IPSASB also considered whether the existence of contractual arrangements with employees and other third parties such as suppliers created an indirect and implicit commitment to citizens sufficient to give rise to a present obligation to citizens at a point when the contractual arrangements are entered into with third parties. The IPSASB concluded that entry into such contractual arrangements was too remote to be deemed an obligating event in the context of the government's commitments to citizens.

#### *Cash Transfers and Individual Goods and Services*

BC23. The IPSASB considered at what point a present obligation arises for cash transfers. The IPSASB considered whether a present obligation might not arise until the transfer becomes legally payable, although the individual has satisfied all eligibility criteria. The IPSASB concluded that a present obligation arises when all eligibility criteria have been satisfied, because at that point the transferor has no realistic alternative but to settle, even though the date at which the payment becomes legally enforceable has still to occur.

BC24. Recognizing that many individual goods and services also have eligibility criteria the IPSASB gave particular consideration to the issue of whether a present obligation to beneficiaries arises for individual goods and services. The IPSASB concluded that for individual goods and services there is no present obligation to beneficiaries. This is because recognition of an expense and liability for goods or services prior to their delivery in substance involves recognition of an expense for:

- a. Services to be rendered by employees in future periods where the service is delivered by the entity's own employees; or
- b. Good and services under executory contracts with third parties, which have not yet been delivered.

Were both a liability to the beneficiary and an expense to be recognized for the estimated cost of, for example, medical care at the time at which eligibility is satisfied that liability could only be extinguished by recognition of an equal liability to employees-in this case medical and ancillary staff- or third parties.

BC25. The IPSASB debated at length whether “staying alive” might operate as an implicit eligibility criterion for cash transfers and for individual goods and services. The IPSASB concluded that such a mechanism would be an artificial construct and that it would be inappropriate to adopt it as an implied universal feature of all cash transfer programs. The IPSASB acknowledged that there may be rare cases where “staying alive” or demonstrating “continuing existence” would be an explicit eligibility criterion laid down in governing legislation or regulation. There may even be cases where an individual's eligibility might not be validated until after that individual's death, such as when an individual's military service over a specified period gives rise to a cash payment and that program is retrospective. There may also be cases where an individual's death may itself be the obligating event, such as when the widows or widowers of combatants killed on active duty receive a cash payment.

### **Impact of contributions and earmarked taxes on present obligations**

BC26. The IPSASB considered whether the contributory nature of a program providing cash transfers or whether such a program is financed or partially financed by earmarked taxes might have an impact on when a present obligation arises. It acknowledged the view that the making of

contributions by, or on behalf, of an individual or the payment of earmarked taxes might give rise to a present obligation at an earlier point than for cash transfers that are not contributory. According to this view, the payment of contributions or earmarked taxes might be obligating events that create a valid expectation, or reinforcing existing expectations, that an individual may receive benefits and the public sector entity may have no realistic alternative but to settle those benefits.

BC27. The IPSASB concluded that development of a globally applicable Standard on the basis that, for contributory programs or those financed by earmarked taxes, the obligating event giving rise to a present obligation occurs at a point before all eligibility criteria have been satisfied was not feasible because:

- Whilst a number of different points are possible, dependent upon the nature of the program and the jurisdiction, it is difficult to ascertain with sufficient precision the point at which an obligating event occurs;
- It is far from clear that the payment of contributions or earmarked taxes will always be obligating events giving rise to constructive obligations that leave government or other public sector entities no realistic alternative but to settle. This is particularly the case where outflows of benefits will not occur for a number of years after contributions have been paid; and
- Even where a scheme is non-contributory individuals may have as strong an expectation of receiving benefits on the grounds that they are contributing “indirectly” through general taxation as if the program or activity is contributory.

### **Measurement of liabilities for cash transfers**

BC28. Having established that a present obligation for cash transfers arises when all eligibility criteria have been satisfied the IPSASB considered the extent of the liability and whether detailed guidance should be provided on the liabilities related to particular kinds of cash transfer program. The IPSASB considered that the provision of detailed guidance would not be consistent with a principles based Standard. The IPSASB concluded that the amount of the liability that arises from such a

present obligation is the amount that the entity has no realistic alternative but to settle. In most cases this will be the accrued amount of the next payment to which an applicant is entitled as a result of satisfaction of the eligibility criteria which relates to the reporting period. There may be cases where governing legislation or regulations specify otherwise. In such cases the liability may be for the full amount of the next payment, although part of that payment relates to the next reporting period, or even a series of payments covering the current reporting period and one or more future reporting periods. It is for accounts-preparers to assess the position for each cash transfer program or activity by reference to the legislation and regulations governing that program or activity.

### **Disclosures on fiscal sustainability and the projected future costs of cash transfer programs**

BC29. The IPSASB considered whether the Standard should require or encourage the disclosure of information on the fiscal sustainability of social security pensions and other major cash transfer programs. It was acknowledged that statements and disclosures addressing long-term fiscal sustainability can provide the users of general purpose financial statements with highly relevant information on the viability of key programs that is not conveyed in the statement of financial position and statement of financial performance.

BC30. The IPSASB decided that it would be inappropriate to mandate additional primary statements or disclosures on fiscal sustainability in this Standard because;

- At this stage of the global development of accrual financial reporting in the public sector mandating requirements for the presentation or disclosure of information on fiscal sustainability would make adoption of the Standard difficult for many entities operating in jurisdictions where such information is not currently produced; and
- It is possible that in the future the IPSASB will initiate a project on fiscal sustainability and other prospective information. Such a project will examine this issue in detail and evaluate the various approaches in different jurisdictions.

BC31. The IPSASB also considered whether it should require disclosures of the prospective costs of social security pensions and other major cash transfer programs over a medium term period, for example five years. Such disclosures would not include estimates of inflows such as contributions and earmarked taxes. It was acknowledged that such disclosures might provide relevant information on expenditure trends and thereby enhance users' ability to assess the viability of key programs. There is also a view that such disclosures might be a stepping stone in the development of more detailed disclosures of fiscal sustainability.

BC32. The IPSASB decided not to include such disclosure requirements. This is because:

- The benefits of prospective cost information without estimates of inflows are questionable. Estimating inflows is problematic, giving rise to issues such as the basis on which appropriations and transfers from higher to lower tiers of government should be estimated; and
- As for more sophisticated fiscal sustainability disclosures the IPSASB is reluctant at present to mandate requirements that might deter entities in some jurisdictions from adopting this Standard.

### **Consistency of approach in this ED with IPSAS 19**

BC33. The IPSASB considered whether Example 9 in this ED, which deals with disaster relief is consistent with "Example 2B: *Contamination and Constructive Obligation*" in IPSAS 19, which concerns environmental damage caused by a government naval vessel. The background to that Example 2B in IPSAS 19 is that the government has a widely published environmental policy in which it undertakes to clean up all contamination that it causes and a record of honoring the published policy, although there is no environmental legislation in place. The conclusion is that a government commitment to meet the costs of both the immediate clean-up and the ongoing costs of monitoring environmental damage to fauna does give rise to a present obligation. In Example 9 in this ED the conclusion is that a government's public and written commitment to provide policing services and medical supplies to a multi-

national disaster relief initiative does not give rise to a present obligation. This is despite the fact that the government has a record of honoring similar previous commitments. The IPSASB concluded that there is no inconsistency in the analysis and conclusions in the two examples. Example 2B in IPSAS 19 relates to an exchange transaction whereas Example 9 in this proposed Standard deals with a non-exchange transaction.

### **Transitional Provisions**

BC34. The IPSASB considered whether transitional arrangements are necessary. In many jurisdictions that are already reporting on the full accrual basis the Standard's requirements on recognition and measurement are likely to involve little change from current accounting policies. This is particularly the case for collective and individual goods and services, where, under the requirements of the Standard, liabilities to beneficiaries do not arise. For cash transfers, the requirement in this Standard that a present obligation arises when all eligibility criteria are satisfied regardless of whether the payment is legally due may differ from the "due and payable" approach to determining liabilities which is current in the public sector in some jurisdictions. The IPSASB acknowledged that this may cause difficulty for some accounts-preparers in obtaining comparative information. The IPSASB therefore considered whether an exemption from the provision of comparative information should be included in the Standard in the first year of adoption. On balance the IPSASB concluded that such a transitional arrangement was unjustified.